

**American Bar Association
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**W-14: COMPLYING WITH NEW PROHIBITIONS OF
QUESTIONNAIRES AND ACKNOWLEDGMENTS WHILE
PROTECTING A FRANCHISOR'S LEGITIMATE INTERESTS**

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Appendix 1 – NASAA Statement of Policy Regarding the Use of Franchise Questionnaires and Acknowledgments

COMPLYING WITH NEW PROHIBITIONS OF QUESTIONNAIRES AND ACKNOWLEDGMENTS WHILE PROTECTING A FRANCHISOR'S LEGITIMATE INTERESTS

I. INTRODUCTION

The North American Securities Administrators Association (“NASAA”) Statement of Policy Regarding the Use of Franchise Questionnaires and Acknowledgments (“Statement of Policy” or “SOP”)¹ became effective on January 1, 2023. The SOP’s stated purpose is “to set standards for the proper use of questionnaires and acknowledgments in franchise offerings.”² Its prohibitions have had, and will continue to have, a direct impact on the way that many franchisors draft their franchise agreements and related documents and conduct certain aspects of their sales processes. While the SOP is not a law, it is expected that most or all of the states requiring franchise registration (“Registration States”)³ that have not already done so will adopt the SOP, and Registration States have, in any event, implemented it with state registration filings in 2023 even without formal adoption.⁴

Section II of this paper discusses what questionnaires and acknowledgments are, how franchisors have historically used them, and franchisees’ concerns about their potential use or abuse. Section III explains NASAA’s role in the franchise regulation process, NASAA statements of policy generally, state anti-fraud and anti-waiver statutes, SOP implementation and timeline, franchisor and franchisee reactions to the SOP, and some of the SOP’s legal implications for franchisors and franchisees. Section IV addresses how some franchisors have changed, or could change, their documents and processes to obtain some of the benefits of using questionnaires and acknowledgments without violating the SOP’s guidance. Section V discusses state adoption of the SOP. Section VI addresses the question of whether the SOP signals, or is part of, a more general shift or increase in the regulation of franchising and franchise sales.

¹ N. AM. SEC. ADM’R ASS’N, NASAA STATEMENT OF POLICY REGARDING THE USE OF FRANCHISE QUESTIONNAIRES AND ACKNOWLEDGMENTS (Sept. 18, 2022), <https://www.nasaa.org/wp-content/uploads/2022/09/NASAA-Franchise-Questionnaires-and-Acknowledgments-Statement-of-Policy-9-18-2022.pdf> [hereinafter “Statement of Policy” or “SOP”].

² *Id.* at 1.

³ The fourteen Registration States that require a franchisor to secure registration with the state administrator prior to engaging in the offer and sale of franchises are California, Hawaii, Illinois, Indiana, Maryland, Michigan, Minnesota, New York, North Dakota, Rhode Island, Virginia, Washington, and Wisconsin. They are sometimes referred to as “registration states” or “filing states.” See CAL. CORP. CODE §§ 31000 through 31516; HAW. REV. STAT. § 482E-1 through § 482E-12; 815 ILL. COMP. STAT. §§ 705/1 through 705/44; IND. CODE §§ 23-2-2.5; MD. BUS. REG. CODE §§ 14-201 through 14-232; MICH. COMP. LAWS §§ 445.1501 through 445.1546; MINN. STAT. §§ 80C.01 through 30C.22; N.Y. GEN. BUS. LAW ART. 331 §§ 680, et seq.; N.D. CENT. CODE §§ 51-19-01 through 51-19-17; R.I. GEN. LAWS §§ 19-28.1-1 through 19-28.1-34; S.D. CODIFIED LAWS §§ 37-5B-1 through 37-5B-53; VA. CODE ANN. §§ 13.1-557 through 13.1-574; WASH. REV. CODE §§ 19.100.010 through 19.100.940; WIS. STAT. §§ 553.01 through 553.78. In addition, Oregon has a franchise disclosure law, The Oregon Franchise Transactions law, ORE. REV. STATUTES TIT. 50, CHP. 650, §§ 650.005 through 650.085. There is no registration or review process, and pursuant to the Oregon Administrative Rules, Division 325 – Franchises, a franchisor must deliver a disclosure document required by Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunities; Final Rule, 72 Fed. Reg. 15444, 15445 (Mar. 30, 2007), codified at 16 C.F.R. Part 436, <https://www.ftc.gov/sites/default/files/070330franchiserulefrnotice.pdf> (the “FTC Franchise Rule”) (see 16 C.F.R. § 441-325-0020). Throughout this paper we refer to these states as “Registration States.”

⁴ See Section V of this paper for a discussion of state adoption.

II. FRANCHISOR USE OF QUESTIONNAIRES AND ACKNOWLEDGMENTS

Franchisors have often, although not uniformly, incorporated questionnaires, acknowledgments, or both in the franchise sales process, but their use has not been without controversy. As discussed in more detail below, franchisors claim legitimate benefits from having prospective franchisees formally acknowledge certain facts relating to their understanding of the franchise offering and the franchise sales process. Franchisors have contended that, among other things, having that information helps them ensure that prospective franchisees sufficiently understand their commitments and are not relying on improper or inaccurate information, and that the information can help them discover salesperson or broker misconduct that they can then address and correct.

When disputes later arise, however, franchisees often complain that they did not have a full understanding of the implication of their answers to questionnaires and acknowledgments when they signed them, and that franchisors unfairly use those answers against them when defending against claims of fraudulent or improper sales practices or other claims.

Since the SOP issued, franchisors have had to take a step back and make sure that they know: (i) what, precisely is a “questionnaire” or an “acknowledgment”; and (ii) whether, how, and why they have included them in their sales processes. Franchisees and their counsel, who may have seen questionnaires and acknowledgments used in ways they did not anticipate, are now re-evaluating their rights in light of the SOP, and prospective franchisees signing post-SOP franchise agreements may be less vulnerable to defenses that their franchisor could assert against future claims.

A. What Are Questionnaires and Acknowledgments?

Franchisors typically think of “questionnaires” as documents separate from the franchise agreement that prospective franchisees are required to complete and sign during the franchise sales process. They are generally questions in list form, with a space for a yes/no checkmark or prospective franchisees’ initials beside each question, with a date and signature line at the bottom. Commonly included in questionnaires, at least before the SOP issued, were questions or disclaimers such as:

- Did you sign and date a receipt for the Franchise Disclosure Document (“FDD”) accurately stating the date you received it?
- Did you receive the FDD together with a copy of all proposed agreements relating to the sale of the franchise business at least the longer of 14 calendar days, or ten business days before you executed this questionnaire and before you paid any consideration in connection with the franchise?
- Did you read and understand the FDD and Franchise Agreement?
- Were you given the opportunity to review the FDD and Franchise Agreement with a lawyer, accountant, or other professional advisor?

- Do you understand that businesses, including franchise businesses, involve risk and may fail, and that success depends on many factors, including, without limitation, economic and geographic conditions, competition, your skills, abilities, and efforts, as well as many other factors beyond your control?
- Is it true that no employee or anyone acting on our behalf made statements regarding the anticipated costs, revenue, or profits that are not contained in the FDD you received?
- Do you understand that your answers are important to us and we will rely on them in deciding whether or not to enter into a Franchise Agreement with you?

Some questionnaires require acknowledgment of a variety of other matters, including territorial rights (or lack thereof), potential competition from the franchisor or other franchisees, and other risk factors. They generally include space for franchisees to explain any negative responses and, as noted, often contain language stating that the franchisor is relying on the truthfulness of the responses in granting the franchise.

“Acknowledgments” have generally included some of the representations described above that are contained in the franchise agreements themselves, rather than (or in addition to) separate questionnaires. Some common acknowledgments in franchise agreements include paragraphs or clauses stating that the franchisees acknowledge that:

- The franchisor’s approval of leases or site selection does not guarantee the success or profitability of the franchised location;
- they independently investigated the franchise offering and are not relying on any oral or other representations made to them regarding the likelihood of success or profitability other than information contained in the FDD;
- they timely received the FDD together with a copy of all proposed agreements relating to the sale of the franchise business; and
- they read and understood the FDD and franchise agreement and had the opportunity to discuss those documents with counsel and business advisors.⁵

These types of acknowledgments might be set off separately (sometimes in capital, bolded letters, and sometimes separately initialed). They may be included in separate paragraphs towards the end of the franchise agreement, in the dispute resolution provision, and in other sections addressing, for example, intellectual property rights, site selection and leasing, or other matters.

⁵ See Section II.B.4 below for examples of specific Questionnaire and Acknowledgment language that courts have considered in litigation.

As the SOP explains,

One type of disclaimer takes the form of a series of acknowledgments (“Acknowledgments”) in the franchise agreement regarding the franchise offering. In addition, many—but not all—franchisors require prospective franchisees, at or prior to signing a franchise agreement, to mark “yes” or “no” to a series of questions or agree to a series of representations about what purportedly occurred, or did not occur, in the franchise sales process (“Questionnaires”). Virtually all Questionnaires and Acknowledgments address whether a prospective franchisee received some type of financial performance information different from what the franchisor disclosed in Item 19 of its FDD.⁶

The SOP criticized the breadth of some franchisors’ use of Acknowledgments and disclaimers by stating,

State regulators have observed that Questionnaires and Acknowledgments currently found in some FDDs and franchise agreements are replete with questions and representations that serve no legitimate purpose. Many Questionnaires and Acknowledgments require a prospective franchisee to acknowledge or answer questions that are subjective, unreasonable, or repeat disclosures required to be stated in the FDD. In some cases, Questionnaires require the prospective franchisee to acknowledge identical facts and statements that the franchisee must acknowledge a second time in the franchisor’s franchise agreement. In other cases, these Questionnaires and Acknowledgments require prospective franchisees to agree that they understand specific disclosures made in an FDD or the terms of the franchise relationship.⁷

As discussed in Section III.E below, the SOP, when it applies, prohibits most of the questions and acknowledgments listed above, requiring many franchisors to re-examine some of their long-standing sales practices and procedures.

B. Why Have Many Franchisors Included Questionnaires and Acknowledgments?

Franchisors have historically included Questionnaires and Acknowledgments in their sales processes for a variety of reasons, including clarifying prospective franchisees’ expectations, confirming technical compliance with franchise laws, ferreting out fraud, and improving the franchisor’s position in possible litigation. Each of these reasons is discussed in more detail below. Of course, some franchisors may not have made a conscious decision to include them but simply did so because they were in the template documents prepared and presented to them by their franchise lawyers.

⁶ SOP, *supra* note 1, at 1.

⁷ *Id.* at 5. See also N. AM. SEC. ADM’R ASS’N, NASAA Seeks Public Comment on Proposed Statement of Policy Regarding the Use of Franchise Questionnaires and Acknowledgments (Dec. 7, 2021), <https://www.nasaa.org/61176/nasaa-seeks-public-comment-on-proposed-statement-of-policy-regarding-the-use-of-franchise-questionnaires-and-acknowledgments/>. NAASA noted that the SOP was intended to set regulatory standards because franchisors routinely use questionnaires and acknowledgments to try to limit their potential liability in franchise offerings, and some franchisors are doing so inappropriately.

1. Clarity of Disclosure and Franchisee Expectations

Any lawyer who has counseled prospective franchisees about the risks of entering into franchise agreements has seen many candidates with rose-colored glasses firmly affixed to their faces. No prospective franchisee expects to fail. Franchise agreements and FDDs are long documents, full of information that prospective franchisees may choose to skip over and ignore, or review without the aid of sophisticated and experienced franchise counsel. They are also documents to which the “MEGO”⁸ phenomenon may apply. As the SOP recognized,

By the time prospective franchisees are presented with a franchise agreement or Questionnaire to sign, many are emotionally and financially invested in completing the transaction. As one commenter has noted, “[n]obody buys a franchise in a vacuum. They typically do so after being convinced of the attractiveness of the brand, the strength and utility of the franchisor’s system, the support they will receive from the franchisor, and the enthusiasm they encountered at Discovery Day. None of these factors are the result of reading an FDD.”⁹

However, unlike FDDs and franchise agreements, Questionnaires are typically a page or two of short sentences or questions. Prospective franchisees must read and think separately about these statements or questions in order to agree or disagree. It is undoubtedly the case that some franchisees will simply check “yes” or “true” or insert their initials for each question or representation just to get past yet another document to sign before becoming franchisees. Indeed, it is easy to imagine that unethical franchisors or their staff could instruct the franchisees how to answer, and that franchisees may not carefully read what they are initialing or signing. However, before reviewing the Questionnaire, some prospective franchisees may not fully understand or appreciate the differences between information presented during the sales process and the more legally binding information in the formal franchise documents. The simple Questionnaire format could help focus prospective franchisees on some of the key risks they may not have focused on, and could help them think more clear-eyed or realistically about their new business venture.

2. Confirming Compliance with Legal Requirements

Franchisors must comply with various legal regulations, including franchise disclosure laws. Questionnaires help franchisors collect necessary information and can be part of a program to ensure compliance with these laws. Hopefully, franchisors using Questionnaires review responses carefully, particularly if a negative response or explanation is given for any particular question. For example, did the prospective franchisee receive the FDD and sign the FDD receipt, and did they receive it early enough to comply with the required disclosure time period?¹⁰ Were financial promises or projections made during the sales process outside the FDD?¹¹ If responses

⁸ *MEGO* (“my eyes glaze over”), MERRIAM-WEBSTER.COM DICTIONARY (2023).

⁹ SOP, *supra* note 1, at 2.

¹⁰ FTC Franchise Rule, *supra* note 3, at § 436.2(a). The FTC Franchise Rule requires prospective franchisees to receive a legally compliant FDD “at least 14 calendar-days before the prospective franchisee signs a binding agreement with, or makes any payment to, the franchisor or an affiliate in connection with the proposed franchise sale.” State disclosure laws have similar requirements. See also Stephanie J. Blumstein & Elizabeth M. Weldon, *Eureka or Gotcha Moment? Reliance, Materiality, and Loss Causation: Analysis of Key Elements of Franchisee Claims for Franchise Disclosure*, ABA 44TH ANNUAL FORUM ON FRANCHISING W-1, at 2 (2021).

¹¹ See Section II.B.3 below regarding prohibited financial performance representations.

suggest wrongdoing or are not clear on these points, the franchisor may want to hit the pause button and redisclose¹² the prospect before moving ahead with the transaction or, perhaps stop the transaction altogether. Any unexpected responses should be reviewed to tighten compliance with any technical or substantive legal requirement in the franchise sales process.

