

**SENATE JUDICIARY COMMITTEE**  
**Senator Thomas Umberg, Chair**  
**2023-2024 Regular Session**

SB 919 (Umberg)  
Version: March 14, 2024  
Hearing Date: April 23, 2024  
Fiscal: Yes  
Urgency: No  
ID

**SUBJECT**

Franchise Investment Law: third-party franchise sellers

**DIGEST**

This bill requires third-party franchise sellers to register with the state, provide specified disclosures to any prospective buyer of a franchise, and keep and maintain records of sales for five years.

**EXECUTIVE SUMMARY**

Many businesses across the United States operate as franchises. A franchise is a type of license that grants a franchisee (the person utilizing the license) access to a franchisor's (the person providing the franchise) proprietary business knowledge, processes, and trademarks to sell a product under the franchisor's business name. Franchises are often complex arrangements, in which the franchisee receives certain rights and services from the franchisor, while the franchisor still maintains some control over the franchise and the brand. When franchises are sold by a franchisor, California law requires the franchisor to register with the Department of Financial Protection and Innovation (DFPI) and provide certain information and disclosures to DFPI and to prospective buyers of the franchise. The Commissioner of DFPI can enforce these provisions on a franchisor seller, and a franchisee or sub-franchisor can sue a franchisor seller for damages for the franchisor's violation of the law. However, this arrangement and regulatory apparatus does not apply to third-party franchise sellers, who are not the franchisor and may have perverse incentives to steer prospective franchise buyers toward certain franchises over others. To remedy this lack of transparency, this bill proposes a regulatory scheme similar to the scheme for franchisor sellers, that can be enforced by DFPI and by suit from franchisees or franchisors. SB 919 is sponsored by the American Association of Franchisees & Dealers and the Coalition of Franchisee Associations, and supported by the International Franchise Association and a collection of franchise entities. The Committee has received no timely opposition. SB 919 passed out of the Senate Banking and Financial Institutions Committee on a vote of 6 to 1.

**PROPOSED CHANGES TO THE LAW**

Existing law:

- 1) Provides that it is unlawful for any person to offer or sell any franchise in the state unless the offer of the franchise has been registered or is exempt, as specified. (Corp. Code § 31110.)
- 2) Requires that an application for registration of an offer be filed with the commissioner of the Department of Financial Protection and Innovation (DFPI) on the Uniform Franchise Registration Application, and the application must be signed and verified by the franchisor or sub-franchisor. (Corp. Code § 3111-3112.)
- 3) Provides that the commissioner may, for the protection of prospective franchisees or sub-franchisors because a franchisor failed to demonstrate adequate financial arrangements have been made, require the escrow or impound of franchisee fees and other funds paid by the franchisee or sub-franchisor until such obligations have been satisfied. (Corp. Code §31113.)
- 4) Requires that a franchisor seller's registration application must be accompanied by a proposed franchise disclosure document, and additional disclosures the commissioner requires. (Corp. Code § 31114.)
- 5) Provides that the Commissioner may issue a stop order ending or suspending the registration of the franchise sale if they determine that the rules relating to registration and disclosure have not been complied with. Requires the Commissioner to provide a notice to the applicant for the registration, and allow the applicant to request a hearing on the order within 30 days of the notice, to be held within 15 days of receipt of a request for a hearing. (Corp. Code §§ 31115-31117.)
- 6) Makes it unlawful to sell any franchise in the state that is subject to registration without first providing the prospective franchisee with a copy of the franchise disclosure document, together with a copy of all proposed agreements, at least 14 days before the execution of the agreement by the prospective franchisee or the receipt of any consideration, whichever occurs first. (Corp. Code § 31119.)
- 7) Prescribes that a franchise sale is registered for a one year period from the effective date of the registration, unless the commissioner specifies a different period, and provides that registration may be renewed as specified. (Corp. Code §§ 31120-31121.)
- 8) Requires that a franchisor promptly notify the commissioner in writing of any material change to the information contained in the franchisor sale application. (Corp. Code § 31123.)

