

FDD and Franchise Agreement Summary Review

McDonald's FDD Review

We have reviewed the Franchise Agreement (the "FA") and the Franchise Disclosure Document ("FDD") that you provided. We have not reviewed any other documents. We are pleased to give you the following comments and advice with regard to these documents.

Generally, franchise agreements are one sided and you need to be aware of the rights and remedies that the franchisor has under the agreements that you will sign. With certain important exceptions, we did not find the arrangement to have particularly onerous terms. With those same important exceptions in mind we would say that the arrangement is fairly typical, and it is largely fair to the franchisee in comparison to franchise industry norms. We will point out some of the greatest limitations and most important dangers for a franchisee below.

This summary of some of the high points of this franchise agreement is not a substitute for studying and understanding the entire agreement. Just because we do not mention a term or condition below does not mean it is not important. If you have questions about issues that we do not review below, please discuss them with us.

Be sure to also check our <u>FDD Review Mastery Companion Course</u>. This course has additional comments and details about why we point out these points of interest to you in the Summary Review Letter. These videos are available on-demand and you can hop to whichever topics you have questions about. It should help you understand these deeper even before our conference call together. The Companion Course video number will be noted by a [CC: X] at the end of any applicable comment, with the number of the video replacing the X. If you are logged into Reidel Law Firm Academy already, the link will take you directly to the correct video.

This summary review is not intended to be delivered to or shown to the franchisor or its employees or agents such as a broker. There is tactical advice concerning negotiation with the franchisor in this summary and showing it to the franchisor would compromise your position in these negotiations. Also, should you ever get into a dispute with the franchisor, this detailed evidence of what counsel you received could be used against you. As long as you do not voluntarily discuss the contents of this letter, you could assert attorney/client privilege to protect it in future litigation.

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B U S I N E S S L A W

Торіс	Summary	Our Recommendation
💰 Fees & Costs	Initial franchise fee: \$45,000.00 . Ongoing royalties: []% (see FDD Item 6, Footnote 2). Brand fund or marketing fee: 4% of Gross Sales .	These fees are within the typical ranges for franchises these days You may consider negotiating the initial fees though franchisors generally do not negotiate these unless it is a multi-unit deal of you are bringing significant experience the system.
† Territory Rights	Your protected territory is based on [describe area here]. You are not permitted to operate outside of your protected territory.	You should be 100% confident the size and fit of your territory to the franchise business. If you have questions or concerns abo the territory, these should be made known to the franchisor. Generally, modifying the territory to the best fit is one of the easier revision requests.
1 Liquidated Damages	The agreement does require liquidated damages as part of any termination or exit from the system. The amount of liquidated damages will be ~.	You should request a limited exception from liquidated damages in the event of a closu of your franchise unit due to financial issues or the unit bein commercially non-viable.
🙀 Personal Guaranty	The agreement does require a personal guaranty , meaning your personal assets may be at risk if the business fails. These are extremely difficult to revise. Though limiting liquidated damages can be a significant risk reduction on the amount relevant to any personal guaranty.	While these are very unlikely to be revised by the franchisor, some potential requests include a monetary or time cap on yo personal liability.

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FDD Notes:

Item 1: This is a well established franchise system. This is a great sign in that the franchise is likely developed internally and proven in many markets. The downside to a more established franchise system is that the franchisor is typically less likely to consider many revisions to the FA. One note I would also add about this system is that it is owned by a larger private equity group. This is not necessarily a bad thing in itself but PE ownership of franchisors is very controversial lately in the industry due to the tendency of PE owners to monetize every interaction with franchisees and sometimes unsustainable debts. I cannot say that is the case here but it is important to recognize that some PE owners vision may not align long term with your vision as a franchise (most PE groups look to exit in less than 10 years which is shorter than the typical franchise agreement term. Note that the restaurant industry has unique challenges including: difficulty finding and retaining good employees and being highly competitive. You should think deeply about how these may be unique to your specific market and what potential plans you may have for addressing these. The franchisor and their system may help to some extent but you will be solely responsible for how your unit performs.

