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Glossary of Franchise Terms, Part 1

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Feb 14, 2015

We find in our discussions with clients, potential clients and other interested parties that we frequently use terms of art in the franchising field whose meaning may not be known to the layperson. We thought it might be useful to start to introduce some definitions to these discussions, so that those reading the blog and our website can refer to this entry for guidance. Keep in mind, this is just the beginning:

GLOSSARY OF TERMS

1. **Franchise** means a business arrangement where the franchisor promises that:
 - The franchisee will obtain the right to operate a business using the franchisor's trademark;
 - The franchisor will exert control over the franchisee's method of operation or will provide assistance in the franchisee's method of operation; and
 - The franchisee pays or promises to pay a fee to the franchisor or its affiliate, such as an initial franchise fee or royalties.
2. **Franchisor** means any person who grants a franchise and participates in the franchise arrangement.
3. **Franchisee** means any person who is granted a franchise.
4. **Amended FTC Rule** means the federal regulation that governs franchise sales in the United States. The amended FTC Rule requires franchisors provide to prospective franchisees a franchise disclosure document.
5. **Franchise Disclosure Document ("FDD")** means an offering prospectus containing 23 specific disclosure items that must be provided to a prospective franchisee. Disclosure items include but are not limited to, a description of the franchisor's history, tables indicating the franchisee's estimated initial investment as well as the types of fees and expenses that the franchisee will pay during the term of the franchise agreement and a list of the franchisor's obligations to the

franchisee as well as financial performance representations, if the franchisor elects to make any.

6. **Financial Performance Representation** means a representation made within the FDD stating a specific level or range of actual or potential sales, income, gross profits, or net profits. Financial performance representations are optional and some franchisors choose not to make them.
7. **Master Franchisor** means any person who grants to another (the master franchisee) the right to sell franchises within a certain geographic territory.
8. **Master Franchisee (also referred to as a Sub-Franchisor)** means any person who is granted the right to sell sub-franchises within a certain geographic territory. The master franchisee will enter into a franchise agreement with each of its sub-franchisees. The master franchisee receives a percentage of the initial franchise fees and royalties paid by sub-franchisees.
9. **Sub-Franchisee** means any person that is granted a unit or individual franchise by a master franchisee.
10. **Area Developer** means any person that is granted the right to open a pre-determined number of units in a certain geographic territory. The Area Developer is obligated to own and operate each one of the units without sub-franchising.
11. **Multi-Unit Operator** means a franchisee that operates multiple franchises. A franchisee may become a multi-unit operator by opening a number of units as an area developer or may acquire additional franchises in a series of one-off deals.
12. **Area Representative** means a person that acts as an agent or sales broker for the franchisor within a geographic territory. The area representative will be required to recruit a minimum number of franchisees. Area representatives are generally compensated by earning commissions when the franchisor enters into a franchise agreement with a franchisee and an area representative may also receive commissions in the form of a percentage of the royalties collected by the franchisor from the franchisee.