



A Special Q&A Session with the Franchise Regulators

IFA CORONAVIRUS
UPDATES



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INTERNATIONAL FRANCHISE ASSOCIATION

Speaker(s)

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State Responses to COVID-19

IFA COVID-19 State Spread Sheet:

<https://drive.google.com/file/d/1FYfFLauNLJvyZ1IfPINF2oSA5GJj3zjB/view>

Filing Extensions Generally

Federal and State franchise laws require franchisors to update disclosure documents annually.

A concern with granting filing extensions is that it could allow franchisors to give inaccurate and/or outdated information to prospects.

Record Unemployment

- **Millions of Americans are newly unemployed.**
- **Millions more are at risk of layoffs.**
- **It is reasonable to expect that the unemployed may investigate franchise opportunities.**

Expect an Increase in Scams

- **Fraudsters feed on fear / uncertainty**
 - Scams related to COVID-19 vaccines and cures
- **FDDs need to accurately disclose the rewards and risks of franchising**
 - The unemployed are seeking stability and security
 - The unemployed may be vulnerable to franchise sellers who over promise financial returns and/or job security

COVID-19 Disclosures

- **Purpose of Franchise Disclosure Document**
- **What Do We Know?**
- **Update as you learn more**
 - ▶ Post-Effective Amendment

COVID-19 Disclosures

Do not add to:

- **State Cover Sheet as a risk factor**

Do not add disclaimers in:

- **Item 1**
- **Item 19**

Disclaimers are Prohibited

- **Disclaimers that require franchisees to waive reliance on any representation made in a disclosure document are prohibited.**
- **Preserves integrity of material information disclosed in the disclosure document.**
- **Prevents deception.**

Item 19 Admonition

Historical Representation:

“Some outlets have earned this amount. Your individual results may differ. There is no assurance that you’ll earn as much.”

Sample Disclaimer in Item 19

- Depending on how long the global pandemic continues, its severity in your region, and any unknown, long-term impacts on consumer behavior, you could earn substantially less than our 2019 figures suggest.
- Because of the COVID-19 Risk, we do not represent or warrant in any way to you that your business will be able to be opened by you, will be able to stay open after any commencement of business, or will not suffer any impairment in its ability to operate.

Disclaimers in Item 19

Can you disclose anything about COVID-19 in Item 19?

Making an FPR

“.... In your response, explain why the Franchisor believes that it is reasonable and not misleading to present a financial performance representation based solely on results from a period prior to the COVID-19 pandemic.”

FPRs

Material Changes to FPRs:

- If the seller knows of any material changes to FPR at the time the FDD is delivered, federal law requires that the seller must notify the prospective franchisee.
- State anti-fraud provisions prohibit inaccurate statements or omissions of material facts.

New State Cover Sheets

- Only add risk factors if required in the instructions or by a state regulator.
- The page titled “**State Effective Dates**” has moved to the end of the FDD, the page before the receipt.
- <https://www.nasaa.org/wp-content/uploads/2019/06/New-Franchise-State-Cover-Sheets-Instructions.pdf>

ASC 606 Implementation Deferred

On 4/8/2020, FASB agreed to defer for one year the required implementation of ASC 606:

- Franchisors that have already completed their audit before this announcement presumably complied with ASC 606.
- Franchisors that have not yet completed their audits can wait to implement.

ASC 606 Comment Letters

Regulators are seeing Audits that disclose adoption of ASC 606 but use Legacy disclosures.

If you receive a letter asking for clarification this might be because it is impossible to tell from the notes to the financial statements what was implemented.

ASC 606 Adoption

Notes to the financial statements should include:

- **Method of adoption**
 - Full or Modified Retrospective
- **A table showing line items within the financial statements that were adjusted**

ASC 606 Adoption

- **Discussion of the 5 steps to recognizing revenue**
 - This is where you identify performance obligations under the franchise agreement.
- **Disclose how the initial franchise fees are to be allocated**
 - Over the term of the franchise agreement
 - Upfront for separate performance obligations

Changes to DocQNet on June 26, 2020

California's online portal searches will display search results in an index format:

- Results will no longer link to viewable documents
- Searches will be limited to the past 10 years
- To view a document, submit a Public Records Act (PRA) request at <https://docqnet.dbo.ca.gov/create-pra/>.

Changes to DocQNet on June 26, 2020

Any questions or comments about this change
may be directed to ASK.DBO@dbo.ca.gov

Questions?



Speaker(s) Contact Info

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