

FRANCHISING AND FRANCHISE LAW

The D.C. Bar
Continuing Legal Education Program

February 22, 2007

Copyright © 2007 Nicholas G. Karambelas
All Rights Reserved

Presented By:

Nicholas G. Karambelas, Esq.
Sfikas & Karambelas, LLP
1201 Pennsylvania Avenue, N.W. Suite 300
Washington, D.C. 20004
Tel. (202) 661-4614
FAX (202) 363-2882
E-Mail: nick@ngklaw.com

FACULTY

Nicholas G. Karambelas is a founding partner of Sfikas & Karambelas, LLP with offices in Washington, D.C., Baltimore, Maryland, New York City, New York and affiliated offices in Montreal Canada and Athens, Greece. He practices in the areas of business entity organization, international law and business transactions, e-commerce, securities, franchising and appellate litigation. He has written numerous articles on corporate, commercial and transactional law and has authored a three-volume treatise entitled “Limited Liability Companies: Law, Practice and Forms” published in its second edition by Thomson West Company. He is writing a treatise on international business transactions which will be published by Thomson West company in the spring of 2007. He participated in the drafting of the District of Columbia Limited Liability Company Act of 1994 and drafted the Limited Liability Company Amendment Act of 2000. He is admitted to practice law in New York, Washington, D.C., Maryland, the federal courts and the Supreme Court of United States.

Mr. Karambelas holds a Bachelor of Arts from Union College, a Juris Doctor from Fordham University School of Law and a Master of International Affairs (M.I.A.) from Columbia University School of Public and International Affairs. He was elected as Secretary of the D.C. Bar and served for 2004-2005. He is a member of Publications Committee of the D.C. Bar and the Mandatory Continuing Legal Education Committee of the New York State Bar Association. He served as Co-Chair of the Continuing Legal Education (CLE) Committee of the D.C. Bar and teaches numerous CLE courses. He is an arbitrator for the Superior Court of the District of Columbia. Mr. Karambelas chairs the American Hellenic Lawyers’ Society of Greater Washington, D.C.

AGENDA

Page

TAB 1

FRANCHISING IN PERSPECTIVE..... 5

TAB 2

THE FRANCHISOR - FRANCHISEE RELATIONSHIP..... 8

- I. The Word “Franchise”
- II. Statutory Definition of a Franchise
- III. Factors Supporting the Existence of a Franchise Relationship
- IV. Franchises Distinguished from Other Legal Relationships
- V. Fiduciary Duty Between Franchisor and Franchisee

TAB 3

FTC FRANCHISE RULE..... 14

- I. Significant Provisions of the Revised FTC Franchise Rule - 16 CFR Part 436
- II. Penalties for Violations

TAB 4

STATE FRANCHISE REGULATION..... 19

- I. Registration
- II. Disclosure But No Registration; Mandated Termination/Non-Renewal Provisions
- III. Exemption from Registration

IV. Penalties for Violation

V. Antitrust Issues

TAB 5

UNIFORM FRANCHISE OFFERING CIRCULAR (UFOC). 25

I. Time for Providing UFOC and Agreements

II. Contents of the UFOC

III. Negotiated Franchise Agreements

IV. Liability of Controlling Person for UFOC

V. Professional Liability for UFOC

TAB 6

THE FRANCHISE AGREEMENT. 34

I. Know the Business of the Franchise

II. Organization of the Written Contract

TAB 7

FRANCHISING AND THE INTERNET. 43

I. Offers of Franchises Over the Internet

II. Revised FTC Franchise Rule on Electronic Disclosure

III. “Cybersquatting” on Franchisor’s Domain Name

TAB 8

INTERNATIONAL ASPECTS OF FRANCHISING..... 46

I. Extra-Territorial Application of U.S. Franchise Laws

II. Franchising in the European Union (EU) and Other Countries

III. UNIDROIT - Guide to Master Franchise Agreements and Model Franchise Disclosure Law

TAB 9

CONTRACT DRAFTING TECHNIQUES..... 49

TAB 10

PRINCIPLES OF INTERPRETING CONTRACTS. 56

TAB 11

SAMPLE FRANCHISE AGREEMENT..... 62

TAB 12

SAMPLE UFOC..... 106

TAB 1

FRANCHISING IN PERSPECTIVE

FRANCHISING IN PERSPECTIVE

In its current form, franchising is a relatively new form of legal relationship. The modern era of franchising dates only from the mid-1960s. Yet, franchising has become an enormous component of the Gross Domestic Product (GDP) and grows in its significance to the national economy in each year. The International Franchise Association (IFA), which is the industry trade association, estimates that there are more than 300,000 franchised operating in the United States, generating \$1 trillion in revenues and employing 8 million people. While there are a number of franchisors with hundreds even thousands of franchisees, over 80% of all franchisors have 50 or less franchisees.

It is inaccurate to refer to franchise law as a legal “specialty”. Franchising is actually a trans-disciplinary area of law. The franchise relationship involves antitrust law, commercial contracts, business organization, consumer protection, bankruptcy, intellectual property, litigation, secured interests, real estate and taxation. The aspect of franchising that may properly be considered a “specialty” is the international, federal and state regulation of the franchise relationship. By the late 1970s, due to the disparate bargaining positions between the franchisor and the franchisee, abuses in the franchisor-franchisee relationship developed. These abuses came to the attention of the Federal Trade Commission (FTC) as well as state regulators. The FTC and many states promulgated rules and legislation that were meant to balance the bargaining positions and, thereby, prevent at least the most flagrant abuses. Consequently, the offer and sale of franchises are actually more highly regulated than the offer and sale of securities. While the fundamental policy underlying the securities law and regulations is to cause issuers to fully disclose all material aspects of an investment, the fundamental policy underlying the franchise laws is to enable franchisees to determine whether the purchase and operation of a franchise is a “good” investment.

The primary responsibility of an attorney who acts as franchise counsel is to:

- A. Recognize a legal relationship that is a franchisor-franchisee relationship and implicates a government regulatory scheme,
- B. Know which government authorities regulate franchises and the regulatory scheme that each such authority administers, and
- C. Advise the client as to compliance with the applicable regulatory scheme.

