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CAUGHT IN THE WEB OF FEDERAL AND STATE BUSINESS OPPORTUNITY LAWS: MANAGING AND AVOIDING THE ENTANGLEMENT OF REGULATIONS

Beata Krakus
Greensfelder, Hemker & Gale, P.C.
Chicago, Illinois

and

Alexander Tuneski
Kilpatrick Townsend & Stockton LLP
Washington, DC

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I. INTRODUCTION

A. What is a Business Opportunity?

Many franchise lawyers perceive business opportunities much like traffic jams – ideally avoided and frustrating to deal with if you encounter them. The purpose of this paper is to show that business opportunities statutes, while different from franchise statutes, are not all that onerous and relatively manageable once you familiarize yourself with them.

26 states as well as the federal government regulate business opportunities.[1] A complete list of state business opportunity statutes, including statutory references, is included in Appendix A. A "business opportunity" is defined differently in federal and state laws and regulations, but the definition under the Indiana business opportunity law fairly well represents how the concept is defined in most state laws:

> "Business opportunity" means an investment that:
>
> (1) involves the sale or lease or offer to sell or lease any goods or services to an investor that are to be used by the investor in beginning or operating a business;
>
> (2) involves an initial payment by the investor of more than five hundred dollars ($500) and an initial cash payment of less than fifty thousand dollars ($50,000); and
>
> (3) involves a solicitation of investors in which the seller represents that:
>
> (A) the investor may or will earn an amount in excess of the initial payment as a result of the investment;
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> (B) a market exists for any goods to be made or services to be rendered by the investor;
>
> (C) the seller may buy from the investor any goods to be made or services to be rendered by the investor;
>
> (D) the seller or a person referred by the seller to the investor may or will sell, lease, or distribute the goods made or services rendered by the investor; or

[1] The following states have business opportunity statutes, which are explored in more detail in the Appendices: Alaska, Arizona, California, Connecticut, Florida, Georgia, Illinois, Indiana, Iowa, Kentucky, Louisiana, Maine, Maryland, Michigan, Minnesota, Nebraska, New Hampshire, North Carolina, Ohio, Oklahoma, South Carolina, South Dakota, Texas, Utah, Virginia, and Washington.

> (E) the seller may or will pay to the investor the difference between the initial payment and the investor's earnings from the investment.[2]

There are three elements to the definition. The first element is that the seller must sell or lease goods or services to the buyer that the buyer uses to start a new business. This is not unlike the common franchise definition element of a marketing plan or support being provided by the franchisor to the franchisee: the buyer/franchisee is receiving valuable information and assistance in how to operate a business.

The second element requires there to be at least a minimum payment, again akin to the fee element in the typical franchise definition. In the Indiana statute included above there is also a maximum payment. While not all state business opportunity laws include this type of maximum payment, it is not unusual.

As already pointed out, the definition of a business opportunity is not unlike that of a franchise, and indeed most franchises would satisfy the first two elements of the business opportunity definition. Where the franchise and business opportunity definitions part ways, however, is by the third element. While generally the third element in a franchise definition would be a trademark license, a business opportunity does not necessarily involve trademark association between the seller and the buyer. In fact, the existence of such trademark association is a common exception in state business opportunity laws, taking a distribution relationship that would otherwise be defined as a business opportunity outside of the scope of the business opportunity law.[3] Instead, the focus of the business opportunity statutes are on different types of representations that the seller makes to the buyer: promises about income in excess of the initial investment, promises of buy-back of inventory if the buyer is dissatisfied, or promises to purchase all products grown or produced by the buyer. While far from all franchise systems make such promises in the sales process, there are many that do, and if so, they may find themselves subject to state business opportunity laws.

Perhaps even more so than franchises, it is difficult to capture an image of what a typical business opportunity looks like. Business opportunities can run the gamut from vending machines to restaurants to worm farms to medical billing businesses. A summary of advisory opinions from the Connecticut Department of Banking lists the following as examples of potential business opportunities: a marketing plan to sell long distance telecommunications

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[2] Ind. Code, 24-5-8-1 (2012). One peculiarity of the Indiana definition is that it applies both to the situation where the buyer/investor is starting a business, as well as is already operating the business. Most state business opportunity laws only apply when the buyer is starting a business. This distinction is not necessarily relevant to most business opportunity sellers and franchisors, but for franchisors franchising in reliance on the fractional franchise exemption it is highly relevant. Those franchisors are by definition only selling franchises to somebody who is in business already, and can therefore avoid most business opportunity laws. Arguably, as a fractional franchise is not exempt by the Indiana business opportunity statute’s general exemption for franchises subject to Indiana franchise laws, , fractional franchise system franchisors must find another exemption under the Indiana business opportunity statute, or will be subject to its disclosure requirements.

[3] An important note in this regard is that it is *not always* that a trademark license takes a distribution relationship entirely outside the scope of a state business opportunity law. While many state business opportunity laws contain an exemption for business opportunities in which the seller grants a buyer a license to use a registered trademark, some statutes only exclude such business opportunities from applicability assuming the seller has not made any of the other representations relating to the business opportunity, such as promises regarding investment return or inventory buy-backs.

services, sale of “no run” panty hoses on a multi-level basis, multi-level marketing program offering travel club and car incentive program, sale of Victorian ovens and related equipment, offer to sell distributors materials to be used for craft and artistic products, and a motor vehicle consignment program.[4] Due to the broad scope of many of the laws, they can have an impact on many industries and businesses ranging from large, sophisticated operations to home-based businesses.

B. Why are Business Opportunities Regulated?

The answer to the question “Why is there business opportunity regulation?” is the same as to the question “Why is there franchise regulation?” As business opportunities abound in all kinds of different fields and industries, legislators have found that unfair and deceptive practices may be prevalent among franchisors and business opportunity sellers. As a result, they have concluded that regulations are necessary to protect unsuspecting investors.

According to surveys done by the FTC, such fraudulent activity is indeed widespread. For example, a recent report from the FTC indicated that in 2011 about 1.8 million individuals experienced some type of work-at-home fraud.[5] The same report found that approximately 1.1 million individuals experienced business opportunity-related fraud aside from the work-at-home schemes.[6] The website of every state agency administering a business opportunity law, either by general reference or by links to enforcement activities,[7] tells the same story. There is a concern that unscrupulous business opportunity sellers will overpromise the likelihood of success as well as the support to be provided to buyers and will overcharge for initial inventory and sales equipment. The FTC has over and over again brought enforcement actions against such business opportunity sellers.[8]

C. How Do Business Opportunity Laws Affect Franchisors

For most franchisors business opportunity laws have a limited impact on how they operate. Franchisors are usually not subject to the federal business opportunity regulation and by complying with the FTC Franchise Rule and having a federally registered trademark are, in most part, exempt from state business opportunity laws.

In the start-up phase of a franchise program initial filings will be required under the Connecticut, Kentucky, Nebraska and Texas business opportunity laws, and annual filings are required in Florida and Utah. If the franchise program does not yet have a registered trademark additional business opportunity filings will be required in Connecticut, Georgia, Louisiana,

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4 *See* Index to Business Opportunity Advisory Opinions, available at www.ct.gov/dob/lib/dob/legal_nonHTML/boaoi.doc.

5 *See* Consumer Fraud in the United States: The Third FTC Survey (April 2013) at 18, available at http://www.ftc.gov/os/2013/04/130419fraudsurvey.pdf.

6 Under the 2011 survey fraudulent activity included a buyer making less than half of what was promised by the business opportunity seller as well as a buyer not receiving assistance promised by the seller.

7 *See, e.g.,* the Connecticut Department of Banking website: http://www.ct.gov/dob/cwp/view.asp?a=2246&q=515008.

8 *See, e.g., FTC v. Darling Angel Pin Creations, Inc.,* 2011 WL 65917; FTC v. Route Wizard, Inc., 2007 WL 1266636; *FTC v. The Online Entrepreneur, Inc.*, No. 12-2500 (M.D. Fla. filed Nov. 2012); *FTC v. N. Am. Mktg. & Assoc., LLC*, No. 12-0914 (D. Ariz. filed May 2012); *FTC v. Ivy Capital, Inc.*, 2011 WL 2118626.

Maine, North Dakota and South Carolina. Aside from the annual filings, however, the other business opportunity filings are usually a one-time action.

Relying on the above generalities, however, may be deceptive. As will be discussed below, the state business opportunity laws are not uniform, and small differences in statutory language may make a big difference to franchisors. For example, several state business opportunity laws include exemptions for business opportunity sellers that have a registered trademark and offer their buyers a marketing plan. Some of these exemptions apply to the business opportunity statute as a whole but that is not universally true. Other, very similar exemptions only apply if the franchisor does not make any other representations included in the statutory definition of a business opportunity. Such representations may include buy-back obligations and promises of certain income[9] levels. Not every franchise program makes representations regarding profits or buy back obligations, but it is not uncommon.

Another group of franchisors that need to carefully examine federal and state business opportunity laws are those that operate exemption based programs. In many instances franchisors avoid state business opportunity laws because of explicit exemptions for sellers that comply with the FTC Franchise Rule and provide the buyer with an FDD. Where the franchisor does not provide an FDD it may be subject to both state and federal business opportunity regulation.

II. FEDERAL BUSINESS OPPORTUNITY RULE

A. <u>History</u>

As with the advent of franchise laws, most state business opportunity laws were adopted between 1973 and 1985, with a few outliers being enacted more recently (Illinois in 1995 and Arizona in 2012).[10] The FTC has regulated business opportunity sales since the adoption of the original franchise and business opportunity rule titled "Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures" on December 21, 1978 (the "Original Rule").[11] In the Original Rule, as suggested by its title, both franchises and business opportunities were regulated under the same regulation in Title 16 Part 436 of the Code of Federal Regulations. It was not until the Original Rule was amended in 2007 that the franchise regulations and business opportunity regulations were separated. We refer to the 2007 amendment to the Original Rule as the "FTC Franchise Rule."

The required disclosures in the Original Rule and the FTC Franchise Rule were broad and lengthy. These complex disclosures don't always fit business opportunities well as they are often low investment distribution systems. As a result, hiring attorneys to prepare a lengthy document constitutes a significant cost to the business opportunity seller compared to the likely return.

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9 What is meant by "income" differs between state statutes. Often the focus is on the buyer making more money than he or she invested into the business.

10 *See* James A. Meaney and John R.F. Baer, *The Business Opportunity Laws: An Enforcement and Litigation Trap?* ABA Forum on Franchising, October 10-12, 2001.

11 F.R. Vol. 76, No. 236, December 8, 2011, 76816.

To counteract the potentially high cost of compliance, the FTC created a number of exemptions to limit applicability to those business opportunities that truly warranted disclosure.[12] The $500 minimum payment exemption[13] is commonly known to franchise counsel, as is the exclusion from the minimum payment of reasonable amounts of inventory purchased at bona fide wholesale prices. The most significant exemption or limitation, however, was that the Original Rule only applied to those types of business opportunities that the FTC deemed were most likely to cause serious consumer injury.[14] In particular, the Original Rule focused on business opportunities where the seller helped the buyer locate locations or accounts.[15] As a result, most business opportunities fell outside of the scope of the Original Rule.