- 9) Specifies that every franchisor or sub-franchisor offering franchises for sale must keep and maintain a complete set of books, records, and accounts of such sales. (Corp. Code § 31150.)
- 10) Prohibits the publication of any advertisement in the state offering a franchise subject to registration unless a copy of the advertisement is provided to the commissioner at least three business days prior, and prohibits the publication of any advertisement the commissioner finds contains any statement that is false or misleading, or omits to make a necessary statement. (Corp. Code §§ 31156-57.)
- 11) Provides that any person who offers or sells a franchise in violation of specified sections of the Franchise Investment Law is liable to the franchisee or sub-franchisor, who may sue for damages, and for rescission if the violation is willful, unless for specified violations the defendant proves that the plaintiff knew the facts concerning the untruth or omission, or that the defendant exercised reasonable care and did not know or would not know of the untruth or omission. (Corp. Code § 31300.)

This bill:

- 1) Defines a third-party franchise seller as a person who directly or indirectly engages in the business of the offer or sale of a franchise, including a franchise broker, broker network, broker organization, and a franchise sales organization. Excludes from this definition: a franchisor or its officers, directors, or employees; a subfranchisor or its officers, directors, or employees; an area representative or its officers, directors, or employees; an employee of a wholly owned affiliate for a franchisor or subfranchisor; and a franchisee of the franchise being presented to a prospective franchisee, unless the franchisee operates a franchise broker business.
- 2) Makes it unlawful for any person to effect or attempt to effect the sale of a franchise, unless they are either identified in an application or amended application, or they are registered as a third-party franchise seller.
- 3) Makes any third-party franchise seller that offers or sells a franchise in violation of the bill's third-party franchisor provisions liable to the franchisee, and provides that the franchisee may sue for damages, rescission if the violation was willful except as specified. Provides that a third-party franchise seller that offers or sells a franchise in violation of the bill's third-party franchisor provisions is also liable to the franchisor, who may sue for damages or may assert claims of indemnity against the third-party franchise seller.
- 4) Provides for specified fees for the filing of an application for registration, renewal, or amendment to a registration as a third-party franchise seller under the bill's provisions.

- 5) Requires a third-party franchise seller to register by filing specified information with the commissioner, including a completed uniform third-party franchise seller disclosure form and document and any additional documents.
- 6) Provides that this registration expires within one year after the effective date of the registration. Provides for renewal of registration through the filing of specified documents at least 14 days before the seller's current registration expires, and requires that the renewal shall be effective at midnight on the fifth business day after filing of the necessary documents for the renewal, unless the commissioner determines an earlier time.
- 7) Requires a third-party franchise seller to promptly notify the commissioner in writing through an application to amend its registration of any material change in the information continued in the latest Uniform Third-Party Franchise Seller Disclosure Form, and specifies that a material change includes: a change in litigation history; a change in services provided; a change in compensation; or any other change the commissioner determines constitutes a material change. Provides that the commissioner may issue a stop order as specified if they find that any material change constitutes a failure to comply with this bill or any rule issued pursuant to it.
- 8) Provides that the commissioner may summarily issue a stop order suspending or denying any registration if the commissioner finds that the third-party franchise seller has failed to comply with any of the provisions of this bill or any rule issued by the Commissioner, and requires that in such a scenario the commissioner must issue a notice to the third-party franchise seller notifying it of that fact and providing specified information. Provides that the stop order may be modified, vacated, or extended until there has been a final determination of the matter at a hearing.
- 9) Provides that a third-party franchise seller may request a hearing on the Commissioner's stop order within 30 days of receiving notice of the order, and that the order will remain in effect until it is modified or vacated by the Commissioner if no hearing is requested.
- 10) Prohibits a third-party franchise seller from offering a franchise for sale in the state while a stop order of the Commissioner is issued.
- 11) Requires a third-party franchise seller to keep and maintain a complete set of books, records, and accounts for at least five years.
- 12) Requires a third-party franchise seller comply with a variety of code sections that prohibit advertisements offering a franchise unless a copy is filed with the commissioner, prohibit the publishing of any advertisement if the commissioner finds it contains false or misleading statements, and that permit the commissioner to

prescribe circumstances under which electronic records or signatures may be accepted.