TAB 2

THE FRANCHISOR - FRANCHISEE RELATIONSHIP

THE FRANCHISOR - FRANCHISEE RELATIONSHIP

I. The Word “Franchise”

The root of the word “franchise” is the Germanic word “frank” which meant free in the sense that in medieval Frankish Gaul, only men who were Franks as opposed to conquered peoples were free, *i.e.*, able to own property, bear arms and have the right of descent. The word “frank” was imported into English and came to mean free in the sense of being liberal or generous. The word evolved into “franchise” which came to mean a royal privilege granted to a subject by the crown. The term “franchise” came to mean either a political franchise which was the right to exercise political rights or a commercial franchise which was the right to use the property of another for commercial purposes.

There are two types of commercial franchises: public franchises and private franchises. A public franchise is a right granted by a government authority to a private entity to perform on a commercial basis a function that is otherwise a government function. Cable television, ambulance service, recycling services are examples of public franchises. A private franchise is the right granted by a private entity to another private entity to use property owned by the former private entity for a commercial purpose in exchange for a fee or percentage of revenues.

II. Statutory Definition of a Franchise

Only a legal relationship that constitutes a franchise relationship is subject to regulation under the franchise statutes. Therefore, it is essential to understand the legal definition of a franchise as well as the legal nuances of the term. Every legal relationship that is a franchise relationship must comply with the FTC Franchise Rule and any applicable state franchise laws and regulations. The mere fact that parties did not intend or even expect to form a franchise relationship will be irrelevant in an

enforcement action if the relationship satisfies the definition of a franchise.

The term “franchise” is a defined statutory term. The definition is a functional definition that examines the legal and financial terms of the relationship and the conduct of the parties. Refraining from using the terms of a franchise will not exclude a particular relationship from the franchise regulatory scheme if the substance of the relationship satisfies the definition of a franchise. Although the statutory definitions differ somewhat from state to state and between and among the states and the FTC Franchise Rule, each of these definitions contains, at a minimum, the following elements:

- A. The franchisor grants the right to use intellectual property in combination with a business method or format such that part of the bargained for exchange that the franchisee receives is a certain brand identification.
- B. The franchisor maintains a measure of quality control and uniformity over the products or services offered for sale by the franchisee as a result of the use of the franchisor’s property or method by the franchisee.
- C. The franchisor provides assistance to the franchisee in the form of common buying arrangements, site location or cooperative advertising.
- D. The franchisee pays a fee to the franchisor that is not a *de minimus* fee. The FTC Franchise Rule and most state statutes define a *de minimus* fee as a fee that is \$500.00 or less.

III. Factors Supporting the Existence of a Franchise Relationship

In determining whether a particular legal relationship satisfies the foregoing elements, courts and regulators will consider the following factors:

- A. Whether the franchisees pays fees on a continuing and regular basis,
- B. The nature and extent of quality control that the franchisor exercises over the franchisee’s operation,
- C. The nature and extent of the disparity of the positions between the franchisor and the franchisee,

- D. Whether the franchisee has made a significant investment in the franchise such that the franchisee would stand to lose the investment if the relationship with the franchisor was terminated,
- E. Whether within the scope of the quality control exercised by the franchisor, the franchisee exercises the incidents of ownership and proprietorship.

IV. Franchises Distinguished From Other Legal Relationships

A. Distributorships

An exclusive right to distribute products or services within a specified geographical area or demographic segment is not a franchise relationship as long as the owner does not control the method or means of distribution. However, where the distributor is granted the right to use the owner's trademark or associate that trademark with the general business of the distributor, then a franchise relationship may arise, *In re Matterhorn Group*, 2000 WL 1174215.

B. Trademark or Tradename License

The primary difference between a license and a franchise is the extent to which the licensor exercises quality control over the activities of the licensee. A license that does not involve the right to use a trademark or a common business format will rarely be deemed a franchise. A license that involves the right to use a trademark or common business format will always risk being deemed a franchise because a certain but indeterminate amount of control is implied in any right to use a trademark, *Dawn Donut Co. v. Hart's Food Stores, Inc.*, 267 F.2d 358 (2d. Cir.1959).

C. Partnerships and Joint Ventures

A partnership is defined as an agreement between 2 or more persons to engage in a business for profit. A joint venture is a partnership that lasts for a limited time or to accomplish a specified business purpose. A partnership will rarely be deemed a franchise because the partners exercise joint

ownership over the assets of the partnership and are jointly liable for the debts and liabilities of the partnership. Under a franchise, the franchisee and not the franchisor owns the business assets and the franchisor is not liable for the debts and liabilities incurred by the franchisee.

D. Brokers and Sales Agents

Brokerage and agency agreements will rarely be deemed franchises because brokers and agents act either on behalf of a principal or on behalf of the transaction in exchange for a commission. The commission is usually a percentage of the value of the transaction and is paid only if the transaction is completed. A broker or an agent does not pay a continuing and regular fee.

E. Business Opportunity Ventures

Business Opportunity ventures are essentially enhanced distributorship arrangements. Such ventures are generally prepackaged business deals offered mainly to novice entrepreneurs through some form of public advertising. Such ventures include sale of vending machines, pay telephones, telephone cards, amusement devices and “work at home with your computer” deals. Although these ventures are not franchises, they are regulated by the FTC and many states in the same manner as franchises but under a separate regulatory scheme.

VI. Fiduciary Duty Between Franchisor and Franchisee

A fiduciary duty in a legal relationship means that the parties owe such duties of trust and confidence that are not owed by parties dealing in an “arms-length” relationship. Fiduciary duties are not implied in the franchise relationship, *McDonald’s Corp. v. Hinkman et al.*, 1999 WL 441468 (EDNY, 1999).

VI. Other Forms of Franchisor - Franchisee Relationship

A. Area Development Franchise

The franchisor grants to the franchisee the right (usually exclusive) to establish and open a specified number of units within a defined geographic area over a defined period of time in exchange for an initial fee and a percentage of the gross revenues on a recurring basis. The franchisee either executes a franchise agreement for each unit or the franchise relationship is governed by single development agreement.