In 1999 the FTC announced that it would seek to create a separate rule for business opportunities.[16] Though the FTC Franchise Rule was revised in 2007, it was not until December 8, 2011 that the FTC finally adopted a rule entitled "Disclosure Requirements and Prohibitions Concerning Business Opportunities" (16 C.F.R. 437) (which will be referred to in this paper as the "Federal Rule") which went into effect on March 1, 2012.[17] The Federal Rule addresses the ailments of the Original Rule. It is both broader in scope, capturing more business opportunities, and less onerous with respect to disclosures, allowing for a significantly shorter disclosure document than the average franchise disclosure document.

B. Scope of the New Rule/Definition of Business Opportunity

The Federal Rule defines a business opportunity in the following manner:

> Business opportunity means a commercial arrangement in which:
>
> (1) A seller solicits a prospective purchaser to enter into a new business; and
>
> (2) The prospective purchaser makes a required payment; and
>
> (3) The seller, expressly or by implication, orally or in writing, represents that the seller or one or more designated persons will:
>
> (i) Provide locations for the use or operation of equipment, displays, vending machines, or similar devices, owned, leased, controlled, or paid for by the purchaser; or
>
> (ii) Provide outlets, accounts, or customers, including, but not limited to, Internet outlets, accounts, or customers, for the purchaser's goods or services; or

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12 *Id.* at 76817.

13 The minimum payment has been adjusted to $540 and can be further amended by the FTC.

14 F.R. Vol. 76, No. 236, December 8, 2011, 76817.

15 *Id.*

16 *Id.*

17 *Id.* at 76816.

> (iii) Buy back any or all of the goods or services that the purchaser makes, produces, fabricates, grows, breeds, modifies, or provides, including but not limited to providing payment for such services as, for example, stuffing envelopes from the purchaser's home.[18]

There are several noteworthy points about the above definition. First, the Federal Rule, as the Original Rule, covers business opportunities where the seller helps the buyer locate outlets or accounts. However, the Federal Rule also covers business opportunities where the seller promises to buy back goods or services that the buyer "makes, produces, fabricates, grows, breeds, modifies, or provides." By adding this provision, the Federal Rule captures many work-at-home business opportunities that were previously outside the scope of the Original Rule. Second, there is no minimum payment threshold in the definition meaning that businesses that previously escaped federal business opportunity regulation solely by keeping initial fees low now are likely within its scope.

C. Comments During the Federal Rule Making Process Affecting Its Scope

The Federal Rule remains narrower than most state business opportunity laws, but this doesn't mean there were no objections to the scope of the Federal Rule during the rule making process. In particular, significant concern was voiced by the Direct Sellers Association ("DSA") and its members who are primarily multi-level marketing systems ("MLMs"). The FTC received more than 17,000 comments in response to the Initial Notice of Proposed Rulemaking, almost all of which came from MLMs.[19]

MLMs are in many ways similar to franchise systems: an MLM buyer gets the right to sell goods or services under a specific trademark, there is often some type of training provided or control exercised by the seller, and there is a fee paid. MLMs can usually avoid state franchise and business opportunity laws by structuring the initial investment to be below the minimum payment threshold. In the past this technique also avoided federal regulation. With the Federal Rule not having a minimum payment threshold, the DSA was concerned that its members would be subject to it, as MLMs are frequently structured so as to grant the buyer a buy-back right. This means that if the buyer is dissatisfied with the business opportunity the seller will buy back inventory and sales materials that it initially sold, or "provided" to the seller. The DSA in fact requires its members to include buy-back rights in their agreements requiring the members to offer to buy back at 90% of the MLM participant's cost, all resalable inventory and sales materials.[20] Subsection 3(iii) above was therefore troubling to the MLM industry. Subsection

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18 16 C.F.R. 437.1(c).

19 F.R. Vol. 76, No. 236, December 8, 2011, 76818.

20 The DSA Code of Ethics requires sellers to buy back both inventory and sales aids and kits for 12 months. Section 7(a) of the DSA Code of Ethics (applicable to inventory) states:

> Any member company with a marketing plan that involves selling products directly or indirectly to independent salespeople shall clearly state, in its recruiting literature, sales manual, or contract with the independent salespeople, that the company will repurchase on reasonable commercial terms currently marketable inventory, in the possession of that salesperson and purchased by that salesperson for resale prior to the date of termination of the salesperson's business relationship with the company or its independent salespeople. For purposes of this Code, "reasonable commercial terms" shall include the repurchase of marketable inventory within twelve (12) months from the salesperson's date of purchase at not less than 90 percent of the salesperson's original net cost less appropriate set offs and legal claims, if any. For purposes of this Code, products shall not be considered "currently marketable" if returned for

3(iii) creates a business opportunity (where the other definitional elements are satisfied) where the seller must buy back goods or services "provided" by seller to buyer. It is not an unreasonable reading of that section that a company offering an inventory buy-back would fall within the scope of the Federal Rule. The FTC considered this issue at length and found that, while MLM companies may of course occasionally subject consumers to fraud and unfair trade practices, the MLM industry as such was not the target of the business opportunity regulation and concluded that the word "provide" should not be read to cover inventory buy-backs.[21]

In response to the comments from the MLM industry, the business opportunity definition under the Federal Rule was also narrowed to exclude assistance with tracking payments and providing training. Another significant change made from the initially proposed Federal Rule was to exclude purchases of reasonable amounts of inventory at bona fide wholesale prices from the definition of "required payment."[22]

D. The FTC Disclosure Document

The main consequence of a distribution model satisfying the definition of a business opportunity is that it must provide prospective business opportunity buyers with a disclosure document. A disclosure document under the Federal Rule is extremely simple and short, at least from the perspective of a franchise practitioner. There are a total of six categories in the document:

(i) Identifying information;

(ii) Earnings claims;

(iii) Legal actions;

(iv) Cancellation and refund policy;

(v) References; and

(vi) Receipt.[23]

1. Identifying Information

The identifying information consists of basic contact information: the seller's name, business address and telephone number; the name of the sales person; and the date the

(Continued)

repurchase after the products' commercially reasonable usable or shelf life period has passed; nor shall products be considered "currently marketable" if the company clearly discloses to salespeople prior to purchase that the products are seasonal, discontinued, or special promotion products and are not subject to the repurchase obligation.

The full DSA Code of Ethics is available at http://www.dsa.org/ethics/code/

21 F.R. Vol. 76, No. 236, December 8, 2011, 76832. Further, the FTC found that MLMs were still subject to Article 5 of the FTC Act and that such regulation was at this time sufficient.

22 F.R. Vol. 76, No. 236, December 8, 2011, 76819.

23 16 C.F.R. 437.3 (2011).

disclosure document is being furnished.[24] The obligation to include the date that the disclosure document is being furnished to the prospective buyer means that the document needs to be continuously updated, as opposed to a franchise disclosure document where the date on cover page is required to be the document issuance date.

2. **Earnings Claims**

The FTC decided to keep the old term "earnings claim" instead of the "financial performance representation" term now used in the FTC Franchise Rule. An earnings claim is defined as:

> any oral, written, or visual representation to a prospective purchaser that convey, expressly or by implication, a specific level or range of actual or potential sales, or gross or net income or profits. Earnings claims include, but are not limited to:
>
> (1) Any chart, table, or mathematical calculation that demonstrates possible results based upon a combination of variables; and
>
> (2) Any statements from which a prospective purchaser can reasonably infer that he or she will earn a minimum level of income (e.g., "earn enough to buy a Porsche," "earn a six-figure income," or "earn your investment back within one year").[25]

Many of the requirements for earnings claims are not dissimilar to those for financial performance representations made by franchisors. The seller has to have a reasonable basis for its claim; it must make written substantiation available upon request; and the earnings claim must include information about the time period it relates to, the number and percentage of people who achieved at least the stated level of earnings, and the characteristics of the buyers who achieved the levels.[26]

If the seller is making an earnings claim it must check the box on the form disclosure document and also attach the earnings claim. All earnings claims must be included in a single document. Sellers may not make earnings claims outside of those that are explicitly included in the disclosure document.

3. **Legal Actions**

Again, similar to what is required in a franchise disclosure document, the seller must disclose information about the types of legal actions most likely to impact a buyer's decision to purchase the business opportunity. Specifically, a seller has to disclose if the seller, any affiliate or prior business of the seller or any of the seller's officers, directors, sales managers, or any person who fulfills a similar function as a director or officer, or a sales manager have been subject to any civil or criminal action for misrepresentation, fraud, securities law violations, or

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[24] 16 C.F.R. 437.3(a)(1).

[25] 16 C.F.R. 437.1(f).

[26] 16 C.F.R. 437.4.

unfair or deceptive practices, including violations of any FTC Rule, within the 10 years immediately preceding the business opportunity offered.[27] If there are no such actions to disclose, the seller simply checks a box on the disclosure form. If there are one or more actions, the seller must include an attachment with the disclosure form that discloses the caption of each action and a summary of the action. The summary may be no longer than 100 words. The 100 word limit seems questionably short, but fits the apparent intention to make the disclosure document very brief itself.

4. Cancellation or Refund Policy

The fourth disclosure category is the seller's cancellation or refund policy. Again, if the seller offers such a policy it must check a box so indicating on the disclosure form and include information about the policy in an attachment. The attachment should disclose material terms and conditions of the policy.

5. References

The last substantive disclosure category is references. The seller must disclose the name, state and telephone number of all buyers who purchased the business opportunity within the last 3 years, except that if there are more than 10 buyers, the seller can provide the contact information for the 10 buyers located closest to the buyer's location.[28] If the seller chooses to provide a list of all buyers, this can be done in an attachment to the disclosure form.

6. Receipts

The last disclosure is not so much a substantive requirement as a formality. In the case of a federal business opportunity disclosure document, the disclosure document itself is the receipt, since there is room on the disclosure form for a signature line and date line. The seller is required to provide the buyer the form in duplicate, one of which is to be returned to the seller after the buyer's signature as a receipt. It is not clear from the Federal Rule whether attachments that are part of the disclosure document need to be provided with the duplicate copy.

7. Foreign Language Requirement

One interesting aspect of the Federal Rule is that the FTC looked closely at the groups of individuals that were being targeted by business opportunity fraud and found that many such groups are ethnic groups and immigrants that may only have a rudimentary knowledge of the English language. Thus, the Federal Rule requires a seller to provide the disclosure document in the language that the seller "conducts the offer for sale, sale, or promotion of the business opportunity."[29] Presumably because of the size of the Spanish speaking population in the U.S., the Federal Rule even goes so far to include the Spanish language version of the disclosure form. For disclosures in other languages, the seller must translate the form itself.

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[27] 16 C.F.R. 437.3 (a) (3).

[28] 16 C.F.R. 437.3 (a) (5).