- 13) Makes it unlawful for a third-party franchise seller to offer to sell a franchise in the state unless a third-party franchise seller is registered, and specifies that an offer or sale of a franchise occurs in the state in any of the following circumstances: the prospective franchisee resides in the state; the prospective franchisee has its principal place of business in the state; or the franchised business will be located in the state.
- 14) Makes it unlawful for a third-party franchise seller to engage with a prospective franchisee about a franchise opportunity unless the third-party franchise seller first provides to the prospective franchisee a copy of the completed Uniform Third-Party Franchise Seller Disclosure Document, which it can provide electronically.
- 15) Requires the Uniform Third-Party Franchise Seller Disclosure document to contain specified information, including:
  - a) the types of sellers;
  - b) the third-party franchise sellers' role in the franchise sales process;
  - c) services a third-party franchise seller might provide;
  - d) different ways a third-party franchise seller might be compensated for its services;
  - e) examples of questions a prospective franchisee might ask a third-party franchise seller;
  - f) the third-party franchise seller's legal name, trade name, year and state of incorporation, principal place of business, owners, directors and officers, contact information;
  - g) the third-party franchise seller's professional experience during the last five years;
  - h) the administrative, civil, or criminal actions alleging that the third-party franchise seller, owner, officer, or director violated any franchise, antitrust, or securities law, or committed fraud, unfair or deceptive practices, or similar violations within the last five years;
  - i) the industries of the brands that the third-party franchise seller represents, and how many brands within each industry the third-party franchise seller represents;
  - j) the description of the services performed by the third-party franchise seller;
  - k) how the third-party franchise seller is compensated, including how the amount of any consideration they receive is calculated;
  - l) whether a broker network, broker organization, or franchise sales organization may receive any additional consideration; and

- m) the name and contact information for all franchisees to whom the third-party franchise seller sold a franchise anywhere in the United States or its territories during the last calendar year, including the total number of units sold to each.
- 16) Specifies that its provisions become operable on July 1, 2025.

### COMMENTS

#### 1. Author's statement

According to the author:

Senate Bill 919 increases transparency in the franchise sales process for prospective franchisees in the State by providing information not only about what the prospective franchisee is buying (a franchise opportunity) but also who is selling it to them. SB 919 ensures that a prospective franchisee understands the role of the third party franchise seller and the incentives they may receive for referring the prospective franchisee to one franchise opportunity over another. By improving franchise presale disclosures, prospective franchisees will be better able to evaluate and make investment choices among the wide range of franchise opportunities presented to them and to choose from those that meet their goals, ambitions, financial and other requirements.

#### 2. Third-party franchise sellers

Many businesses across the United States operate as franchises. A franchise is a type of license that grants a franchisee (the person utilizing the license) access to a franchisor's (the person providing the franchise) proprietary business knowledge, processes, and trademarks to sell a product under the franchisor's business name.<sup>1</sup> When a franchisee buys a franchise, they are able to open a shop of the same name and brand as the franchisor, selling the franchisor's product. Many major businesses in the United States are franchises, including many major fast food and automotive businesses.

When someone buys a franchise, there are a variety of costs and limits on what they can do with the franchise. They must pay an initial franchise fee for the franchise, and may have to pay continuing royalty payments to the franchisor based on a percentage of the franchise's weekly or monthly gross income.<sup>2</sup> The franchisee may also have to contribute to an advertising fund that the franchisor uses for national advertising or to

---

<sup>1</sup> Adam Hayes, What is a franchise, and how does it work?, Investopedia (Feb. 29, 2024), available at <https://www.investopedia.com/terms/f/franchise.asp>.