B. Subfranchising

The franchisor grants to the subfranchisor the right (usually exclusive) to offer and sell franchises within a defined geographic area for a defined period of time in exchange for an initial fee and a percentage of the gross revenues on a recurring basis. The subfranchisor usually has the same rights and obligations as the franchisor although the franchisees are and remain the franchisees of the franchisor.

C. Area Representative Franchise

The representative acts essentially as a franchise broker or agent for the franchisor and is compensated based on a percentage of gross revenues.

D. Co-Branding

The franchisor grants the franchisee of another franchisor (referred to as the host franchisor) the right to the business of the franchisor in or alongside the business of the host franchisor.

TAB 3

FTC FRANCHISE RULE

FTC FRANCHISE RULE

The Federal Trade Commission (FTC) Franchise Rule was promulgated in 1979 to regulate the offer and sale of franchises, *16 C.F.R. Part 436*. Note the FTC Franchise is cumulative with but does not pre-empt or displace any state laws or regulations. Where the state law or regulation is more stringent than the FTC Franchise Rule, the state law or regulation will prevail within the jurisdiction of that state. Where the state law or regulation is less stringent than the FTC Franchise Rule or where a state has no such law or regulation, the FTC Franchise Rule will prevail.

In 1995, the FTC commenced a review of the Franchise Rule. After determining that fundamental changes were necessary, the FTC initiated a rulemaking process. In 1999, the FTC published a Notice of Proposed Rulemaking and a draft of proposed changes to the Franchise Rule. In August, 2004, the FTC issued a report prepared by its staff which sets forth recommendations on how the Franchise Rule should be revised. On January 23, 2007, the FTC announced that the revised Franchise Rule was final and will take effect on July 1, 2007. Franchisors may voluntarily comply the Franchise Rule after that date. After July 1, 2008, every franchisor must comply with the rule. The Final Franchise Rule is available at www.ftc.gov.

In concept and purpose, the FTC Franchise Rule defines the franchise relationship, obligates franchisors to provide prospective franchisees with a written document which contains certain mandated disclosures and enables the FTC to impose penalties on franchisors for failing to comply with the disclosure requirements.

I. Significant Provisions of the Revised FTC Franchise Rule - 16 CFR Part 436

A. Non-Disclosure Documents Revisions

1. Franchises and Business Opportunity Offers - The Franchise Rule applies only to sales of

franchises sales and not to business opportunity sales. Business opportunity sales are governed by a separate rule set forth in 16 CFR Part 437.

2. No International Application - The Franchise Rule applies only to domestic franchise sales and not to international franchise sales.

3. Time to Deliver Disclosure Document - Eliminates the requirement to provide disclosure at the first personal meeting and require franchisors to provide disclosure at least 14 calendar days before the execution of the franchise agreement or other binding agreements or payment of any fees in connection with the franchise sale.

4. Pre-Signing Contract Review Period - Eliminates the contract review period entirely, unless the franchisor has materially altered the terms and conditions of the standard contract attached to the disclosure document and such changes were not requested by the prospective franchisee. In which case the franchisor must deliver the completed franchise agreement 7 calendar days before execution.

5. Liability of Third-Party Brokers and Franchisor Employees - Franchisors and brokers jointly and severally liable for content of the FOC only if they either directly participated in drafting or were authorized to control content.

B. Disclosure Document Revisions

1. Uniform Franchise Offering Circular (UFOC) Guidelines - Conforms the disclosure requirements of the Franchise Rule with the UFOC Guidelines.

2. Litigation by Franchisor Against Franchisees - Must disclose litigation by franchisor to enforce franchise agreements.

3. Earnings Claims - Earnings claims need only be reasonable.

4. Outlets and Franchisee Information - Must disclose the following for each of the last 3 fiscal years:

- a. the status of a franchisor's system, including the number of franchised and company-owned outlets at the beginning and end of each of the last three fiscal years, and the total net change;
- b. transfers in each state;
- c. the turnover rate of franchised outlets, including the number of franchised outlets at the beginning of the year, new outlets opened, terminations, non-renewals, reacquisitions by the franchisor, outlets that ceased to do

business, and outlets at the end of the year;

- d. the turnover rate at company-owned stores, including the number of company-owned outlets at the beginning of the year, new outlets, reacquired outlets, closed outlets, outlets sold to franchisees and outlets open at the end of the year;
- e. projected openings and the number of franchise agreements signed in the previous year where a store has not yet been opened;
- f. For each existing unit, franchisor must give to the prospective franchisee a history of that unit for the last three fiscal years, including the names, addresses, and telephone numbers of each previous owner and the reasons for the change in ownership.

5. Confidentiality Agreements - If a franchisee signed a contract containing a confidentiality clause in the last 3 fiscal years, the franchisor must provide a statement alerting prospective franchisees to the fact that some franchisees may not be able to speak openly with prospects because of these clauses. The franchisor must provide the number and percentage of current and former franchisees who have signed confidentiality provisions and the circumstances under which the provisions were signed.

6. Financial Statements of Parent and Subfranchisor - The parent of a franchisor must disclose its financial statements if the parent either commits to perform post-sale obligations for the franchisor or if the parent guarantees the obligations of the franchisor. Subfranchisors must disclose financial statements where subfranchisor acts as a franchisor in selling franchises and in performing post-sale obligations.

7. Audited Financial Statements - Financial statements must be prepared according to US GAAP or as permitted by the SEC, subject to any future government mandated accounting principles.

8. New Exemptions from Rule - The following transactions are exempt from the Franchise Rule:

- a. Petroleum marketers
- b. The large investment exemption - total investment made in acquiring the franchise totals at least \$1 million, excluding the cost of real estate and excluding any financing provided by the franchisor.
- c. The large franchisee exemption - franchise sales to an entity that has been in business for at least five years and has a net worth of at least \$5 million including affiliated entities.

- d. The officer, owner and manager exemption - sales to owners, operators and those with direct management experience over a franchise system when the owner, operator or manager purchases an outlet from such franchisor as long as the prospective franchisee has been employed by the franchisor for at least 2 years, and the relationship between the franchisor and prospective franchisee has existed within 60 days of the sale.

II. Penalties for Violation

The FTC is empowered to seek injunctions, asset freezes, civil penalties and monetary redress.