3. Ferretting Out Fraud

Franchise salespeople and brokers are generally paid on a commission basis, which can mean that a salesperson is motivated to make sure that a franchise deal is consummated. Ethical franchisors live in fear of “rogue” salespeople who may be misrepresenting the franchise offering and providing prohibited (and potentially fraudulent) financial performance representations (“FPRs”)¹³ and other information inconsistent with statements in the FDD. Investigating unexpected prospective franchisee responses to Questionnaires can help franchisors discover fraudulent or other unethical behavior by those involved in the promotion and sales process to improve (and rectify) it and reduce legal, relational, and other risks.

Although many franchisors may disagree, the SOP took the position, using anecdotal evidence, that, “Questionnaires and Acknowledgments are not the most effective mechanisms for preventing fraud,” stating,

“[a]lthough at least one court has opined that Questionnaires and Acknowledgments can be useful to help franchisors ‘root out dishonest sales personnel and avoid sales secured by fraud,’ they do so by shifting the compliance burden from franchisors to prospective franchisees. It should be the franchisor’s burden to police its own sales personnel and agents; franchisees should not have to confirm that no violations of law have occurred during their own sales process.”¹⁴

4. Providing a Sword or a Shield in Litigation or Arbitration

Experienced lawyers representing franchisors accused of making misrepresentations, or providing prohibited information (whether accurate or not) such as FPRs in addition to or different than those in the FDD, have learned to scour the applicable franchise agreement for relevant Acknowledgments and ask for any Questionnaires that franchisees may have signed during the franchise sales process. That is because courts in many jurisdictions have held franchisees to these pre-sale acknowledgments, representations, and disclaimers, particularly when coupled with standard merger and integration clauses.¹⁵ For example, in *Yogo Factory Franchising, Inc.*

¹² To “redisclose” is to give a prospective franchisee another FDD and have them sign a new FDD receipt acknowledging receipt, which generally should be done any time there is a question as to whether proper FDD disclosure was initially made.

¹³ See, e.g., Dale Cantone, Lulu Gomez & David Gurnick, *Promises, Promises: Financial Performance Representations – Advanced Issues*, ABA 43RD ANNUAL FORUM ON FRANCHISING W-16 (2020).

¹⁴ SOP, *supra* note 1, at 2 (citing *Emfore Corp. v. Blimpie Assocs., Ltd.*, 51 A.D.3d 434, 435 (N.Y. App. Div. 2008)).

¹⁵ See, e.g., *Cook v. Little Caesar Enterprises, Inc.*, 210 F.3d 653 (6th Cir. 2000) (reliance on prior oral representations and documents unreasonable, even if false, and precluded fraud claim); *Trident Atlanta, LLC v. Charlie Graingers Franchising, LLC*, No. 7:18-CV-10-BO, 2020 WL 6889208, at *6 (E.D.N.C. Nov. 23, 2020). (granting summary judgment for the franchisor on misrepresentation and statutory claims because, among other reasons, the franchisees had “responded to a questionnaire used by defendants stating [they] had the opportunity to discuss the benefits and risks of being an area representative with a professional advisor and understood those risks and that no person on behalf of defendant had made any promise regarding the amount of money plaintiffs may earn, the amount of success plaintiffs

v. Ying,¹⁶ a franchisee claimed that the franchisor had fraudulently induced it to enter into its franchise agreements by, among other things, misrepresenting the support it would provide and the prospects for success. The United States District Court for the District of New Jersey dismissed the franchisee's claims, noting that one franchise agreement provision "states that the franchisee has conducted an independent investigation of the franchise business, and realizes the business venture involves risk."¹⁷ The franchise agreement also contained a provision in which the franchisee acknowledged that:

Your success in this business is not guaranteed, is speculative and depends, to an important extent, upon your ability as an independent business person. [Franchisor] does not represent or warranty that the Store will achieve a certain level of sales or be profitable.... [Franchisor] expressly disclaims the making of, and you acknowledge you have not received, any warranty or guarantee, express or implied, as to the potential volume, profits or success of the business venture contemplated by this Agreement.¹⁸

The court further stated that "[t]he franchise agreements contain a 'franchise disclosure questionnaire'" that the franchisee had signed.¹⁹ The Questionnaire at issue asked:

could expect, or the support service or assistance that defendants would provide to plaintiffs"); *Massey, Inc. v. Moe's Sw. Grill, LLC*, No. 1:07-CV-0741-RWS, 2015 WL 438513, at *21 (N.D. Ga. Feb. 3, 2015), *aff'd sub nom.* *Tronnes v. Moe's Sw. Grill, LLC*, 664 F. App'x 828 (11th Cir. 2016) (franchise agreement disclaimer language barred Tennessee Consumer Protection Act claims); *Governara v. 7 Eleven, Inc.*, No. 13-cv-6094, 2014 WL 4476534 (S.D.N.Y. Aug. 20, 2014) (granting franchisor's motion to dismiss plaintiff's claims under the anti-fraud provisions of the New York Franchise Act based in part on non-reliance disclaimers executed by the plaintiff); *Guesthouse Int'l Franchise Sys., Inc. v. British Am. Props. MacArthur Inn, LLC*, 2009 WL 278214, at *6-*7 (M.D. Tenn. Feb. 5, 2009) (citing *Burton v. Hardwood Pallets, Inc.*, No. E200301439COAR3CV, 2004 WL 572350, at 2* (Tenn. Ct. App. Mar. 22, 2004)) (finding it unreasonable for a franchisee to rely on representations contradicting terms plainly expressed in the written contract); *Siemer v. Quizno's Franchise Co.*, No. 07-cv-2170, 2008 WL 904874 (N.D. Ill. Mar. 31, 2008) (franchisor's defense based in part on disclosure acknowledgment statement through which franchisee was put on notice of potential business risks); *Jackson Hewitt Inc. v. Childress*, No. CIVA 06-CV-0909 DMC, 2008 WL 834386, at *11 (D.N.J. Mar. 27, 2008) (integration clauses or disclaimers in franchise agreements make "alleged reliance on any prior representations not contained in the Franchise Agreements... unreasonable as a matter of law"); *Lady of Am. Franchise Corp. v. Malone*, No. 05-61304-CIV, 2006 WL 7354110, at *5 (S.D. Fla. Feb. 13, 2006) (dismissing Florida Franchise Act claim because franchisee failed to establish any set of facts circumventing the franchise agreement's unambiguous disclaimer language); *Hotels of Key Largo, Inc. v. RHI Hotels, Inc.*, No. 96-328P, 694 So. 2d 74, 76-78 (Fla. Dist. Ct. App. 1997) (licensees failed to state a claim for fraud, breach of implied covenant, rescission, or violation of the Florida Franchise Act where they could not have justifiably relied on the alleged representations; evidence of representations further barred by the parol evidence rule); *Frank Collier Auction & Realty Co. v. Rice*, No. 01A01-9608-CH-00384, 1997 WL 71817 (Tenn. Ct. App. Feb. 21, 1997) (contractual disclaimers bar fraud and Consumer Protection Act claims); *Hall v. Burger King Corp.*, 912 F. Supp. 1509, 1529 (S.D. Fla. 1995) (franchisees could not have relied on pre-contract representations at odds with their acknowledgments in franchise agreement and in light of merger and integration clause); see also SOP, *supra* note 1, at n.1 (citing *Martrano v. Quizno's Franchise Co.*, No. 08-cv-0932, 2009 WL 1704469, at *5 (W.D. Pa. June 15, 2009) ("Defendants pointedly assert, in their December 2008 Motion before this Court, that 'Each Plaintiff was asked directly to disclose any representation he had received other than those contained in the UFOC. In the space provided, each and every one of the plaintiffs wrote 'None.'").

¹⁶ *Yogo Factory Franchising, Inc. v. Ying*, No. CIV.A. 13-630 JAP TJ, 2014 WL 1783146 (D.N.J. May 5, 2014) (dismissing fraud, negligent misrepresentation, and RICO claims in light of disclaimer and integration language in franchise agreement).

¹⁷ *Id.* at *4.

¹⁸ *Id.*

¹⁹ *Id.*

Has any employee or other person speaking on behalf of [Franchisor] made any statement or promise concerning the revenue, profits or operating costs of [the] store or business operated by [Franchisor] or its franchisees except as expressly provided in Item 19 of the Franchise Disclosure Document?

Has any employee or other person speaking on behalf of [Franchisee] made any statement or promise concerning a Yogo Factory store, kiosk or cart that is contrary to, or different from, the information contained in the Disclosure Document?

Has any employee or other person speaking on behalf of [Franchisor] made any statement or promise regarding the amount of money you may earn in operating a Yogo Factory store or business?

Has any employee or other person speaking on behalf of [Franchisor] made any statement, promise or agreement concerning the advertising, marketing, training, support service or assistance that [Franchisor] will furnish to you that is contrary to, or different from, the information contained in the Disclosure Document?²⁰

The franchisee had answered “No” to each of these questions, and answered “Yes” to the question asking if “the franchisee understand[s] that the approval of [Franchisor] of the Approved Store Location for a Yogo Factory store does not constitute an assurance, representation, or warranty of any kind as to the successful operation or profitability of a Yogo Factory store at the Approved Store Location?”²¹ The court relied on all of these facts in dismissing the franchisee’s claims.

However, this approach has not been universal, as the SOP recognized, stating that, “[a]lthough not all courts agree, many courts have concluded that franchise contractual disclaimers, including Questionnaires and Acknowledgments, violate state anti-waiver provisions²² when they serve as a release or waiver of a franchisee’s rights under a state franchise law.”²³

As an example, in *Randall v. Lady of America*,²⁴ the United States District Court for the District of Minnesota stated,

²⁰ *Id.*

²¹ *Id.*

²² SOP, *supra* note 1, at 3. As the SOP explains, most state franchise laws “include provisions (“Anti-Waiver Provisions”) that prohibit or render void any provision or condition requiring a prospective franchisee to agree to a release, waiver or estoppel that would relieve a person from liability under that law.” (citing CAL. CORP CODE § 31512; HAW. REV. STAT. § 482E-6; 815 ILL. COMP. STAT § 705/41; IND. CODE § 23-2-2.7-1; MD. BUS. REG. CODE § 14-226; MICH. COMP. LAWS § 445.1527(b); MINN. STAT. § 80C.21; N.Y. GEN. BUS. LAW ART. 33 § 687(4); R.I. GEN. LAWS § 19-28.1-15; S.D. CODIFIED LAWS §37-5B-26(8); N.D. CODE § 51-19-16(7); VA. CODE ANN. § 13.1-571(c); WASH. REV. CODE § 19.100.180(2); WIS. STAT. § 553.76).

²³ SOP, *supra* note 1, at 3.

²⁴ *Randall v. Lady of Am. Franchise Corp.*, 532 F. Supp. 2d 1071 (D. Minn. 2007). This case is cited in the SOP, *supra* note 1, at 3-4.

The disclaimer cannot change the historical facts; if the dishonest franchisor made misrepresentations, then he made misrepresentations, no matter what the franchise agreement says. Thus, the disclaimer can only be an attempt to change the legal effect of those misrepresentations. That is precisely what [the Minnesota] anti-waiver language forbids.²⁵

However, other courts, including those in the same district, have disagreed with this precedent.²⁶

Similarly, in *Hanley v. Doctors Express*,²⁷ the United States District Court for the District of Maryland “held that disclaimers and acknowledgments contained in a franchise agreement and FDD were legally inoperative to bar a franchisee’s claims under the Maryland Franchise Law based on the Anti-Waiver Provision of that law to the extent that they would operate as a release, waiver, or estoppel.”²⁸ The *Hanley* court also “noted that integration clauses and waivers are not necessarily wholly irrelevant, citing the issue of reliance.”²⁹ According to the court, “the disclaimers remain factually relevant, and might be persuasive to a fact finder with respect to the materiality of the alleged misrepresentations and omissions and the reasonableness of plaintiffs’ reliance on them.”³⁰

The SOP emphasized this aspect of Questionnaires and Acknowledgments by stating that “[o]ver at least the last 30 years, franchisors have included in their franchise agreements and FDDs language that they can later use as a disclaimer of liability” and that they “routinely seek to use Questionnaires, Acknowledgments, and other forms of contractually required disclaimers to insulate themselves from potential liability by franchisees alleging fraud or misrepresentations in the offer and sale of a franchise.”³¹

C. Franchisee Concerns

As discussed above, prospective franchisees often confuse what is in the sales material, what they heard (or thought they heard) at Discovery Day,³² and what is in the FDD or franchise agreement. In addition to concerns about the legal implications of signing Questionnaires and Acknowledgments (discussed below) that may arise later, franchisees have other concerns and

²⁵ *Randall*, 532 F. Supp. 2d., at 1088-89.

²⁶ *Moxie Venture L.L.C. v. UPS Store, Inc.*, 156 F. Supp. 3d 967 (D. Minn. 2016) (dismissing Minnesota Franchise Act claim because franchisee could not reasonably have relied on franchisor’s alleged income projections when the franchise agreement “expressly disclaimed any reliance on the defendant’s representations about projected future income.”).

²⁷ *Hanley v. Doctors Express Franchising, LLC*, No. 12-cv-794, 2013 WL 690521, at *29 (D. Md. Feb. 25, 2013). This case is cited in the SOP, *supra* note 1, at 4.

²⁸ SOP, *supra* note 1, at 4.

²⁹ *Id.* at n. 13.

³⁰ *Hanley*, 2013 WL 690521, at *29.

³¹ SOP, *supra* note 1, at 1.

³² “Discovery Day” is a common term franchisors use for their initial sales presentations where groups of prospective franchisees learn about the brand and the franchise offering.

considerations regarding the use of Questionnaires and Acknowledgments during the sales process.

1. Alignment with Franchise Documentation

With respect to any ancillary document relating to the overall franchise relationship, franchisees want to ensure consistency and alignment with terms and conditions of the main franchise documentation (e.g., the FDD and franchise agreement). Naturally, franchisees could be concerned that there could be inconsistencies or discrepancies between the information provided in the Questionnaires and the actual contractual obligations to which they will eventually be bound. They may also not have enough clarity to know the difference between information in the FDD and franchise agreement or other information provided during the sales process.