[29] 16 C.F.R. 437.5

8. Lack of Integration with State Laws

The Federal Rule does not permit business opportunity sellers to include information in the federal disclosure document beyond what is required by the Federal Rule. As will be discussed in the next section of this paper exploring state business opportunity law disclosure requirements, those requirements are usually more far reaching and extensive that those of the Federal Rule. Consequently, business opportunity sellers that offer their program in states with business opportunity laws cannot combine the federal disclosure document with their state disclosure documents. This creates additional complexity for business opportunity sellers.

As will be discussed below, it is virtually impossible to create a single business opportunity disclosure document that can be used in all states because of different state law disclosure requirements both with respect to substance and form of the disclosure. Business opportunity sellers subject to the Federal Rule may be required not just to have different disclosure documents for different states, but may also have to provide prospective buyers with two documents: a state disclosure document and a separate federal disclosure document.

III. STATE BUSINESS OPPORTUNITY LAWS

A. Introduction to State Business Opportunity Laws

While the Federal Rule rarely impacts traditional franchise arrangements, 26 states have business opportunity laws, which often are expansive enough to cover relationships ranging from traditional franchises to the placement of vending machines, racks, display cases, and amusement machines. These statutes, which are listed in Appendix A, protect investors purchasing goods and services that will allow them to begin operating businesses. As a result, these statutes sometimes provide protection for purchasers of franchises as well as purchasers of other business opportunities.

On the state level, business opportunities may be regulated within state business opportunity laws, seller-assisted marketing plan statutes, franchise disclosure laws, or consumer protection laws. Seller-assisted marketing plans and business opportunities are largely interchangeable terms, and there are not significant differences between the two statutes, besides the labeling used. For business opportunities regulated by consumer protection laws, such as Little FTC Acts or Deceptive Trade Practices Acts (these states include Alabama, District of Columbia, Oregon, and Tennessee), these laws typically only prohibit sellers from making misrepresentations in the course of selling such opportunities and do not require disclosures or further regulate the sales process or business relationship. We have not included these consumer protection states in the tally of business opportunity laws.

Though many business opportunity statutes were originally enacted in the 1970s, there have been some recent developments in this field of law. Most notably, Arizona enacted a business opportunity statute that took effect in 2012.[30] Moreover, Ohio amended its existing

[30] The Arizona statute was integrated into an existing statute that applied to telephone solicitations only. As a result, the Arizona statute at first look appears to be quite different than most business opportunity statutes. However, upon closer examination, the provisions that were added are quite similar to those of other states.

statute in 2012, clarifying the scope of certain statutory provisions, such as buyer cancellation rights, and expanding its scope in some respects.[31]

While there are some similarities between the various state business opportunity laws, the challenge facing practitioners is that the provisions within the state laws can vary significantly. Thus, if a business opportunity is being offered nationwide, care must be taken to determine which state laws apply and whether those states impose special requirements on sellers in the state. What is acceptable in one state often is not sufficient to satisfy the statutes of other states. As a result, nationwide sellers often must adopt a lowest common denominator approach, structuring sales processes and disclosures to satisfy the requirements of the most stringent state statutes.

In this section, we will review different definitions of business opportunities as well as exemptions and exclusions, which may be available for a sales program to fall outside the scope of the laws. We will highlight certain states that have statutes that are likely to impact all franchise sales, as well as those that may impact a more limited selection of franchisors. Then, we will focus on complying with the business opportunity laws, examining common disclosure requirements, bonding requirements, and conditions that must be included in business opportunity contracts. Finally, we will look at the penalties for non-compliance, which can be significant.

B. <u>The Definition of Business Opportunity – A Trap for the Unwary</u>

Though the state laws vary, there are common elements of the definition of business opportunity that appear in most laws. One thing that most of them have in common is that they can be read expansively to cover some of the representations and obligations that are commonly found in franchise agreements. As we will see, there are a number of ways that a traditional franchise and other selling programs can come within the purview of business opportunity statutes.

As previewed in the introduction, to be a business opportunity or a seller assisted-marketing plan, in most state statutes, the following elements must be satisfied:

1. The seller must sell or lease products, equipment, supplies or services to the purchaser,

2. For the purpose of enabling the purchaser to start a business,

3. With the purchaser making an initial investment of over $500 (as low as $200 in some states), including amounts paid for inventory through the first six months of operation,

4. And the seller making one or more of the following representations:

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[31] Among other changes, the Ohio statute updated the existing statute to reference the Federal Rule and increased monetary amounts (such as increasing the maximum investment level from $50,000 to $100,000 and increasing the large seller exemption net worth requirement from $5,000,000 to $15,000,000). For further analysis of the revisions to the Ohio statute, *see* G. Jack Donson, *What All Franchise Lawyers Should Know About the Recent Changes to Ohio's Business Opportunity Law*, The Franchise Lawyer, Vol. 16. No. 1.

a. That the seller will provide locations or assist the purchaser in finding locations for the use or operation of vending machines, racks, display cases or other similar devices, or currency-operated amusement machines or devices, on premises neither owned nor leased by the purchaser or seller; OR

b. That the seller will provide or assist the buyer in obtaining accounts, customers, or other markets; OR

c. That the seller may, in the ordinary course of business, purchase any or all products made, produced, fabricated, grown, bred or modified by the purchaser using in whole or in part, the supplies, services or chattels sold to the purchaser; OR

d. That the seller guarantees that the purchaser will derive income from the business opportunity which exceeds the price paid for the business opportunity; OR

e. That the seller will refund all or part of the price paid for the business opportunity, or repurchase any of the products, equipment, supplies or chattels supplied by the seller, if the purchaser is unsatisfied with the business opportunity; OR

f. That the seller will provide a sales program or marketing program which will enable the purchaser to derive income from the business opportunity which exceeds the price paid for the business opportunity; OR

g. That there is a market for the products.

With these elements in mind, we will discuss each of the elements in greater detail.

Element 1: The seller must sell or lease products, equipment, supplies or services to the purchaser,

This includes both the sale of products, equipment, and supplies for resale to customers or for the use in establishing a purchaser's business. In addition, the provision of a marketing plan, training services, or sales services by the seller to the purchaser is enough to constitute the sale of a service.

Element 2: For the purpose of enabling the purchaser to start a business,

Nearly all business opportunity statutes cover only sales or leases to a purchaser for the purpose of assisting them to start a business. From a policy perspective, purchasers starting a business need additional regulatory protection; because they are presumably not experienced in the business they are becoming involved in and may be more reliant on the purchaser for assistance. However, some states, including California and Indiana, have more expansive statutes that also cover sales and leases to ongoing businesses, which significantly expand the scope of those statutes.

Element 3: With the purchaser making an initial investment of over $500 (as low as $200 in some states), including amounts paid for inventory through the first six months of operation,

The initial investment can include both fees, such as royalties, initial fees, or advertising fees, and payments for goods or services. Unlike under the Franchise Rule, in most states, payments paid for the purchase of goods at bona fide wholesale prices are not exempted from the calculation of the amount of the initial investment. In Alaska, Ohio, South Carolina and Washington, however, payments made for the purchase of inventory at bona fide prices do not count towards the initial investment calculation.

Element 4: And the seller must make one or more of the following representations:

Note, in Appendix B, we have included a chart detailing which state statutes are triggered by the inclusion of these representations.

Representation 1: That the seller will provide locations or assist the purchaser in finding locations for the use or operation of vending machines, racks, display cases or other similar devices, or currency-operated amusement machines or devices, on premises neither owned nor leased by the purchaser or seller;

This provision relating to vending machines, racks, display cases, and amusement machines is largely responsible for a common misconception amongst practitioners about the limited scope of business opportunity laws. While this is one of the possible triggers for a business opportunity statute and describes a variety of business opportunities that have historically been ripe for fraud, it is not the most expansive trigger. A seller may be found to have assisted a purchaser in finding a location by providing a locator company, supplying names, collecting a fee on behalf of a locator company, or even approving a site proposed by a purchaser. In Texas, the statute covers providing locations or assisting in finding locations for the sale of products or services, but does not refer to vending machines, racks, display cases, or amusement machines.

Representation 2: That the seller will provide or assist the buyer in obtaining accounts, customers, or other markets;

This representation is included in a little over a third of the business opportunity statutes. A seller that simply provides a list of customers to a purchaser can be found to have assisted the purchaser in obtaining customers.

Representation 3: That the seller may, in the ordinary course of business, purchase any or all products made, produced, fabricated, grown, bred or modified by the purchaser using in whole or in part, the supplies, services or chattels sold to the purchaser;

This buy-back provision is present in nearly all of the business opportunity statutes. From a policy perspective, if a seller promises that they will buy back all of the products that a purchaser produces, the purchaser's business is wholly reliant on the purchaser's ability to follow through on this obligation. As a result, this representation can trigger the protection of the business opportunity statutes. Moreover, many states require sellers to secure surety bonds or trust accounts if the seller makes this representation, to ensure that the purchaser will be able to recover some monies if the seller fails to follow through with its obligations.

Representation 4: That the seller guarantees that the purchaser will derive income from the business opportunity which exceeds the price paid for the business opportunity;

The representation that the purchaser will make a profit is also a trigger present in nearly all of the business opportunity statutes. In Nebraska, this provision is even more expansive, covering any seller that represents that the purchaser will, is likely to, or can derive income which exceeds the initial payment; even if the seller does not guarantee that the purchaser will do so. Even for statutes that explicitly require the seller to guarantee profits, the provisions may be interpreted expansively enough to cover oral representations of future success.

For example, in *Martin v. Pilot Industries, et al.*, 632 F.2d 271 (4th Cir. 1980),[32] the Fourth Circuit Court of Appeals held that advertised claims that a business opportunity would produce "substantial profit" and that the tested procedures would "make your business into an exclusive money machine," combined with the provision of a profit projection estimating $25,670 in net income, constituted a guarantee of income, despite the fact that the contract explicitly stated that "no representations, inducements, promises, or agreements, oral or otherwise, between the parties not embodied herein shall be of any force or effect" and a disclosure document provided to the seller also disavowed any guarantee of profit. The Fourth Circuit concluded that the prior representations could convey to a reasonable person that income was being guaranteed, triggering the protection of the business opportunity law.

In contrast, a Maine state trial court reached a different conclusion when faced with a similar statute and representations that it deemed to constitute less of an assurance than in the *Martin* case.[33] The court focused on the meaning of "guarantee," noting that the provision was not just triggered by a representation that the seller would make a profit. The court concluded that "the statute thus makes plain that a seller must go beyond a mere representation of what is to happen and guarantee the occurrence."[34]

Taken together, there is a risk that the mere representation of potential profit is sufficient to trigger the business opportunity statutes. Certainly, a financial performance representation or other earnings claim could be enough to satisfy this condition, even if accompanied by disclaimers indicating that the results are not guaranteed and may not be representative. Thus, many franchisors could fall within the scope of this provision.

Representation 5: That the seller will refund all or part of the price paid for the business opportunity, or repurchase any of the products, equipment, supplies or chattels supplied by the seller, if the purchaser is unsatisfied with the business opportunity;

This provision, also present in the majority of state statutes, is intended to protect purchasers from fraudulent schemes guaranteeing that the seller can be made whole again if they purchase the opportunity. This provision can also be expansively interpreted to include

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32 *Martin v. Pilot Industries, et al.*, 632 F.2d 271 (4th Cir. 1980).