<sup>2</sup> Federal Trade Commission, A Consumer's Guide to Buying a Franchise (Sept. 2020), available at <https://www.ftc.gov/business-guidance/resources/consumers-guide-buying-franchise#right-for-you> (hereafter Consumer's Guide).

attract new franchise owners. Additionally, franchisors usually control how the franchisee conducts business, such as by controlling the design or appearance of the business, and restricting how the franchise operates and where it sells.<sup>3</sup>

Business franchises are popular businesses, as they come with ready name recognition and infrastructure, and business franchises often look to sell more franchises in order to grow the brand and their income streams from additional franchises. To facilitate the sale of franchises, franchise sellers work to find individuals and investors interested in a franchise opportunity. A franchise seller is someone who offers for sale, sells, or arranges for the sale of a franchise.<sup>4</sup> Franchise sellers include the franchisor and its employees, representatives, agents, sub-franchisors, and third-party brokers. Franchise brokers are considered franchise sellers, and usually work with a person interested in buying a franchise to identify opportunities that match their interests and investment capacity and helps with the sale process.<sup>5</sup>

### 3. Current laws relating to franchises

Both federal and state laws regulate franchises and sales of franchises. The Federal Trade Commission's Franchise Rule requires that franchisors provide all potential franchisees and purchasers of a franchisee with material information that the potential buyer needs to assess the franchise and weigh the risks and benefits of purchasing it. The Rule requires that the franchisor complete a Franchise Disclosure Document (FDD), which contains 23 specific items of information about the offered franchise.<sup>6</sup> The 23 items include information on: the franchisor and any parent entities, predecessors, and affiliates; the franchisor's business experience; current or past litigation; any bankruptcy history; the required initial fees; other fees required to purchase the franchise; the estimated initial investment required; any restrictions on sources of products and services; the franchisee's obligations; financing; assistance, advertising, computer systems, and training that the franchisor provides; the territory of the franchise; trademarks; patents, copyrights, and proprietary information; a franchisee's obligation to participate in the actual operation of the franchise business; the restrictions on what the franchisee may sell; provisions on renewal, termination, or transfer of the franchise, and dispute resolution; public figures; any financial performance representations; the franchisor's other outlets and franchisees; the franchisor's financial statements; contracts; and the franchisor's receipts.<sup>7</sup> The FDD must be provided to the prospective buyer at least 14 days before the close of the sale.<sup>8</sup>

---

<sup>3</sup> *Id.*

<sup>4</sup> See the Federal definition of franchise seller provided in 16 CFR § 436.1.

<sup>5</sup> Consumer's Guide, *supra* note 2.

<sup>6</sup> 16 CFR §§ 436-437.

<sup>7</sup> *Id.*, LII Legal Information Institute, FTC franchise rule, Cornell Law School (Jul. 2021), available at [https://www.law.cornell.edu/wex/ftc\\_franchise\\_rule](https://www.law.cornell.edu/wex/ftc_franchise_rule).

<sup>8</sup> 16 CFR § 436.2.

At the state level, the California Legislature enacted the Franchise Investment Law in 1970, the first franchise disclosure law in the country. The Franchise Investment Law requires franchisors to register with the Department of Financial Protection and Innovation (DFPI) in order to be able to sell or offer franchises in California. (Corp. Code § 31000 et seq.) It also requires the disclosure of specified documents and the final franchise agreement to the prospective buyer at least 14 days before the sale. (Corp. Code § 31119.) Registration of a franchise sale lasts for one year, and can be renewed. (Corp. Code § 31120.) The Commissioner may issue a stop order ending or suspending the registration of the franchise sale if they determine that the rules relating to registration and disclosure have not been complied with, upon which the Commissioner must provide a notice to the applicant for the registration, and allow the applicant to request a hearing on the order within 30 days of the notice, to be held within 15 days of receipt of a request for a hearing. (Corp. Code §§ 31115-31117.) The Franchise Investment Law also provides for a private right of action for franchisees for specified violations of its provisions by franchisors. (Corp. Code § 31300.) However, the Franchise Investment Law does not apply to entities other than a franchisor offering a franchise for sale.