The FTC can also seek remedies against individuals who are responsible for violations and impose personal liabilities on such persons. The Franchise Rule does not authorize private actions to enforce the Rule.

TAB 4

STATE FRANCHISE REGULATION

STATE FRANCHISE REGULATION

Prior to 1979, the states generally relied on their consumer protection statutes to redress any abuses by franchisors. Recognizing that such statutes were inadequate, all states have enacted some form of franchise regulation. There are generally two types of regulatory schemes: one, disclosure and registration and, two, disclosure, no registration but mandated termination/renewal provisions. About 14 jurisdictions require that a franchisor doing business in the jurisdiction or offering franchises in the jurisdiction must register the disclosure document with the attorney general of the jurisdiction. The rest of the jurisdictions require that a disclosure document be provided but it need not be registered and that a franchise can only be terminated or renewed as mandated by statute.

I. Registration

Maryland (Md. Code Business Regulation, tit. 14, §§ 14-201 - 14-233), Virginia (Va. Code tit. 13.1, §§ 13.1-557-13.1574; tit.59.1, §§ 59.1-196-59.1-207) and New York (McKinney's General Business Law Art.33, §§680-695) are among the 15 states that require a franchisor which offers franchises in the state or who is located in the state to register or submit a disclosure document with the state attorney general's office. In Maryland and Virginia, a disclosure document that satisfies the UFOC requirements will satisfy their respective statutes. Although New York generally accepts the UFOC, New York has certain additional requirements. The District of Columbia does not have any franchise related statute so that only compliance with the FTC Franchise is required in the District of Columbia.

The franchisor is prohibited from offering or selling any franchises in those states until the disclosure document has been accepted for registration. In this respect a franchise is treated like a security. After the disclosure document is filed, the franchisor must amend it if there has been a

material change in the information contained in the registered disclosure document. The disclosure document must contain an audited financial statement for each of the past 3 consecutive fiscal years. Changes in financial statements are deemed to be material changes. Therefore, as a practical matter, the franchisor must amend its disclosure document at least once every 12 months and the amendment must be approved.

A franchisor may continue to offer franchises while the approval of an amendment to its disclosure document is pending. The franchisor may even sell franchises while the approval to an amendment is pending as long as the franchisor escrows any funds received from any franchisee, provides a copy of the amended disclosure document to the franchisee and provides a reasonable opportunity to the franchisee to rescind the sale.

II. Disclosure But No Registration; Mandated Termination/Non-Renewal Provisions

Most jurisdictions do not require a franchisor to register or submit its disclosure document. They expressly require either that the franchisor provide a disclosure document or coordinate with the disclosure provisions of the FTC Franchise Rule.

Many of these jurisdictions impose mandated termination provisions which require that the franchisee receive reasonable notice of termination and the cause for the termination. The term “cause” is defined as failure to renew at least 60 days prior to expiration, failure to substantially comply with the terms of the franchise agreement, lack of good faith in performing under the franchise agreement and voluntarily abandoning the franchise. The franchisee must also be afforded a reasonable opportunity to cure, *see e.g. New Jersey Code §56:10-1-10-7*. The District of Columbia had mandated termination/non-renewal provisions but they were repealed in 1998.

III. Exemption from Registration

The jurisdictions that require registration exempt certain franchisors and certain types of sales from registration. Generally, a franchisor is exempt from registration if it has a net worth on a consolidated basis of \$5 million or more according to its most recent audited financial statements or a franchisor with a net worth of \$1 million or more in according to its most recent audited financial statements and it at least 80% owned by a corporation that has a net worth on a consolidated basis of \$5 million or more according to its most recent audited financial statements. To qualify for the exemption, the franchisor must duly apply for the exemption and provide franchisees with substantially the same information as does a non-exempt franchisor. A franchisor that has a net worth of \$15 million need not apply for the exemption but still must provide the required information to franchisees.

Sales of franchises to banks or other financial institutions are exempt from registration. Isolated sales of franchises not made to as part of a plan of distribution are exempt. Sales not effected through a franchisor are exempt, *i.e.*, sales from a franchisee to another franchisee as long as the transferee franchisee receives the current disclosure document of the franchisor. Also, offers over the Internet are exempt under certain circumstances, *see TAB 7*.

IV. Penalties for Violation

The states are generally empowered to seek injunctions, asset freezes, civil penalties and monetary redress. The regulators can also seek remedies against individuals who are responsible for violations and impose personal liabilities on such persons. The statutes do not authorize private actions to enforce violations of the statute.

V. Antitrust Issues

In the typical franchise, the franchisor limits the geographical area in which a franchisee can operate, restricts the types or products or services a franchisee can offer and requires the franchisee to buy from approved sources. In such an arrangement, antitrust issues can easily arise. The courts have developed a substantial and complicated body of case law that adapts antitrust concepts to the franchise relationship.

A. Territory Restrictions

A requirement that the franchisee operate only within a specified territory is not a *per se* violation of the antitrust laws. Such territorial restriction will be analyzed to determine whether they are reasonable, *Continental TV Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977).

B. Restriction on Sale of Product and Services (Tie-Outs)

The franchisor may impose restrictions on the categories of products and services that a franchisee is permitted to sell as long as the restrictions are reasonably necessary to assure quality and to protect the business format of the franchisor, *Susser v. Carvel Corp.*, 332 F2d 505 (2d Cir.1964); *Mumford v. GNC Franchising LLC*, 437 F Supp 2d 344 (W.D. Pa. June 29, 2006).

C. Tying-In Arrangements

The franchisor may require a franchisee to sell only products licensed/approved by franchisor or produced from ingredients supplied by the franchisor as reasonably necessary to assure quality and to protect the business format of the franchisor. The franchisor may also require a franchisee to purchase from approved sources as long as the franchisor sets standards and specifications and that requirement is reasonably necessary to assure quality and to protect the business format of the franchisor. However, a franchisor cannot coerce a franchisee to simply sell the products of third

person to which the franchisor has no organic connection, *Atlantic Refining Co. v. FTC*, 381 U.S. 357 (1965); *F.F. Orthotics Inc. v. Joe Paul*, 2006 WL 1980270.