33 *Elliott Speers & Kennebunk Care, Inc. v. Downey*, 1992 Me. Super. LEXIS 236 (Me. Super. Ct. Oct. 19, 1992).

34 *Id.* at 2.

many provisions that are common within franchise agreements, such as provisions promising to buy back inventory upon termination, as well as provisions promising the refund of initial fees if a franchisee is unable to find a suitable site or to satisfactorily complete training.

Representation 6: That the seller will provide a sales program or marketing program which will enable the purchaser to derive income from the business opportunity which exceeds the price paid for the business opportunity; or

The marketing program representation is the one that has the potential to impact nearly all franchisors, since franchise sales typically involve the offer and sale of marketing programs and assistance. While many states do not explain what constitutes a sales or marketing program, some, such as Oklahoma, explicitly define a marketing plan as advice or training pertaining to the sale of any products, equipment, supplies or service, including (i) preparing or providing promotional literature, brochures, pamphlets or advertising materials, (ii) training regarding the promotion, operation or management of the business opportunity; or (iii) operational, managerial, technical, or financial guidelines or assistance.[35]

In ten states, however, the marketing program representation only applies to sales or marketing programs that are not made in conjunction with the licensing of a registered trademark or service mark.[36] Thus, in these states, sellers can represent that they will provide a marketing program in conjunction with a registered trademark or service mark without triggering the business opportunity statute. However, in these ten states, an offering could still fit the definition of a business opportunity if the seller makes any of the other representations that trigger the statute.

In another five states, any sale of a marketing program that is made in conjunction with a registered mark is explicitly excluded from the definition of a business opportunity, provided that the seller has a net worth in excess of $1,000,000.[37] In Washington, the sale of a marketing program made in conjunction with the licensing of a registered mark is excluded from the statute if no consideration is paid. In these six states, the presence of a marketing plan made in conjunction with a registered mark, combined with the large seller (or lack of consideration for Washington), knocks the offering out of the scope of the statute altogether, even if the seller makes other representations that would otherwise trigger the statute.

Thus, the marketing program element does not apply to many franchisors as a result of these exclusions, which can be used to protect franchisors from the applicability of these statutes.[38] However, in eleven states, these exclusions and exemptions are limited to only sellers who offer marketing programs in conjunction with federally registered marks.[39] For the

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[35] Okla. Stat., tit. 71, § 802 (2013). See also *Matter of Commercial Monetary Dev., Inc.*, BFG ¶10,000. (Conn Dept. Banking 1991) (concluding that the sales, promotion, and operations advice promised by a loan brokerage company to purchasers was the equivalent of a "sales program or marketing program" within the statutory definition).

[36] These states include: Arizona, Connecticut, Florida, Georgia, Illinois, Louisiana, Maine, Michigan, North Carolina, and South Carolina.

[37] These states include: Alaska, Iowa, Maryland, Oklahoma, South Dakota.

[38] See, e.g., *Am. Casual Dining, L.P. v. Moe's Southwest Grill, L.L.C.,* 426 F.Supp.2d 1356 (N.D. Ga. 2006) (holding that the Georgia Business Opportunity Act clearly did not apply to a franchise offering a marketing plan in conjunction with a registered trademark).

[39] These states include: Arizona, Connecticut, Illinois, Iowa, Maine, Maryland, Michigan, North Carolina, Oklahoma, South Dakota, and Washington.

remaining five states that do not specify the type of registration required,[40] there is little official guidance as to whether registration of a state mark is sufficient, but, in practice, state registrations are typically considered to be acceptable.

In states that require federal trademark registrations in conjunction with marketing programs, many new franchisors may be subject to the business opportunity laws until their trademarks have been federally registered. If a franchisor is already operating company-owned units within the state, it is often fairly quick, easy, and inexpensive to secure a state registration, which would enable them to avoid the application of these statutes. However, if a franchisor is not already operating within a state, there may be no option other than to comply with the disclosure and sales requirements set forth in the statute.

Representation 7: That there is a market for the products.

This element only appears in six of the business opportunity statutes, but it too can be particularly expansive and can impact franchisors.[41] In *Ohio Learning Centers, LLC, et al. v. Sylvan Learning, Inc.*,[42] a federal district court concluded in an unreported decision that the sale of an existing Sylvan Learning Center business was sufficient to satisfy the trigger that the seller makes a representation that a market exists. The court found that the defendant could not argue that it did not represent that a market existed, because such a representation was implicit in the sale of the business. As a result, the court denied a motion to dismiss the plaintiff's Ohio business opportunity claims.

C. <u>Exclusions from the Statutes: Escaping the Scope</u>

As you can see, many sales relationships could technically fall within the scope of these business opportunity laws. However, there are also a number of exclusions and exemptions available in most states that trim back the reach of these statutes. The following describes the exemptions and exclusions available, which are outlined for each state in a chart in Appendix C.

i) **Franchisor Exemptions.** Most franchisors rely on an exclusion for business opportunities that meet the definition of franchise under the FTC Franchise Rule or applicable state laws. Eighteen state statutes[43] explicitly exclude franchises from the business opportunity laws, provided that sellers comply with these franchise statutes, including furnishing Franchise Disclosure Documents to purchasers.[44] Florida, Kentucky, Nebraska, Texas, and Utah require franchisors seeking to claim a franchisor exemption to file a notice with the state, along with a nominal filing fee. These notices require the franchisor to affirm that it is in compliance with the FTC Franchise Rule.

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40 These states include: Alaska, Florida, Georgia, Louisiana, and South Carolina.

41 These states include: Arizona, California, Indiana, Kentucky, Nebraska, and Ohio.

42 *Ohio Learning Centers, LLC, et al. v. Sylvan Learning, Inc.*, 2012 WL 3025106 (D. Md. July 24, 2012).

43 These states include: Alaska, Arizona, California, Florida, Illinois, Indiana, Iowa, Kentucky, Maryland, Michigan, Nebraska, Ohio, Oklahoma, South Dakota, Texas, Utah, Virginia, and Washington.

44 See *Saydell v. Geppetto's Pizza & Ribs Franchise Sys.*, 652 N.E.2d 218, 228-29 (Ohio Ct. App. 1994) (franchisor failed to provide a complete disclosure document and was therefore found to have violated applicable state business opportunity law).

ii) **Trademark Exclusion**. As mentioned above in the discussion of Representation 6, many state statutes do not apply to marketing or sales programs made in conjunction with the licensing of a registered trademark. Six states exclude marketing programs made in conjunction with a registered trademark (sometimes only federal marks) from the entire business opportunity statute, even if the offering would trigger other elements of the definition.[45] However, to take advantage of this exclusion in Alaska, Iowa, Maryland, Oklahoma, and South Dakota, the seller must also have a net worth in excess of $1 million. In Washington, this exclusion is available only if no consideration is paid for the right to use the trademark.

iii) **Large Seller Exemption.** Fourteen states exempt sellers with high net worth, ranging from $1,000,000 to $25,000,000.[46] These include the states discussed in the previous section, which require a registered trademark in addition to the seller's large net worth. For the other eight states with large seller exemptions[47], there are a number of other conditions that may need to be satisfied. For example, the exemption is available in California for only certain product distributors that meet a number of conditions.[48] In Georgia, the seller must have a net worth of $15 million and be publicly traded to take advantage of the exemption. In Ohio, the seller must have a net worth of $15 million and either have 25 purchasers in operation or have been in business for at least five years.

For most of these states, the net worth requirement is determined on the basis of the seller's most recent audited financial statement prepared within 13 months of the first offer to sell in the state. States allow net worth to be determined on a consolidated basis if one person who satisfies the net worth requirement owns at least 80 percent of the seller and expressly guarantees the obligations of the seller that arise under the sale or offer.

v) **Large Purchaser Exemption**. Illinois and Oklahoma exempt sales to purchasers who have a net worth in excess of $250,000. Connecticut exempts sales to purchasers who have a net worth of at least $1,000,000. In calculating the purchaser's net worth under these state laws principal residence, furnishings, and automobiles are excluded.

vi) **Minimum Initial Investment.** Like the Federal Rule, many state business opportunity laws require a minimum investment; these are listed in Appendix C. The majority of states have set the minimum investment required at $500 before the business begins operating and during the first six months of operation. Ten states have set the bar between $200 and $300.[49] Sellers may be able to restructure payments and services so that there is no or little initial investment, with subsequent payments due after the statutory time period comes into effect.

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[45] These states include: Alaska, Iowa, Maryland, Oklahoma, South Dakota, and Washington.

[46] These states include: Alaska, Arizona, California, Georgia, Illinois, Indiana, Iowa, Maryland, North Carolina, Ohio, Oklahoma, South Carolina, South Dakota, and Texas.

[47] These states include: California, Georgia, Illinois, Indiana, North Carolina, Ohio, South Carolina, and Texas.

[48] See Cal. Civ. Code § 1812.201 (2013). This so-called Responsible Sellers exemption also requires the purchaser to sell products at wholesale and requires the seller to grant the purchaser a license to use a federally registered trademark, in addition to other elements.

[49] These states include: Alaska, Connecticut, Louisiana, Maine, Maryland, Minnesota, North Carolina, South Carolina, South Dakota, and Washington.

vii) **Maximum Initial Investment.** If the investment necessary to purchase and begin operating the opportunity is in excess of a certain amount, some state statutes exempt the opportunity, as also outlined in Appendix C. One court interpreting the Ohio statute explained that the purpose of the business opportunity statute was to protect small investors, rather than larger investors who are more sophisticated and expected to seek their own legal advice.[50]

In California, Indiana, and Michigan, the maximum investment is $50,000. However, in Michigan, there is no cap if the seller guarantees that the purchaser will derive income from the purchase. In Illinois, Oklahoma, and South Dakota, sales with initial payments above $25,000 are excluded, provided that the initial payment is not more than 20% of the purchaser's net worth, excluding the purchaser's principal residence, vehicles, and furnishings. In Ohio, the state legislature raised its cap from $50,000 to $100,000 in 2012.

vii) **Not-for-profit Sales.** The overwhelming majority of statutes exclude or exempt the not-for-profit sale of sales demonstration equipment, materials, or samples (which are used to assist the seller in making sales but not available for resale), provided that the purchase price is $500 or less. In Alaska, South Carolina, and Virginia, there is no cap. The cap is set at $750 in Oklahoma and $300 in Utah.

viii) **Wholesale Sales**. Many state statutes exclude or exempt product inventory sold to a purchaser at a bona fide wholesale price.[51] While Alaska does not provide a cap on the purchase price of such inventory, most state laws cap the purchase price at $500 in the same provision as the not-for-profit sales exemption.

ix) **Sales of Ongoing Businesses**. Similarly, the overwhelming majority of statutes exclude the sale of an ongoing business where the owner of the business is selling a single business and does not intend to sell additional businesses. As a result, the owner of a business opportunity does not need to provide a disclosure statement and otherwise comply with the statute when transferring its business to a third party.

x) **General Merchandise Retailer**. A handful of states (California, Nebraska, Ohio, Texas, and Virginia) specifically exempt sales to general merchandise retailers, which sell diverse goods to the public. In some of the statutes, the general merchandiser must have been in business for at least five years in order to take advantage of this exemption.[52]

xi) **Other Exclusions**. In addition to the exemptions and exclusions described above, there are a number of other exemptions available in states. For example, the statutes exempt sales of securities. Many exempt sales to a purchaser that is a bank, savings and loan association, trust company, insurance company, credit union, investment company, pension or profit sharing trust, or other financial institution.

