

## **Franchise Act Interpretive Statement FIS-08**

### **RE: Financial statement requirements for experienced franchisors seeking exemption from franchise registration in reliance upon RCW 19.100.030(4)(a) and (b)(i)**

#### **Questions Presented:**

1. May a franchisor demonstrate its satisfaction of the net worth requirements set forth in RCW 19.100.030(4)(b)(i)(A) by submitting its own unaudited financial statements along with audited financial statements of its parent?
2. If a franchisor submits audited financial statements for its parent but cannot create its own financial statements without undue expense, may the franchisor alternatively submit a guarantee of performance by the parent and a signed affidavit concerning the net worth of the franchisor?

#### **Statute**

RCW 19.100.030(4)(a) and (b)(i) set forth an exemption from franchise registration for experienced franchisors that meet certain thresholds.

This provision provides an exemption from franchise registration for offers and sales of franchises by franchisors that (1) meet certain net worth requirements, (2) have at least 25 franchisees that have conducted business for a period of at least 5 years, and (3) require an initial investment of at least \$100,000 be made by franchisees. In order to meet the net worth requirements, the franchisor must demonstrate through audited financial statements that it either (1) has a net worth of at least \$5,000,000, or (2) has a net worth of at least \$1,000,000 and is at least 80% owned by a corporation that has a net worth of at least \$5,000,000.

#### **Discussion**

Many franchisors seeking to demonstrate a net worth of at least \$1,000,000 in combination with being at least 80% owned by a corporation that has a net worth of at least \$5,000,000 are unable to produce audited financial statements separate from the parent company. Under these circumstances, it is acceptable for a franchisor to submit unaudited financial statements demonstrating that the franchisor has a net worth of at least \$1,000,000 in addition to submitting the consolidated audited financial statements of the parent.

In very limited circumstances, a franchisor may be unable to produce unaudited financial statements without incurring excessive costs. For example, if the parent company is publicly traded, producing and disclosing unaudited financial statements for a subsidiary may trigger SEC reporting requirements. Under these circumstances, it is acceptable for a franchisor to submit the following in lieu of unaudited financial statements, provided the consolidated audited financial statements of the parent are submitted:

- (1) An executed Guarantee of Performance between the parent company and the franchisor wherein the parent company absolutely and unconditionally guarantees the performance of the franchisor; and
- (2) A statement made under penalty of perjury by an officer of the franchisor confirming that the franchisor has a net worth of not less than \$1,000,000 for the immediately preceding fiscal year.

### **Conclusion**

A franchisor that claims exemption from franchise registration in reliance upon RCW 19.100.030(4)(a) and (b)(i) and that has a net worth of not less than \$1,000,000 and is at least 80% owned by a corporation which has a net worth on a consolidated basis of not less than \$5,000,000 must demonstrate it has met the net worth requirement. If it is unable to submit audited financial statements separate from the parent company, unaudited financial statements are acceptable. Alternatively, if unaudited financial statements cannot be obtained without incurring excessive costs, the franchisor may submit an executed Guarantee of Performance and signed affidavit in addition to the audited financial statements of the parent.

**Adopted June 8, 2015**

**William M. Beatty, Securities Administrator**

**Prepared by Daniel P. Matthews, Financial Legal Examiner**