

The Franchise Offering Circular “Everything The FTC Wants You
To Know About The Franchisor”

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Background and Summary

The Franchise Offering Circular, also known as the UFOC, is the disclosure document provided to all potential franchisees to review in order to evaluate the franchise. This article outlines and summarizes the disclosures required by the Federal Trade Commission. (3 Pages)

Once you have decided that owning a franchised business is for you, the Franchisor will present you with a document or “Offering Circular” that contains certain disclosures required by the Federal Trade Commission (FTC). A thorough review of the offering circular is a necessity for any serious prospective franchisee.

The FTC requires the Franchisor to disclose information on twenty (20) different subjects:

- 1- Identifying information about the Franchisor;
- 2- Business experience of the Franchisor’s directors and key executives;
- 3- The Franchisor’s business experience;
- 4- Litigation history of the Franchisor and its directors and key executives;
- 5- Bankruptcy history of the Franchisor and its directors and key executives;
- 6- Description of the franchise;
- 7- Money required to be paid by the franchisee to obtain or commence the franchise operation;
- 8- Continuing expenses to the franchisee in operating the franchise business that are payable in whole or in part to the franchisor;
- 9- A list of persons who are either the franchisor or any of its affiliates, with whom the franchisee is required or advised to do business;
- 10- Realty, personalty, services, etc. which the franchisee is required to purchase, lease or rent, and a list of any persons from whom such transactions must be made;
- 11- A description of consideration paid by third parties to the franchisor as a result of a franchisee’s purchase from such third parties;

- 12- Description of any franchisor assisted financing;
- 13- Restrictions placed on a franchisee's conduct of its business;
- 14- Required personal participation by the franchisee;
- 15- Termination, cancellation and renewal of the franchise;
- 16- Statistical information about the number of franchises and their rate of termination;
- 17- Franchisor's right to select or approve a site for the franchise;
- 18- Training programs for the franchisee;
- 19- Celebrity involvement with the franchise;
- 20- Financial information about the franchisor.

The FTC further requires that the offering circular be furnished to the prospective franchisee at the earlier of either (1) the prospective franchisee's first personal meeting with the franchisor, or (2) ten days before the signing of a contract or payment of money relating to the franchise.

The FTC prohibits the franchisor from making representations regarding earnings unless the franchisor has reasonable proof to support the claims, has in its possession documents to support the claims, and the claims are geographically relevant to the franchisee's proposed location. In practice, however, few franchisors currently make earnings claims.

Although each category of required disclosure is important in evaluating the franchise opportunity, certain categories are of critical importance.

The disclosures regarding fees, including the initial fee, royalties (a set percentage of monthly or weekly gross income), and any required contributions to a national advertising fund (a percentage of revenues) must be carefully reviewed. The potential franchisee must determine whether the business can generate a profit after the payment of these fees and all other normal operating expenses.

It is critical to ascertain under what circumstances the franchisor can terminate the relationship, since fees paid to the franchisor are never refundable once the business begins operation. The ability of a franchisee to sell or transfer the business is an important concern. Can the business be sold at a profit after years of hard work? What will happen to the business if you die? The rights granted in a franchise agreement is only transferable as permitted in the franchise agreement. All franchise agreements require a transfer fee to be paid and give the franchisor the right to a transferee (with certain limitations). Is there a right to renew the agreement and what are the fees, if any, associated with renewal? Some franchisors provide no contractual right to

renew while others condition the right upon payment of additional fees (typically, the franchise fee, or a portion thereof prevailing at the time of renewal).

It is critical to review the statistical information pertaining to the number of franchisees, particularly the number of franchisees that have left the “system” within the preceding year and the reasons for their departure. Turnover in franchisees can be a problem, however, the reasons for the turnover can vary from bona fide resales to terminations by the franchisor.

The franchisor will always provide training. It is typical for the franchisee to be responsible for its expenses for travel to and from the training site (typically out of state), lodging, meals, and salaries for attending employees. Most franchisors will not make a specific commitment for training and assistance after the opening of the business, but will agree to provide such assistance and training as it “deems necessary”.

The franchisor is required to disclose its financial condition. This information is quite technical and should be reviewed by an accountant. This is particularly true in the case of a new franchisor.

Although the offering circular is intended to protect the prospective franchisee, it is prepared by the franchisor to sell franchises. A thorough review of the offering circular is an indispensable step in the due diligence process.

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