Item 5: The initial franchise fee is \$45,000.00. This is within the typical range for franchises these days.

Item 6: The royalty fees are []% (see FDD Item 6, Footnote 2). This is typical in the franchise industry. The advertising contribution fee is 4% of Gross Sales and your renewal fee is ~. These are also usual. Other various fees of the franchise system include: []. I cannot say that these are too high or not based on the FDD but as long as you understand and agree with the value that you receive for these fees, then I do not have any objections.

Item 8:

Item 11:

Item 12: *F* **Recommendation:** Discuss with the franchisor your specific territory limitations and **any concerns or questions you have about the size and business viability** based on trends, target demographics, etc.

Item 19: The financial performance representations have some good information here but as usual be sure to compare it against your own projections and market.

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Item 20: [small, big system comments, terminations] *F* **Recommendation:** You should **speak with as many current franchisees** as you can. Also, if you can talk to **franchisees who have left the system**, this is a great source of information. If you try to speak to franchisees who have left the system and you are told that they are under a confidentiality agreement, that is a bad sign.

Item 21:

📋 FA Notes:

I. The following are issues that we believe require negotiation with the franchisor or some other immediate action on your part:

1. You are required to secure a site within ~ of the date of this agreement. FA Section ~. You will breach this agreement if you don't have a lease by that time. Do you feel that that is enough time? In this market, it very well may be. **FRecommendation:** It might make sense, however, to try to **negotiate a longer period** just in case. [CC: 1]

2. You are required in Section 9 of the FA to open your business within 365 days (1 year) of execution of the Franchise Agreement. There is no financing or other contingency built into this time frame. **Fraccommendation:** If you are going to seek financing or have other considerations, you may want to **ask for a revision of this section** or deal with this issue in a side letter to the franchisor explaining the situation and your needs. [CC: 2]

3. Note the minimum performance requirements detailed in Section ~. If you fail to meet these requirements at any time during the term of the Agreement, you will be in default and could be terminated. This represents a major risk factor should this concept not do well at your location or within your proposed market. **The Recommendation:** Typically it makes sense to have a **grace period before any mandatory minimums** kick in, something like 6-9 months would be a reasonable request. We can discuss this further if you have additional concerns. [CC:9]

4. FA Section \sim is very important. This clause requires you to pay liquidated damages in the event that your franchise agreement is terminated because of your default. The amount of liquidated damages will be \sim . This could be a substantial amount. Many franchise agreements provide for a harsh penalty like this in the event of a franchise closing, and it is unlikely that the franchisor will be willing to delete this continuing royalty requirement. Some franchisors use this clause as a way to force a struggling franchisee to stay open even while suffering large continuing losses. Your exposure under this clause would be greatly reduced if you could get the franchisor to change the clause to say that



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these amounts will not be due after termination if your business fails and you close for financial reasons. **Recommendation:** You should **request a limited exception or waiver to liquidated damages** in the event of a closure of your unit or termination of your franchise agreement due to financial issues or the commercially unsustainability of your unit. [CC: 4]

5. Be aware of your minimum royalty fees that you must pay the franchisor in the event that your monthly royalties paid on the percentage basis are below the minimum threshold. See FA Section ~. This means that in any week or month that you are below the threshold, you will be required to pay the franchisor out of your pocket. **Recommendation:** If you don't have any grace period built into this minimum royalty, I would recommend we request that the franchisor **waive the minimum royalty for the first few months of operations** to allow your unit to build a book of business and get your feet under you. You may also want to consider any seasonality this type of business and request any adjustments that should be factored in for seasonal changes in the business revenues. [CC:13]