2. Legal Implications of Questionnaires and Acknowledgments

Franchisees asserting claims in litigation or arbitration regarding alleged pre-sale misconduct are often cross-examined about Acknowledgments and disclaimers in Questionnaires and franchise agreements they signed, in some cases years earlier. Not surprisingly, franchisees and their counsel may feel that this “gotcha” use of those documents is unfair and unduly prejudicial. They may further complain that the franchise agreements and related documents are unconscionable contracts of adhesion³³, that the franchisor engaged in high-pressure sales tactics or was otherwise deceitful, and that they had no choice but to sign. Franchisees may also claim that their lack of sophistication, business experience or, in some cases, English language skills, mean that they should not be held to the representations or disclaimers in those documents. As a result, some commenters have expressed concern “that Questionnaires and Acknowledgments limit a franchisee’s ability to hold a franchisor accountable for fraud and deceit, irrespective of the underlying facts of a franchisee’s claims.”³⁴

According to the SOP, “[i]n the opinion of the Section and the Project Group, Questionnaires and Acknowledgments violate state anti-waiver provisions when they are used as contractual disclaimers that release or waive a franchisee’s rights under a state franchise law,” and that “[t]he prospective franchisee who signs a Questionnaire or series of Acknowledgments and later denies the accuracy of what was signed would have to explain such a discrepancy, but they should have that opportunity before a factfinder, rather than have their claims dismissed based solely on having signed a Questionnaire or series of Acknowledgments.”³⁵

³³ “Typical contracts of adhesion are standard-form contracts offered by large, economically powerful corporations to unrepresented, uneducated, and needy individuals on a take-it-or-leave-it basis, with no opportunity to change any of the contract’s terms.” *Aviall, Inc. v. Ryder Sys., Inc.*, 913 F. Supp. 826, 831 (S.D.N.Y. 1996), *aff’d*, 110 F.3d 892 (2d Cir. 1997). However, the fact that a court determines a particular contract to be one of adhesion is not sufficient, on its own, for the contract to be deemed unconscionable and therefore unenforceable. See, e.g., *Mance v. Mercedes-Benz USA*, 901 F. Supp. 2d 1147, 1162 (N.D. Cal. 2012) (“while the contract was adhesive, this fact, alone . . . does not render the arbitration provision procedurally unconscionable”).

³⁴ SOP, *supra* note 1, at 3.

³⁵ *Id.* at 4.

D. Franchisor Counterarguments

Many franchisors would take the position that the SOP's prohibitions, discussed in Section III.E below, go much farther than making sure that franchisees have the opportunity to explain any discrepancies between their version of the truth during litigation or arbitration and the "accuracy" of their representations in Questionnaires and Acknowledgments they may have signed. Those franchisors might point out that the SOP throws out the baby with the bathwater by prohibiting those representations *in toto*, rather than simply ensuring that franchisees be given the opportunity to contradict their own earlier representations or explain the circumstances surrounding them.

It is well-established that parties are generally presumed to have read and understood the contracts they have signed and that, if they fail to do so, they are nonetheless bound by the terms of those contracts.³⁶ If this is so, franchisors ask, then why should it be objectionable to ask prospective franchisees simple, factual questions to which they know, or should know, the answers? That is, if a franchisor seeks to determine what occurred during the sales process – it is likely that the most appropriate person to ask is the person involved and impacted – the franchisee.³⁷

Further, Questionnaires may encourage discussion between the parties in situations where franchisees' Questionnaire responses suggest misunderstanding or potential non-compliance. It is therefore unsurprising that some franchisors and franchise lawyers have taken the positions, among others, that the SOP "is too broad," that Questionnaires and Acknowledgments help "identify prospective franchisees who have not done sufficient diligence to buy a franchise and may not understand the risks and the details of the offer," and that Questionnaires and Acknowledgments give those prospective franchisees "the opportunity to better understand the contract terms and franchise relationship before signing the franchise agreement."³⁸

Accordingly, many franchisors believe that Questionnaires and Acknowledgments "act as a factual record that does not waive any rights and therefore do not violate the law."³⁹ Additionally,

³⁶ See, e.g., *Preferred Cap., Inc. v. Power Eng'g Grp., Inc.*, 860 N.E.2d 741, 745 (Ohio 2007) (reiterating the "long-held principle that parties to contracts are presumed to have read and understood them and that a signatory is bound by a contract that he or she willingly signed"). "It is... undisputed that the parties to a contract are presumed to have read and understood the terms of the contract into which they have entered." *State Farm Fire & Cas. Co. v. Wallace*, 997 F. Supp. 2d 439, 447 (W.D. Va. 2014) (citing *Calbreath v. Va. Porcelain & Earthenware Co.*, 63 Va. (22 Gratt.) 697, 717 (1872)); see also *Gibbes, Inc. v. Law Eng'g, Inc.*, Case No. 91-1048, 1992 WL 78830, at *5 (4th Cir. Apr. 20, 1992); *In re Prudential Ins. Co. of Am.*, 148 S.W.3d 124, 134 (Tex. 2004) (noting the presumption applies "absent some claim that [the parties] were tricked into agreeing to" the terms of a contract). If a party fails to read a contract which he signs, he does so at his peril. See *Metro Realty of Tidewater, Inc. v. Woolard*, 223 Va. 92, 99, 286 S.E.2d 197 (1982) ("In the absence of fraud, duress, or mutual mistake, a person 'having the capacity to understand a written document who reads it, or, without reading it or having it read to him, signs it, is bound by his signature.'") (quoting *Rossi v. Douglas*, 203 Md. 190, 199, 100 A.2d 3 (1953)) (emphasis added).

³⁷ See, for example, comments to NASAA Proposed SOP, *infra* note 58, of Lathrop GPM ("[Acknowledgments and Questionnaires] are simply factual statements regarding what did or did not occur during the franchise sales process, or that document the prospective franchisee's knowledge of certain facts contemporaneous with the signing of the franchise agreement.") A number of similar comments were submitted from franchisor counsel to the NASAA Proposed SOP.

³⁸ Dale Cantone, Mark A. Kirsch & Theresa Leets, *The 2022 NASAA Statement of Policy and Other Regulatory Developments*, ABA 45TH ANNUAL FORUM ON FRANCHISING W-13, at 6-7 (2022).

³⁹ *Id.* at 7.

Questionnaires and Acknowledgments can be helpful tools to gather information, assess potential franchisees, comply with legal requirements, and establish clear communication and understanding between the parties, which in turn serves to protect the interests of franchisors and franchisees and to help ensure a smooth and compliant franchise relationship.

III. STATEMENT OF POLICY REGARDING THE USE OF FRANCHISE QUESTIONNAIRES AND ACKNOWLEDGMENTS

A. The Role of NASAA

NASAA is the oldest international organization devoted to investor protection, which represents state, provincial, and territorial securities administrators in the fifty states, the District of Columbia, Puerto Rico, the U.S. Virgin Islands, Canada, and Mexico.⁴⁰ While NASAA does not have direct regulatory authority over franchising, its primary objective is to protect investors and it does so by, among other things, facilitating regulatory coordination and promoting best practices among state securities (including, franchise) regulators.⁴¹ NASAA primarily accomplishes this by, among other things, protecting investors from fraud and abuse, conducting investor education, providing guidance and assistance via the established regulatory framework, and advocating passage of strong, sensible, and consistent state securities laws and regulations in various industries⁴², including franchising, that its members can adopt and implement at the state, provincial, and territorial levels.

NASAA's Franchise and Business Opportunity Project Group (the "Franchise Project Group"), a standing committee formed in the 1980s, provides a forum where regulators can address issues relating to franchises and business opportunities.⁴³ The Franchise Project Group studies and makes recommendations to NASAA about model acts, statements of policy, and interpretive commentaries with a goal to benefit investors of franchises and business opportunities and those industries.⁴⁴

⁴⁰ See NASAA: ABOUT US, <https://www.nasaa.org/about/> (last visited July 10, 2023). According to the NASAA website, members of NASAA have a "multifaceted mission of protecting investors from fraud and abuse, conducting investor education, providing guidance and assistance via the established regulatory framework, and ultimately helping power the North American economy by ensuring the integrity of the financial markets"; see *also* Cantone, Kirsch & Leets, *supra* note 38, at 3.

⁴¹ Cantone, Kirsch & Leets, *supra* note 38, at 3. Noting that because most state franchise administrators are also the state's securities regulators, NASAA's mission includes protecting franchise investors, and NASAA has established a standing project group to coordinate projects for franchising and business opportunity investments.

⁴² See *generally* NASAA: ABOUT US, <https://www.nasaa.org/about/> (last visited July 10, 2023); NASAA: INDUSTRY RESOURCES, <https://www.nasaa.org/industry-resources/> (last visited July 10, 2023). The following industry resources are available on the NASAA website: (i) Broker-Dealers; (ii) Investment Advisers; (iii); Securities Issuers; (iv) Franchise Resources; (v) Senior Issues; (vi) Uniform Securities Acts; (vii) Uniform Forms; and (viii) Central Registration Depository (CRD) and the Investment Adviser Registration Depository (IARD) systems.

⁴³ See N. AM. SEC. ADM'R ASS'N, NASAA FRANCHISE AND BUSINESS OPPORTUNITIES PROJECT GROUP RESPONSE TO SOLICITATION FOR PUBLIC COMMENTS ON PROVISIONS OF FRANCHISE AGREEMENTS AND FRANCHISOR BUSINESS PRACTICES DOCKET ID FTC-2023-0026, June 8, 2023, https://www.nasaa.org/wp-content/uploads/2023/06/NASAA-Franchise-PG-Comment-Letter-re-FTC-RFI-Docket-FTC-2023-0026_6-8-2023.pdf.

⁴⁴ *Id.*

In addition to the SOP Regarding the Use of Franchise Questionnaires and Acknowledgments, NASAA has issued four other statements of policy.⁴⁵

B. Statements of Policy Generally

NASAA statements of policy cover a wide range of areas, including securities regulation, enforcement actions, examination practices, and coordination among securities regulators (including, state franchise regulators). These statements serve as a framework for state securities regulators in developing and implementing their own rules and regulations. NASAA makes the statements of policy publicly available on its website.⁴⁶

While NASAA has no direct authority over franchising, the Federal Trade Commission (“FTC”) and states that regulate franchising have historically given great weight to the recommendations, commentaries, and policy initiatives of NASAA’s Franchise Project Group and, in many cases, states have specifically incorporated them into their franchise laws.⁴⁷ The SOP has no legal effect unless it is adopted by a state that regulates the sale of franchises. Many franchise Registration States have chosen to adopt NASAA’s policies and guidelines as a framework for their own franchise registration requirements.⁴⁸

Most Registration States have statutory or regulatory provisions that expressly or impliedly grant the state’s franchise regulators discretion to interpret the FTC Franchise Rule’s disclosure requirements and add to or modify the FDD for use in those states.⁴⁹ In turn, state adoption of NASAA guidance is often considered to create consistency and uniformity in franchise regulation across different states and promotes coordination and cooperation among states in enforcing franchise regulations and protecting franchisees. As such, and as discussed above, it should

⁴⁵ See, e.g., 2009 N. AM. SEC. ADM’R ASS’N, NASAA STATEMENT OF POLICY: UNIFORM FRANCHISE DELIVERY REQUIREMENTS, September 20, 2009, https://www.nasaa.org/wp-content/uploads/2011/08/4-Uniform_Franchise_Delivery.pdf; 2003 N. AM. SEC. ADM’R ASS’N, NASAA Statement of Policy Regarding Electronic Delivery of Franchise Disclosure Documents, September 14, 2003, https://www.nasaa.org/wp-content/uploads/2011/08/8-Electronic_Delivery_Franchise_Disclosure.pdf; 2001 N. AM. SEC. ADM’R ASS’N, NASAA STATEMENT OF POLICY REGARDING FRANCHISE ADVERTISING ON THE INTERNET, September 9, 2001, https://www.nasaa.org/wp-content/uploads/2011/08/9-Franchise_Advertising_Internet.pdf; 1998 N. AM. SEC. ADM’R ASS’N, NASAA STATEMENT OF POLICY REGARDING OFFERS OF FRANCHISES ON THE INTERNET, May 3, 1998, https://www.nasaa.org/wp-content/uploads/2011/08/12-Internet_Offers_Franchises.pdf.

⁴⁶ See N. AM. SEC. ADM’R ASS’N, NASAA FRANCHISE RESOURCES, <https://www.nasaa.org/industry-resources/franchise-resources/> (last visited June 10, 2023).

⁴⁷ See generally NASAA NEW FRANCHISE STATE COVER SHEETS INSTRUCTIONS, May 19, 2019, <https://www.nasaa.org/wp-content/uploads/2019/06/New-Franchise-State-Cover-Sheets-Instructions.pdf>. As an example, to better help franchisees understand the FDD, NASAA adopted the State Cover Sheets in May 2019, and the State Cover Sheets became effective January 1, 2020, replacing the State Cover Page in the FDD. The new guidelines for State Cover Sheets required changes to the structure, content, and overall format of the FDD State Cover Page and the Effective Date Page. All Registration States effectively require the new format and can also ask franchisors to add financial related risk factors to the NASAA State Cover Sheets.

⁴⁸ In states where there is no franchise registration and disclosure law, violation of NASAA guidance could potentially be found to violate state unfair trade practice statutes or other laws.

⁴⁹ See generally, WASH. REV. CODE § 19.100.040(1) (“An application for registration of the offer,... must be filed with the director and shall contain... Such other information as the director determines, by rule or order, to be necessary or appropriate to facilitate the administration of this chapter”); CAL. CORP. CODE § 31114; HAW. REV. STAT. § 482E-3(22); N.Y. GEN. BUS. LAW § 683.2(u) (noting that “additional” disclosures may be required by the commissioner or may be required the state franchise regulator’s discretion).

come as no surprise that NASAA statements of policy – while discretionary – have been adopted or followed in most franchise Registration States.

C. Applicability To Offers and Sales / State Anti-Waiver or Anti-Fraud Provisions

At a high level, state anti-waiver provisions are designed to protect individuals or businesses from being forced to waive important rights or legal protections through contractual agreements. In franchising, such state anti-waiver provisions are typically aimed at safeguarding franchisees from waiving rights granted to them by state franchise laws (e.g., termination rights, renewal rights, or post-termination competitive activities). In other words, state anti-waiver provisions can ensure that franchisees are not coerced into giving up their state statutory rights through contractual provisions or waivers included in their franchise agreements.⁵⁰ Of course, state franchise anti-waiver laws are statutory provisions specifically enacted by state legislatures to regulate the franchising relationship and protect franchisees and are laws specific to the franchise context, while common law anti-waiver laws are principles derived from court decisions and judicial precedent that apply more broadly to contractual agreements.