TAB 5

UNIFORM FRANCHISE OFFERING CIRCULAR (UFOC)

UNIFORM FRANCHISE OFFERING CIRCULAR (UFOC)

The UFOC was promulgated by the North American Securities Administrators Association (NASAA), www.nasaa.org, in an effort to standardize the disclosure requirements for franchisors who offer and sell franchises in more than one jurisdiction. Most if not all of the jurisdictions, including Maryland and Virginia, that require registration accept the UFOC although some jurisdictions like New York impose some additional requirements. Therefore, counsel must examine the disclosure requirements, which are usually contained in regulations rather than statutes, of each jurisdiction to be certain that the disclosure document satisfies the requirement for registration. Note that while the UFOC satisfies the disclosure requirements of the FTC Franchise Rule, a document that satisfies the FTC disclosure requirements does not satisfy the disclosure requirements of the jurisdictions that require registration. If the franchisor is or may be offering or selling franchises in any jurisdiction that requires registration, it should use the UFOC.

I. Time for Providing UFOC and Agreements

A. UFOC Guidelines and Original FTC Franchise Rule: The franchisor must provide the UFOC to the prospective franchisee at the earlier of :

1. The first personal meeting between franchisor or its agent and prospective franchisee, or
2. 10 business days prior to signing a binding franchise agreement, or
3. 10 days before a payment to franchisor or its agent.
4. The franchisor must provide a franchise agreement to the prospective franchisee containing all material terms at least 5 business days before execution.

B. Revised FTC Franchise Rule: The franchisor must provide the disclosure document at least 14 full calendar days before the franchisee does any one of the following:

1. Signs a binding franchise, or
2. Makes a payment to franchisor.
3. The franchisor must also provide the disclosure earlier than required in the negotiating process if the prospective reasonably requests the disclosure document.
4. The franchisor must provide to the prospective franchisee a complete franchise agreement at least 7 full calendar days before franchisee executes the agreement.

II. Contents of the UFOC

The UFOC lists 23 Items, each of which consists of a description of certain types or categories of information that the UFOC must contain. The disclosure document should be arranged so that each Item is addressed. If the franchisor has no information that responds to a particular Item or an Item is not relevant, the UFOC should affirmatively so state. The following list is a summary of the information required under each Item. Refer to the UFOC and the state regulations for a complete description of the information required under each Item. In those Items for which the FTC Franchise Rule adds requirements, a summary of that requirement is preceded by **FTC Rule**.

Item 1

Description and identity of the franchisor, business organization, franchisor's experience, predecessors and affiliates. **FTC Rule:** In addition, disclose any parent of franchising subsidiary but not business experience unless parent is also franchisor or provides products/services to franchisees and disclose any competition franchisee may encounter from any business in which officer of franchisor owns an interest.

Item 2

Names, titles, positions of persons who have management responsibility for the franchisor.

FTC Rule: No disclosure of franchise brokers required.

Item 3

Civil and criminal litigation history of franchisor and its principals. **FTC Rule:** Franchisor must disclose litigation by franchisor against franchisees and litigation history of parent or affiliate involved in franchising.

Item 4

Bankruptcy history of franchisor, its principals and affiliates. **FTC Rule:** Subsidiary franchisor must disclose bankruptcy history of parent.

Item 5

Description of initial franchise fees to be paid before franchise operates, if they are deferred, when they are paid, whether any franchise fees are refundable and, if so, the terms of any refund.

Item 6

Description of any continuing franchise fees such as royalties, how calculated, when paid, whether refundable.

Item 7

Description in tabular form of the total investment that franchisee must make in order to open the franchise such as real property/construction costs, equipment/fixtures, initial inventory, to whom money is paid, whether refundable, whether financed by franchisor.

Item 8

Description of obligation of franchisee to purchase goods and services from franchisor or

franchisor approved sources. Include the interest, if any, of any principal of franchisor in any third party supplier.

Item 9

Description in tabular form the principal obligations of franchisee under the franchise agreement and cross cite to franchise agreement.

Item 10

Description of financing arrangements offered by franchisor.

Item 11

Description of franchisor's obligations such as site selection, training, assistance during operation, required computer systems time for commencing operations. If training is offered or required, describe training course. Include in as an appendix the table of contents of the training manual.

Item 12

Description of exclusive territory, if any. **FTC Rule:** In addition, description of any restriction on operating outside territory, competition from Internet or catalog sales and, if no exclusive territory, affirmatively so state.

Item 13

Description of trademarks or service marks.

Item 14

Description of patents and copyrights.

Item 15

Description of obligation of franchisee to personally participate in or operate the business of the franchise.

Item 16

Description of restrictions on products sold, customers, sources.

Item 17

Description in tabular form with cross references to the franchise agreement of the terms of termination, renewal, transfer and dispute resolution. **FTC Rule:** Define renewal and, if applicable, that franchisor may require different terms in renewal franchise agreement.

Item 18

Description of arrangements with public figures.

Item 19

Description of earnings claims, basis for claims, supplemental claims for particular locations. **FTC Rule:** Information regarding a franchisee's prospective costs or expenses, standing alone, is not an earnings claim. Franchisors may disclose to prospective franchisees expense or cost information even though they make no earnings claim. Franchisors must state as follows- (i) the Franchise Rule permits franchisors to disclose financial performance in their disclosure documents if they so choose and (ii) if no earnings claim, that no earnings claim is made and warn prospective franchisees not to rely on any unauthorized earnings claim they may otherwise receive.

Item 20

Number and locations of franchisees, terminations, cancellations, non-renewals, re-acquisitions within the last 3 years. **FTC Rule :** The information must be arranged in 5 separate tables stating number of units in the network; number of transfers over the past three years; turnover rate of franchised outlets; turnover rate of company-owned units; and, projected openings. Disclose use of "confidentiality clauses" prohibiting franchisees from discussing with prospective franchisees

the experiences with franchisor. Disclose all franchisee associations that the franchisor endorses or supports or ask to be included in the disclosure document.

