

105TH CONGRESS
1ST SESSION

H. R. 1083

To establish certain uniform rights, duties, and enforcement procedures
relating to franchise agreements.

IN THE HOUSE OF REPRESENTATIVES

MARCH 17, 1997

Mr. ACKERMAN introduced the following bill; which was referred to the
Committee on Commerce

A BILL

To establish certain uniform rights, duties, and enforcement
procedures relating to franchise agreements.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Federal Fair Franchis-
5 ing Practices Act of 1997”.

6 **SEC. 2. DUTY OF GOOD FAITH.**

7 (a) IN GENERAL.—A franchise shall include an im-
8 plied duty on the part of a party to the franchise to act
9 in good faith in the performance and the enforcement of
10 the rights and duties established in the franchise.

1 (b) INTERESTS OF OTHER PARTIES.—The duty de-
2 scribed in subsection (a) shall include an obligation on the
3 part of a party to a franchise, in making a decision or
4 in exercising a power that directly affects the franchise
5 or the franchised business concerned, to give due and
6 equal regard to an interest of any other such party that
7 is likely to be affected by the decision made or the power
8 exercised.

9 **SEC. 3. DUTY OF COMPETENCE.**

10 (a) IN GENERAL.—In a franchisor's undertaking
11 with a franchisee, the franchisor shall exercise the skill
12 and knowledge normally possessed by franchisors in good
13 standing in similar communities or trade areas, unless the
14 franchisor—

15 (1) represents that it has greater skill or knowl-
16 edge; or

17 (2) conspicuously disclaims that it has the nor-
18 mal skill or knowledge.

19 (b) EFFECT OF DISCLAIMER.—The duty described in
20 subsection (a) may not be disclaimed or qualified by agree-
21 ment or by conduct, but a franchisor may by written
22 agreement define specifically the nature and scope of its
23 skill or knowledge and of its undertaking with a
24 franchisee.

1 **SEC. 4. NEGOTIATED CHANGES.**

2 A franchisor that has delivered to a prospective
3 franchisee a valid offering circular may negotiate with the
4 prospective franchisee concerning the terms of a franchise
5 and may execute with the prospective franchisee a fran-
6 chise whose terms reflect negotiated changes from the ini-
7 tial offering.

8 **SEC. 5. INDEPENDENT SOURCING.**

9 (a) IN GENERAL.—A franchisee may obtain equip-
10 ment, fixtures, supplies, and services used in the establish-
11 ment and operation of a franchised business from any
12 source, if the goods and services meet any reasonable
13 standard regarding their nature and quality that may be
14 promulgated by the franchisor concerned.

15 (b) EXCEPTION.—Subsection (a) shall not apply to
16 a reasonable quantity of inventory goods or services, in-
17 cluding display and sample items, that—

18 (1) a franchisor requires a franchisee to obtain
19 from the franchisor or its affiliate;

20 (2) are a central feature of the franchised busi-
21 ness concerned; and

22 (3) are manufactured or produced—

23 (A) by the franchisor or its affiliate; or

24 (B) solely for the account of the franchisor
25 or its affiliate and incorporate a trade secret of
26 the franchisor or its affiliate.

1 **SEC. 6. TERMINATION AND NONRENEWAL.**

2 A franchisor may not terminate or refuse to renew
3 a franchise whose term is indeterminate without good
4 cause.

5 **SEC. 7. TRANSFER.**

6 (a) IN GENERAL.—A franchisee may transfer a
7 transferable interest to a transferee who meets a
8 franchisor’s reasonable, essential, and nondiscriminatory
9 standards for new franchisees or transferees, as the stand-
10 ards are in effect on the date the franchisee and the trans-
11 feree agree to the transfer. A franchisor may not withhold
12 its consent to such a transfer without good cause.

13 (b) NOTICE OF PROPOSED TRANSFER.—A franchisee
14 shall give a franchisor not less than 30 days written notice
15 of a proposed transfer of a transferable interest, and on
16 request shall advise the franchisor in writing of the owner-
17 ship interests of all persons holding or claiming an equi-
18 table or beneficial interest in the franchise, the franchised
19 business, or the franchisee.

20 (c) CONSENT TO PROPOSED TRANSFER.—A
21 franchisor may not unreasonably withhold its consent to
22 a proposed transfer of a transferable interest. A transfer
23 is deemed approved 30 days after a franchisee submits
24 the proposed transaction for consent, unless the franchisor
25 earlier disapproves the transaction by written notice speci-
26 fying each basis for the disapproval or exercises a right

1 of 1st refusal. Such a notice is privileged against a claim
2 of defamation.

