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The Honorable Gavin C. Newsom  
Governor of the State of California  
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Re: SB 919: Franchise Investment Law: franchise brokers

Dear Governor Newsom:

SB 919 is an essential addition to The State of California's Franchise Investment Law (CFIL), and California Franchise Relations Act (CFRA), and I encourage you to sign this bill into law.

In recent years, the role of third-party franchise sellers in the franchisee recruitment process (including franchise brokers and franchise sales organizations) has continued to grow. Today, approximately one-fifth of the more than 3,000 franchisors leverage third-party franchise sellers to support franchisee recruitment. Despite the significant role that these third-party franchise sellers play in a prospective franchisee's journey to invest in a franchise opportunity, including being the first point of contact for the prospective franchisee, the regulation of third-party franchise sellers is minimal.

There are significant ramifications due to the absence of meaningful franchise seller regulation. In addition to their impact on single-unit franchisees, there exists a current environment of prospective franchisees being pressured to purchase multi-unit franchise development rights despite their business experience and financial condition not supporting the successful execution of those rights. Also, early-stage franchisors, lacking the infrastructure, capital and experience to support rapid growth within their franchise systems, are being pressured by third-party franchise sellers to offer multi-unit franchise development rights. This benefits no one, except for the third-party seller which earns significant compensation on these transactions. The registration and disclosure requirements that will be implemented through SB 919 are long overdue and will establish California as the leader in protecting small business owners, including franchisees and franchisors.

By way of background, I am the founder and Managing Director of MSA Worldwide, a well-known and respected consulting firm in franchising. MSA's clients range from small emerging brands looking to develop franchise systems to some of the world's leading franchisors, domestically and internationally. The majority of our clients offer franchises in the State of California.

I am an author, speaker, university professor, social franchisor in Sub-Saharan Africa and serve on the Board of Directors of the International Franchise Association (IFA). The Department of Financial Protection and Innovation for the State of California has published a due diligence workbook for franchisees that I authored and which I have provided to DFPI at no cost. ([dfpi.ca.gov/wp-content/uploads/sites/337/2021/10/Making-the-Franchise-Decision-Workbook-2021.pdf](https://dfpi.ca.gov/wp-content/uploads/sites/337/2021/10/Making-the-Franchise-Decision-Workbook-2021.pdf))

The selection of any franchise offering is a complex undertaking for prospective franchisees and the franchise selection process is lengthy, generally conducted electronically, and often takes months or longer to complete. During this period, prospective franchisees, who are generally uneducated regarding franchise investments, often work with third-party franchise sellers. While the CFIL and CFRA provide substantial information and protection to prospective franchisees, it has a glaring omission when it comes to providing essential information about third-party franchise sellers.

Third-party franchise sellers frequently do not identify as franchise brokers and instead self-identify as experienced experts, consultants, coaches and advisors to prospective franchisees, who they will often refer to as their clients. However, the third-party franchise seller makes their living introducing prospective franchisees to their actual client – the franchisor. They do so in exchange for significant compensation for the introduction and sale. In addition to earning a sales commission paid from the initial fees received by the franchisor from the prospective franchisees, in some cases third-party sellers also earn a share of the continuing royalty received by the franchisor during the term of the franchisee's investment, and equity in the franchisor in some cases.

Under current law, the background (work history, experience in franchising, litigation, bankruptcy, regulatory history) of the franchise seller; their relationship with their franchisor client; the types and amount of the fees they are paid by their franchisor clients; and, the identification of the franchisors they represent, are not disclosed to the prospective franchisees. Prospective franchisees often believe that the franchise seller is representing them and acting in their best interest. Self-identifying as an expert does not equate to actually having any expertise and prospective franchisee investors are entitled to understand third-party sellers' background, qualifications, methods, amounts and types of compensation, and who they actually represent in the relationship.

While the prospective franchisee may frequently receive beneficial advice and guidance from the franchise seller, there exists a substantial conflict of interest as the third-party seller is not paid by the prospective franchisees and instead is a commissioned salesperson for the franchisor. By requiring easily assembled information from the third-party seller to the prospective franchisee in the form of disclosure, SB 919 is designed to provide transparency to a prospective franchisee about this conflict of interest.

Registration requirements for franchise sellers have existed for many years in Washington and New York, and franchise development in those states has continued to flourish. You should also be aware that the North American Securities Administrators Association (NASAA), currently headed by a State of California regulator, has recently issued a proposed Model Broker Registration Act that provides for registration and disclosure by third-party franchise sellers. Their model broker registration largely tracks the requirements of SB 919. In passing SB 919, California can establish precedent that NASAA and other states may follow with respect to a registration and disclosure regime for third-party franchise sellers.

As you are aware, there is a significant difference between people that self-proclaim themselves as influencers and those who are actually influential. In this regard, I am aware that a relatively small group of third-party franchise sellers, with little support or influence in franchising, have made claims that SB 919 creates additional legal risk to them in offering

franchises and have lobbied you for substantial changes to SB 919. They also claim that the State of California will suffer economically because the offering of franchises will be reduced should SB 919 be enacted into law.

SB 919 will be beneficial to franchising for a variety of reasons. In addition to providing essential information to prospective franchisees, it will also provide information to franchisors on the brokers they work with. Franchisors in California naturally want to ensure that the franchisee recruitment practices associated with their brands be conducted in the best way possible. The bad actors in the broker community will be identified and eliminated, which will benefit everyone, including the responsible brokers. The pushback on SB 919 all seems to focus only on how it impacts brokers but there is no one that claims it does not benefit franchisors, franchisees and franchising overall.

In requiring the preparation of a Broker Disclosure Document (with the possible exception of their being suspended from being able to offer franchises in California for violating SB 919 and existing law), SB 919 does not create any additional liability for third-party sellers under either the CFIL or CFRA. In addition, as a well-respected and recognized expert in franchising, I can also assure you that there will be zero impact on franchisee recruitment in the State of California because of SB 919. Instead, SB 919's transparency will strengthen the economy in California because of the additional stability it will create in franchising and, the additional revenue that SB 919 will bring in fees to the State will more than make up for the anticipated costs of its implementation.

I have served on the IFA Board of Directors for over fifteen (15) years and in some leadership positions (including on its executive committee) for many years more. During that lengthy period, this is the first time that I can recall the three organizations that represent franchisors and franchisees, the IFA, CFA and AAFD, aligning on any franchise regulation in California. This alignment signifies the importance of SB 919 to franchising and to the State of California. Because of its vital importance, I encourage you to sign SB 919.

I am available to you for any discussions or questions you may have regarding SB 919.

Respectfully,



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