In Ohio, there is a rather significant and unique exclusion available for any transaction that complies in all material respects with the FTC Franchise Rule or the Federal Rule.[53] If a

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50 *Stanley Steemer International Inc. v. Frazier,* 1984 WL 4279 (Ohio App. 1984).

51 These states include: Alaska, California, Illinois, Iowa, Minnesota, Nebraska, Ohio, South Carolina, South Dakota, and Washington.

52 *See, e.g.,* Cal. Civ. Code § 1812.201 (2013).

53 See, Ohio Rev. Code. Ann. §1334.13 (2013).

seller complies with either federal rule, the seller is not required to comply with the provisions of the Ohio statute, except for the obligation to obtain a bond or establish a trust account in instances where the seller represents that a purchaser's initial payment or note is secured or that the seller provides a buy-back arrangement. Thus, in Ohio, a seller that falls within the scope of the federal statute may use a federal disclosure document rather than tailoring one to comply with the more comprehensive disclosures required by Ohio law.

xii) **Exemption By Order**. If a seller has exhausted all other possible exclusions or exemptions, they still can consider applying to state regulators for a discretionary exemption by order. Some such as Illinois outline in detail the information that must be provided to seek an exemption by order.[54] In making such a request, the purchaser should make clear to the regulators why the seller is unlikely to take advantage of the purchaser or why the purchaser does not require the protection of the statute.

D. Inescapable Obligations.

The determination of whether a business opportunity statute applies is a fact-specific exercise for each seller. For franchise sellers, there are, however, some state laws, which regularly come into play. In this section we will highlight some of these laws, which franchisors may need to pay special attention to when designing compliance programs.

i) **Franchise Exemption States**. As discussed previously, in a handful of states, franchisors must file exemption notices in order to take advantage of available business opportunity exemptions. In Kentucky, Nebraska, and Texas, sellers must make a one-time notice filing along with a fee $100 in Nebraska and $25 in Texas. In Florida and Utah, annual filings are required along with a $100 filing fee.

While franchisors regularly file exemptions notices in these states, in Florida, a strong argument can be made that the franchise exemption filing is not required for franchisors that have a registered trademark, because marketing plans offered in conjunction with registered marks are excluded from the definition of business opportunity. The exemption notice provision was added to the Florida statute in 1993. In *Barnes v. Burger King Corp.*,[55] Burger King successfully argued that franchises offering marketing programs were excluded from the definition of business opportunity, provided that they were offered in conjunction with a registered mark. This ruling suggests that the Florida exemption filing may only be required for franchisors that offer marketing programs, but do not have registered trademarks.

Despite this, most practitioners recommend filing in Florida to ensure that the seller is completely protected and that there is no question that the seller is exempt. Moreover, the filing of an exemption notice can be helpful, because media outlets may ask for a franchisor's business opportunity registration number before accepting advertisements from a franchisor.

ii) **Unregistered Mark States**. Connecticut, Georgia, Maine, South Carolina, and North Carolina are states whose business opportunity statutes apply if the franchisor does not have a registered trademark. In these states, there is no franchise exemption available and the trademark exemption requires a registered trademark.

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[54] Ill. Admin. Code tit. 14A §135.100 (2013).

[55] *Barnes v. Burger King Corp.*, 932 F. Supp. 1420 (S.D. Fla. 1996).

For new franchisors, in particular, which may not have registered trademarks, filings may need to be made and bonds or escrow accounts may need to be created to comply with these statutes. Georgia does not require a filing, but requires sellers to put into escrow 85% of the initial payment owed by the purchaser. Maine requires a filing and requires sellers to post a surety bond of $30,000 or establish an escrow account in the state in the same amount. In the Carolinas and Connecticut, a disclosure document must be filed in the state. These three states also require a bond or trust account to be established of at least $50,000 if the seller guarantees that the purchaser will derive income or promises to refund the purchaser's initial payment (or, in Connecticut, if the seller promises to buy back the purchaser's inventory).

While Connecticut, Maine, and North Carolina require a federally registered trademark to take advantage of the trademark exemption, in Georgia and South Carolina, any registered trademark, whether state or federal, is sufficient to trigger the trademark exemption. Once the trademark has been secured, a franchisor typically will no longer have to comply with the state statute, unless it triggers another one of the elements of the business opportunity definition.

IV. COMPLYING WITH BUSINESS OPPORTUNITY LAWS

If an arrangement is a business opportunity, there can be a number of additional registration, disclosure, and sales requirements imposed on the seller by the state. As we have discussed, these requirements can vary significantly between states. Thus, once you have determined that a seller must comply with the statutes, it is important to familiarize the seller with the specific requirements of each state law, which are discussed below in greater detail and are also described in Appendix D.

A. Required Contractual Terms.

Unlike franchise statues, business opportunity laws typically include controls or conditions on the business relationship between the seller and purchaser. Business opportunity statutes typically require contracts to be in writing and to require certain terms. At a minimum, states typically require these contracts to include:

(1) The terms and conditions of any and all payments due to the seller;

(2) The seller's principal business address and the name of the seller's agent to receive process in the state;

(3) The business form of the seller (corporation, partnership, etc.);

(4) Detailed description of the services that the seller will provide the buyer;

(5) The delivery date or the approximate delivery dates for periodic deliveries or the products, equipment, or supplies necessary to start the business; and

(6) Whether the products, equipment or supplies will be delivered to the purchaser's home or business or will be placed by the seller at locations owned or managed by persons other than the purchaser.

B. Drafting Disclosure Documents.

In the business opportunity states, most states require disclosures to be made to prospective purchasers that far exceed the relatively simple disclosures required under the Federal Rule. The required disclosures vary by state, creating even more complexity for a seller attempting to comply. Virtually all states require that state-specific cover pages be used or that state-specific disclosures be made.

Recognizing this issue, when the Original Rule was in place, a number of states were willing to accept a disclosure document that was compliant with the disclosures required by the Original Rule in order to promote uniformity. The Connecticut statute actually explicitly directed its administrators to work with the Federal Trade Commission and other state administrators to enact rules to effectuate a policy of maximum uniformity in regulations.[56] Since the required disclosures under the Original Rule were broad and comprehensive, the federal disclosure often would be more or equally extensive as the disclosures required under the state statutes.

Now that the current Federal Rule requires simpler disclosures than state business opportunity laws, in some cases, it is unclear whether the federal disclosure is still acceptable in lieu of the state disclosures. Illinois, Ohio, and South Dakota's statutes have been revised to explicitly state that a disclosure that complies with the Federal Rule is acceptable, though South Dakota requires a state-specific cover sheet to be included. A number of other states' statutes which allowed disclosures under the Original Rule have not been revised to reference the new Federal Rule and continue to reference the Original Rule by statutory reference (16 C.F.R. 436) or by name.[57] It is quite possible that they were intentionally not revised, since the statutes still make sense if read to allow franchise disclosure documents compliant with the FTC Franchise Rule to be used instead of state business opportunity disclosures. However, it is possible that some of these states may interpret, or later revise, their statutes to allow the use of the federal business opportunity disclosure documents.[58]

On the other hand, in a few states, it is clear that the limited federal business opportunity disclosure would not be acceptable. Oklahoma's statute was revised in 2011 to update its cross references to make clear that only disclosures compliant with the FTC Franchise Rule would be acceptable, rather than the simpler disclosures required by the Federal Rule. Thus, Oklahoma took the opposite approach of Illinois, Ohio, and South Dakota by not loosening its disclosure obligations. In Maine and Texas, a federal disclosure document is acceptable, provided it meets or exceeds the disclosures required by the state statutes. In both instances, the disclosures required by the Federal Rule fall short of those required by the statutes.

For those states that do not accept the federal disclosure documents, sellers must produce disclosures that comply with all of the provisions of the applicable state law. As a result, sellers may need to produce a disclosure document to comply with the Federal Rule and another one to comply with state laws, which may need to be further supplemented or modified for individual states. The time and expense needed to comply with the laws of all the states can quickly multiply, but it is possible to develop a disclosure document that is comprehensive

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[56] Conn. Gen. Stat. §36b-77 (2013).

[57] These states include: Connecticut, Florida, Georgia, Iowa, Maryland, and Nebraska.

[58] Notably, the Connecticut statute references 16 C.F.R. 436 as amended from time to time and the Nebraska's statute references 16 C.F.R. 436 or any successor regulations, opening the door for an argument that the Federal Rule is an amendment or successor to the Original Rule.

enough to satisfy the disclosure requirements of the state laws, though some variations may still be required to the base document to fully comply with particular laws.

i) **Common Elements in Disclosure Documents**. Though the state requirements vary, there are some basic disclosures common in nearly all statutes. In Appendix G, a chart summarizes some of the disclosures required in each state. The most common required disclosures include the following:

(1) Disclaimers that the disclosure document has not been verified by the state.

(2) Name of the seller, information concerning the seller's corporate entity, and names of affiliates involved in transactions or responsible for business activities of seller. Some states require litigation disclosures and bankruptcy disclosures for the seller too.

(3) The name, addresses, and titles of any officers, directors, trustees, partners, managers, executives, or other individuals responsible for the seller's business activities related to the sale of business opportunities. Many states also require comprehensive disclosures about these individuals, including their past seven to ten years of business experience, including educational and professional background, as well as their litigation and bankruptcy history. These disclosures can be more comprehensive than those required under the FTC Franchise Rule.

(4) The experience of the seller selling business opportunities and the current business opportunity.

(5) A full and detailed description of the services that the seller will provide.

(6) The nature of any services that the seller will provide in connection with the placement of equipment, product, or supplies at various locations, as well as the nature of any agreement made with such outlets.

(7) A complete description of any training to be provided, including the length of training and any training fees.

(8) A financial statement that is either audited or, for some states, signed by an officer under penalty of perjury.

(9) A notice of any bonds or trust deposits established, as required by state statute.

(10) A notice of the seller's right to rescind the agreement in accordance with applicable state laws if products, equipment, or supplies are not delivered by a certain period of time.

(11) If the seller makes any statement concerning sales or earnings that may be made, a disclosure regarding the number of purchasers who have achieved such levels within 3 years of the disclosure date compared to the number of total purchasers.

ii) **Additional Required Disclosures**. Some states require additional disclosures beyond these basic ones.[59] These additional disclosures may include:

(1) A detailed description of any licenses or permits required for the purchaser to engage in or operate the business opportunity.

(2) Details concerning any guarantees made to the seller.

(3) Details concerning the number of similar businesses that have been sold, the number that have requested and received a refund or rescission, and the number of sales expected in the next year.