3 (d) CONDITIONS ON TRANSFER.—

4 (1) PERMISSIBLE CONDITIONS.—A franchisor
5 may condition its consent to a proposed transfer by
6 a franchisee of a transferable interest on—

7 (A) the transferee’s successful completion
8 of a reasonable, essential, and nondiscrim-
9 inatory training program;

10 (B) the payment of a transfer fee to the
11 franchisor to reimburse it for its reasonable, ac-
12 tual, out-of-pocket expenses directly related to
13 the transfer; or

14 (C) the payment of any amount the
15 franchisee owes to the franchisor or its affiliate.

16 (2) IMPERMISSIBLE CONDITIONS.—A franchisor
17 may not condition its consent to a transfer described
18 in paragraph (1) on a franchisee—

19 (A) undertaking new or different obliga-
20 tions than those contained in the franchise con-
21 cerned;

22 (B) forgoing existing rights other than
23 those contained in the franchise concerned; or

1 (C) entering into a release of claims broad-
2 er in scope than a counterpart release of claims
3 offered by the franchisor to the franchisee.

4 (e) RIGHT OF 1ST REFUSAL.—A franchisor may ex-
5 ercise a right of 1st refusal in connection with a proposed
6 transfer by a franchisee of a transferable interest, if such
7 right is reserved in the franchise. A franchisor may not
8 exercise such right more than 30 days after the date it
9 receives a franchisee's request for consent to the proposed
10 transfer. A franchisor may not exercise such right if doing
11 so would result in it holding a minority ownership interest
12 in the franchised business or the franchisee concerned. A
13 franchisor may determine whether to exercise such right
14 based only on the merits and circumstances of the pro-
15 posed transfer.

16 (f) CONSENT TO PUBLIC OFFERING.—A franchisor
17 may not withhold its consent to a franchisee making a
18 public offering of its securities without good cause, if the
19 franchisee or the owner of the franchisee's interest in the
20 franchise retains control over more than 50 percent of the
21 voting power in the franchisee.

22 (g) CONSENT TO POOLING OR EXCHANGE.—A
23 franchisor may not withhold its consent to a pooling of
24 interests or an exchange of assets by its existing
25 franchisees.

1 (h) ASSIGNMENT.—A franchisee may assign its inter-
2 est in a franchise for the unexpired term of the franchise.
3 A franchisor may not require the franchisee or the as-
4 signee to enter into a new or different franchise as a result
5 of the assignment.

6 (i) NONINTERFERENCE.—A franchisor may not
7 interfere with—

8 (1) the succession to ownership or management
9 of a franchisee or a franchised business upon the
10 death or disability of a franchisee, or of an owner,
11 officer, or director of a franchisee, by a spouse,
12 child, fellow shareholder or partner of the deceased
13 or disabled franchisee, owner, officer, or director;

14 (2) incorporation of a proprietorship franchisee
15 or franchised business;

16 (3) transfers within an existing ownership
17 group of a franchisee or franchised business of less
18 than a controlling interest in the franchisee or fran-
19 chised business;

20 (4) transfers of less than a controlling interest
21 in a franchisee or franchised business to the
22 franchisee's (or its owners') spouse or child;

23 (5) transfers of less than a controlling interest
24 in a franchisee or a franchised business to an em-

1 ployee stock ownership plan or employee incentive
 2 compensation or deferred benefit plan;

3 (6) a grant or retention of a security interest
 4 in a franchise, a security or ownership interest in a
 5 franchised business or its assets, or a security or
 6 ownership interest in a franchisee, if the agreement
 7 that governs the grant or retention is a franchisor-
 8 notice security agreement; or

9 (7) the use of a management consultant or hir-
 10 ing of a professional manager by a franchisee or a
 11 franchised business.

12 (j) SECURITY INTEREST OF FRANCHISEE.—A
 13 franchisor may not prevent a franchisee that transfers a
 14 transferable interest from retaining or foreclosing a secu-
 15 rity interest in any asset transferred, including a fran-
 16 chise, if—

17 (1) the security interest is created to secure ob-
 18 ligations of the transferee to the franchisee; and

19 (2) the security agreement that governs the se-
 20 curity interest is a franchisor-notice security agree-
 21 ment.

22 (k) EFFECT OF CERTAIN COVENANTS.—

23 (1) IN GENERAL.—After the transfer of a
 24 transferor's complete interest in a franchise, a
 25 franchisor may not enforce against the transferor

1 any covenant of the franchise purporting to prohibit
2 the transferor from engaging in any lawful occupa-
3 tion or enterprise.