Similarly, anti-fraud franchise laws are legal provisions designed to protect prospective franchisees from fraudulent or deceptive practices in franchising. These laws aim to ensure that franchisors provide accurate and truthful information to prospective franchisees, maintain fair business practices, and prevent fraudulent schemes or misrepresentations (e.g., require that franchisors provide comprehensive and timely disclosures to prospective franchisees; prohibit franchisors from making false or misleading statements, representations, or omissions in their communications with prospective franchisees; and provide franchisees with remedies in case of fraud or misrepresentation).⁵¹

The SOP applies to Questionnaires and Acknowledgments and similar documents that appear in FDDs and applicable attachments and exhibits used in the offer and sale of franchises

⁵⁰ See CAL. CORP CODE §31512 (limited to “waiv[ing] compliance with any provision of this law or any rule or order hereunder”); HAW. REV. STAT. § 482E-6(2)(F) (limited to “waiv[ing] any compliance with any provision of this chapter or a rule promulgated hereunder”); 815 ILL. COMP. STAT § 705/41 (limited to “waiv[ing] compliance with any provision of this Act or any other law of this State”); IND. CODE § 23-2-2.7-1, Sec. 1(5) (limited to “reliev[ing] any person from liability to be imposed by this chapter”); MD. BUS. REG. CODE § 14-226 (limited to “reliev[ing] a person from liability under this subtitle”); MICH. COMP. LAWS § 445.1527(b) (limited to “depriv[ing] a franchisee of rights and protections provided in this act”); MINN. STAT. § 80C.21 (limited to “waiving compliance with any provision of sections 80C.01 to 80C.22 or any rule or order thereunder”); N.Y. GEN. BUS. LAW ART. 33 § 687(4) (limited to “waiv[ing] compliance with any provision of this law, or rule promulgated hereunder”); N.D. CODE § 51-19-16(7) (limited to “waiv[ing] compliance with any provision of this chapter or any rule or order hereunder”); R.I. GEN. LAWS §19-28.1-15 (limited to “waiv[ing] compliance with, or relieving a person of, a duty of liability imposed by or right provided by this act or a rule or order under this act”); S.D. CODIFIED LAWS § 37- 5B-21 (limited to “waiv[ing] compliance with or relieving a person of a duty or liability imposed by or a right provided by this chapter or a rule or order under this chapter”); VA. CODE ANN. § 13.1-571(c) (limited to “waiv[ing] compliance with any provision of this chapter or of any rule or order thereunder”); WASH. REV. CODE § 19.100.180(2)(g) (limited to “waiver which would relieve any person from liability imposed by this chapter”) and WASH. REV. CODE § 19.100.220(2) (limited to “waiv[ing] compliance with any provision of this chapter or any rule or order hereunder”); and WIS. STAT. § 553.76 (limited to “waiv[ing] compliance with any provision of this chapter or any rule or order under this chapter”).

⁵¹ SOP, *supra* note 1, at n. 10 (listing statutes).

where an Anti-Waiver Provision⁵² or Anti-Fraud Provision⁵³ applies to the offer or sale.⁵⁴

As the SOP explains,

Questionnaires and Acknowledgments violate state anti-waiver provisions when they are used as contractual disclaimers that release or waive a franchisee's rights under a state franchise law. Courts that have found otherwise have not recognized or appreciated the history and purpose of state franchise registration and disclosure laws. The state legislatures that enacted these franchise laws intended to protect franchisees from the effect of contractual disclaimers, including those that may take the form of Questionnaires and Acknowledgments.⁵⁵

In the SOP, NASAA cited examples of franchisees changing their Questionnaire answers in order to avoid the possibility of being prevented from going through with the sale based on those answers.⁵⁶ While acknowledging the helpfulness of Questionnaires and Acknowledgments, NASAA nevertheless expressed concern in the SOP that that the harm done by such Questionnaires and Acknowledgments in allowing franchisors to use them to defeat claims of fraud and misrepresentation outweighs any benefit.⁵⁷

D. Timeline

On December 6, 2021, NASAA, through its Corporation Finance Section and Franchise Project Group, stated that it was developing a potential policy on franchise Questionnaires and Acknowledgments, with the release of a proposal for a Statement of Policy on Franchise Questionnaires and Acknowledgments ("Proposed SOP").⁵⁸ Upon the release of the Proposed SOP, NASAA stated that it would seek to "address the problem of inappropriate uses of franchise questionnaires and acknowledgments in franchise offerings", and that "[f]ranchisors routinely seek to use Questionnaires, Acknowledgments, and other forms of contractually required

⁵² *Id.* at 3. ("Anti-Fraud Provisions" refer to provisions in state franchise laws that prohibit any person from committing fraud, making untrue statements of material fact, or omitting to state a material fact regarding a franchise offering).

⁵³ *Id.* at 3. ("Anti-Waiver Provisions" refer to provisions that prohibit or render void any provision or condition requiring a prospective franchisee to agree to a release, waiver or estoppel that would relieve a person from liability under that law).

⁵⁴ *Id.* at 5.

⁵⁵ *Id.* at 4.

⁵⁶ *Id.* at 5 (citing *Braatz v. Red Mango*, 2015 WL 1893194 (N. D. Tex. Apr. 27, 2015), *aff'd sub nom. Braatz, L.L.C. v. Red Mango FC, L.L.C.*, 642 F. App'x 406 (5th Cir. 2016) (franchisees alleged they changed their answers in Questionnaire about receiving financial information because the franchisor told them that they could not open the franchise without the Questionnaire being completed in the form the franchisor required)); Comment from Anonymous, posted by the FTC on December 9, 2020 ("While I signed a questionnaire saying I didn't rely on information outside of that disclosure document, that was not true, however, I knew that would preclude me from making the franchise purchase if I answered truthfully"), <https://www.regulations.gov/comment/FTC-2020-0064-0042> (last visited July 2, 2023).

⁵⁷ SOP, *supra* note 1, at 1.

⁵⁸ N. AM. SEC. ADM'R ASS'N, REQUEST FOR PUBLIC COMMENT: PROPOSED STATEMENT OF POLICY REGARDING THE USE OF FRANCHISE QUESTIONNAIRES AND ACKNOWLEDGMENTS, Dec. 6, 2021, <https://www.nasaa.org/wp-content/uploads/2021/12/Request-for-Public-Comment-SOP-on-Franchise-Questionnaires-12-6-2021.pdf> [hereinafter "NASAA Proposed SOP"].

disclaimers to insulate themselves from potential liability by franchisees alleging fraud or misrepresentations in the offer and sale of a franchise.”⁵⁹

NASAA requested public comments to the Proposed SOP. The public comment period on the Proposed SOP commenced on December 6, 2022 and ended on January 5, 2022.⁶⁰ A total of 39 comments were submitted to NASAA.⁶¹ On September 18, 2022, NASAA announced that its members had formally adopted a Statement of Policy Regarding the Use of Franchise Questionnaires and Acknowledgments.⁶² At the same time, NASAA announced that the SOP would become effective starting January 1, 2023.⁶³ The final SOP adopted by NASAA was not significantly modified from the original Proposed SOP. A copy of the final SOP, as adopted by NASAA, is attached as Appendix 1. The final SOP adopted by NASAA was not significantly modified from the original Proposed SOP.

E. SOP Requirements

The SOP states that if a franchisor requires prospective franchisees to sign Questionnaires and Acknowledgments or similar documents prior to signing a franchise agreement, the proposed form must be attached to the FDD under Item 22.⁶⁴ Further, the written script of any video or electronic recording of Questionnaires and Acknowledgments must be included in Item 22.⁶⁵

Section II of the SOP sets forth certain prohibitions within Questionnaires and Acknowledgments. Specifically, Section II.A of the SOP states that the SOP uses the definitions from the NASAA 2008 Franchise Registration and Disclosure Guidelines including “Franchise,” “Franchise Seller,” “Franchisor,” “Person,” and “Prospective franchisee.”⁶⁶

⁵⁹ *Id.* at 1. To support this position, NASAA cited two cases: (i) *Martrano v. Quizno’s Franchise Co.*, No. 08-cv-0932, 2009 WL 1704469, at *5 (W.D. Pa. June 15, 2009) (“Defendants pointedly assert, in their December 2008 Motion before this Court, that ‘Each Plaintiff was asked directly to disclose any representation he had received other than those contained in the UFOC. In the space provided, each and every one of the plaintiffs wrote ‘None.’”); and (ii) *Siemer v. Quizno’s Franchise Co.*, No. 07-cv-2170, 2008 WL 904874 (N.D. Ill. Mar. 31, 2008) (franchisor’s defense based in part on disclosure acknowledgment statement through which franchisee was put on notice of potential business risks). NASAA went on to state that some franchisors “have been successful” at insulating themselves from potential liability by franchisees alleging fraud or misrepresentations in the offer and sale of a franchise, citing *Governara v. 7 Eleven, Inc.*, No. 13-cv-6094, 2014 WL 4476534 (S.D.N.Y. Aug. 20, 2014) (granting franchisor’s motion to dismiss plaintiff’s claims under the anti-fraud provisions of the New York Franchise Act based in part on non-reliance disclaimers executed by the plaintiff).

⁶⁰ NASAA Proposed SOP, *supra* note 58, at 1.

⁶¹ See N. AM. SEC. ADM’R ASS’N, COMMENT LETTERS TO NOTICE OF REQUEST FOR PUBLIC COMMENT REGARDING PROPOSED STATEMENT OF POLICY REGARDING THE USE OF FRANCHISE QUESTIONNAIRES AND ACKNOWLEDGMENTS, December 7, 2021, <https://www.nasaa.org/nasaa-proposals/?t=franchise&y=2021> [hereinafter “SOP Comments”].

⁶² See generally SOP, *supra* note 1.

⁶³ *Id.* at 1.

⁶⁴ *Id.* at 6.

⁶⁵ *Id.*

⁶⁶ *Id.* at 5-6. The SOP specifically lists the following defined terms within the SOP: “Franchisee” means any person who is granted a franchise; “Franchise seller” means a person that offers for sale, sells, or arranges for the sale of a franchise. It includes the franchisor and the franchisor’s employees, representatives, agents, subfranchisors, and third-party brokers who are involved in franchise sales activities. It does not include existing franchisees who sell only their

Section II.C.1 of the SOP prohibits Questionnaires and Acknowledgments that are subjective or unreasonable, or that:

- a. Would cause a reasonable Prospective franchisee to surrender or believe that they have surrendered rights to which they are entitled under federal or state law;
- b. Would have the effect of shifting Franchisor's disclosure duties under federal or state law to the Prospective franchisee; or
- c. Are otherwise Prohibited Statements under this Statement of Policy or are similar to the Prohibited Statements (as described below).⁶⁷

Section II.C.2 of the SOP enumerates the following eleven Prohibited Statements in Questionnaires and Acknowledgments:

- a. That the Prospective franchisee has read or understands the FDD or any attachments thereto, including the franchise or other agreement.
- b. That the Prospective franchisee understands or comprehends the risks associated with the purchase of the franchise.
- c. That the Prospective franchisee is qualified or suited to own and operate the franchise.
- d. That, in deciding to purchase the franchise, the Prospective franchisee has relied solely on the FDD and not on any other information, representations, or statements from other Persons or sources.
- e. That neither Franchisor nor Franchise seller has made any representation, including any financial performance representation, outside of or different from the FDD and attachments thereto.
- f. That the success or failure of the franchise is dependent solely or primarily on Franchisee.
- g. That the Franchisor bears no liability or responsibility for Franchisee's success or failure.

own outlet and who are otherwise not engaged in franchise sales on behalf of the franchisor; "Franchisor" means any person who grants a franchise and participates in the franchise relationship. Unless otherwise stated, it includes subfranchisors. For purposes of this definition, a "subfranchisor" means a person who functions as a franchisor by engaging in both pre-sale activities and post-sale performance; "Person" means any individual, group, association, limited or general partnership, corporation, or any other entity; and "Prospective franchisee" means any person (including any agent, representative, or employee) who approaches or is approached by a franchise seller to discuss the possible establishment of a franchise relationship.

⁶⁷ *Id.* at 6.

- h. That reiterates or duplicates any representation or statement already made elsewhere in the FDD and attachments thereto.
- i. That the Prospective franchisee has had the opportunity to or has/has not actually consulted with professional advisors or consultants or other franchisees.
- j. That the Prospective franchisee agrees or understands that the Franchisor is relying on the Questionnaire, Acknowledgments, or similar documents, including to ensure that the sale of the franchise was made in compliance with state and federal law or that no unauthorized, inaccurate, or misleading statements were made.
- k. That requires or suggests that the Prospective franchisees must agree to any Questionnaires, Acknowledgments, or similar documents prohibited by this Statement of Policy or provide false answers as a condition to the purchase of the franchise.⁶⁸

Section II.C.3 of the SOP states that the franchisor must include in its FDD and franchise agreement, or applicable state-specific addenda to the FDD and franchise agreement, the following:

No statement, questionnaire, or acknowledgment signed or agreed to by a franchisee in connection with the commencement of the franchise relationship shall have the effect of (i) waiving any claims under any applicable state franchise law, including fraud in the inducement, or (ii) disclaiming reliance on any statement made by any franchisor, franchise seller, or other person acting on behalf of the franchisor. This provision supersedes any other term of any document executed in connection with the franchise.⁶⁹

F. Franchisor Reaction to the SOP

While franchisors, their counsel, and the International Franchise Association (“IFA”)⁷⁰ have reiterated a desire for honest, accurate and transparent disclosure to prospective franchisees, many are strongly opposed to the SOP, which they believe creates a number of legal, practical, and commercial concerns.

⁶⁸ *Id.* at 6-7.

⁶⁹ *Id.* at 7.

⁷⁰ See Int’l Franchise Ass’n, FranBlog Press Release, *IFA files comments with the North American Securities Administrators Association (NASAA) in response to their Proposed Statement of Policy Regarding the Use of Franchise Questionnaires & Acknowledgments*, <https://www.franchise.org/blog/ifa-files-comments-with-the-north-american-securities-administrators-association-nasaa-in> (last visited July 30, 2023). After filing comments with NASAA regarding the SOP, the International Franchise Association noted that it viewed “the appropriate use of acknowledgements and questionnaires as a useful tool in the franchise sales process, especially to ensure franchisors and franchisees are on the same page and any inappropriate sales are stopped before moving forward. [The IFA does] however agree with NASAA that questionnaires and acknowledgements should not be a broad liability shield. Ideally, NASAA will soften their policy approach and continue to allow the use of questionnaires and acknowledgements in appropriate fashions.”

