From: Brenan
To: NASAA Comments; Theresa Leets; bill.beatty@dfi.wa.gov; Erin Houston
Subject: [EXTERNAL]Public Comments
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June 12, 2024
Via Electronic Mail

To:
Theresa Leets, Chair of the Project Group
Bill Beatty, Co-chair of the Section
Erin Houston, Co-chair of the Section

Re: Public Comments on Proposed NASAA Model Franchise Broker Registration Act (the "Act")

To NASAA,

My name is Brenan Compretta, and I am the President of Beacon Franchise Brokers, a franchise consulting firm. I have extensive experience in the franchise industry.

The recent addition of private equity and FSOs into the franchise sales industry has changed the environment quite dramatically in a short time. In many ways, it has gotten better and professionalized the industry. There are many wonderful benefits and some growing pains. At the same time, there have been some who have disregarded the already-in-place guidelines for franchise sales.

I appreciate the efforts to increase transparency and support the sentiment behind the proposed Act. Franchising is a wonderful business opportunity when the franchise and the franchise owner are matched properly and developed to be their best. It encourages small business ownership and local economic advancement in communities all over the country. It fosters competition and in so doing, plays an important role in increasing consumer choices and keeping retail prices competitive.

Regarding the Act, I have several concerns and suggestions that I hope will be considered for the final draft. As it currently stands, there were likely to be some unintended consequences and I'd like to point them out to provide a clearer picture. Below, I outline my specific concerns and suggestions:

Intended Goal of the Act

The intended goal of the Act is to provide a layer of protection for prospective franchisees and franchisors in the franchise sales process. However, the repercussions of the Act on the franchise broker are not for "bad acts" but rather for registration, disclosure, and fee mistakes. The Act does not address actual bad acts of franchise brokers, does not fix bad franchising practices of franchisors, and makes lack of registration, disclosure, and payment "bad acts" without providing any further protection to the franchise candidate.

A - Broadening Scope of the Industry

The franchise broker and third-party seller industry is relatively small with roughly 2,000

franchise brokers and roughly 20 Franchise Sales Organizations. The FRBA increases the industry's scope far beyond its current size and makes a large percentage of those with any role in or connected to the franchise sales and new franchisee establishment process "franchise brokers" or compensated "franchise broker representatives."

For instance, because the compensation or value requirements are so minimal and only require "indirect" involvement in an offer or actual sale of a franchise, the covered individuals and entities include lead sources, funding sources and all employees and contractors involved with lead sources and funding sources, existing franchisees who refer prospects to the franchise brand and receive a referral fee of more than $1,000 in a year, and employees and contractors of the franchise sale organizations, broker networks and franchise suppliers.

Questions

- Is this the intended goal of the act?
- Does this protect potential franchisees or provide more confusion to the transaction?

Suggestions

Reduce the definition of Franchise Broker and Franchise Broker Representative to exclude unintended parties. The definition should not include everyone involved in the franchise sale in any capacity.

B - Reduces requirements of what is considered an "offer" and applies whether or not a sales transaction actually occurs

The Act uses language like "is promised a fee, commission or other forms of consideration from a franchisor." This does not require direct payment or actual involvement in the sales process. Gifts, outings, referral fees, and events, for example, can be considered other forms of consideration. It uses language like "indirectly engage" in the franchise offer or sale of a franchise. This has a broad impact. For example, a funding source can have an employee doing administrative work to obtain the loan who would be considered indirectly engaged in the franchise offer - whether or not any purchase or sale transaction occurred. There are a host of other applications as well including social media posts, validations, and testimonials, that could constitute being indirectly engaged and require disclosure and registration. It uses terms like "offer" of a sale which includes simply discussing the franchise opportunity. With no transaction required, this leaves the door open for anyone discussing franchising to require disclosure and registration under the Act.

Suggestions

We suggest adding a definition to more surgically define an "offer" and "offer to sell" and to clearly identify what a sales transaction is and remove non-transactions from the disclosure requirements. Also, add a definition for "indirectly engage."

C – Unwittingly Increases liability

The Act increases the liability of a wide range of people and entities because it makes it illegal to sell without registration. But a registration is required for all non-transactions. Franchise brokers know they are in the franchise brokerage industry. However, a large population of people who are not acting as franchise brokers will not know nor have reason to suspect that

they are violating the registration requirements. Also, the franchise broker or franchise broker representative generally lacks any authority or capacity to stop a sales transaction, control the transaction, influence it, or in many cases, even knowingly participate in it. This control rests with the franchisors who already are issuing Franchise Disclosure Documents to all candidates. In addition to this, the requirement of jurisdiction and venue in the state of the registration would unfairly disadvantage the party seeking to defend themselves as the industry is a national industry.

D - Disclosure requirements require excessive burden and easily create mistakes in disclosure compliance

There are many parties required to disclose under the Act. The franchisor, the broker, the broker network, the franchise broker representative, and all the unintended parties are now caught up in the definitions of "franchise broker" and "franchise broker representative." The industry has a constant movement. For example: franchises move in and out of broker inventory and in and out of business; commissions change daily; and "franchise broker representatives" would (under the current draft) include employees, suppliers, contractors, vendors, and so on for the industry. Coordinating these daily changes with all companies and interested persons will be impossible as a practical matter.

Suggestions

Narrow down on what is required to be disclosed to create a more seamless and less burdensome compliance process.