4 (2) EXCEPTION.—This subsection shall not
5 limit the right of a franchisor to enforce contractual
6 covenants of a transferor not to exploit the
7 franchisor's trade secrets or intellectual property
8 rights (including protection of trade dress) except by
9 agreement with the franchisor.

10 (1) TRANSFER BY FRANCHISOR.—A franchisor, or its
11 owner, may not transfer a transferable interest unless it
12 takes reasonable steps to ensure that the transferee, the
13 franchisor, or the owner will perform the franchisor's obli-
14 gations under the franchise concerned. A franchisor, or
15 its owner, shall give a franchisee notice of such a proposed
16 transfer at the time the notice is required to be given by
17 the franchisor, or its owner, under applicable securities
18 laws, if the franchisor or its owner is publicly traded. If
19 the franchisor or its owner is not publicly traded, then
20 the notice shall be given at the time the notice would be
21 required if the franchisor or its owner were publicly trad-
22 ed.

1 **SEC. 8. ANTICOMPETITIVE COVENANTS.**

2 (a) IN GENERAL.—A franchisor may not prohibit, or
3 enforce a prohibition against, a franchisee engaging in any
4 lawful business at any location—

5 (1) after expiration of the term of the franchise
6 concerned;

7 (2) after termination of the franchise by the
8 franchisee for good cause; or

9 (3) after a transfer by the franchisee of its full
10 interest in the franchise.

11 (b) EXCEPTION.—Subsection (a) shall not apply if 10
12 or more days before the effective date of an expiration,
13 termination, or transfer described in such subsection, a
14 franchisor offers in writing to purchase the franchised
15 business concerned for its fair market value as a going
16 concern. Such offer may be conditioned upon the ascer-
17 tainment of the fair market value by an impartial ap-
18 praiser.

19 (c) ENFORCEMENT OF CERTAIN FRANCHISE PROVI-
20 SIONS.—This section shall not prohibit a franchisor from
21 enforcing provisions of a franchise obligating a franchisee
22 after expiration or termination of the franchise—

23 (1) to alter the appearance of the premises and
24 the manner of operation of the franchised business
25 concerned to avoid the likelihood of confusion as to
26 the affiliation of the business with its former

1 franchisor or the origin of goods or services it offers;
2 or

3 (2) to cease and refrain from using a trade se-
4 cret of the franchisor or of its affiliate.

5 **SEC. 9. FREEDOM OF ASSOCIATION.**

6 (a) ASSOCIATION OF FRANCHISEES.—A franchisor
7 may not directly or indirectly inhibit its franchisees from
8 forming an association or from associating with other
9 franchisees for any lawful purpose. A franchisor may not
10 directly or indirectly penalize a franchisee for organizing
11 or participating in an association of franchisees.

12 (b) COLLECTIVE BARGAINING.—A franchisor that
13 has more than 500 franchises outstanding, or more than
14 300 franchisees, in the United States, shall bargain in
15 good faith with an organization of its franchisees that—

16 (1) represents generally, or on a specific issue
17 or set of issues, a majority of its franchisees in the
18 United States; and

19 (2) requests such bargaining.

20 **SEC. 10. ENCROACHMENT.**

21 (a) IN GENERAL.—A franchisor may not place, or li-
22 cense another to place, a new outlet in unreasonable prox-
23 imity to an established franchised outlet, if—

24 (1) the intent or probable effect of establishing
25 the new outlet is to cause a diminution of gross sales

1 by the established outlet of more than 10 percent in
2 the 12 months immediately following establishment
3 of the new outlet; and

4 (2) the established outlet—

5 (A) offers goods or services identified by
6 the same trademark as those offered from the
7 new outlet; or

8 (B) has premises that are identified by the
9 same trademark as the new outlet.

10 (b) EXCEPTION.—This section shall not apply if, be-
11 fore a new outlet described in subsection (a) opens for
12 business, a franchisor offers in writing to each franchisee
13 of an established outlet concerned to pay to the franchisee
14 an amount equal to 10 percent of the gross sales (net of
15 sales taxes, returns, and allowances) of the new outlet for
16 the 1st 24 months of the new outlet's operation, if the
17 sales of the established outlet decline by more than 10 per-
18 cent in the 12 months immediately following establishment
19 of the new outlet as a consequence of the opening such
20 outlet.