6. You are required to have employees keep a neat and clean appearance as the franchisor requires. FA Section 12(h). You should discuss this with representatives of the franchise company and with other franchisees. The prevalence of piercings and tattoos among young employees today makes it important that you understand these requirements up front. You don't want to hire staff and then find out that you have employment disputes because you were unaware of the requirements imposed by the franchisor. **Cecheramendation:** Ask the franchisor about **what constitutes a 'neat and clean appearance'** and if employees with tattoos or piercings for example would not be permitted. [CC: 5]

7. Franchisors take the confidentiality obligations that their franchisees agree to quite seriously. Carefully review Franchise Agreement Section 4 and note that you must secure the signature on a confidentiality agreement of every employee and owner who will have access to the operating manual. This is an important requirement. You must not allow a situation to exist where one of your employees can make unlawful disclosures with impunity. All people with access to the manual have to be bound by a confidentiality agreement in favor of the franchisor. This is actually as much for your protection as for the franchisor's. [CC: 6]

8. FA Section 17 describes the insurance coverages that the franchisor requires you to have. You should copy this section and give this to your insurance broker as soon as possible so that he or she can start shopping these insurance requirements and confirm the availability and price of the necessary insurance. Also note that you are required at all times

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to have delivered a valid certificate of each of the coverages to the franchisor. **Freeommendation:** Reach out to insurance brokers for competitive rate quotes. [CC: 7]

9. I strongly urge you to establish the legal entity that will serve as the franchisee before the franchise agreement is signed. There is no reason to assume personal liability for operational risks even temporarily, so you should establish your entity up front. **Fecommendation: Form an entity** (usually an LLC or corporation) to be the actual franchisee and operate the business rather than owning and operating your franchise unit in your individual capacity. [CC: 8]

10. There are certain restrictions on what the remaining owners or the owner's family must do in the event that one of the owners dies or becomes disabled. See FA Section 15(a). In the event of a death or disability, your heirs or estate will be required to transfer the franchise to an approved operator within 12 months. In addition to these requirements, you should consider creating a written agreement among the partners which would, among other things, deal with how interests are handled in the event of a partner's death, disability, bankruptcy, divorce, etc. If you establish a limited liability company, you should have an operating agreement and possibly a buy/sell agreement which would clarify what happens to a partner's interests after one of these eventualities. I would be happy to counsel you about some of the options and to draft the appropriate agreements. Note that the size of this investment may very well justify some key man life insurance to provide liquidity for the business in the event an owner's death or disability. If you have questions about these issues, please don't hesitate to ask me about them. [CC: 10]

Matters Relating to Personal Assets:

11. FA Section 15(a), 15(d) requires the principal owners of the franchisee entity to execute a personal guaranty. This includes anyone who owns any of the equity of the franchisee entity. This may significantly restrict your ability to raise capital from minority investors now or in the future. **The Recommendation:** Whether or not you intend to bring in minority partners, it is probably a good idea to ask that this be changed to **require the personal guaranty only of investors who have a controlling interest** in the franchisee. I suspect that the franchisor may object to this proposal but it is worth the try. [CC: 11]

12. If you were to become ill or disabled and could not continue to operate the franchise, you will still be personally liable for its obligations under the franchise agreement because of the personal guaranty. Should you pass away, your estate may be responsible. Therefore, you may wish to explore options in moving personal funds into a trust, for example, or into retirement funds, or even into offshore holdings, which are usually fairly well protected from creditors' claims. *C* **Recommendation:** Sit down with an estate

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planning attorney to understand the best options and risk reduction strategies for your state. [CC: 12]

13. The requirement of a personal guaranty in your franchise agreement commits your personal assets but does not restrict your ability to manage those assets as you see fit. You may wish to do some asset protection planning. This could take the form of transferring assets to a spouse or a relative, depending on the state of operation. Retirement accounts and life insurance products are also insulated from creditor claims in some ways. Offshore holdings companies or bank accounts are another option which may offer additional protection. You may wish to explore these and other techniques to protect your personal wealth from exposure to personal guaranties to both the franchisor and your landlord, if applicable. Feel free to reach out to me if you would like more information on small business wealth and asset protection.

