10 Stress-Reducing Tips for Updating Franchise Disclosure Documents and Renewing State Registrations

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Federal law requires all franchisors to update their franchise disclosure document (FDD) within 120 days after their fiscal year end (FYE). Likewise, state registrations must be renewed annually. Since most franchisors have a December 31 FYE, this is "renewal season," the annual rite of racing the clock to meet updating and filing deadlines to prevent the lights from going out on franchise sales activities. Whether 12/31 or some other date is your company's FYE, here are 10 stress-reducing tips for getting the job done right.

1. **Know Your Deadlines**. A franchisor violates federal and state franchise sales laws by offering or selling franchises with an out-of-date FDD or expired registration. Some states set registration periods to expire earlier than 120 days after a company's FYE despite federal law. For example, Hawaii requires updating and filing by March 31, and California requires updating and filing within 110 days after the FYE. Docket all deadlines. Most states grant automatic renewal (subject to clearing comments) to early filers (e.g., California provides automatic renewal to franchisors that file the renewal application at least 15 business days before the current registration expires). Check states laws for automatic renewal deadlines and treat these as the real filing deadline, not the registration expiration date. Missed deadlines will force you to go "dark," which means suspending all solicitation activities, including advertisements, trade shows and casual discovery days, and not closing sales in the pipeline, until you complete FYE updates and receive registration orders. Franchise registration states will not excuse late filings regardless of how compelling the excuse may be.

2. **Call Your Outside Auditor Now.** Cycling through FYE updates includes adding the latest FYE audit to your FDD. Late audits are the primary reason for missed deadlines. For 12/31 FYE franchisors who may need their audit by the end of March (depending on where they sell) and certainly by the end of April, you'll be competing with April 15th tax season for your auditor's attention. Impress on your auditor that filing deadlines are fixed by law and a late audit can cost you franchise sales.

3. **Compile FYE Updates Now**. All franchisors must update certain information in the FDD even if they make no program changes requiring modifications to the franchise agreement. E.g., Item 2 (changes in key management); Items 3 (litigation) and 4 (bankruptcy) (changes in the status of pending matters, new cases in which Item 2 individuals are defendants, and actions you've initiated against your franchisees during the last fiscal year (FY)); Item 7 (changes in opening costs based on recent experiences); Item 8 (payments from suppliers during

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the last FY and updates about officers who own an interest in recommended or mandatory suppliers); Item 11 (percentage breakdown on advertising fees used during the last FY); Item 13 (updates about trademarks and known infringers); Item 20 (franchise statistics and corresponding lists of existing franchise outlets and recent terminations); and Item 21 (adding the new audit). You'll also need to update franchise seller disclosure forms. All of this information must be current as of the FYE, which means you have the data to compile updates now. Don't wait until your audit is done to begin work.

4. **Give a Heads Up to Your Franchise Sales Team.** Let your franchise sales and operations teams know about impending deadlines so that pending franchise sales, discovery days and other franchise sales activities can be coordinated and, if possible, completed ahead of time. A few states do not provide for automatic renewal, which may cause a company temporarily to go "dark" if a state franchise examiner cannot process the renewal application before the registration expires (a frequent occurrence). If sales go dark because of a delayed audit or renewal application, explain to your sales team that they'll need to re-disclose prospects in the pipeline with the new FDD and restart the 14 day waiting period once you clear hurdles. Discipline your sales team to comply with your directions for handling "dark" periods and powering up afterwards.

5. **Take Stock of Your Contracts**. FYE updating season is a convenient time to take stock of your contract commitments. Re-read all of the contracts that you ask franchisees to sign. Make sure that all of the obligations you impose on them are important and being enforced. Check that you still provide all of the services that Item 11 of your FDD claims you offer. Have your attorney re-read the contracts and advise you of any changes in the law that might affect the enforceability of any provisions. While you do not have to make any adjustments to your franchise program, it is convenient to do so at renewal time since that eliminates mid-year material changes and extra filings and filing fees.

6. **FPRs: Update or Reconsider.** If your company makes an Item 19 financial performance representation (FPR), the claim must be reevaluated based on FYE results for franchisees who fall within the claim's parameters. If the latest data is not rosy, consider omitting the FPR from your updated FDD (explain what this means to your sales team). If you stick with a FPR, update the numbers (you may change the parameters depending on outcomes; just explain all assumptions). If your current FDD does not include a FPR, but the latest numbers are impressive, consider adding a FPR now since doing so will avoid mid-year material change amendment filings and extra filing fees. Don't finalize the FPR without having your franchise attorney review it first. FPRs are a target for unhappy franchisees who don't achieve disclosed results so it is important to make sure the FPR explains all of the bases and assumptions underlying the claim.

7. **Inventory Your IP.** The annual updating ritual is a convenient time to review your IP portfolio to make sure you've filed applications to protect new logos or brand names introduced during the last FY, filed the necessary applications to maintain existing trademark registrations, and taken steps to protect patents and copyrights valuable to your franchise system.

8. **State Tax Initiatives.** Cash-strapped states are stepping up efforts to impose income taxes and reporting obligations on out-of-state franchisors. Make sure you know about these extra duties in the states where you sell franchises and comply with them.

9. **Review Website Content and Advertising.** Your marketing department may be responsible for keeping your website content current, but may be unaware of what your FDD says. Review your website to make sure it is entirely consistent with the terms of your franchise offering. If your FDD has no FPR, then your website cannot provide any information to prospective franchisees about historical or potential income, sales, earnings, profits or break-even points. Make sure all other forms of advertising used to attract franchise prospects is legally compliant and registered in the states where the you distribute or publish the advertising.

10. **Mandate Refresher Training in Franchise Sales Compliance**. Before you complete FDD updates, schedule refresher training in franchise sales compliance rules and company sales policies for your franchise brokers and management who interact with prospects during the franchise sales process. Use the updated FDD and renewal season to remind your team of the rules of the road. A franchisor's officers, directors, partners, managers, franchise sellers, and key management may be personally, jointly and severally, liable for franchise law violations even when the franchisor is a legal entity. Remember: franchise laws are consumer protection laws that are construed liberally in favor of franchisees even when the franchisee is sophisticated. Ignorance of the law or a lack of any intent to violate the law is no defense. Given the significant penalties involved, annual franchise sales compliance training is an ounce of prevention that is worth far more than a pound of cure.