For example, in its response to the Proposed SOP, the IFA articulated concerns with, at the time, the Proposed SOP. IFA interpreted the Proposed SOP to: (i) prohibit some business practices that really are not at the root of NASAA's concerns; (ii) inhibit legitimate due diligence by both franchisees and franchisors before they commit to long-term relationships; (iii) interfere unduly with franchisors' and franchisees' freedom to contract on terms to which they agree; (iv) potentially harm the very franchisees whom NASAA seeks to protect; (v) reflect an outdated view of franchisee experience and sophistication; and (vi) create a standard for evaluation that cannot, as a practical matter, be administered by state franchise regulators consistently, objectively, or timely because each regulator necessarily will be called upon to view—through her or his own prism and with her or his own biases—nuanced language in Questionnaires and Acknowledgments used by franchisors operating in myriad industries and then subjectively judge whether or not that language complies with the policy ultimately issued.⁷¹

Many franchisors have proactively complied with the SOP since its issuance, despite its formal adoption in only some of the Registration States (as discussed in Section IV below). A common franchisor complaint is the lack of uniformity in interpretation and approach among the Registration States with respect to the SOP, and, in the face of examiner comments, no clear explanation as to why certain statements are prohibited even when there is a “catch-all” reference back to the SOP making clear that any statements violating the SOP would not apply in Registration States.

G. Franchisee Reaction to the SOP

In light of the fact that many franchisors have unilaterally (as discussed in Sections IV.A and B. below), and in the face of comment letters (as discussed in Section V below), elected to remove Questionnaires and Acknowledgments from their franchise documents, the SOP has been well-received by franchisees and their counsel, especially those that have long taken the position that Questionnaires and Acknowledgments allow franchisors to unfairly defeat claims of fraud and misrepresentation and violate anti-fraud and anti-waiver provisions in state franchise laws.⁷²

IV. THE AFTERMATH – FRANCHISOR CHANGES AND ADAPTATIONS

When the SOP was issued, franchisors questioned, among other things, its timing of applicability, whether and how changes should be made for use in non-Registration States, the use of, or effect on, state addenda, and how to compensate for any loss of information useful for ferreting out fraud, ensuring compliant pre-sale processes, and how to protect themselves in

⁷¹ See Int'l Franchise Ass'n, *Letter Regarding Request for Public Comment: Proposed Statement of Policy Regarding the Use of Franchise Questionnaires and Acknowledgments*, December 6, 2021, <https://www.nasaa.org/wp-content/uploads/2021/12/IFA-Response-to-NASAA-Request-for-Comment-on-Acknowledgments-and-Questionnaires.pdf>.

⁷² See generally American Ass'n of Franchisees & Dealers, *The Center for Total Quality Franchising, Statement of Support for the Proposed NASAA Statement of Policy Regarding the Use of Franchisee Questionnaires and Acknowledgments*, January 4, 2022, <https://www.nasaa.org/wp-content/uploads/2021/12/Support-of-NASAA-SOP-on-Disclaimers.pdf>. In a brief letter to NASAA, the American Association of Franchisees and Dealers stated that it “wholeheartedly supports the [Proposed SOP].” *Id.* See also, for example, comments to NASAA Proposed SOP, Keith R. Miller, Franchisee Advocacy Consulting, January 4, 2022, <https://www.nasaa.org/wp-content/uploads/2021/12/Support-of-NASAA-SOP-on-Disclaimers.pdf>. (“[I]t’s not okay to shield responsibility by having franchisees quickly sign off on questionnaires and acknowledgments.”) A number of similar comments were submitted by franchisees and their counsel to the NASAA Proposed SOP.

litigation from unmeritorious claims.

A. Registration vs. Non-Registration States

Franchisors that did not see significant value from their use of Questionnaires and Acknowledgments generally made a prompt decision to remove them altogether, at least upon annual renewal in 2023. Those that found them to be a valuable tool have considered whether they should use different FDD versions in non-Registration States than in Registration States. While possible, doing so makes the sales process more cumbersome and, potentially, prone to inadvertent error because of the risk of providing the wrong form document to a Registration State candidate. If this occurs, among other things, it could lead to grounds for rescission under state registration and disclosure laws.⁷³

B. State Addenda

As noted above, the SOP states that a franchisor must include in its FDD and franchise agreement, or applicable state-specific addenda to the FDD and franchise agreement, the following provision:

No statement, questionnaire, or acknowledgment signed or agreed to by a franchisee in connection with the commencement of the franchise relationship shall have the effect of (i) waiving any claims under any applicable state franchise law, including fraud in the inducement, or (ii) disclaiming reliance on any statement made by any franchisor, franchise seller, or other person acting on behalf of the franchisor. This provision supersedes any other term of any document executed in connection with the franchise.⁷⁴

This language could lead a franchisor to reasonably conclude that it could leave Acknowledgments in its standard franchise agreements as long as its Registration State addenda contained this curative language and its franchise agreements made clear that the Acknowledgments did not apply where they were prohibited.

However, there have been some differences in approaches, even within the same states, as to whether changes can be made to the state addenda rather than in the franchise agreement itself. Some regulators have taken the position that franchisors cannot leave Acknowledgments in their franchise agreements, even if the addenda make clear that the Acknowledgments do not apply with respect to Registration State transactions. Some individual regulators have also reportedly insisted that form Questionnaires be removed from the FDD, even if those Questionnaires clearly state on their face that they are not to be signed by franchisees in Registration States. Some franchisors have found these approaches inconsistent with past regulatory practice and the fundamental purpose of state-specific addenda and have also expressed concern about what could be perceived as regulators' improper attempt to exercise

⁷³ For more discussion on rescission, see generally Harris J. Chernow & Michael D. Joblove, *Rescission and Restitution: Remedies for Private Causes of Action—Be Concerned? Maybe? Maybe Not?*, ABA 44th ANNUAL FORUM ON FRANCHISING W-7 (2021).

⁷⁴ SOP, *supra* note 1, at 7.

extraterritorial regulatory powers.⁷⁵

C. Other Ways to Ferret Out Fraud and Ensure Compliant Pre-sale Processes

As discussed in Section II.B above, franchisors have used Questionnaires and Acknowledgments to help ferret out fraud by rogue salespeople and to help them develop and ensure legally-compliant pre-sale processes. Since the SOP issued, franchisors have been considering alternative ways to obtain these benefits without using Questionnaires and Acknowledgments.

The SOP states, in a footnote, that it “is not intended to prohibit a franchisor from conducting factfinding or asking prospective franchisees questions about the sales process, but franchisors may not require a prospective franchisee to document and sign statements that act as waivers in violations of state law.”⁷⁶ However, it does not provide specific examples of compliant “factfinding” that would not risk violating the SOP.

Franchisors have been brainstorming with counsel about a variety of options. Some ideas considered or implemented have included email surveys and compliance calls.

1. Email Surveys

Some franchisors have considered or implemented programs that include sending follow-up emails to prospective franchisees asking them for (but not requiring them to provide) feedback about the sales process or to volunteer any representations made to them at odds with the FDD provided. These email surveys can be simple to implement and may also be automated. If implemented, for quality control purposes, the email inquiry or survey should not be sent (and direct responses should not be received) by any individual who interacted with the prospect in the actual sales process.

Even though, as noted above, email survey programs can be easy to implement, response rates to email surveys can be disappointing, so the utility of this approach will depend in large part on the response rate obtained. Although this could be seen as an “end run” around the SOP, such surveys, if optional, should not run afoul of the SOP’s prohibitions because they would not be required, even if they are later used for litigation purposes.⁷⁷ However, franchisee lawyers may still challenge these approaches or object to their use in litigation, and regulators could find that they violate the SOP’s spirit, if not its letter.

2. Compliance Calls

Franchisors may also implement a pre- or post-sale voluntary, interview process or “compliance call,” asking scripted questions and memorializing the responses. Again, this process should not involve individuals who were directly involved in the sales process, since a primary goal would be to monitor and assess the compliance of the sales team. As long as this interview

⁷⁵ For more discussion on extraterritorial application of regulatory powers, see generally Bryan Dillon & Ann H. MacDonald, *The Long Arm of the Law: The Extraterritorial Scope of State Franchise Registration and Disclosure and Relationship Laws in Litigation*, ABA 45TH ANNUAL FORUM ON FRANCHISING W-5 (2022).

⁷⁶ SOP, *supra* note 1, at n.15.

⁷⁷ *Id.* at 6 (“The Franchisor and its Franchise seller(s) shall not *require* the Prospective franchisee to make any statement in any Questionnaires, Acknowledgments, or similar documents...” (emphasis added)).

is completely voluntary, recordings may be permissible as long as any other applicable laws relating to notice or other recording requirements are followed.⁷⁸ However, there is always a risk that franchisees could claim that they felt coerced into participating so that participation was not truly voluntary, thereby violating the SOP. Notes could also be taken, although franchisors may want to consider also disclosing that fact.

The compliance call option is, by its nature, more labor intensive than a follow-up email. Franchisors should also be aware that, for Registration States, if the franchisor “requires the prospective franchisee to verbally respond to any Questionnaires, Acknowledgments, or similar statements on video or other electronic media recording before entering into the franchise agreement, a written script of the proposed form of such Questionnaires, Acknowledgments or similar statements must be referenced in Item 22 of the FDD and attached as an exhibit.”⁷⁹

3. Enhanced Compliance Training and Audits

Franchisors may decide to review their current procedures and implement enhanced compliance training to help compensate for potentially reduced pre- and post-sale feedback about the process. Franchisors should include in that training information about the SOP, where and how it applies, and questions or practices that could violate it. Such compliance training should include a review of the Questionnaire (if used), discussion of its use and purpose as a compliance tool.

4. Compliance Audits

Franchisors may also want to develop or enhance sales audit procedures through more frequent review of sales scripts, Discovery Day presentations, and printed and online brochures and other sales material. Franchisors should also very carefully train sales staff and any outside parties involved in the sales process to make sure that they understand and embrace compliance and compliance strategies. Further, questions within Questionnaires should be as short as possible, should only elicit factual information, and should be easy for a layperson to understand.

Of course, audit procedures are worthless without action and follow-up. Franchisors should take steps immediately to investigate and correct any identified or suspected non-compliant processes or behavior, including terminating sales staff or broker relationships, if appropriate.

5. Use of Qualifying Language Before Questionnaires and Acknowledgments

In response to the SOP, some franchisors have attempted to retain Acknowledgments within their franchise agreements that contain the types of statements that are prohibited by the SOP, but qualify them to apply only to non-Registration States. For example, introductory language to the franchisee Acknowledgments provisions in the franchise agreement may state:

⁷⁸ See, e.g., Ed Finkel, *The Two Faces of Eavesdropping*, 103 Ill. B.J. 20, 23 (2015) (discussing state “one-party” and “two party” consent laws applicable to making audio recording of conversations).

⁷⁹ SOP, *supra* note 1, at 6. In addition, if the franchisor decides to require completion of Questionnaires or similar documents that do not include the forbidden questions or Acknowledgments “before entering into the franchise agreement, the proposed form of such Questionnaires, Acknowledgments or similar documents must be referenced in Item 22 of the FDD and attached as an exhibit.” *Id.*

The following acknowledgments below apply to all franchisees and franchises except not to any franchisees and franchises that are subject to the state franchise registration/disclosure laws of California, Hawaii, Illinois, Indiana, Maryland, Michigan, Minnesota, New York, North Dakota, Rhode Island, South Dakota, Virginia, Washington, and Wisconsin.

Similarly, some franchisors have attempted to retain Questionnaires that contain the types of questions that are otherwise restricted by the SOP, but qualify them to apply only to franchises to be operated in non-Registration States. For example, introductory language to the Questionnaires may state:

This Questionnaire will not be used if the franchise is to be operated in, or you are a resident of, California, Hawaii, Illinois, Indiana, Maryland, Michigan, Minnesota, New York, North Dakota, Rhode Island, South Dakota, Virginia, Washington, or Wisconsin.

So far, acceptance of the foregoing has been varied, including varied approaches within the same Registration States (i.e., no comments for a particular brand; but comments for a different brand using the same approach above).

6. Different FDDs

While perhaps as a last resort, some franchisors – especially those that determine that having Questionnaires and Acknowledgments is valuable – may have two forms of FDD. One form will have Questionnaires and Acknowledgments for use in the states that allow them (including, any Registration States that elect not to adopt or follow the SOP, and the 36 so-called “non-Registration States” that are subject to only the FTC Franchise Rule), and another form that excludes Questionnaires and Acknowledgments for use in the states that follow the SOP. As discussed above in Section IV.A, while having two forms of FDD may be challenging, especially for the franchisor’s sales and development team, it may be a path forward to allow something like a continuation of “business as usual” in a majority of the states.

D. Litigation and Arbitration Considerations

Although the techniques above could be useful in detecting rogue or non-compliant sales behaviors, their potential usefulness to franchisors in later litigation has not yet been tested. If, for example, franchisees eventually claim that improper FPRs were provided, franchisors may be able to present evidence that the franchisees did not mention that fact in their responses to an email survey (or did not respond to the email survey at all after being given the opportunity to do so), or in a follow-up compliance call.

Franchisors should, however, expect franchisee counsel to object to admission of such evidence, arguing that it is an end-run around the SOP’s prohibitions. It is also worth noting that because these alternative methods are evidence outside the agreement itself, it may be less likely that a court or arbitrator would find it to be dispositive. Accordingly, using the information in that way would be less likely to implicate the SOP’s concern that franchisees signing Questionnaires or Acknowledgments would later be denied the opportunity to explain any discrepancies to “a

factfinder, rather than have their claims dismissed based solely on having signed a Questionnaire or series of Acknowledgments.”⁸⁰

E. Reading the Tea Leaves

As of the presentation of this paper, the SOP will still be less than year old, calculated from its January 1, 2023 effective date. Not all questions have been answered and, as discussed in Section IV.B above, there is still no uniformity in implementation or approach among the states, or even with respect to different examiners in the same states.

It is too soon to tell for sure how the SOP will affect new or existing franchise relationships. Will franchisors still be able to rely on “old” Questionnaires for Registration State franchisees who signed their franchise agreements and Questionnaires before January 1, 2023? Will that determination depend on the litigation or arbitration forum or the contractual choice of law provision? How will anti-waiver statutes be taken into account in this determination?⁸¹

Going forward, how will the SOP affect the franchise relationship and litigation strategy? Will franchisors be able to continue to rely on “old” Questionnaires and Acknowledgments in future litigation if they were signed pre-SOP?⁸² Will there be any difference in non-Registration States or under non-Registration State law? Will email surveys (or lack of response) and compliance calls have any value in arbitration or litigation? Only time will tell, although franchise lawyers on both sides are undoubtedly already framing their arguments.