14. This project probably represents a big change in your personal financial circumstances. If you have worked for a corporation in the past, you may have relied on group health, disability and life insurance benefits to protect your family and your assets. These sorts of "safety net" programs are not automatic for small business owners. You should explore private health insurance, and disability and life insurance with your broker. If you need a referral, I would be happy to put you in touch with someone that can assist you with this.

Real Estate Matters:

15. The franchise agreement runs for ~ and you have ~ ~ renewal (see FA Section 2(b)). \leftarrow **Recommendation:** When you approach landlords, you should insist on a lease that is coterminous with the franchise agreement term and renewals. This should be included in a Request For Proposals that we recommend you use to specify site attributes and lease terms that you require at the time of your initial contact with potential landlords. [CC:15]

16. FA Section 12(k) makes it clear that the franchise is responsible for obtaining zoning and building permits as well as ongoing permits and licenses that may be required by local law to operate your business. You should look into these requirements early on. [CC: 3] [CC: 16]

17. Franchise companies usually tell prospective franchisees that they or their broker or representative will handle the job of locating your site and negotiating your lease. You must recognize that no one will examine sites as rigorously as you or negotiate with the landlord as aggressively as you. The franchisor and the broker have a clear conflict of interest and often do not represent the franchisee's interests very well. Whereas you need the site to be optimal, the franchisor often just wants to get the deal done. The broker has even

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less interest in whether the franchise is successful. Always keep this in mind when making decisions about your site selection and your lease. [CC: 17]

18. FA Section 1(b) requires a real estate site control document. This is a document that you are required to have your landlord agree to so that the franchisor can take over the lease and assign it to a new franchisee if you default under the franchise agreement or under the lease. This sort of site control document is a typical feature of franchise arrangements. You should include this site control arrangement in your Request for Proposals to be given to landlords at your initial contact so that they know this is a requirement. Sometimes landlords will object to these documents, so it is best to find out early whether there is any opposition. [CC: 18]

19. Despite the franchisor's willingness to get deeply involved in the real estate transaction, FA Section 9 makes it clear that you are solely responsible for site selection and that the company does not guarantee the appropriateness of the site. You must learn all you can about good site selection criteria from the franchisor, from existing franchisees and from the company's competitors if possible.

II. The following issues are ones that we have observed which may not require immediate action but are issues that we want you to give special attention to:

Matters Relating to Exit Strategy:

There are several attributes of a franchise investment that impact a franchisee's exit strategy. Understanding the potential obstacles to an effective exit strategy is an important part of planning your long term success. The following issues need to be considered as you think about how you will grow value over the long term and eventually be able to realize that value:

20. Section 15 describes significant restrictions on your right to transfer your business, i.e. to sell an equity interest in your business, to sell assets or to transfer an interest in the franchise agreement. If you have questions about these restrictions, we should discuss them. One important restriction that clients often don't expect is the covenant against creating encumbrances. FA Section ~ says that you may not pledge any voting or ownership interest in the franchise entity or in its assets nor may you pledge any interest in the franchise agreement. Some lenders will assume that such collateral is available. If you will need to pledge any assets to finance your business we should discuss that. These restrictions, though, are typical in the franchise industry. [CC: 20]

21. Important restrictions on your ability to transfer an interest in the business include your obligation as the seller to sign a release in favor of the franchise company. You will also need to be in strict compliance with the franchise agreement to qualify to sell your

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franchise. The franchisor has to approve the transferee, and the transferee must successfully complete initial training. The transferee will have to refurbish the location to qualify for a transfer. See FA Section 15(d). [CC: 21]

22. FA Section 15(c) contains a right of first refusal in favor of the franchisor in the event that the franchisee or one of the partners wishes to sell an interest in the business. This is typical. [CC: 22]

