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## Disclosure Acknowledgment Statements - the Importance of "None"

Renewal season is an especially appropriate time to share a recent victory highlighting the importance of disclosure acknowledgement statements in the franchise sales process. What may seem like tedious paperwork can have huge implications if the franchise relationship later sours.

In *Fantastic Sams Salons Corp. v. PSTEVO, LLC*, 2016 U.S. Dist. LEXIS 5590 (N.D. Ill. Jan. 15, 2016), an underperforming franchisee abandoned two franchised businesses just a few years into the franchise agreements' ten-year terms. The franchisor filed a lawsuit seeking past due amounts owed and lost future royalties, and the franchisee asserted counterclaims for, among other claims, fraud. The franchisee alleged that the FDD suggested (and franchisor's representatives allegedly confirmed) that the franchisee would break even after just three months in operation.

A tortured interpretation of Item 7—not anything in Item 19—served as the basis for this claim. The franchisee alleged that Item 7's disclosure of estimated additional funds that a typical franchisee may need for the first three months of operations implied that the stores would break even after that initial three month period.

In dismissing franchisee's fraud counterclaim, the court relied entirely on the franchisee's disclaimer of "any oral, written or visual claim or representation" concerning "sales, income, or profit levels" and its confirmation of that disclaimer in a disclosure acknowledgement statement. The franchisee's counterclaim, the court held, was clearly premised on the assertion that the franchisor misrepresented profit levels, *i.e.*, that the franchisee could expect to be profitable three months after opening. Therefore, the court ruled, the franchise agreement's express disclaimer and the franchisee's confirmation of it in the disclosure acknowledgement statement barred the fraud claim as a matter of law.

The crucial point here is that the franchisor saved substantial time and money by not having to conduct discovery on the fraud issue and also reduced its potential damage exposure simply by providing the court a basis on which to dismiss, at the outset, the franchisee's fraud claim. This case serves as a good reminder of the benefits of (1) including adequate disclaimers in your form franchise agreements and disclosure acknowledge statements and (2) maintaining safeguards to ensure that those forms are properly executed for every franchise sale.

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Cheng Cohen LLC represents Fantastic Sams Salons Corp. in this case.

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