(4) Any contractual restrictions, prohibitions, or limitations on the purchaser's conduct.

(5) The rights and obligations of the seller and purchaser regarding termination of the contract.

(6) A statement concerning how the seller may initiate legal proceedings.

(7) A list of states in which the disclosure document is registered, filed, or denied, suspended or revoked.

(8) A list of risk factors that the purchaser should be cognizant of prior to purchase.

iii) **Audited Financial Statements**. Ten states require the purchaser to provide audited financial statements as part of their disclosure document.[60] As audits can be expensive and time-consuming, this can be a particularly onerous requirement for small sellers.

C. Registering Business Opportunities.

Most business opportunity laws require the seller to register with the state prior to beginning to sell opportunities in the state. The registration fees range from $15 to $500, with annual renewal fees ranging from $10 to $500, as outlined in Appendix D. Georgia, Iowa, Louisiana, Ohio, and Virginia do not require a disclosure document to be filed. Many states also require additional filings in addition to filing a disclosure document or a notice regarding the offering. These additional filings include:

i) **Registration of Sales Personnel**. Fourteen states require sellers to provide a complete listing of sales personnel, including names and addresses, who will be offering the business opportunity to prospective purchaser located in the state.[61] Some states

59 For an example of a statute requiring comprehensive disclosures, see the South Carolina Business Opportunity Sales Act, S.C. Code Ann. § 39-57-30 (2013).

60 These states include: Alaska, Connecticut, Illinois, Iowa, Kentucky, Maryland, Minnesota, New Hampshire, Oklahoma, and South Dakota.

61 These states include: Alaska, Arizona, California, Connecticut, Florida, Illinois, Iowa, Kentucky, Maryland, Nebraska, North Carolina, Oklahoma, South Dakota, and Texas.

require this list to be included in the disclosure documents provided to purchasers, while others require the list to be filed with the state. Some such as Connecticut and Florida require salespeople to file individually with the state. While some states require the listing to be updated annually, some states require the list to be updated every six months.

ii) **Advertising Filing**. Six states require all advertisements directed towards prospective purchasers in the state to be filed with the state.[62] Florida, Indiana, Kentucky, and South Carolina require the seller to include the state registration number on all advertisements, but do not require the advertisements to be filed. California, Louisiana, and Nebraska require advertisements to include the name and address of the seller, although Louisiana and Nebraska do not require the advertisements to be filed.

iii) **Registered Agents**. California, Michigan, and South Carolina require sellers to name a person or entity located in the state as an agent to receive service of process. In other states, it is acceptable to use the Secretary of State or other government officials as agents.

iv) **Additional Required Information**. Some states require the seller to file additional information concerning the offering, beyond what is required to be disclosed in the disclosure document. For example, some require the seller to file a statement of oral, written, or visual representations that will be made to prospective purchasers about specific levels of potential sales, income, profits, or any other financial representations. Others require sellers to provide information regarding voluntary terminations by purchasers. Because the information required varies and is often too specific to summarize in this paper, it is important to check what exactly must be filed, once it is determined that you must register in a given state.

D. Bonds and Escrow Requirements.

i) **Surety Bonds and Trust Accounts.** In order to protect purchasers, most states require the seller to post a surety bond, open a trust or escrow account, or obtain a letter of credit under certain circumstances, as described in Appendix E. Eight states require all sellers to post a bond or establish an escrow account.[63] Maine requires a bond, unless the seller has an office in the state. New Hampshire's Attorney General has the right to impose a bond or escrow requirement.

Eleven states require a bond or account if the seller guarantees that the purchaser will derive income or promises to refund the purchaser's investment or to buy back the purchaser's inventory.[64] However, in Illinois and South Dakota, a bond is only required if the seller has a net worth of less than $25,000 and would like to make any of those representations. Oklahoma does not require a bond, but prohibits sellers from representing that they will guarantee that a purchaser will derive income from their purchase or that the seller will refund the purchase price or buy back inventory, unless the seller has a net worth in excess of $50,000.

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[62] These states include: Alaska, California, Minnesota, Oklahoma, Utah, and Washington.

[63] These states include: Alaska, Arizona, California, Indiana, Kentucky, Louisiana, Nebraska, and Virginia.

[64] These states include: Connecticut, Florida, Georgia, Illinois, Maryland, North Carolina, Ohio, South Carolina, South Dakota, Texas, and Washington.

The minimum bond to be posted ranges from $10,000 to $100,000, as described in Appendix E. California, Indiana, Kentucky, and Ohio set the bond amount based on the initial payments collected in the past year. While most states do not set a maximum bond amount, California and Nebraska cap the amount of the bond required at $300,000.

ii) **Escrow Accounts for Initial Payments.** Some states protect purchasers by requiring sellers to establish escrow accounts for initial fees, which are also detailed in Appendix E. Specifically, Alaska, California, Georgia, Illinois, Indiana, Kentucky, Nebraska, and Ohio require the seller to collect a deposit of only 15-20% of the total initial payments from the purchaser, with the remainder being placed in an escrow account in the state. The statutes provide various mechanisms for the seller to obtain the remainder of the funds once the seller has fulfilled its obligations to the purchaser.

E. Selling Business Opportunities.

Once a business opportunity disclosure document and the offering are properly registered, business opportunity statutes also regulate certain aspects of the sales process.

i) **Timing of Disclosures**. State business opportunity statutes require sellers to provide disclosures anywhere from 2 to 14 days prior to collecting any monies or executing any agreements, as described in Appendix D. For states with a shorter period than the 10 business days required under the Federal Rule, if the Federal Rule is applicable, it supersedes the shorter period mandated by the state.[65]

ii) **Prohibited Representations**. Many statutes prohibit sellers from representing that the business opportunity will provide income or earnings, unless data to substantiate the claim is provided to the purchaser prior to the sale.[66] Sellers are also prohibited from making any statements that are inconsistent with the contents of their disclosure document, making any untrue statements of material fact or omitting facts in a misleading manner, or using any device or scheme to defraud.

Many statutes also prohibit sellers from using the trademark, service mark, trade name, logotype, advertising, or other commercial symbol of a business unless, the business controls the ownership interest in the seller; the business accepts responsibility for each representation that the seller makes about the business opportunity; or it is clear from the circumstances that the owner of the commercial symbol is not involved in the sale of the business opportunity.[67]

F. Rescission Rights.

In addition to protecting purchasers through disclosure and registration requirements, business opportunity laws also provide the purchaser with strong rescission rights, which are summarized in Appendix F. Ten states include a right allowing the seller to cancel the purchase for a given period of time after the sale is complete, ranging from 3 business days to 30 days.[68]

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[65] 16 C.F.R. 437.9(b).

[66] As mentioned before, Oklahoma prohibits a seller from guaranteeing income, buy-backs of inventory, or refunds of investments unless the seller has a net worth in excess of $50,000.

[67] See, e.g., Maryland, Md. Code. Ann., Business Regulation §14-123 (2013).

[68] These states include: Alaska, Arizona, California, Indiana, Iowa, Kentucky, Maine, Nebraska, Ohio, and Washington.

Most states also provide the purchaser with a right to rescind the contract if the seller does not deliver any products purchased within 45 days (in some states, the limit is 30 days) from a date specified in the contract.[69]

If the seller makes any misrepresentations in the sales process or fails to comply with the business opportunity statute, in eighteen states, the right of rescission extends even longer.[70] Many of these states allow the purchaser to rescind due to a representation for up to a year after the purchase (Ohio and Oklahoma afford two years and South Dakota affords three years). In Iowa and New Hampshire, the right of rescission is triggered when the purchaser learns of the misrepresentation and extends one year after the discovery in Iowa and 90 days after the discovery in New Hampshire. In Alaska, no time limit is specified.

If the seller fails to register a business opportunity with the state, Arizona and Kentucky allow the seller to rescind at any time. In a number of states, the statute does not address the right of rescission after a misrepresentation, leaving open the question of what rescission rights a purchaser may have, if any.[71]

Courts may also interpret these rescission rights expansively to provide adequate protection to the buyer. In one case in Ohio, a purchaser sought to cancel its business opportunity contract more than five years after the sale was made, because the seller never made the required disclosures.[72] The seller argued that the claim was barred by Ohio's five-year statute of limitations. The court disagreed, concluding that because the seller did not make required disclosures to the purchaser and never complied with the business opportunity statute, the violation was a continuing one, tolling the statute of limitations. As a result, the purchaser could rescind its franchise agreement, because the seller never disclosed to the seller that the seller was entitled to a five-day rescission period. The Court stated that reading the statute of limitations to commence to run on the date the parties entered into their agreement where the franchisor never made the required disclosures "would allow a franchisor to completely disregard all of the state's disclosure requirements and argue … that the franchisee did not timely pursue its remedies even though it didn't have notice of those remedies because the franchisor did not comply with its duty to so inform the franchisee under the Act."[73]

In its 2012 amendment, the Ohio legislature modified these provisions of the law, establishing (i) a one-year statute of limitations on the cancellation right, even if the five-day notice of cancellation is not given, (ii) a three-year statute of limitations on claims for rescission, and (iii) a five-year statute of limitations on damage claims. However, the case remains a good warning that even in states with specified rescission periods, if the seller never makes the required disclosures; it is possible that the statute of limitations may be tolled and the right to rescind may continue to be available to purchasers.

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[69] These states include: Alaska, California, Connecticut, Florida, Georgia, Indiana, Kentucky, Maryland, Nebraska, North Carolina, South Carolina, Texas, and Virginia.

[70] These states include: Alaska, Arizona, California, Connecticut, Florida, Georgia, Illinois, Indiana, Iowa, Kentucky, Maryland, Nebraska, New Hampshire, Ohio, Oklahoma, South Carolina, South Dakota, and Virginia.

[71] These states include: Illinois, Louisiana, Maine, Michigan, Minnesota, Texas, Utah, and Washington.

[72] *Ry/Eh Inc. v. Arthur Treachers, Inc.,* 115 Ohio App.3d 332, 335 (Ohio Ct. App. 1996).

[73] *Id.* at 319.

In Nebraska, the statute softens the potential impact of these rescission rights, by giving the seller the opportunity to cure any inadvertent failures to make required disclosures or to include required provisions in contracts.[74] The seller may cure these failures by providing the purchaser with corrected documents and providing fifteen days to cancel the contract and receive a refund of their investment. If the purchaser does not exercise its cancellation right during such period, the seller cannot later attempt to use its cancellation rights.

G. <u>Remedies for Failing to Comply with Statutes.</u>

Though it can be an expensive exercise to come into compliance with state business opportunity laws, the statutes provide ample reasons to make this investment of time and money worthwhile. Most business opportunity statutes provide both civil and criminal remedies for non-compliance, providing a broad array of tools for states and purchasers to use to combat those who fail to comply or make misrepresentations during the sales process.