V. THE AFTERMATH – STATE ADOPTION AND IMPLEMENTATION

As noted, the SOP became effective on January 1, 2023. Franchisors should now comply with the SOP when filing any application in a Registration State and assume and expect that state regulators in the fourteen Registration States will likely implement the SOP, whether or not formally adopted. As such, state franchise examiners may deny franchise registration applications on the basis of franchisors’ failure to remove or appropriately revise Questionnaires and Acknowledgments.

A. California

Although California has not formally adopted the SOP, on September 29, 2022, in response to the SOP, the state of California amended its franchise law effective January 1, 2023,

⁸⁰ *Id.* at 4.

⁸¹ *Id.* at 3 (citing CAL. CORP CODE § 31512; HAW. REV. STAT. § 482E-6; 815 ILL. COMP. STAT § 705/41; IND. CODE § 23-2-2.7-1; MD. BUS. REG. CODE § 14-226; MICH. COMP. LAWS § 445.1527(b); MINN. STAT. § 80C.21; N.Y. GEN. BUS. LAW ART. 33 § 687(4); R.I. GEN. LAWS § 19-28.1-15; S.D. CODIFIED LAWS §37-5B-26(8); N.D. CODE § 51-19-16(7); VA. CODE ANN. § 13.1-571(c); WASH. REV. CODE § 19.100.180(2); WIS. STAT. § 553.76).

⁸² See generally State of Was. Dep’t. of Financial Institution Securities Div., Notice of Preproposal Statement of Inquiry Concerning the NASAA Statement of Policy Regarding the Use of Franchise Questionnaires and Acknowledgments, Jan. 23, 2023, <https://dfi.wa.gov/sites/default/files/cr-101-memo-nasaa-sop-franchise.pdf> [hereinafter “Washington SOP Notice”]. As an example, in its preproposal notice relating to possible adoption of the SOP, the Washington Department of Financial Institutions Securities Division noted that “adoption of the [NASAA SOP] does not represent a material change in requirements for franchise offerings in Washington”, which implies that adoption by the state of SOP is clarifying, and not a deviation from current practices.

with the enactment of Assembly Bill no. 676 (the “CA AB-676”).⁸³ CA AB-676 changes the California Franchise Investment Law (“CFIL”) by adding § 31512.1, which prohibits any provision in a franchise agreement, FDD, or other writing, disclaiming: (i) representations made by franchisors or their personnel or agents to prospective franchisees; (ii) reliance by franchisees on any representations made by franchisors or their personnel or agents; and (iii) reliance by franchisees on the FDD and any FDD exhibits.⁸⁴ Any such disclaimers are deemed contrary to public policy and void and unenforceable.⁸⁵

CA AB-676 also puts new restrictions on the approval process for transferring a franchise. The new law requires prospective franchisees who wish to purchase an existing franchise or the assets of an existing franchise business, to provide specified information, including their name, address, agreements related to the purchase of the franchise business, and an application, to the franchisor, after which the franchisor must notify the prospective franchisee, within 15 days of any additional information or documentation needed.⁸⁶ The franchisor must notify a prospective franchisee of the approval or disapproval of an application to purchase an existing franchise business within sixty days and if the application is not approved, notify the applicant of the reason for disapproval.⁸⁷

Additionally, among other things, CA AB-676 adds a new provision that prohibits a franchisor from refusing to grant a franchise or provide financial assistance to a prospective franchisee or an existing franchisee based on discriminatory criteria (including the franchisee’s sex, race, color, religion, ancestry, national origin, disability, medical condition, genetic information, marital status, sexual orientation, citizenship, immigration status) or any characteristic of the composition of the neighborhood or geographic area where the franchise would be located.⁸⁸

B. Washington

On January 23, 2023, the state of Washington issued a Notice of Preproposal Statement of Inquiry Concerning the NASAA Statement of Policy Regarding the Use of Franchise Questionnaires and Acknowledgments, stating that the Washington Department of Financial Institutions Securities Division was considering proposing an amendment to the state’s franchise law to formally adopt the SOP.⁸⁹ In the Notice, the Washington regulator notes that provisions that would require prospective franchisees to make statements that are subjective, unreasonable, or that attempt to absolve the franchisor or its agents of liability in connection with the sale of a franchise are “inconsistent with the Franchise Investment Protection Act’s anti-waiver

⁸³ Assemb. Bill 676, 2021-2022 Reg. Sess. (Cal. 2022) (enacted), <https://legiscan.com/CA/text/AB676/id/2292494> (last visited July 13, 2023).

⁸⁴ CAL. CORP. CODE § 31512.1.

⁸⁵ *Id.* As noted, while the SOP was not formally adopted, CA AB-676 clarifies California’s anti-waiver provision in CFIL to specifically state that asking a franchisee to disclaim or deny reliance on representations made by the franchisor or its agents is contrary to California public policy, void and unenforceable.

⁸⁶ CAL. CORP. CODE § 31126.

⁸⁷ CA AB-676, *supra* note 83.

⁸⁸ CAL. CORP. CODE § 31212.

⁸⁹ Washington SOP Notice, *supra* note 82.

provisions”⁹⁰ and that the “the adoption of the [NASAA SOP] does not represent a material change in requirements for franchise offerings in Washington.”⁹¹ The Washington regulator also stated that “adoption of the [NASAA SOP] would aid franchisors in complying with existing Washington law by providing specific examples of prohibited questionnaires and acknowledgments, while also increasing compliance with anti-waiver and anti-fraud requirements across the states with such requirements.”⁹² In practice, the Washington franchise examiners have already been issuing comments requiring revisions to the Questionnaires and Acknowledgments used by franchisors.

On August 23, 2023, the Washington Securities Division notified franchisors with offerings in Washington that the Securities Division will amend the Washington Administrative Code to adopt the SOP, effective September 18, 2023.⁹³ The section of the franchise rules reflecting the adoption of the SOP will be located at Washington Administrative Code 460-80-325.⁹⁴ Once the amendment becomes effective on September 18, 2023, the SOP will apply to registered and exempt franchise offerings in Washington, and the Washington Securities Division will review franchise offering materials submitted to the Division for compliance with the SOP.⁹⁵ Franchisors may include the legend required by Section II.C.3 of the SOP (as discussed in Section III.E of this paper) in the Washington Addendum to the Franchise Agreement and the Washington Addendum to the FDD.⁹⁶

C. Maryland

On January 23, 2023, the Securities Division of the Office of the Attorney General of the State of Maryland issued Interpretive Opinion/No Action Position Adopting NASAA Statement of Policy Regarding the Use of Franchise Questionnaires and Acknowledgment (the “Maryland Opinion”), adopting the SOP as of January 30, 2023. In the Maryland Opinion, the Maryland Attorney General’s office noted that:

For the past several years, Securities Division examiners have required franchisors to include a legend in franchise offering materials, including Questionnaires and Acknowledgments, to address the concern that those materials may violate the Maryland Anti-Waiver Provision. That legend states that “all representations requiring prospective franchisees to assent to a release, estoppel or waiver of liability are not intended to nor shall they act as a release, estoppel or waiver of any liability incurred under the Maryland Franchise

⁹⁰ See RCW §§19.100.220(2), 19.100.180(2)(g).

⁹¹ Washington SOP Notice, *supra* note 82, at 1.

⁹² *Id.*

⁹³ See *generally* State of Was. Dep’t. of Financial Institution Securities Div., Notice of Adoption of the NASAA Statement of Policy Regarding the Use of Franchise Questionnaires and Acknowledgment, Aug. 23, 2023, <https://dfi.wa.gov/rulemaking/nasaa-statement-policy-regarding-use-franchise-questionnaires-and-acknowledgments>.

⁹⁴ *Id.* Washington Administrative Code 460-80-325 will be amended as follows: “NASAA statement of policy regarding the use of franchise questionnaires and acknowledgments. In order to promote uniform regulation, the administrator adopts the North American Securities Administrators Association (NASAA) Statement of Policy Regarding the Use of Franchise Questionnaires and Acknowledgments, as adopted September 18, 2022.”

⁹⁵ *Id.*

⁹⁶ *Id.*

Registration and Disclosure Law.” The Securities Division allows a franchisor to include this legend in a Maryland Addenda to their franchise offering, if the franchisor’s offering materials are designed to be used in multiple states.⁹⁷

In light of the foregoing, and the stated reasons for the SOP, the Maryland Securities Commissioner found “good cause” to follow the SOP in order to provide a “uniform approach to review of franchise offering materials for compliance under [Maryland’s] anti-waiver provisions, including the Maryland Anti-Waiver Provision.”⁹⁸

While the SOP is effective in Maryland, the Maryland Opinion includes a no action clause, meaning that franchise regulators will not require registered franchisors to immediately file an amendment to conform with the SOP.⁹⁹ If a franchisor sells a franchise in Maryland before its next renewal or amendment filing, however, the franchisor must include the legend described in the SOP, delete its Questionnaires and Acknowledgments that contravene the SOP or include a statement that those do not apply to prospective Maryland franchisees, and update its materials in the next renewal or amendment of franchise registration filed in Maryland.¹⁰⁰ The Maryland Opinion clarifies that, consistent with the instructions of the SOP, a franchisor may make the above changes in its FDD and franchise agreement or in state-specific addenda applicable to both documents.¹⁰¹

D. Others States

While not all Registration States have formally adopted the SOP, they have indirectly through the issuance of comment letters - as expected - essentially required that franchisors remove Questionnaires and Acknowledgments from their FDDs and Franchise Agreements.¹⁰²

As of the date of this paper, it is unclear if and how “Baby FTC Acts” or “Little FTC Acts” (i.e., state laws that mirror the provisions of the FTC Franchise Rule at the state level) may reflect the SOP. For the most part, these acts are aimed to protect consumers and businesses from unfair and deceptive trade practices within the state’s jurisdiction, so some states may find that SOP violations could violate their Little FTC Acts as well.

⁹⁷ State of Maryland Office of the Attorney General Securities Division, Interpretive Opinion/No Action Position Adopting NASAA Statement of Policy Regarding the Use of Franchise Questionnaires and Acknowledgments, Jan. 23, 2023, https://www.marylandattorneygeneral.gov/Securities%20Documents/Franchise%20_SOP_Revised_022323.pdf.

⁹⁸ *Id.* at 2.

⁹⁹ *Id.* at 3.

¹⁰⁰ *Id.*

¹⁰¹ *Id.*

¹⁰² For example, the Minnesota Department of Commerce has sent comment letters to franchisors in 2023 stating that the following must be in both the FDD and agreements, or an addendum to both: “No statement, questionnaire, or acknowledgement signed or agreed to by a franchisee in connection with the commencement of the franchise relationship shall have the effect of (i) waiving any claims under any applicable state franchise law, including, fraud in the inducement, or (ii) disclaiming reliance on any statement made by any franchisor, franchise seller, or other person acting on behalf of the franchisor. This provision supersedes any other term of any document executed with the franchise, including but not limited to [Representations and Warranties by Franchisee / Acknowledgments] Sections of the Franchise Agreement.”

VI. IS THE SOP PART OF A LARGER SHIFT?

Some franchisors may believe that NASAA has a more activist agenda than in the past, and there have been changes in the federal regulatory environment at the FTC as well. Franchisees and their lawyers may see these as welcome changes, while franchisors may be less enthusiastic. Is the SOP part of a larger state and federal shift towards policies, statutes, regulations, and enforcement efforts aimed at protecting parties perceived as vulnerable or having weaker bargaining power?

A. Changes and Other Developments at the FTC

The SOP noted that “the FTC held a public workshop in 2020 to explore issues related to both Questionnaires and Acknowledgments” but had “not yet directly addressed whether or when those provisions violate the FTC Franchise Rule.”¹⁰³

In January 2021, along with the change in the White House administration, former FTC Chair Joseph Simons resigned, “along with members of his senior staff.”¹⁰⁴ On June 15, 2021, Democrat Lina M. Khan, appointed by President Joseph Biden, was sworn in as FTC Chair.¹⁰⁵ Ms. Khan is known for her work in antitrust law and has been associated with advocating for stricter enforcement of antitrust regulations. Her appointment to the FTC was seen as part of a broader conversation about potential changes in antitrust enforcement and policy.

In February 2023, a Bloomberg Law article described how “Christine Wilson, the sole Republican on the Federal Trade Commission, . . . announced she is resigning from the agency over her fierce opposition to progressive FTC Chair Lina Khan’s agenda.”¹⁰⁶ According to that article, Wilson, had “spent months publicly criticizing Khan’s efforts to crack down on corporate power using antitrust laws, said she is resigning due to Khan’s ‘defiance of legal precedent and her abuse of power to achieve desired outcomes.’”¹⁰⁷

In March 2023, a Bloomberg Law article entitled, “FTC Lawyers Leave at Fastest Rate in Years as Khan Sets New Tone,” stated, among other things, that “[t]he Federal Trade Commission’s senior attorneys are leaving at a pace not seen in at least two decades, adding to the challenges facing the agency as it pursues expansive rulemaking.”¹⁰⁸

On March 10, 2023, the FTC issued a press release announcing, “FTC Seeks Public

¹⁰³ SOP, *supra* note 1, at 3.

¹⁰⁴ Reuters Staff, Business News, *U.S. FTC Chair Says He Will Resign Along With Senior Staff*, Jan. 21, 2021, <https://www.reuters.com/article/us-ftc-simons/u-s-ftc-chair-says-he-will-resign-along-with-senior-staff-idUSKBN29O1XB>.

¹⁰⁵ FTC, PRESS RELEASE, LINA M. KHAN SWORN IN AS CHAIR OF THE FTC, Jun. 15, 2021, <https://www.ftc.gov/news-events/news/press-releases/2021/06/lina-m-khan-sworn-chair-ftc>.

¹⁰⁶ Emily Birnbaum, *Republican FTC Official Resigns, Citing Chair Khan’s Agenda*, Feb. 14, 2023, <https://news.bloomberglaw.com/antitrust/republican-ftc-official-resigns-over-chair-lina-khans-agenda>.

¹⁰⁷ *Id.*

¹⁰⁸ Dan Papszun, *FTC Lawyers Leave at Fastest Rate in Years as Khan Sets New Tone*, March 16, 2023, <https://news.bloomberglaw.com/antitrust/senior-ftc-staff-departures-spike-as-ambitious-agenda-looms>.