Item 21

Audited financial statements of franchisor (income and balance sheets) for each of the past 3 years. **FTC Rule:** Include subfranchisors' financial statements and parent financial statements if parent performs post-sale obligations or guarantees the performance of subsidiary franchisor. Financial statements must be prepared according to United States generally accepted accounting principles ("GAAP") unless otherwise permitted by the Securities and Exchange Commission.

Item 22

Each agreement that the franchisee is expected to execute including leases, notes, development agreements.

Item 23

Detachable receipt evidencing fact that franchisee received the UFOC.

III. Negotiated Franchise Agreements

The whole purpose of the UFOC and the registration of the UFOC is to assure that the franchise "deal" is fully disclosed to the franchisee before the franchisee is bound by the franchise agreement. This purpose raises the question of whether the terms of a franchise agreement with a particular franchisee can be negotiated such that the negotiated terms deviate from the terms set forth in the registered UFOC. Virginia and Maryland recognize the right of franchisors and franchisees to negotiate the terms of a particular franchise without requiring the franchisor to amend its UFOC in each instance.

New York took the opposite view and prohibited a franchisor from deviating at all from the

terms of the franchise contained in the registered UFOC. This position was rejected by the court which interpreted the New York disclosure law as permitting negotiated franchise agreements as long as the basic disclosures as to the identity, experience and business of the franchisor and the franchise are accurate, *Southland Corporation v. Abrams*, 560 N.Y.S.2d 253 (Sup.1990).

For further reading on preparing the UFOC see Morton, *Tips from leading Regulators on How to Speed Franchise Registrations*, 22 Franchise L.J. (Summer, 2002).

IV. Liability of Controlling Person for UFOC

If the UFOC is false, misleading or lacks information required by law, an aggrieved franchisee can usually assert common law causes of action such as fraud, negligent misrepresentation and breach of contract against the franchisor. The states take different approaches to whether and the circumstances under which a controlling person of a franchisor can also be liable. A franchisor is rarely an individual and is usually an entity. The issue is whether the officers/directors of a franchisor-corporation, the managers of a franchisor-limited liability company or the partners of a franchisor-partnership as well as an employee are liable in addition to the entity. The New York statute has been interpreted to require that the controlling person must “materially aid” in the conduct that gives rise to the improper disclosure, *A.J. Temple Marble v. Union Carbide Care*, 87 N. Y. 2d 574 (N.Y. 1996); General Business Law Art 33, Sec. 691(3). The California statute, while almost identical to the New York statute, has been interpreted to impose presumptive liability on the controlling person and require that person to affirmatively demonstrate the he or she did not “materially aid” in the conduct that gives rise to the improper disclosure, *Eastwood v. Froehlich*, 131 Cal. Rptr. 577 (Cal. 1976).

V. Professional Liability for UFOC

Increasingly, franchisees have asserted causes of action against persons who participated in drafting the UFOC – usually the attorney or the CPA. Traditional common law contract doctrine required that parties had to be in privity of contract to sustain a cause of action of breach of contract or negligence. At least one court has held that a franchisee can assert the same causes of action against an attorney of a franchisor as it can against a franchisor, *Courtney v. Waring*, 237 Cal. Rptr. 233 (Cal. App. 4 Dist, 1987). The court held only that the complaint stated a cause of action for negligence but did not find that the attorneys were liable to the franchisees, see Meikeljohn, “UFOCs and Common Law Claims against Franchise Counsel for Negligence” 25-FALL Franchise L.J. 45 (2005).

TAB 6

THE FRANCHISE AGREEMENT

THE FRANCHISE AGREEMENT

I. Know the Business of the Franchise

The single most important skill in contract drafting is knowing the subject matter of the contract. Before even drafting a word of a contract the attorney must be satisfied that he or she has at least a working knowledge of the subject matter of the contract. Most often, such working knowledge can be obtained through discussions with the client. Clients may not always see the value of “educating” their attorneys as to the subject matter of the contract. However, it will be quite difficult to write an effective contract and work out solutions to contingencies unless the attorney is familiar with the subject matter.

II. Organization of the Written Contract

A. Identify Parties and Capacities

The contract should reflect on its face the identity of the parties and the capacity in which they undertake the obligations under the contract. While this may be simple where the parties are individuals, but it can become complicated where the parties are actually levels of corporate bureaucracy or government agencies.

1. Private Entity- Is the party a parent corporation/LLC or a subsidiary or affiliate of a parent corporation/LLC? If the party is a subsidiary or affiliate, does it have the authority to bind the parent for performance or payment?
2. Partnership- If the party is a partnership and the partnership is governed by the Revised Uniform Partnership Act (RUPA), is a statement of authority or statement of

denial on file with respect to the individual negotiating and signed on behalf of the partnership? (see *D.C. Code §33-153.3 and 153.4*).

3. Government Agency or Instrumentality -If the party is a government agency or instrumentality, it has the authority to enter into contracts only if that authority is set forth in the enabling legislation creating the agency or instrumentality.

B. Terms and Conditions; The “Bargained For” Exchange

The “bargain-for” exchange is the heart of the contract. It must be articulated as clearly and in as much detail as possible. The following is a list of items that should be considered in drafting the “bargained-for” exchange for a franchise:

1. Description of the Business of the Franchise - Business Format
2. Site Location and Approval - Holding the Real Estate
3. Term of Franchise
4. Initial Franchise Fee
5. Recurring Franchise Fee - Formula
6. Exclusive Territory
7. Restrictions on Categories of Products/Services Offered
8. Restrictions on Purchase of Products/Services/Equipment/Ingredients/Sources
9. Proprietary Marks - Domain Names

10. Reports, Records and Documentation
11. Right to Estimate Sales - Placement of Observer
12. Training
13. Insurance Requirements
14. Non-Compete Covenant
15. Maintenance and Protection of Business Format
16. Termination - Renewal - Extension
17. Definition of Event in Default, Curing Event in Default
18. Consequences of Failing to Cure Event in Default
19. Remedies, Limitation on Liability, Liquidated Damage
20. Holds Harmless and Indemnification
21. Terms of Transfer or Assignment
22. Personal Guaranty of Performance - Payment

C. Contract Governance

The contract governance provisions set forth the basic “legal ground rules” by which the legal relationship created by the contract is to be conducted. Including governance provisions in the contract will generally avoid the application of many default provisions/principles in contract law. The following is a list of governance provisions that should be considered for every contract. There are numerous permutations on the principles contained in each provision. However, if the attorney chooses not to include one or more of the following governance provisions, he or she should be able to articulate a reason for not including any such provision.