23. FA Section 1(c) raises an issue which many clients find surprising. This subsection says that all of the goodwill that arises out of your operation of your business in your local area becomes the property of the franchisor. This illustrates the sometimes surprising fact that a franchisee does not own the goodwill associated with its own business. The trademark is yours to use only so long as you have a valid franchise agreement – a license to use the trademark and the system. In a sense you are "renting" the goodwill of the franchisor's system and trademark. This is not necessarily a bad thing but it is important to understand. The long term implication for your business is that you must remain in compliance with your franchise agreement and make sure that your potential buyer will be prepared to sign a new franchise term or (less likely) assume the remainder of your franchise term. [CC: 23]

24. In the event of termination, the franchisor has the right to purchase your assets at a depreciated value. This most likely means that the evaluation would be done at "liquidation value" rather than at "going concern value". This is a harsh remedy but the franchisor is unlikely to be willing to negotiate a change. This remedy reflects the reality that a franchisee has little to sell once his franchise agreement expires or is terminated. See FA Section 20(b), 20(c). [CC: 24]

Other Important Matters for You to Understand:

25. Section 2(a) of the FA makes it clear that your license is to operate from only one location. In fact, per Section 28(e) you are not allowed to operate outside of your territory. [CC: 25]

26. Note that FA Section 6 requires that a principal and a designated manager of the business be trained at the franchisor's initial training program. Further, the franchisor reserves the right to require you to send subsequently hired managers to the initial training program at your expense (including a training fee). And you and your employees may be required to attend additional training sessions from time to time. See FA Section 6. You just need to be aware of this requirement. It is typical that a failure to satisfactorily complete training can result in termination of this agreement. [CC: 26]

27. You should study FA Section 3 and FA Section 12, which describe the fairly +1(832)510-3292

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limited duties of the franchisor, on the one hand, and the extensive duties of the franchisee on the other. Most franchise agreements, like this one, basically limit the franchisor's obligations to licensing the franchisee to use the systems and trademarks of the company, training the franchisee, assisting with getting the operation open and lending the franchisee a copy of the manual. Be aware that all of the services that are typically referred to as "support" in the franchise industry will be supplied by the franchisor in amounts and in forms that it determines in its discretion. If you request specific services or advice, you may have to pay for them on a per diem basis. See FA Section 6. [CC: 27]

28. The initial franchise fee, royalties and advertising contributions are described in FA Section 8-9. If you have questions about any of those, please ask me once you have reviewed this summary. These fees are also summarized and described in FDD Items 5 and 6. [CC: 28]

29. In Section 12(e) of the FA you are required to perform any maintenance or appearance upgrades that the franchisor requires. This is not a negative comment. Although it means you may be required to spend money more frequently than you would like, it also means that their system is kept fresh and good looking all the time. [CC: 29]

30. Although it may be obvious, I want to point out the requirements of FA Section 4. You must operate your business strictly in compliance with the franchisor's operations manual and all of its standards and specifications. Often, clients unfamiliar with the franchise industry don't realize how little freedom to make their own decisions they will really have once in a franchise investment. [CC: 30]

31. FA Section 13 specifically anticipates that you may have a manager operate the business. [CC: 31]

32. FA Section 13 requires that the franchisee, if a person, or an equity owner of the franchisee, if it is any entity, work full time in the business. [CC: 31]

33. You are given limited rights to use the Franchisor's trademarks. For example, you cannot use the trademark in your corporate name. You should review Section 2(a), 28(g) carefully to understand the limitations on what you can and cannot do with the trademarks. [CC: 32]

34. Although you are given a protected territory in this agreement (See FA Section 28(e)), the franchisor has a broad reservation of rights including the right to carry out strategic transactions with other brands that may be similar to McDonald's. Also, the franchisor has the right to sell products and services just like your products and services within the territory through alternative channels of distribution. See Section ~. [CC: 33]