Comment on Franchisors Exerting Control Over Franchisees and Workers,” citing “growing concern around unfair and deceptive practices in the franchise industry.”¹⁰⁹ One commenter has called this request for information, or RFI, “the most severe and far-reaching investigation the federal government has engaged in and around franchising in history.”¹¹⁰ But he also blamed the franchise industry for bringing this investigation on itself, opining that,

The overreach in the typical franchise agreement will cause a need for correction at some point, and as is the case with most corrections that come from legislation and regulation, over-correction is a real risk. Franchisors and their lawyers would be well advised to consider that as they continue to exert more and more control over their franchisees.¹¹¹

This RFI follows a 2021 push on the federal legislative end by Nevada Senator Catherine Cortez Masto, who published a report entitled *Strategies to Improve the Franchise Model: Preventing Unfair and Deceptive Franchise Practices*.¹¹² The report was cheered by some franchisees and denounced as inaccurate and biased by some franchisors.¹¹³

The FTC has also added a specific franchise category to its online “Report Fraud” reporting tool for individuals to report franchisors allegedly engaging in fraudulent conduct directly to the FTC.¹¹⁴ The Director of the FTC Bureau of Consumer Protection publicized this new feature in an August 2022 FTC Business Blog post entitled, “Holding Franchisors Accountable for Illegal Practices.”¹¹⁵

¹⁰⁹ FTC, PRESS RELEASE, FTC SEEKS PUBLIC COMMENT ON FRANCHISORS EXERTING CONTROL OVER FRANCHISEES AND WORKERS, Mar. 10, 2023, <https://www.ftc.gov/news-events/news/press-releases/2023/03/ftc-seeks-public-comment-franchisors-exerting-control-over-franchisees-workers>; see also FTC, SOLICITATION FOR PUBLIC COMMENTS ON PROVISIONS OF FRANCHISE AGREEMENTS AND FRANCHISOR BUSINESS PRACTICES, Mar. 9, 2023, https://www.ftc.gov/system/files/ftc_gov/pdf/Franchise-RFI.pdf.

¹¹⁰ Ronald K. Gardner, *The Giant Has Awoken: Franchisors in the FTC’s Crosshairs*, NEW YORK LAW JOURNAL, LAW.COM, April 6, 2023, <https://www.law.com/newyorklawjournal/2023/04/06/the-giant-has-awoken-franchisors-in-ftcs-crosshairs/?sreturn=20230311154635>.

¹¹¹ *Id.*

¹¹² See *From the Office of Senator Cortez Masto: Strategies to Improve the Franchise Model: Preventing Unfair and Deceptive Franchise Practices*, April 2021, <https://www.cortezmasto.senate.gov/imo/media/doc/Franchise%20Report%20from%20the%20Office%20of%20Senat%20or%20Cortez%20Masto.pdf> (last visited Apr. 9, 2023); see also Press Release, *Cortez Masto Leads Legislation to Curb Harmful Practices in the Franchise Sector, Protect Small Business Owners* (Apr. 14, 2021), <https://www.cortezmasto.senate.gov/news/press-releases/cortez-masto-leads-legislation-to-curb-harmful-practices-in-the-franchise-sector-protect-small-business-owners> (last visited April 9, 2023); Press Release, *Cortez Masto calls on Small Business Administration to Take Action Against Harmful Practices in Franchise Sector* (Mar. 16, 2022), https://www.cortezmasto.senate.gov/news/press-releases/cortez-masto-calls-on-small-business-administration-to_take-action-against-harmful-practices-in-franchise-sector (last visited Apr. 9, 2023).

¹¹³ See Nicholas Upton, *‘Unfair’ Franchise Practices Are Focus of Sen. Cortez Masto’s Report*, FRANCHISE TIMES (Apr 15, 2021 Updated Apr 16, 2021), https://www.franchisetimes.com/franchise_news/unfair-franchise-practices-are-focus-of-sen-cortez-masto-s-report/article_a5651728-9e25-11eb-970b-c336f71927cb.html.

¹¹⁴ The tool, including the franchise selection option, is available at: <https://reportfraud.ftc.gov/#/assistant> (last visited July 10, 2023).

¹¹⁵ Samuel Levine, Director, FTC Bureau of Consumer Protection, *Holding Franchisors Accountable for Illegal Practices*, FTC BUSINESS BLOG, (Aug. 3, 2022), <https://www.ftc.gov/business-guidance/blog/2022/08/holding-franchisors-accountable-illegal-practices> (last visited July 10, 2023).

With all of this federal activity, some franchisors are anticipating an increase in FTC enforcement actions. For example, although it appears to be an extreme case, the FTC filed an enforcement action against the BurgerIM franchisor for alleged wrongdoing in the sales process.¹¹⁶ However, there is now some increased judicial oversight of FTC action, with the U.S. Supreme Court recently unanimously ruling that parties facing agency investigations or complaints can go straight to federal court with some constitutional challenges.¹¹⁷

Although there does seem to be a renewed interest in possible additional oversight of the franchise sector, but it is unclear how many initiatives will come to fruition in the coming years.

B. Does Increased FTC Scrutiny Portend Increased State Attention on Franchising?

Watching the activity at the federal level, franchisors may wonder whether states will follow suit. Some may point out that in many regards, the states, not the federal legislators or regulators, seem to be leading the charge. NASAA's SOP, of course, is part of that state-led effort.

On the state legislative side, California has been particularly active. For example, we have seen California's passage of CA AB-676 (discussed in Section V.A above) and California Assembly Bill no. 257,¹¹⁸ known as the FAST Act, which, among other things, would create a ten-member Fast Food Council to review and establish pay and health and safety standards for covered restaurants. although the latter is not currently in effect because of judicial intervention after a successful voter petition initiative under California state law.¹¹⁹ California Assembly Bill no. 1228 is also currently under consideration, which would create restaurant franchisor joint liability.¹²⁰

California is not alone. For example, earlier this year, House Bill ("HB") 2404¹²¹ was introduced in the Arizona legislature. If ultimately enacted, HB 2404 would be Arizona's first franchise relationship law, and is in large part modeled after the extremely franchisee-friendly California Franchise Relations Act. New Jersey's pending Assembly Bill 1958,¹²² if passed, will add new restrictions relating to vendor rebates, mandated product purchases, and loyalty program requirements, among other things.

¹¹⁶ Complaint for Permanent Injunction and Monetary Judgments for Civil Penalties and Consumer Redress, and Other Relief, U.S. v. BurgerIM Group USA, Inc., No. 2:22-cv-00825 (C.D. Cal. Feb. 7, 2022), ECF No. 1.

¹¹⁷ Axon Enter., Inc. v. Fed. Trade Comm'n, No. 21-1239, 2023 WL 2938328 (U.S. Apr. 14, 2023).

¹¹⁸ Assemb. Bill 257, 2021-2022 Reg. Sess. (Cal. 2022) (enacted), https://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=202120220AB257 (last visited July 13, 2023).

¹¹⁹ Save Local Restaurants v. Hagen, Doc. 32, Case No. 2022-80004062-CV, Order on Preliminary Injunction (Cal. Sup. Ct., Jan. 24, 2023).

¹²⁰ Assemb. Bill 1228, 2023-2024 Reg. Sess. (Cal. 2023), https://leginfo.legislature.ca.gov/faces/billTextClient.xhtml?bill_id=202320240AB1228 (last visited Apr. 15, 2023).

¹²¹ House Bill 2404, 2023 Reg. Sess. (AZ 2023), <https://www.azleg.gov/legtext/56leg/1R/bills/HB2404P.htm> (last visited Apr. 15, 2023).

¹²² Assemb. Bill 1958, 2022-2023 Reg. Sess. (NJ 2023), <https://legiscan.com/NJ/text/A1958/id/2754959> (last visited July 12, 2023).

Arkansas House Bill (“HB”) 1783, which, in the words of the IFA, would have been “the most extreme franchising legislation in the country, significantly altering the franchise business model and making it harder for franchises to do business in the state of Arkansas.”¹²³ The bill’s stated purpose was, among other things, to “[p]rotect franchisees from unreasonable termination by franchisors that may result from the economic imbalance between franchisors and franchisees, the absence of free bargaining, and the commercially unreasonable practices of some franchisors engaging in business in this state” and to “protect the public interest in regulation of franchise agreements.”¹²⁴ After a letter signed by over 100 franchisors¹²⁵ in cooperation with the IFA was sent to the Arkansas State Legislature on March 31, 2023, HB 1783 was substantially modified before passage on April 13, 2023, through the removal of multiple provisions including those relating to renewal, transfers, and terminations for multiple breaches, reducing its potential impact on franchising in Arkansas.¹²⁶

Franchisors may also be concerned about State Attorney General activity, increased regulatory enforcement actions generally, and possible expansion of State Little FTC Act application. But again, that activity still remains to be seen.

VII. CONCLUSION

By the time this paper is published, presumably most franchisors will have adjusted their agreements and processes in an attempt to address the effects of, and comply with, the SOP. But further adjustments may be necessary as states, arbitrators, and courts, grapple with its interpretation and effects, and as franchisors seek other methods to obtain the benefits they perceive that Questionnaires and Acknowledgments provide. In addition, if the SOP is only the tip of the iceberg, then franchisors and franchisees would be well advised to continue monitoring additional state and federal statutes, regulations, and possible shifting climates with respect to franchise law, as well as its interpretation, and enforcement.

¹²³ Int’l Franchise Ass’n, *Government Relations Press Release, Local Arkansas Businesses and Franchise Brands Release Letter Opposing HB 1783*, April 1, 2023, <https://www.franchise.org/media-center/press-releases/local-arkansas-businesses-and-franchise-brands-release-letter-opposing>.

¹²⁴ House Bill 1783, 2023 Reg. Sess. (AR 2023) <https://www.arkleg.state.ar.us/Home/FTPDocument?path=%2FBills%2F2023R%2FPublic%2FHB1783%2FHB1783032920231530.pdf> (last visited July 2, 2023).

¹²⁵ Int’l Franchise Ass’n, *Government Relations Letter to Hon. Matthew Shepherd, Franchise Opposition to Arkansas House Bill 1783*, (March 31, 2023), <https://www.franchise.org/media-center/press-releases/franchise-opposition-to-arkansas-house-bill-1783> (last visited July 10, 2023).

¹²⁶ House Bill 1783, 2023 Reg. Sess. (AR 2023) (enacted), <https://www.arkleg.state.ar.us/Bills/Detail?id=HB1783&ddBienniumSession=2023%2F2023R> (last visited Apr. 15, 2023).

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NASAA STATEMENT OF POLICY REGARDING THE USE OF FRANCHISE QUESTIONNAIRES AND ACKNOWLEDGMENTS

(Adopted September 18, 2022; Effective January 1, 2023)

I. Introduction

This Statement of Policy Regarding the Use of Franchise Questionnaires and Acknowledgments was prepared by the Corporation Finance Section (“Section”) and the Franchise and Business Opportunities Project Group (“Project Group”) of the North American Securities Administrators Association, Inc. (“NASAA”) to set standards for the proper use of questionnaires and acknowledgments in franchise offerings.

Background

Federal and applicable state franchise laws require a franchisor to make certain pre-sale disclosures to prospective franchisees. The disclosures are made with a Franchise Disclosure Document (“FDD”) consisting of 23 items of information, with applicable attachments, including the franchise and other related agreements.

Over at least the last 30 years, franchisors have included in their franchise agreements and FDDs language that they can later use as a disclaimer of liability. One type of disclaimer takes the form of a series of acknowledgments (“Acknowledgments”) in the franchise agreement regarding the franchise offering. In addition, many—but not all—franchisors require prospective franchisees, at or prior to signing a franchise agreement, to mark “yes” or “no” to a series of questions or agree to a series of representations about what purportedly occurred, or did not occur, in the franchise sales process (“Questionnaires”). Virtually all Questionnaires and Acknowledgments address whether a prospective franchisee received some type of financial performance information different from what the franchisor disclosed in Item 19 of its FDD.

Franchisors routinely seek to use Questionnaires, Acknowledgments, and other forms of contractually required disclaimers to insulate themselves from potential liability by franchisees alleging fraud or misrepresentations in the offer and sale of a franchise.¹ Some have been successful.²

¹See, e.g., *Martrano v. Quizno’s Franchise Co.*, No. 08-cv-0932, 2009 WL 1704469, at *5 (W.D. Pa. June 15, 2009) (“Defendants pointedly assert, in their December 2008 Motion before this Court, that ‘Each Plaintiff was asked directly to disclose any representation he had received other than those contained in the UFOC. In the space provided, each and every one of the plaintiffs wrote ‘None.’”); *Siemer v. Quizno’s Franchise Co.*, No. 07-cv-2170, 2008 WL 904874 (N.D. Ill. Mar. 31, 2008) (franchisor’s defense based in part on disclosure acknowledgment statement through which franchisee was put on notice of potential business risks).

²E.g., *Governara v. 7 Eleven, Inc.*, No. 13-cv-6094, 2014 WL 4476534 (S.D.N.Y. Aug. 20, 2014) (granting franchisor’s motion to dismiss plaintiff’s claims under the anti-fraud provisions of the New York Franchise Act based in part on non-reliance disclaimers executed by the plaintiff).

The Practical Effect of Acknowledgments and Questionnaires

By the time prospective franchisees are presented with a franchise agreement or Questionnaire to sign, many are emotionally and financially invested in completing the transaction. As one commenter has noted, “[N]obody buys a franchise in a vacuum. They typically do so after being convinced of the attractiveness of the brand, the strength and utility of the franchisor’s system, the support they will receive from the franchisor, and the enthusiasm they encountered at Discovery Day. None of these factors are the result of reading an FDD.”³

Questionnaires and Acknowledgments are not the most effective mechanisms for preventing fraud.⁴ They are, however, powerful defense mechanisms that franchisors can use to defeat claims of fraud and misrepresentation regardless of what has occurred in the franchise sales process. As a result, Questionnaires and Acknowledgments can allow unscrupulous franchisors to avoid the consequences of franchise fraud. Although at least one court has opined that Questionnaires and Acknowledgments can be useful to help franchisors “root out dishonest sales personnel and avoid sales secured by fraud,”⁵ they do so by shifting the compliance burden from franchisors to prospective franchisees. It should be the franchisor’s burden to police its own sales personnel and agents; franchisees should not have to confirm that no violations of law have occurred during their own sales process.

The FTC Franchise Rule’s Position on Franchise Waivers, Disclaimers and Questionnaires

In 2007, the Federal Trade Commission (“FTC”) promulgated an amended FTC Franchise Rule that included a limited ban on disclaimers made in the FDD itself and its exhibits or attachments. When the FTC promulgated the FTC Franchise Rule, it did not specifically address a franchisor’s use of Questionnaires or the effect of Acknowledgments on franchisee fraud claims. In 2019, the FTC announced it was soliciting public comments on the FTC Franchise Rule. One issue the FTC raised related to the impact the FTC Franchise Rule has had on the flow of truthful information and on the flow of deceptive information to prospective franchisees.⁶

³ S. Dub, B. Napell, D. Oates, “Dueling Perspectives on Selected Franchise Agreement Provisions,” American Bar Association 43rd Annual Forum on Franchising, at 20 (October 27-30, 2020), available at <https://www.americanbar.org/content/dam/aba/events/franchising/2020/w18.pdf>.