21 (c) BURDEN OF PROOF.—A franchisor shall have the
22 burden of proof to show that, or the extent to which, a
23 decline in sales of an established franchised outlet de-
24 scribed in subsection (a) occurred for reasons other than
25 the opening of the new outlet concerned—

1 (1) if the franchisor makes a written offer
2 under subsection (b); or

3 (2) in an action or proceeding brought under
4 section 12.

5 **SEC. 11. PROHIBITION ON DISCRIMINATION.**

6 In granting franchises, considering approval of trans-
7 fers of transferable interests, and in administering its
8 franchise system, a franchisor shall not discriminate
9 against any person on the basis of race, color, religion,
10 national origin, sex, physical handicap, or sexual pref-
11 erence.

12 **SEC. 12. PRIVATE RIGHT OF ACTION.**

13 (a) IN GENERAL.—A party to a franchise who is in-
14 jured by a violation or impending violation of this Act or
15 of section 436.1 of title 16, Code of Federal Regulations
16 (relating to disclosure requirements and prohibitions con-
17 cerning franchising and business opportunity ventures)
18 may bring an action for rescission, damages, or other ap-
19 propriate relief in a court of competent jurisdiction.

20 (b) COST RECOVERY.—The prevailing party in an ac-
21 tion brought under subsection (a) may recover its costs,
22 including its reasonable attorneys' fees.

23 (c) INJUNCTIVE RELIEF.—A party to a franchise
24 may bring an action to enjoin a violation of this Act. For
25 purposes of determining whether to issue an injunction or

1 a restraining order, a court may presume irreparable harm
 2 from a violation of this Act or of section 436.1 of title
 3 16, Code of Federal Regulations. Notwithstanding rule
 4 65(c) of the Federal Rules of Civil Procedure or any other
 5 provision of law, a court of the United States may award
 6 preliminary injunctive relief without bond or other finan-
 7 cial security in an action brought under subsection (a).

8 **SEC. 13. PROCEDURAL FAIRNESS.**

9 (a) IN GENERAL.—This Act shall apply to a fran-
 10 chised business that is operated in whole or in part in the
 11 United States, to a franchise that grants the right to en-
 12 gage in such a franchised business, and to the parties to
 13 such a franchise.

14 (b) WAIVER OR AVOIDANCE.—This Act may not be
 15 waived, and its application may not be avoided in whole
 16 or in part, by agreement or by conduct, except as part
 17 of a settlement of a bona fide dispute.

18 (c) EFFECT OF CHOICE-OF-LAW PROVISIONS.—A
 19 franchisee may not be deprived of the application and ben-
 20 efits of this Act by a provision of a franchise purporting
 21 to designate the law of a country other than the United
 22 States as governing the franchise or the interpretation of
 23 the franchise, or to designate a venue outside of the Unit-
 24 ed States for the resolution of disputes.

1 (d) EFFECT OF EXCLUSIONARY PROVISIONS.—A per-
 2 son’s obligation to comply with this Act may not be ex-
 3 cused or avoided, and evidence of a violation of this Act
 4 may not be excluded from evidence, because of a provision
 5 of a franchise, the parol evidence rule, or any other rule
 6 of law purporting to prohibit a factfinder from considering
 7 matters other than the text of a franchise.

8 (e) EFFECT OF CERTAIN STIPULATIONS.—A liq-
 9 uidated damages provision, a confession of judgment pro-
 10 vision, or any other provision in a franchise pursuant to
 11 which a party to the franchise is or would be deprived of
 12 an opportunity to prove or contest a fact that is relevant
 13 to this Act shall be unenforceable.

14 **SEC. 14. DEFINITIONS.**

15 For purposes of this Act:

16 (1) AFFILIATE.—The term “affiliate” means a
 17 person who controls, is controlled by, or is under
 18 common control with, a franchisor.

19 (2) FRANCHISE.—The term “franchise” means
 20 a contract or agreement between 2 or more persons
 21 by which—

22 (A) a franchisee is granted the right to en-
 23 gage in a franchised business;

24 (B) operation of the franchised business is
 25 substantially associated with the franchisor’s

1 trademark, service mark, trade name, logotype,
2 advertising, or other commercial symbol des-
3 ignating the franchisor or the franchisor's affili-
4 ate; and

5 (C) the franchisee pays or is required to
6 pay, directly or indirectly, a franchise fee.

7 (3) FRANCHISE FEE.—

8 (A) IN GENERAL.—The term “franchise
9 fee” means a fee or charge for the right to
10 enter into or maintain a franchise, including
11 any payment for goods or services.