#### 4. There have been concerns over the operations of third-party franchise sellers

While franchisors selling a franchise are covered by the regulations of the Franchise Investment Law and the FTC's Franchise Rule, third-party franchise sellers are not. This blindspot in regulation may allow bad actors to thrive and take advantage of investors looking to buy a franchise without knowing the interests and conflicts of the person helping them through the franchise purchase process. For example, a third-party franchise seller may have agreements with different franchisors to find franchisees, and may receive a commission when a sale of a franchise is made.<sup>9</sup> One franchisor may offer the third-party franchise seller a larger commission than another, providing a perverse incentive for the third-party franchise seller to direct a potential franchisee toward one franchisor over another, regardless of the financial strengths or fit of either franchisor to the buyer. In a recent case, a lawsuit was brought against a franchise brokerage firm and its brokers over claims that the brokers attempting to extend franchise laws to these brokers for deceptive practices and misrepresentation of facts to potential franchisees.<sup>10</sup> However, that particular lawsuit involved an interpretation of New York state law on franchise sellers to find that the franchise brokers involved were covered.

---

<sup>9</sup> Consumer's Guide, *supra* note 2.

<sup>10</sup> Beth Ewen, New set of lawsuits target FranChoice, other franchise brokers, Franchise Times (Mar. 24, 2020), available at [https://www.franchisetimes.com/franchise\\_insights/new-set-of-lawsuits-target-franchoice-other-franchise-brokers/article\\_7a7db8fc-4620-5f74-997e-a0d080d4e460.html](https://www.franchisetimes.com/franchise_insights/new-set-of-lawsuits-target-franchoice-other-franchise-brokers/article_7a7db8fc-4620-5f74-997e-a0d080d4e460.html).



5. SB 919 proposes to combat bad actors in the third-party franchise seller industry by establishing a regulatory framework for the entities

SB 919 aims to provide increased transparency to the franchise sales process when a third-party franchise seller is involved, since these entities are otherwise currently not covered by disclosure and registration laws. SB 919 expands the prohibition on selling or attempting to sell a franchise without being registered under the California Franchise Investment Law. The bill requires third-party franchise sellers to be registered under the California Franchise Investment Law and subjected to disclosure requirements, and prescribes a registration process for these sellers as well. It defines third-party franchise sellers as: “a person who directly or indirectly engages in the business of the offer or sale of a franchise, including, but not limited to, a franchise broker, a broker organizations, and a franchise sales organization.”

The registration requirements in this bill require a third-party franchise seller to complete a Uniform Third-Party Franchise Seller Disclosure Form created by the DFPI Commissioner and file the completed form with the commissioner, along with a disclosure document, any additional documents or exhibits prescribed by the commissioner, and to pay a specified registration fee. As with the registration of franchisors who are selling franchises, SB 919’s provisions make third-party franchise sellers’ registration annual. Like with the registration provisions for franchisor sellers, the bill’s third-party franchise seller registration provisions require a third-party franchise seller to promptly notify the commissioner and amend their registration if there are any material changes to their registration, as specified.

It also provides the same mechanism as currently exists for franchisor sellers for the commissioner to issue a stop order for a violation of the registration provisions, including the provisions requiring the commissioner issue a notice of the stop order, allow 30 days for it to be disputed, and hold a hearing within 15 days of a request for review by the third-party franchise seller.

Additionally, SB 919 requires a third-party franchise seller to keep and maintain a complete set of books, records, and accounts of any franchise sale offers for five years, and to provide a copy of the Uniform Third-Party Franchise Seller Disclosure Document to a prospective franchisee before engaging with the prospective franchisee about a franchise opportunity. The Uniform Third-Party Franchise Seller Disclosure Document must contain specified information, including information regarding the third-party franchise seller’s role in the franchise sales process, the different ways the third-party may be compensated, the industries or brands they represent, and their professional experience and administrative, civil, or criminal actions initiated against the third-party franchise seller in the last five years.

Through this thorough process, SB 919 aligns the requirements for third-party franchise sellers with those currently in the Franchise Investment Law for franchisor sellers,

mirroring the registration requirements and process and transparency requirements that currently apply to franchisor sellers.