35. FA Section 4 contains a provision that even seasoned business people outside the franchise industry sometimes find difficult to understand. The franchisor, here, reserves the

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right to change the operating system and the manual in its absolute discretion. The manual is incorporated into the franchise agreement and the franchisee is required to follow all of the standards and methods and requirements of the manual. This amounts to a unilateral right in the franchisor to amend the franchise agreement. Unless the franchisor behaves in a very arbitrary and unreasonable way, a court is likely to enforce the unilateral changes that the franchisor makes. Think of Dunkin' Donuts adding bagels. Think of McDonald's adding breakfast years ago. [CC: 34]

36. In the event that the franchisor adopts new trademarks, you may be required to use those addition trademarks or even abandon the original trademarks and adopt whatever new trademarks the franchisor instructs you to use. This change has to be made at your expense if it ever comes up. See FA Section ~. [CC: 35]

37. Significant restrictions on your right to conduct local advertising are contained in Section 5. It requires that you spend Minimum 4% of Gross Sales annually for advertising and promotion on local advertising and note, too, that you are not permitted to maintain a web site without the franchisor's consent. See FA Section 5. You should be aware that all of your advertising activities are subject to the right of the franchisor to pre-approve. [CC: 36]

38. FA Section 10 covers the accounting, record keeping and reporting that you are required to do. Be aware that you must submit the following reports: Required reports include monthly receipts statement (by 1st business day), monthly operating statement and statistical report (by 25th), and annual profit/loss statement and balance sheet (within 90 days of fiscal year end). [CC: 37]

39. The termination provisions are very important. Review FA Section 18 carefully. These are typical but be aware that your FA can be terminated for any default of the franchise agreement including: failure to pay any sums owed to franchisor, failure to furnish any required reports, declaring bankruptcy, making a material misrepresentation, failure to maintain required insurance, any conduct that may harm the brand, or abandoning the business. [CC: 38]

40. I note that Section 9 is actually favorable to you. Most franchise agreements do not give the franchisee a right to terminate in the event of a violation by the franchisor. That may seem surprising, but most franchise agreements do not give the franchisee such a right. [CC: 50]

41. FA Section \sim is a typical "grant back clause" which requires you to surrender ownership of any innovations that you may develop that the franchisor adopts as part of its system. First, you are not permitted to make unilateral changes to the system. Second, if you propose changes that are approved, accepted by the franchisor and become part of its operating system, you grant ownership of those developments without compensation to the

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franchisor. [CC: 39]

42. The covenants against competition in FA Section 11 are fairly typical, but they are very important. Franchisors get involved in more litigation with franchisees over these clauses than any other issue. You should make sure that you and your employees subject to noncompete agreements are fully aware of their obligations. During the term of the agreement, you may not have an interest in any competing business. After the term of the agreement, for 18 months thereafter, you may not have an interest in a competing business within Cannot engage in similar restaurant business within 10-mile radius of the Restaurant. [CC: 40]

43. FA Section 2(a) requires that you notify the public of the identity of the operator of the business (i.e. the franchisee) and its status as an independent contractor of the franchisor. The exact method of providing this notice is not specified in the agreement, so you should discuss the specifics with the company. [CC: 41]

44. As an independent contractor doing business for your own account using a licensed trademark, you are made to indemnify the franchisor for any liability that it may suffer as a result of or growing out of your operations. See FA Section 24. If the franchisor is sued by someone injured as a result of your activities, you are on the hook for the franchisor's defense and for any damages it might be called upon to pay. This is not likely going to be a negotiable issue. [CC: 42]

45. FA Section ~ is a clause that has recently been added to most franchise companies' agreements that requires the franchisee to reimburse the franchisor for state taxes the franchisor has to pay on its income derived from its relationship with you. In recent years, state tax authorities has started to claim that franchise companies have sufficient nexus with a state by virtue of its franchise agreement alone, to levy income and other taxes on revenues the out-of-state franchisor receives from the in-state franchisee. Many franchise companies do not pay these taxes, but they want to be able to collect reimbursement from the franchisee if they do have to start paying the taxes. [CC: 43]