1. Independent Contractors. The Parties are strictly independent contractors. The FRANCHISEE is not, in any way, an employee, partner, joint venturer or agent of FRANCHISOR. A shall not, in any way, bind FRANCHISOR to any person unless FRANCHISEE has received the written consent of FRANCHISOR. FRANCHISEE shall undertake all reasonable measures in its operation to inform Third Parties that FRANCHISOR has no direct or indirect liability for any act or agreement taken by FRANCHISEE and that FRANCHISOR does not control the performance of FRANCHISEE. The FRANCHISOR has no fiduciary duties to the FRANCHISEE.

2. Strict Compliance. No failure of a Party to exercise any right or to insist upon strict compliance by the other Party with any obligation and no custom or practice of the Parties at variance with this Agreement shall constitute a waiver of the right of a Party to demand exact compliance. Waiver by one Party of any particular default by the other Party shall not affect or impair a Party's rights in respect to any subsequent default of the same or of a different nature, nor shall any delay or omission of a Party to exercise any rights arising from such default affect or impair the rights of that Party as to such default or any subsequent default.

3. Severability and Independent Covenants. If any covenant or other provision of this Agreement is invalid, illegal or incapable of being enforced by reason of any rule of law, administrative order, judicial decision or public policy, all other conditions and provisions shall remain in full force and effect. No covenant shall be deemed dependent upon any other covenant or provision unless so expressed in this Agreement.

4. Governing Law and Forum. The terms of this Agreement shall be governed exclusively by the Laws of the State of _____, not including the law on conflicts of law, and the rules, regulations and procedures of agencies of the State of _____. Any dispute arising from this Agreement that is not resolved through Arbitration shall be resolved only in the Courts and regulatory agencies of or in the State of _____.

5. Full Agreement and Merger. The terms and conditions of this Agreement constitute the full and complete agreement between the Parties. No other verbal or written agreement shall, in any way, vary or alter any provision of this Agreement unless both Parties consent to vary or alter any provision of this Agreement in a signed writing. This Agreement is intended to be an integrated writing and any prior oral or written agreements between the Parties are merged into this Agreement and extinguished. No custom, industry standard or course of dealing between the Parties shall in any way vary or alter the terms and conditions of this Agreement.

6. Jointly Drafted. This Agreement shall be deemed to have been drafted by both Parties and, in the event of a dispute, shall not be construed against either party. OR Each Party waives the defense of *contra proferentum*.

7. Waiver of [Equitable] Remedies. The Parties waive all [equitable] remedies including equitable rescission and rescission at law.

8. Bankruptcy. If, at any time, [a Party] seeks the protection of the U.S. Bankruptcy Act of 1978, as amended, or any applicable state bankruptcy law and:

- a. Has a receiver in equity appointed for its property requests or consents to the appointment of a receiver, or
- b. Has a trustee in reorganization appointed for its property, or
- c. Files a voluntary petition for reorganization or arrangement, or
- d. Files a voluntary petition in bankruptcy, or
- e. Files an answer admitting bankruptcy or agreeing to a reorganization or arrangement, or
- f. Makes an assignment for the benefit of its creditors,

then this Agreement shall expire. Any payments due from the bankrupt Party to the other Party under this Agreement shall be deemed an administrative expense under 11 U.S.C. § 503. This Paragraph shall not apply in the event of a withdrawal or discharge of any petition that occurs within 45 days of the date on which any such petition is filed.

9. Further Assurances. If requested by one Party, the other Party shall execute and deliver such other documents and take such other action as may be necessary to effect the terms of this Agreement.

10. Arbitration. Any controversy or claim arising out of, incident or related in any way to this Agreement or the breach of this Agreement shall be submitted to and resolved by to the American Arbitration Association (AAA) in accordance with its Commercial Arbitration Rules and at its office located in the _____. The resolution of the AAA shall be binding on the Parties and either Party may enter any judgment or award rendered by the AAA in any court of competent jurisdiction.

- A. Each Party shall be subject to the personal jurisdiction of the courts located in _____ and waives the right to assert lack of personal jurisdiction in any legal proceeding.
- B. Each Party shall bear any cost imposed on that party by the AAA. The Parties share equally any cost imposed on both parties by the AAA.
- C. Each Party shall bear its own attorneys' fees. The arbitrator shall not order nor have the power to order a Party to pay or reimburse the other Party for attorneys' fees, expert fees or any other fees incurred in connection with,

preparing, presenting or defending its case.

- D. The arbitrator shall not award nor be empowered to award punitive or exemplary damages.
- E. The arbitrator shall not nor have the power to grant any form of injunctive relief.
- F. The arbitrator shall award interest on a money damage award. Interest shall be calculated at _____% or the rate imposed on judgments by the courts of or in _____. Interest shall begin to accrue on the date on which the breach or injury occurred and continue to accrue on a compounded/non-compounded basis until the date on which the prevailing Party actually receives the dollar amount of the award plus accrued interest.

11. No Assignment or Delegation. Neither Party shall assign any right under this Agreement nor delegate any duty under this Agreement unless the other Party has consented to any such assignment or delegation in a signed writing.

12. Authority to Execute. The undersigned individuals represent and warrant that they are expressly and duly authorized by their respective entities or agencies to execute this Agreement and to legally bind their respective entities or agencies as set forth in this Agreement.

13. No Third Party Beneficiary. This Agreement shall not and is not intended to benefit nor to grant any right or remedy to any person or entity that is not a party to this Agreement.

14. Notices. All notices shall be sent by the most expeditious means available including but not limited to facsimile, overnight courier or certified or registered mail to the addresses set forth below the signatures. Any such notice shall be deemed delivered when received.

15. Limitation on Actions. The statute of limitations on any claim or cause of action by FRANCHISEE arising from or incident to any violation of any franchise law or regulation shall be 1 year from the date on which the violation occurred or should have been discovered.