6. SB 919 is enforced by DFPI and by a private right of action

SB 919 ensures compliance both through DFPI, and through the same private right of action currently available in the franchisor seller context. As previously described, the DFPI Commissioner will enforce the provisions of SB 919 relating to registration. In addition, SB 919 adds the new provisions it creates relating to third-party franchise sellers to Corporations Code Section 31300, which provides that any person who offers or sells a franchise in violation of the specified Franchise Investment Law provisions is liable to the franchisee or sub-franchisor. SB 919 allows a franchisee or sub-franchisor to sue for damages caused by the seller's violation. It further allows for rescission in the case of a willful violation of the registration requirements, unless the defendant proves that the plaintiff knew the facts concerning the false statement or omission, or that the defendant exercised reasonable care and did not know or would not have known of the falsity or omission. However, unlike the private right of action for a franchisor seller, SB 919's private right of action also allows the franchisor to sue for damages or any claims of indemnity against the third-party franchise seller caused by the violation.

Thus, if a third-party franchise seller offers to sell or sells a franchise while not being registered as required, or does so without providing the franchisee the required disclosure documents, they could be liable to the franchisee or the franchisor for any damages from the violation. Because there are often three parties in such sales – the franchisee, the franchisor, and the third-party seller – the additional provision allowing the franchisor to sue would ensure that blame and indemnity can be properly placed on the party at fault, even when a franchisee may have claims against both the franchisor and the third-party seller. Through these mechanisms, SB 919 attempts to regulate the third-party franchise seller industry, ensure transparency for those considering buying a franchise through such a third-party seller, and provide a judicial remedy when a party is injured by a third-party franchise seller's failure to provide transparency.

7. Arguments in support

According to the Coalition of Franchisee Associations, which is a co-sponsor of this bill:

Senate Bill 919 will specifically require franchise sellers to register with the state, provide significant disclosures to its clients, and assign liability if they don't provide accurate information on the franchise they are selling. Currently, franchise sellers, often called franchise brokers, have no requirements. For example, to become a franchise broker, all you have to do is call yourself one. The importance of registration and disclosure is because buying a franchise puts the franchisee at significant risk. Most franchises, and often the loans required to obtain the franchise, require personal guarantees by the franchisee. Unlike most

other large investments where only the investment is at risk, buying a franchise can put ALL your assets at risk. Because of these risks it is critical that franchise sellers have disclosure requirements and liability if they provide improper information about the franchise they are selling.

### SUPPORT

American Association of Franchisees & Dealers (co-sponsor)

Coalition of Franchisee Associations (co-sponsor)

Amazing Lash Studio

Beauty Bungalows

Bishops Cut and Color

Brain Balance

Bright Stare Care

Camp Bow Wow

Cappriotti's

CertaPro Painters

Church's Texas Chicken

City Wide Facility Solutions

College H.U.N.K.S. Hauling Junk

Drybar

EatGatherLove

Elements Massage

Elmer's Restaurants, Inc.

FASTSIGNS

FirstService Brands/California Closets

Fitness Together

Floor Coverings International

Frenchie's Modern Nails

Great Clips

GoJoe Patrol, Inc.

GYMGUYZ

Home Helpers Home Care

iKids U Franchise, LLC

Instant Imprints

International Franchise Association

InXpress

MSA Worldwide

NextHome, Inc.

Paul Davis

Payroll Vault

Pillar To Post Home Inspectors

Pizza Factory

PuroClean

Radiant Waxing  
Season 2 Consign  
Season 2 Franchising  
Senior Care Authority, LLC  
Sports Clips  
Stratus Building Solutions  
Supercuts Franchise Association  
The Goddard School  
The Joint Chiropractic  
The Lash Lounge  
Tootl Transport  
Trash Butler  
Tropical Smoothie Café  
Wild Birds Unlimited, Inc.  
WingZone  
Wise Coatings Franchises

**OPPOSITION**

None received

**RELATED LEGISLATION**

Pending Legislation: None known.

Prior Legislation: AB 676 (Holden, Ch. 728., Stats. 2022) provides that the Commissioner of the DFPI has the authority to summarily issue a stop order on a registration of a franchisor seller, among other provisions.

**PRIOR VOTES:**

Senate Banking and Financial Institutions Committee (Ayes 6, Noes 1)

\*\*\*\*\*