Most of the statutes provide the state with civil enforcement powers, except Georgia, Louisiana, Maryland, New Hampshire, North Carolina, South Carolina, and Virginia. These enforcement actions typically involve cease and desist orders or consent orders related to registration and disclosure violations. Monetary penalties are often included too.[75]

Most states also provide for criminal penalties for non-compliance, except Michigan, New Hampshire, Texas, and Utah. While criminal complaints are possible, they are relatively rare, resulting in few reported decisions. However, violations may be misdemeanors or felonies, depending on the state. Many criminal statutes also include monetary penalties of up to $10,000 per violation.

Unlike the Federal Rule, all states provide buyers with a private remedy for violations of the business opportunity laws. These remedies include the right for the prevailing party to receive its attorneys' fees and, in some cases, treble or punitive damages. In states which require bonds, purchasers may be able to recover up to the amount included in the bond. As discussed above, these laws also provide rescission rights to purchasers.

V. CONCLUSION

Given the variances in the federal and state business opportunity statutes, it is not surprising that sellers often prefer to develop strategies to avoid the scope of these statutes, even resorting to restructuring their offerings to avoid triggering the statutes. In many instances, however, there is no other option but to prepare the required disclosures and to make the required filings. Moreover, in our experience, the time and effort that businesses take to attempt to avoid the applicability of these statutes often exceeds the time and effort that it would take to comply with the statutes.

Once a practitioner becomes familiar with these statutes, the path to compliance can be quite manageable. The simplified disclosures required under the Federal Rule, while expanding the scope of the statute, made it much easier for businesses to efficiently comply with the Federal Rule. Though the state statutes continue to be diverse, comprehensive disclosures can be drafted that satisfy nearly all of the disclosure requirements of these statutes. While other

74 Neb. Rev. Stat. § 59-1753 (2013).

75 For example, South Carolina includes a $200 per day penalty for seller's who fail to register.

state-specific requirements, such as bonding or escrow requirements, may need to be satisfied, once a compliance program is implemented, it can be relatively easy to maintain.

VI. APPENDICES

Appendix A: List of Business Opportunity Statutes

State	Title of Law	Code Reference
Alaska	Sale of Business Opportunities	Alaska Stat. §§ 45.66.010 through 45.66.900
Arizona	Business Opportunity Sales	Ariz. Rev. Stat. Sec. 44-1271 - 44-1280
California	Seller Assisted Marketing Plans	Cal. Civ. Code §§ 1812.200 through 1812.221
Connecticut	Business Opportunity Investment Act	Conn. Gen. Stat. §§ 36b-60 through 36b-80
Florida	Sale of Business Opportunities Act	Fla. Stat. §§ 559.80 through 559.815
Georgia	Business Opportunity Sales Law	Ga. Code Ann. §§ 10-1-410 through 10-1-417
Illinois	Business Opportunity Sales Law of 1995	Ill Comp. Stat. Ch. 815, §§ 602/5-1 through 602/5-135
Indiana	Business Opportunity Transactions Law	Ind. Code §§ 24-5-8-1 through 24-5-8-21
Iowa	Business Opportunity Promotions Law	Iowa Code §§ 523B.1 through 523B.13
Kentucky	Sale of Business Opportunities Law	Ky. Rev. Stat. Ann. §§ 367.801 through 367.819 and 367.990
Louisiana	Business Opportunity Sellers and Agents Law	La. Rev. Stat. Ann. §§ 51:1821 through 51:1824
Maine	Sale of Business Opportunities Law	Me. Rev. Stat. Ann. Tit. 32, §§ Sections 4691 through 4700-B
Maryland	Business Opportunity Sales Act	Md. Code Ann., Bus. Reg. §§ 14-101 through 14-129
Michigan	Michigan Consumer Protection Act	Mich. Comp. Laws §§ 445.902 and 445.903b
Minnesota	Minnesota Franchises Act	Minn. Stat. §§ 80C.01 through 80C.22
Nebraska	Seller-Assisted Marketing Plan Act	Neb. Rev. Stat. §§ 59-1701 through 59-1762
New Hampshire	Distributorship Disclosure Act	N.H. Rev. Stat. Ann. §§ 358-E 1 through 6
North Carolina	Business Opportunity Sales Law	N.C. Gen. Stat. §§ 66-94 through 66-100
Ohio	Business Opportunity Purchasers Protection Act	Ohio Rev. Code Ann. §§ 1334.01 through 1334.15 and 1334.99
Oklahoma	Business Opportunity Sales Act	Okla Stat. tit. 71, §§ 801 through 829
South Carolina	Business Opportunity Sales Act	S.C. Code Ann. §§ 39-57-10 through 39-57-80
South Dakota	Business Opportunities	S.D. Codified Laws §§ 37-25A-1 through 37-25A-54
Texas	Business Opportunity Act	Tex. Bus. & Com. Code §§ 41.001 through 41.303
Utah	Business Opportunity Disclosure Act	Utah Code Ann. §§ 13-15-1 through 13-15-6
Virginia	Business Opportunity Sales Act	VA. Code §§ 59.1-262 through 59.1-269
Washington	Business Opportunity Fraud Act	Wash. Rev. Code §§ 19.110.010 through 19.110.930

Appendix B: Business Opportunity Statute Triggers

State	Seller Will Provide Locations for Business	Seller Will Provide Outlets for Accounts	Seller Will Buy Back Products	Seller Will Guarantee Income	Seller Will Refund Purchase Price	Seller Will Provide Marketing Plan	Seller Guarantees Market for Products
Alaska	X	X	X	X	X	X	
Arizona	X		X	X		X	X
California			X	X			X
Connecticut	X		X	X	X	X	
Florida	X		X	X	X	X	
Georgia	X		X			X	
Illinois	X	X	X	X	X	X	
Indiana			X	X			X
Iowa	X	X	X	X	X	X	
Kentucky	X	X	X	X			X
Louisiana	X		X	X	X	X	
Maine	X		X	X	X	X	
Maryland	X	X	X	X	X	X	
Michigan	X		X	X	X	X	
Minnesota	X		X	X		X	
Nebraska	X	X	X	X	X		X
New Hampshire	X						
North Carolina	X		X	X	X	X	
Ohio	X	X	X	X			X
Oklahoma	X	X	X	X	X	X	
South Carolina	X		X	X	X	X	
South Dakota	X	X	X	X	X	X	
Texas	X		X	X		X	
Utah	X		X	X		X	
Virginia	X		X	X	X	X	
Washington	X		X	X		X	

Appendix C: Exemptions and Exclusions

State	Minimum Investment to be a Business Opportunity	Maximum Investment to be a Business Opportunity	Are Franchises Excluded?	Are Marketing Programs with Trademarks Excluded?	Are Large Sellers Exempt?	Are Large Purchasers Exempt?	Is there an Exemption for General Merchandisers?
Alaska	$250	None	Yes	Excluded from entire statute if federal mark & $1 million net worth	Yes, if seller has a registered mark & $1 million net worth	No	No
Arizona	$500	None	Yes	Federal mark excluded from program definition	Yes, if seller has a registered mark & $1 million net worth	No	No
California	$500	$50,000	Yes	No	Yes, if seller has $10 million net worth (only for certain product distributors)	No	Yes
Connecticut	$200	None	No	Federal mark excluded from program definition	No	Yes, if the purchaser has $1 million net worth	No
Florida	$500	None	Yes, if file notice and $100	Registered mark excluded from program definition	No	No	No
Georgia	$500	None	No	Registered mark excluded from program definition	Yes, if seller has $15 million net worth & is publicly traded	No	No
Illinois	$500	$25,000 (if less than 20% of buyer's net worth)	Yes	Federal mark excluded from program definition	Yes, if seller has $1 million net worth	Yes, if the purchaser has $250,000 net worth	No
Indiana	$500	$50,000	Yes	No	Yes, if seller has $5 million net worth (or $1 million if guaranteed by affiliate with $5 million)	No	No
Iowa	$500	None	Yes	Excluded from entire statute if federal mark & $1 million net worth	Yes, if seller has a federal mark & $1 million net worth	No	No
Kentucky	$500	None	Yes, if file notice	No	No	No	No
Louisiana	$300	None	No	Registered mark excluded from program definition	No	No	No
Maine	$250	None	No	Federal mark excluded from program definition	No	No	No

State	Minimum Investment to be a Business Opportunity	Maximum Investment to be a Business Opportunity	Are Franchises Excluded?	Are Marketing Programs with Trademarks Excluded?	Are Large Sellers Exempt?	Are Large Purchasers Exempt?	Is there an Exemption for General Merchandisers?
Maryland	$300	None	Yes	Excluded from entire statute if federal mark & $1 million net worth	Yes, if seller has a federal mark & $1 million net worth	Yes, if the purchaser has $250,000 net worth	No
Michigan	$500	$50,000 (but no limit if guarantee income)	Yes	Federal mark excluded from program definition	No	No	No
Minnesota	$100	None	No	No	No	No	No
Nebraska	$500	None	Yes, if file notice, ads, and $100	No	No	No	Yes
New Hampshire	None	None	No	No	No	No	No
North Carolina	$200	None	No	Federal mark excluded from program definition	Yes, if seller has $5 million net worth & files notice	No	No
Ohio	$500	$100,000	Yes, unless guarantee buy-back	No	Yes, if seller has $15 million net worth & has 25 purchasers operating or has been operating for 5 years	No	Yes
Oklahoma	$500	$25,000 (if less than 20% of buyer's net worth)	Yes	Excluded from entire statute if federal mark & $1 million net worth	Yes, if seller has $1 million net worth	Yes, if the purchaser has $250,000 net worth	No
South Carolina	$250	None	No	Registered mark excluded from program definition	Yes, if seller has $10 million net worth	No	No
South Dakota	$250	$25,000 (if less than 20% of buyer's net worth)	Yes	Excluded from entire statute if federal mark & $1 million net worth	Yes, if seller has a federal mark & $1 million net worth	No	No
Texas	$500	None	Yes, if file notice and $25	No	Yes, if seller has $25 million net worth	No	Yes
Utah	$500	None	Yes, if file notice	No	No	No	No
Virginia	$500	None	Yes	No	No	No	Yes
Washington	$300	None	Yes	Excluded from entire statute if federal mark & no consideration for mark	No	No	No

Appendix D: Registration and Disclosure Requirements

State	Is Disclosure Required?	Is Registration Required?	How long must disclosures be provided before money is received or contracts are executed?	Registration Fee	Renewal Fee	Amendment Fee	Are Audited Financial Statements Required?	Must a List of Sales People be Filed?	Must Advertising Be Filed or Include Specific Information?
Alaska	Yes	Yes, 30 days before sales begin	10 days	$300	$150	N/A	Yes	Yes	Yes
Arizona	Yes	Yes	5 business days	$500	$500	$25	No	Yes	No
California	Yes	Yes, 30 days before sales begin	48 hours	$100	$100	$30	No	Yes	Yes, and ad must include seller name & address
Connecticut	Yes	Yes	10 business days	$400	$100	N/A	Yes	Yes	No
Florida	Yes	Yes	3 business days	$300	$300	$50	No	Yes	No, but ads must list ad id number
Georgia	Yes	No	48 hours	N/A	N/A	N/A	No	No	No
Illinois	Yes	Yes, 10 days to take effect	14 days	$300	$300	$25	Yes	Yes	No
Indiana	Yes	Yes	72 hours	$50	$10	$10	No	No	No, but ads must include registration #
Iowa	Yes	No	10 business days	N/A	N/A	N/A	Yes	Yes	No
Kentucky	Yes	Yes	Not specified	$150	$50	$25	Yes	Yes	No, but ads must include registration #
Louisiana	Earnings claims only	No	N/A	N/A	N/A	N/A	No	No	No, but ads must list seller name & address