12 (B) EXCEPTION.—The term “franchise
13 fee” shall not include—

14 (i) a payment at a bona fide wholesale
15 price for a reasonable quantity of inven-
16 tory;

17 (ii) a payment of a reasonable service
18 charge to the issuer of a credit or debit
19 card by a person accepting or honoring
20 such card; or

21 (iii) a payment at fair market value
22 for a reasonable quantity of real estate,
23 fixtures, equipment, or other tangible prop-
24 erty to be used in, and necessary for, the
25 operation of the franchisee's business.

1 (4) FRANCHISED BUSINESS.—The term “fran-
2 chised business” means a business of offering, sell-
3 ing, or distributing goods or services under a mar-
4 keting plan or system prescribed in substantial part
5 by a franchisor.

6 (5) FRANCHISEE.—The term “franchisee”
7 means a person to whom a franchise is granted.

8 (6) FRANCHISOR.—The term “franchisor”
9 means a person who grants a franchise.

10 (7) FRANCHISOR-NOTICE SECURITY AGREE-
11 MENT.—The term “franchisor-notice security agree-
12 ment” means a security agreement that creates an
13 obligation on the part of a secured party that is en-
14 forceable by a franchisor to give the franchisor—

15 (A) notice of the secured party’s intent to
16 foreclose on collateral described in the security
17 agreement at the same time as the secured
18 party gives such notice to the franchisee con-
19 cerned or, if the secured party is the franchisee
20 concerned, at a reasonable time; and

21 (B) a reasonable opportunity to redeem the
22 interest of the secured party and to recover the
23 secured party’s interest in the franchise or fran-
24 chised business concerned by paying the secured
25 obligations (or the fair market value of secured

1 obligations not stated as amount payable in
2 cash).

3 (8) GOOD CAUSE.—The term “good cause”
4 means—

5 (A) a complete withdrawal by a franchisor
6 from the conduct of business in a State or in
7 the District of Columbia; or

8 (B) a failure by a party to a franchise who
9 has received a written notice from another such
10 party that describes corrective action that must
11 be taken, and the time period within which such
12 action must be taken to prevent termination of
13 the franchise, to correct a default of a provision
14 of the franchise—

15 (i) within 30 days of receipt of the no-
16 tice, if the notice specifies a default of a
17 material provision of the franchise; or

18 (ii) within 48 hours of receipt of the
19 notice, if the notice specifies a default of a
20 material provision of the franchise that
21 constitutes a clear and present danger to
22 public health or safety.

23 (9) GOOD FAITH.—The term “good faith”
24 means honesty in fact and the observance of reason-
25 able standards of fair dealing in the trade.

1 (10) OUTLET.—The term “outlet” means a
2 place of business from which a person offers prod-
3 ucts or services for sale to another person.

4 (11) TRADE SECRET.—The term “trade secret”
5 means information known to a franchisor or its affil-
6 iate, including a formula, pattern, compilation, pro-
7 gram, device, method, technique, or process, that—

8 (A) derives actual or potential independent
9 economic value from not being generally known
10 to, and not being readily ascertainable by prop-
11 er means by, another person who can obtain
12 economic value from its disclosure or use; and

13 (B) is the subject of efforts to maintain its
14 secrecy that are reasonable under the cir-
15 cumstances.

16 (12) TRANSFER.—The term “transfer” refers
17 to a change in ownership or control. Such term shall
18 not include any of the events in which a franchisor
19 is prohibited from interfering by section 7(i).

20 (13) TRANSFERABLE INTEREST.—The term
21 “transferable interest” means—

22 (A) an interest in a franchisee or a
23 franchisor that is not an individual;

24 (B) a franchisee’s or a franchisor’s interest
25 in a franchised business; or

1 (C) a franchisee's or a franchisor's interest
2 in a franchise.

3 (14) UNITED STATES.—The term “United
4 States”, when used in geographical sense, means the
5 several States and the District of Columbia.

6 **SEC. 15. APPLICABILITY.**

7 This Act shall apply to—

8 (1) a franchise or an interest in a franchise
9 that is entered into, renewed, transferred, assigned,
10 amended, or replaced on or after the date of the en-
11 actment of this Act;

12 (2) a franchise of indefinite duration that is in
13 existence on the date of the enactment of this Act;
14 and

15 (3) a franchisee, franchisor, franchised busi-
16 ness, or other person subject to a franchise described
17 in paragraph (1) or (2).

18 **SEC. 16. NONPREEMPTION.**

19 This Act shall not prevent the establishment, continu-
20 ing in effect, or enforcement of a law of any of the several
21 States or the District of Columbia, except to the extent
22 the law is inconsistent with this Act.

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