⁴ See, e.g., *Braatz v. Red Mango*, 2015 WL 1893194 (N. D. Tex. Apr. 27, 2015), aff’d sub nom. *Braatz, L.L.C. v. Red Mango FC, L.L.C.*, 642 F. App’x 406 (5th Cir. 2016) (Franchisees allege they changed their answers in Questionnaire about receiving financial information because the franchisor told them that they could not open the franchise without the Questionnaire being completed in the form the franchisor required); Comment of Anonymous, posted by the FTC on December 10, 2020 (“While I signed a questionnaire saying I didn’t rely on information outside of that disclosure document, that was not true, however, I knew that would preclude me from making the franchise purchase if I answered truthfully”), available at: <https://www.regulations.gov/comment/FTC-2020-0064-0042>.

⁵ See *Emfore Corp. v. Blimpie Assocs., Ltd.*, 51 A.D.3d 434, 435 (N.Y. App. Div. 2008).

⁶ See Disclosure Requirements and Prohibitions Concerning Franchising, Federal Trade Commission, 84 Fed. Reg. 49 (Mar. 13, 2019), available at: <https://www.govinfo.gov/content/pkg/FR-2019-03-13/pdf/2019-04466.pdf>.

In the years since the FTC promulgated the FTC Franchise Rule, Questionnaires and Acknowledgments have become commonplace in franchising, and some commenters have argued that the FTC should now address or even prohibit them. Those commenters point out that Questionnaires and Acknowledgments limit a franchisee's ability to hold a franchisor accountable for fraud and deceit, irrespective of the underlying facts of a franchisee's claims.⁷

Although the FTC held a public workshop in 2020 to explore issues related to both Questionnaires and Acknowledgments,⁸ the FTC has not yet directly addressed whether or when those provisions violate the FTC Franchise Rule.

The Impact of State Franchise Law Provisions

Several states have enacted franchise registration and disclosure laws that include protections for prospective franchisees that are not found in the FTC Franchise Rule.⁹ Modeled on securities anti-fraud laws, these state franchise laws include provisions that prohibit any person from committing fraud, making untrue statements of material fact, or omitting to state a material fact regarding a franchise offering ("Anti-Fraud Provisions"). Most of those same states also include provisions ("Anti-Waiver Provisions") that prohibit or render void any provision or condition requiring a prospective franchisee to agree to a release, waiver or estoppel that would relieve a person from liability under that law.¹⁰

Although not all courts agree, many courts have concluded that franchise contractual disclaimers, including Questionnaires and Acknowledgments, violate state Anti-Waiver Provisions when they serve as a release or waiver of a franchisee's rights under a state franchise law.¹¹ For example, in *Randall v. Lady of America*, the franchisor argued in a motion for

⁷ See, e.g., Comment from Bundy Law Firm, PLLC, at pp 7-9, posted by the FTC on December 21, 2020, <https://www.regulations.gov/comment/FTC-2020-0064-0118>; comment from Lagarias, Napell & Dillon, LLP, at pp. 8-14, posted by the FTC on December 17, 2020, <https://www.regulations.gov/comment/FTC-2020-0064-0077>.

⁸ A transcript of the November 20, 2020, workshop is available at: https://www.ftc.gov/system/files/documents/videos/reviewing-franchise-rule-workshop-discussion-disclaimers-waivers-questionnaires/franchise_rule_workshop_transcript_-_discussion_of_disclaimers.pdf.

⁹ See Cal. Corp. Code §§ 31000 through 31516; Haw. Rev. Stat. § 482E-1 through § 482E-12; 815 Ill. Comp. Stat. §§ 705/1 through 705/44; Ind. Code §§ 23-2-2.5; Md. Bus. Reg. Code §§ 14-201 through 14-232; Mich. Comp. Laws §§ 445.1501 through 445.1546; Minn. Stat. §§ 80C.01 through 30C.22; N.Y. Gen. Bus. Law Art. 331 §§ 680, et seq.; N.D. Cent. Code §§ 51-19-01 through 51-19-17; R.I. Gen. Laws §§ 19-28.1-1 through 19-28.1-34; S.D. Codified Laws §§ 37-5B-1 through 37-5B-53; Va. Code Ann. §§ 13.1-557 through 13.1-574; Wash. Rev. Code §§ 19.100.010 through 19.100.940; Wis. Stat. §§ 553.01 through 553.78.

¹⁰ See Cal. Corp Code § 31512; Haw. Rev. Stat. § 482E-6; 815 Ill. Comp. Stat § 705/41; Ind. Code § 23-2-2.7-1; Md. Bus. Reg. Code § 14-226; Mich. Comp. Laws § 445.1527(b); Minn. Stat. § 80C.21; N.Y. Gen. Bus. Law Art. 33 § 687(4); R.I. Gen. Laws § 19-28.1-15; S.D. Codified Laws §37-5B-26(8); N.D. Code § 51-19-16(7); Va. Code Ann. § 13.1-571(c); Wash. Rev. Code § 19.100.180(2); Wis. Stat. § 553.76.

¹¹ See *Coraud LLC v. Kidville Franchise Co., LLC*, 109 F. Supp. 3d 615, 621 (S.D.N.Y. 2015) (“[New York’s anti-waiver statute] bars anticipatory waivers of compliance with the NYSFA’s anti-fraud provisions.”); *Hanley v. Doctors Express Franchising, LLC*, No. 12-cv-794, 2013 WL 690521, at *29 (D. Md. Feb. 25, 2013) (“Construed as waivers of plaintiffs’ misrepresentation claims under the Maryland Fraud Law, the disclaimers are legally void.”); *Randall v. Lady of Am. Franchise Corp.*, 532 F. Supp. 2d 1071, 1089 (D. Minn. 2007) (holding that a disclaimer that

summary judgment that a contractual integration clause and certain disclaimers were sufficient to defeat a franchisee's claims under Minnesota's Franchise Act. The court disagreed, holding that the Anti-Waiver Provision of the Minnesota Franchise Act invalidated the contractual disclaimers. The court reasoned that the historical truth of a franchisor's misconduct (in this case, that the franchisor made unlawful earnings claims) could not be negated by a contractual disclaimer without violating the Anti-Waiver Provision. The court explained:

The disclaimer cannot change the historical facts; if the dishonest franchisor made misrepresentations, then he made misrepresentations, no matter what the franchise agreement says. Thus, the disclaimer can only be an attempt to change the *legal effect* of those misrepresentations. That is precisely what [the Minnesota] anti-waiver language forbids.¹²

Similarly, in *Hanley v. Doctors Express*, the court held that disclaimers and acknowledgments contained in a franchise agreement and FDD were legally inoperative to bar a franchisee's claims under the Maryland Franchise Law based on the Anti-Waiver Provision of that law to the extent that they would operate as a release, waiver, or estoppel.¹³ The court relied, in part, on the statement of purpose for the Maryland Franchise Law, which was enacted in response to substantial losses suffered by franchisees when the franchisor or its representatives had not given complete information. The court noted that, given the Maryland General Assembly's clear statement of intent, waivers and releases of a plaintiff's rights under the Maryland franchise laws are void as such clauses violate a fundamental policy of the state.¹⁴

In the opinion of the Section and the Project Group, Questionnaires and Acknowledgments violate state Anti-Waiver Provisions when they are used as contractual disclaimers that release or waive a franchisee's rights under a state franchise law. Courts that have found otherwise have not recognized or appreciated the history and purpose of state franchise registration and disclosure laws. The state legislatures that enacted these franchise laws intended to protect franchisees from the effect of contractual disclaimers, including those that may take the form of Questionnaires and Acknowledgments. The prospective franchisee who signs a Questionnaire or series of Acknowledgments and later denies the accuracy of what was signed would have to explain such a discrepancy, but they should have that opportunity before a factfinder, rather than have their claims dismissed based solely on having signed a Questionnaire or series of Acknowledgments.

has the effect of waiving compliance with the anti-fraud statute's prohibition of material false statements is void under the anti-waiver statute); *but see Governara*, 2014 WL 4476534, at *6-7 (holding anti-waiver statute did not void contractual reliance disclaimer; declined to follow by *Coraud*).

¹² *Randall*, 532 F. Supp. 2d. at 1088-89.

¹³ *Hanley*, 2013 WL 690521 at *29 (the court noted that integration clauses and waivers are not necessarily wholly irrelevant, citing the issue of reliance).

¹⁴ *Id.* (citations omitted).

Inappropriate Questionnaire and Acknowledgment Provisions

State regulators have observed that Questionnaires and Acknowledgments currently found in some FDDs and franchise agreements are replete with questions and representations that serve no legitimate purpose. Many Questionnaires and Acknowledgments require a prospective franchisee to acknowledge or answer questions that are subjective, unreasonable, or repeat disclosures required to be stated in the FDD. In some cases, Questionnaires require the prospective franchisee to acknowledge identical facts and statements that the franchisee must acknowledge a second time in the franchisor's franchise agreement. In other cases, these Questionnaires and Acknowledgments require prospective franchisees to agree that they understand specific disclosures made in an FDD or the terms of the franchise relationship. These provisions are inconsistent with plain English standards and the legislative policies behind state franchise laws, which were passed to protect prospective franchisees by requiring presale disclosure. State franchise laws do not allow FDDs to be used as a defense documents that serve to protect franchisors who commit fraud or make misleading material disclosures or material omissions.

II. Application of the Statement of Policy Regarding the Use of Franchise Questionnaires and Acknowledgments

This Statement of Policy applies to Questionnaires, Acknowledgments, and similar documents that appear in FDDs and applicable attachments and exhibits used in the offer and sale of franchises where an Anti-Waiver Provision or Anti-Fraud Provision applies to the offer or sale.

A. Definitions

This Statement of Policy uses the following terms defined in the NASAA 2008 Franchise Registration and Disclosure Guidelines.

Franchisee - Franchisee means any person who is granted a franchise.

Franchise seller - Franchise seller means a person that offers for sale, sells, or arranges for the sale of a franchise. It includes the franchisor and the franchisor's employees, representatives, agents, subfranchisors, and third-party brokers who are involved in franchise sales activities. It does not include existing franchisees who sell only their own outlet and who are otherwise not engaged in franchise sales on behalf of the franchisor.

Franchisor - Franchisor means any person who grants a franchise and participates in the franchise relationship. Unless otherwise stated, it includes subfranchisors. For purposes of this definition, a "subfranchisor" means a person who functions as a franchisor by engaging in both pre-sale activities and post-sale performance.

Person - Person means any individual, group, association, limited or general partnership, corporation, or any other entity.

Prospective franchisee - Prospective franchisee means any person (including any agent, representative, or employee) who approaches or is approached by a franchise seller to discuss the possible establishment of a franchise relationship.

B. Attachment to FDD

1. If the Franchisor requires the Prospective franchisee to sign any Questionnaires, Acknowledgments, or similar documents before entering into the franchise agreement, the proposed form of such Questionnaires, Acknowledgments or similar documents must be referenced in Item 22 of the FDD and attached as an exhibit.
2. If the Franchisor requires the Prospective franchisee to verbally respond to any Questionnaires, Acknowledgments, or similar statements on video or other electronic media recording before entering into the franchise agreement, a written script of the proposed form of such Questionnaires, Acknowledgments or similar statements must be referenced in Item 22 of the FDD and attached as an exhibit.

C. Prohibited Provisions in Questionnaires and Acknowledgments

1. The Franchisor and its Franchise seller(s) shall not require the Prospective franchisee to make any statement in any Questionnaires, Acknowledgments, or similar documents that is subjective or unreasonable or that:
 - a. Would cause a reasonable Prospective franchisee to surrender or believe that they have surrendered rights to which they are entitled under federal or state law;
 - b. Would have the effect of shifting Franchisor's disclosure duties under federal or state law to the Prospective franchisee; or
 - c. Are otherwise Prohibited Statements under this Statement of Policy or are similar to the Prohibited Statements.¹⁵
2. Prohibited Statements in Questionnaires, Acknowledgments, and similar documents include, but are not limited to, the following:
 - a. That the Prospective franchisee has read or understands the FDD or any attachments thereto, including the franchise or other agreement.
 - b. That the Prospective franchisee understands or comprehends the risks associated with the purchase of the franchise.
 - c. That the Prospective Franchisee is qualified or suited to own and operate the franchise.
 - d. That, in deciding to purchase the franchise, the Prospective franchisee has relied solely on the FDD and not on any other information, representations, or statements from other Persons or sources.

¹⁵ This Statement of Policy is not intended to prohibit a Franchisor from conducting factfinding or asking Prospective franchisees questions about the sales process, but Franchisors may not require a Prospective franchisee to document and sign statements that act as waivers in violations of state law.

- e. That neither Franchisor nor Franchise seller has made any representation, including any financial performance representation, outside of or different from the FDD and attachments thereto.
 - f. That the success or failure of the franchise is dependent solely or primarily on Franchisee.
 - g. That the Franchisor bears no liability or responsibility for Franchisee's success or failure.
 - h. That reiterates or duplicates any representation or statement already made elsewhere in the FDD and attachments thereto.
 - i. That the Prospective franchisee has had the opportunity to or has/has not actually consulted with professional advisors or consultants or other franchisees.
 - j. That the Prospective franchisee agrees or understands that the Franchisor is relying on the Questionnaires, Acknowledgments, or similar documents, including to ensure that the sale of the franchise was made in compliance with state and federal law or that no unauthorized, inaccurate, or misleading statements were made.
 - k. That requires or suggests that the Prospective franchisee must agree to any Questionnaires, Acknowledgments, or similar documents prohibited by this Statement of Policy or provide false answers as a condition to the purchase of the franchise.
3. Franchisor must include in its FDD and franchise agreement, or applicable state-specific addenda to the FDD and franchise agreement, the following provision:

No statement, questionnaire, or acknowledgment signed or agreed to by a franchisee in connection with the commencement of the franchise relationship shall have the effect of (i) waiving any claims under any applicable state franchise law, including fraud in the inducement, or (ii) disclaiming reliance on any statement made by any franchisor, franchise seller, or other person acting on behalf of the franchisor. This provision supersedes any other term of any document executed in connection with the franchise.