State	Is Disclosure Required?	Is Registration Required?	How long must disclosures be provided before money is received or contracts are executed?	Registration Fee	Renewal Fee	Amendment Fee	Are Audited Financial Statements Required?	Must a List of Sales People be Filed?	Must Advertising Be Filed or Include Specific Information?
Maine	Yes	Yes	72 hours or 1st meeting	$25	$10	N/A	No	No	No
Maryland	Yes	Yes, 10 days to take effect	10 business days	$250	$100	$50	Yes	Yes	No
Michigan	No	Yes	N/A	N/A	N/A	N/A	No	No	No
Minnesota	Yes	Yes	7 days	$400	$200	$100	Yes	No	Yes
Nebraska	Yes	Yes	48 hours or 1st meeting	$100	$50	$50	No	Yes	No, but ads must list seller name & address
New Hampshire	Yes	Yes	7 days	$50	N/A	N/A	Yes	No	No
North Carolina	Yes	Yes	48 hours	$250	N/A	N/A	No	Yes	No
Ohio	Yes	No	10 business days	N/A	N/A	N/A	No	No	No
Oklahoma	Yes	Yes, 15 days to take effect	10 business days	$250	$150	N/A	Yes	Yes	Yes
South Carolina	Yes	Yes	48 hours	$100	N/A	N/A	No	No	No, but ads must include registration #
South Dakota	Yes	Yes, 10 days to take effect	10 business days	$100	$50	N/A	Yes	Yes	No
Texas	Yes	Yes	10 business days	$195	$25	$25	No	Yes	No
Utah	Yes	Yes	10 business days	$200	$200	N/A	No	No	Yes
Virginia	Yes	No	48 hours	N/A	N/A	N/A	No	No	No
Washington	Yes	Yes	48 hours	$200	$125	$30	No	Yes	Yes

Appendix E: Bond and Escrow Requirements

State	When is a Surety Bond or Escrow Account Required?	What are the Minimum/Maximum Surety Bond Amounts?	Are There Escrow Requirements for the Initial Payment?
Alaska	Always bond	$75,000/No Maximum	80% of initial payment
Arizona	Always bond or escrow	$100,000 bond required	No
California	Always bond or escrow	$50,000/$300,000 or total amount of initial payments in past year	80% of initial payment
Connecticut	Bond or escrow if guarantee income, refund, or buy-back	$50,000/No Maximum	No
Florida	Bond, certificate of deposit, or letter of credit if guarantee income, refund, or buy-back	$50,000/No Maximum	No
Georgia	Bond or escrow if guarantee refund or buy-back	$75,000/No Maximum	85% of initial payment
Illinois	Bond if guarantee income, refund, or buy-back & if the seller has a net worth of less than $25,000	$25,000/No Maximum	80% of initial payment
Indiana	Always bond or letter of credit	$75,000 or 20 times the initial payment	80% of initial payment
Iowa	Not required	N/A	No
Kentucky	Always bond or certificate of deposit	$75,000 or total amount of initial payments in state in previous year	80% of initial payment
Louisiana	Always bond	$50,000 and $25,000 for each sales person	No
Maine	Always bond or escrow, unless the seller has an office in the state	$30,000/No Maximum	No
Maryland	Bond or escrow if guarantee income or refund	$50,000/No Maximum	No
Michigan	Not required	N/A	No
Minnesota	Not required	N/A	No
Nebraska	Always bond or escrow	$50,000/$300,000	80% of initial payment
New Hampshire	Attorney general may require bond or escrow	No amount specified	No
North Carolina	Bond or trust account if guarantee income or refund	$50,000/No Maximum	No
Ohio	Bond or trust account if guarantee secured or buy-back	Starts at $50,000 but may be adjusted to as low as $10,000	80% of initial payment
Oklahoma	No bond, but seller must have a net worth of $50,000 to guarantee income, refund, or buy-back	N/A	No
South Carolina	Bond or trust account if guarantee income or refund	$50,000/No Maximum	No
South Dakota	Bond if guarantee income, refund, or buy-back & seller net worth less than $25,000	$25,000/No Maximum	No
Texas	Bond, trust account, or letter of credit if represent will earn profit	$25 000/No Maximum	No
Utah	Not required	N/A	No
Virginia	Always bond or escrow	$50,000/No Maximum	No
Washington	Bond or trust account if guarantee income	$50,000/No Maximum	No

Appendix F: Purchaser's Rescission Rights

State	How Long May the Purchaser Cancel A Contract After a Sale?	How Long Does the Purchaser Have to Rescind a Contract After a Misrepresentation?	How Long Does the Seller Have to Deliver Products Before the Purchaser Has the Right to Rescind?
Alaska	30 days	Anytime	30 days
Arizona	10 days	Anytime if unregistered	N/A
California	3 business days	1 Year if unregistered	30 days
Connecticut	N/A	1 Year	45 days
Florida	N/A	1 Year	45 days
Georgia	N/A	1 Year	45 days
Illinois	N/A	N/A	N/A
Indiana	30 days	1 Year	45 days
Iowa	3 business days	1 year after discovery	N/A
Kentucky	30 days	Anytime if unregistered, 1 year if misrepresentation	30 days
Louisiana	N/A	N/A	N/A
Maine	3 business days	N/A	N/A
Maryland	N/A	1 year	45 days
Michigan	N/A	N/A	N/A
Minnesota	N/A	N/A	N/A
Nebraska	3 business days	1 Year	30 days
New Hampshire	N/A	90 days after knowledge	N/A
North Carolina	N/A	1 Year	45 days
Ohio	5 business days	2 years	N/A
Oklahoma	N/A	2 years	N/A
South Carolina	N/A	1 Year	45 days
South Dakota	N/A	3 years	N/A
Texas	N/A	N/A	45 days
Utah	N/A	N/A	N/A
Virginia	N/A	1 Year	45 days
Washington	7 business days	N/A	N/A

Appendix G: Required Disclosure Provisions

State	State Cover Page	Seller Contact Information	System History	Management Bios	Seller Rep Bios	Litigation	Bankruptcy	Description of Program	Seller's Services	Training	Trademarks	Initial Fees	Ongoing Fees	Initial Investment	Earnings Claims	Refund Requirement	Terminations	Financial Statements	List of Buyers
Alaska	X	X	X	X	X	X	X	X	X	X		X		X	X	X	X	X	X
Arizona	X	X						X	X			X	X						
California	X	X	X	X		X	X		X	X		X			X	X		X	
Connecticut	X	X		X	X	X	X	X	X	X	X	X	X		X	X	X	X	X
Florida	X	X	X	X		X	X		X	X					X			X	X
Georgia	X	X	X	X					X	X					X			X	
Illinois	X	X	X	X	X	X	X		X	X		X			X	X	X	X	X
Indiana	X	X	X	X	X	X	X		X	X		X			X	X		X	X
Iowa	X	X	X	X	X	X	X		X	X		X			X	X	X	X	X
Kentucky	N[1]		X	X	X	X	X		X	X	X					X		X	X
Louisiana	No disclosure required																		
Maine	X	X							X		X	X	X	X	X		X		X
Maryland	X	X	X	X	X	X	X		X	X					X	X		X	X
Michigan	No disclosure required																		
Minnesota	X	X	X	X		X	X	X	X	X	X	X	X	X	X		X	X	X
Nebraska	X	X	X	X		X			X	X		X			X		X	X	X
New Hampshire	X		X	X		X	X	X	X	X		X	X		X		X	X	X
North Carolina	X	X	X	X		X	X		X	X					X			X	
Ohio	X	X	X	X		X	X	X	X	X	X	X				X	X	X	X
Oklahoma	X	X	X	X	X	X	X		X	X		X			X		X	X	
South Carolina	X	X	X	X	X				X	X					X			X	
South Dakota	X	X	X	X		X	X		X	X		X			X	X	X	X	X
Texas	X	X	X	X		X	X		X	X					X			X	
Utah	X	X		X		X			X	X	X	X		X	X			X	X
Virginia	X	X	X	X					X	X					X			X	
Washington	X	X	X	X		X	X					X	X		X			X	X

(1) N = Separate notice required.

BEATA KRAKUS

Beata Krakus is an officer in the Chicago office of Greensfelder, Hemker & Gale, P.C., and part of the firm's Franchising & Distribution Practice Group. She works with franchisor clients in domestic and international franchise transactional matters, as well as related areas such as distribution and sales representative arrangements, and other commercial contracts. She has advised, structured, and prepared franchise programs for many different franchise concepts including real estate brokerages, hotels, restaurants, and fitness and personal health systems.

Prior to joining Greensfelder, Ms. Krakus was associated with Sonnenschein Nath & Rosenthal LLP. She also practiced in Warsaw, Poland with the Swedish law firm of Magnusson Wahlin.

Ms. Krakus is a member of the Women's Caucus Steering Committee, has served as an Associate Editor for *The Franchise Lawyer*, has herself written articles for the *Franchise Law Journal*, and other franchise law publications, and has spoken at the ABA Forum on Franchising and International Franchise Association Legal Symposium. She is recognized by International's Who's Who of Franchise Lawyers and by Chambers USA (Franchising, Up and Coming).

ALEXANDER TUNESKI

Alexander Tuneski is a Counsel in the Washington, DC office of Kilpatrick Townsend & Stockton LLP. Mr. Tuneski concentrates his practice on representing franchisors and licensors domestically and internationally in a broad range of transactional and regulatory matters. Mr. Tuneski's clients include franchisors and distributors of all sizes, from start-ups to mature, publicly-traded companies, in a wide variety of industries.

Mr. Tuneski assists clients in the development and maintenance of domestic and international franchise sales programs, including drafting Franchise Disclosure Documents, franchise agreements, development agreements, area representative agreements, master license agreements, and distribution agreements and advising clients on compliance with federal and state franchise and business opportunity statutes. Mr. Tuneski has extensive experience negotiating the sale and renewal of franchise, master license, development, and area representative rights.

In established franchise systems, Mr. Tuneski works with franchisors to help develop and enforce system standards, build and nurture relationships with franchisees and franchisee associations, and resolve disputes and other relationship issues that arise. Mr. Tuneski also advises entities seeking to purchase or sell franchise systems, guiding them throughout the sales process.

Mr. Tuneski has written articles for the *Franchise Law Journal* and other franchise law publications and has spoken at the International Franchise Association Legal Symposium. He is also an active member of the ABA Forum on Franchising Young Lawyer's Committee. In 2012, Mr. Tuneski received the Young Leadership Award from the ABA Forum on Franchising. In 2013, Mr. Tuneski was recognized as a Washington, D.C. "Rising Star" in the area of Franchise/Dealership Law by *Super Lawyers* magazine.