46. The prerequisites for renewing your franchise agreement are contained in FA Section 28(a). They are fairly typical. Note that renewal does not technically mean that the original franchise agreement will be renewed or extended at the end of your initial term. You will have to sign the company's then current form of franchise agreement which may be quite different for the one you are signing now. [CC: 44]

47. Note that you are required to notify the franchisor of your intent to renew the franchise agreement between ~ prior to expiration of its initial term. It is a long time into the future, but you should calendar this deadline so you don't miss it. See FA Section ~. [CC: 45]

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48. Note that any disputes under this agreement will be adjudicated in the franchisor's home state of Illinois. And the laws of Illinois control the agreement. These could be unfavorable to you. Certainly fighting on the franchisor's home turf will be less convenient than doing so in near your home. See FA Section 27. [CC: 46]

49. You are required to waive your right to jury trial by this agreement and you also waive the right to punitive or exemplary damages. See FA Sections $\sim \& \sim$. [CC: 48]

50. This franchise agreement contains a private statute of limitations. FA Section ~ requires that you bring any claim that you might have against the franchisor within ~ from the occurrence of the facts giving rise to the claim. Normally, under state law, you would have up to three years or more to bring a claim for breach of contract or an unfair trade practice. This is not something that the franchisor is likely to be willing to negotiate, so you have to keep in mind that your rights might become stale if you wait too long before formally asserting a claim you might have against the franchisor. [CC: 48]

🔽 Next Steps

When you have had a chance to digest all of this, let's <u>schedule a call</u> to discuss your thoughts, questions and concerns, and a game plan for next steps. Don't forget to check out our <u>Negotiation Success Strategies Course</u> which features our <u>Franchise Negotiation Simulation</u> <u>Chatbot</u> and <u>FDD Review Companion Course</u>.



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Appendix – Background & Public Records Reports

(Read this primer first, then review the attached PDFs)

Why We Include These Reports

The FDD focuses largely on *what the franchisor chooses (or is required) to disclose*. Independent public-records searches help you verify that picture and surface issues that can:

- contradict Item 3 (litigation) or Item 4 (bankruptcies)
- reveal undisclosed liens, UCC filings, or cash-flow stress
- highlight credit-rating trends that may affect the franchisor's ability to support its network
- illuminate the personal track records (business history or criminal history) of the people who will be steering the brand

How to Read the Attached Documents

Key Sections to Review

- **Business Credit Score** / **Financial-Stability Rating** Lower scores can limit the franchisor's access to financing or indicate undercapitalization issues. Compare to Item 21 of the FDD financials of the franchisor. Business credit scores under 40 generally indicate a more risky or early-stage business.
- UCC & Lien Filings Frequent, recent filings may signal liquidity issues.
- Judgments, Bankruptcies & Litigation Must match FDD Item 3-4 disclosures; any mismatch is a red flag.
- **Executive Backgrounds** Personal bankruptcies, prior failed brands, or criminal matters warrant direct questions.

Common Red Flags (When to Hit Pause)

- Credit score < 30 **and** multiple active UCC liens within the last 12 months.
- Litigation or bankruptcy not disclosed (or disclosed differently) in Item 3-4.
- Key officer with repeated business failures or prior franchise terminations.
- Rapid spike in financing statements tied to the franchisor's receivables (suggests cash-flow crisis).

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Limitations & Disclaimers

These reports rely on public databases that may lag real-time events and may contain clerical errors. They are **data-points, not verdicts.** Always combine them with:

- the audited financial statements in Item 21,
 - direct written responses from the franchisor, and
 - your own operational due-diligence (validation calls with existing and former franchisees).



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