Key Concerns

1. **Frequency of Disclosure**

   As stated above, the current required frequency of disclosure would impair the industry and cause harm to all those in franchising. A preferable disclosure rule to follow is the rule of New York. The New York disclosure law provides for actual franchise brokers to be registered and updated when a material change occurs. The Act could follow the same guidelines and effectively achieve the objective without being overly burdensome and harmful to franchising. We suggest an update to the definition not only of "franchise broker" and "franchise broker representative" but that of "material change" to include only bad acts (e.g., a broker has been alleged to have actually made a misrepresentation or a representation inconsistent with the information contained within the FDD).

2. **Disclosure Document Timing**

   The current requirement for early disclosure documents could confuse prospective franchisees. Buyers are not going to understand why they are getting inundated with a large number of disclosures. For example, if you were a franchise buyer and filled out a contact form, then received 25 disclosures full of financial information and other customers' private information before a conversation was even had, you would likely think that is inappropriate. In addition to that, the disclosure contains private information about past clients that would be inappropriate to share with non-prospects. This could be a violation of their privacy. Aligning the timing of the disclosures with existing franchise disclosure law is one suggestion. Under current franchise law, the

FDD is to be provided at least 14 days before a payment or signature. Aligning with a practice already in place would be more practical, support compliance, and avoid confusion for the franchise buyer while still keeping the buyer fully appraised of who they are dealing with and how they are being compensated.

3. **Franchisees who refer someone to become an owner and receive more than $1,000 a year are considered a franchise broker**

   Franchises grow through successful franchisees who discuss their success with their network to bring in more franchisees. Often, franchisees are compensated between $3,000 - $5,000 for the referral. They would now be required to register as a franchise broker under the Act. This harms natural and organic growth in the franchise system by requiring non-franchise brokers to comply and be exposed to the risk. This should be removed from the Act.

4. **Financial or Insurance Requirements**

   It took years of negotiating and working with insurance companies to even be eligible to be covered under insurance as franchise brokers are today. The Insurance companies have strict requirements for its usage and with the newly imposed law, our current insurance options may not be eligible for coverage. This makes it difficult to comply with the law. Furthermore, the proposed financial and insurance requirements are discriminatory to less fortunate applicants looking to enter the field. This should be removed from the Act.

5. **Recordkeeping**

   10-Year Record Keeping: Maintaining records for 10 years places a significant burden on brokers, especially those who have closed their businesses. This requirement needs reconsideration to avoid excessive strain on brokers. If a franchisee has been operating for 10 years, they have successfully operated their business and fulfilled the full term. The IRS requires maintaining records for 3 years. We would like to propose a reduced time for that administration and cost of the business, without it being operational.

6. **Excessive Burdens on Emerging Franchisors / Reducing Competition**

   On policy grounds, the Act also is misguided, in that it: places excessive burdens on emerging franchisors and reduces competition in favor of large franchise systems; it doesn't otherwise fix bad franchising practices of franchisors; and it is unnecessary as laws already exist for dealing with franchise broker's bad acts. Large franchise systems (e.g., Jersey Mike's, McDonald's) don't use franchise brokers. Everyone knows who they are. As a result, they largely control the industries (or portions of industries) in which they operate.

   True emerging franchise brands do use franchise brokers. The excessive burdens on franchise brokers will: cause a disparate impact on those emerging brands; stifle competition; reduce consumer choice; and increase consumer prices (e.g., a 12-inch sandwich with chips and a regular fountain drink at Jersey Mike's is now over $20 before sales tax).

7. **Doesn't Fix Bad Franchising**

There are many thousands of franchisors. Bad franchising exists despite the protections of the FDD or the bad acts of franchise brokers and franchisors through Item 7 misrepresentations, and Item 19 misrepresentations. These all are occurring despite the FDD disclosure requirements. Making Franchise brokers the focal point may distract from bad franchisor actors, and does not fix the problems of bad franchising.

8. **Already Addressed by Existing Law**

   A franchise broker is the sales agent of the franchisor he or she represents. There are already laws to recover damages from sales agents and their principals for the bad acts, misrepresentations, and/or omissions committed by the sales agents. Focusing on the sales agents does not expand any remedies already available to misguided franchisees and acts as an exoneration of the principals who knowingly entered into a principal/agency relationship with those sales agents and who knowingly appointed them with authority as their sales agents, to begin with.

Conclusion

We kindly request that NASAA extend the comment period and engage more comprehensively with all relevant stakeholders to create a balanced and effective regulatory framework. This approach will ensure that the final document serves the interests of all parties and promotes, rather than deters, individuals from exploring franchise opportunities. Thank you for your attention to this matter. We look forward to collaborating with NASAA to achieve our mutual objectives.

Best Regards,
Brenan Compretta
President
Beacon Franchise Brokers

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Best Regards,

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This email does not constitute an offer of a franchise per the registration requirements by the Franchisor in some States. The following are the registration States (CA, HI, IL, IN, MD, MI, MN, NY, ND, RI, SD, VA, WA, WI).

The information provided in any PowerPoint presentation or brochure is found in greater detail in the franchisor's Franchise Disclosure Document. You should review the entire Franchise Disclosure Document carefully and seek the advice of a professional advisor prior to making any decision on whether to purchase this franchise. Do not rely on any information which is not consistent with the information in the Franchise Disclosure Document.