16. Observer. The FRANCHISOR may, in its sole discretion and at any time, place an observer in the Twin Donut Store to verify gross sales upon reasonable evidence that the gross sales are not being reported or not being reported accurately. The FRANCHISEE shall cooperate in good faith with the observer and pay the costs and fees incurred by FRANCHISOR as a result of placing the observer which costs and fees shall be reasonable. The observer shall exercise its best reasonable efforts not to interfere in the business operation of the Twin Donut Store.

17. Administrative Expense in Bankruptcy. If this Agreement is terminated for any reason related to the bankruptcy of FRANCHISEE, the payments due under this Article shall be deemed an

administrative expense under 11 U.S.C. §503.

D. Execution of the Contract and Electronic Signatures

The only persons bound to a written contract are those who executed the contract. If the individual executing a contract is acting on behalf of another person or entity reflect that fact in the signature lines and the authority of the individual should be stated.

1. Uniform Electronic Transactions Act (UETA)

The UETA was drafted by the NUCCSL and approved for enactment in 1999. It provides a set of rules by which electronic signatures and electronic records in any type of transaction are recognized, respectively, as binding legal acts and binding legal documents. The UETA has been enacted by Virginia and took effect on July 1, 2000, *Va. Code Ann. §59.1-467 et seq.* The UETA has been enacted in both D.C. and Maryland and the current law in each jurisdiction recognizes electronic signatures for government communications. For more information on state initiatives on electronic signatures see www.mbc.com.

An electronic signature means an electronic sound, symbol, or process attached to or logically associated with a record and executed or adopted by a person with the intent to sign the record, *UETA, Definitions.*

2. Electronic Signatures in Global and National Commerce Act (E-Sign) S.761

E-Sign was signed into law and took effect on October 1, 2000. It provides that electronic signatures and electronic contracts used in interstate commerce shall not be denied legal effect merely because they are in electronic form. E-Sign does not pre-empt or limit any law that requires that a particular contract or signature be in a form other than an electronic form and it does not require any

person to use electronic signatures or records. Signatures on certain legal documents such as wills, court orders and certain consumer notices are exempt from E-Sign so that signatures on these documents cannot be in electronic form.

E-Sign provides that state law may alter or limit E-Sign as long as the state law is the UETA or another law that specifically provides rules for the validity of electronic signatures. This raises some significant and complicated state pre-emption issues partly because UETA both overlaps with E-Sign and is more comprehensive than E-Sign. Also, with certain issues that UETA and E-Sign have in common, they each deal with those issues in a different manner. For further information, see www.techlawjournal.com.

TAB 7

FRANCHISING AND THE INTERNET

FRANCHISING AND THE INTERNET

I. Offers of Franchises Over the Internet

The issue with respect to offers of franchises over the Internet is whether the franchisor must comply with laws and regulations in each jurisdiction in which any such offer reaches including those jurisdictions that require registration. Obviously, such a requirement would significantly burden franchisors. In 1998, the NASAA adopted a Statement of Policy Regarding Offers of Franchises on the Internet that exempts offers of franchises over the Internet from the registration requirements of jurisdictions that require registration under the following conditions:

A. The Internet Offer indicates directly or indirectly that the franchise is not being offered to residents of the particular jurisdiction,

B. The Internet Offer is not directed to any particular person in the jurisdiction by or on behalf of the franchisor or by anyone acting with the knowledge of franchisor, and

C. No franchise is sold in the jurisdiction by or on behalf of the franchisor until the UFOC is duly registered and provided to the franchisee in compliance with the laws of the jurisdiction.

Most if not all of the jurisdictions that require registration have adopted the NASAA Statement either affirmatively or impliedly, *see 13 NYCRR §200.13*.

II. Revised FTC Franchise Rule on Electronic Disclosure

Franchisors may provide disclosure documents to prospective franchisees by email or by granting access on the Internet as long as the franchisor has advised prospective franchisees how to do so. Franchisors may deliver the disclosure document to the prospective franchisee the disclosure document in tangible electronic form *i.e.* computer disk or CD-ROM. Item 23 franchisee receipts may be executed electronically or receipt otherwise evidenced through the use of security codes,

passwords or similar authenticating means.

III. “Cybersquatting” on Franchisor’s Domain Name

The court decisions are split on the whether and the conditions under which a franchisee can use the domain name of a franchisor. These decisions are non-reported decisions so that the law is still evolving on this issue. *See Travel Impressions LTD v. Kaufman et al*, 1997 WL 1068700 (EDNY, 1997); *Hard Rock Café International (USA) v. Morton et al.*, 1999 WL 350848 (SDNY, 1999). Address the issue in the franchise agreement like any other intellectual property.

TAB 8

INTERNATIONAL ASPECTS OF FRANCHISING

INTERNATIONAL ASPECTS OF FRANCHISING

I. Extra-Territorial Application of U.S. Franchise Laws

U.S franchisors are not required to comply with the FTC Franchise Rule in making offers and sales of franchises to overseas franchisees, *Nieman v. Dryclean USA*, 178 F.3d 1126 (11th Cir.1999). Note, however, that a franchisor that has registered a UFOC in New York is obligated to comply with New York franchise laws and regulations no matter where in the world or to whom in the world it offers or sells franchises.

II. Franchising in the European Union (EU) and Other Countries

The primary issue for franchisors offering or selling franchises in the EU has traditionally been the applicability of the anti-competition provisions of the treaties establishing the EU, *see Article 85(1) of the Treaty Establishing the European Economic Community*. After certain decisions by the European Court of Justice and some narrow regulations, the EU promulgated a regulation that applies to all agreements containing vertical restraints which include franchises, *Commission Regulation EC No. 2790/1999*. The Regulation exempts from Article 85(1) vertical agreements or concerted practices between two or more businesses, each of which operates at a different level of the production or distribution chain, that involve the terms by which the parties may sell, re-sell or purchase their goods and services. The Regulation took effect on June 1, 2000 and will remain in effect until May 31, 2010. The EU is also considering a disclosure regulatory scheme.

Other countries such as China and Italy have recently adopted franchising regulatory schemes. Some countries regulate the actual terms of the agreement while other countries mandate a form of disclosure, Wright and Relf, "International Franchising" 84 DEC Mich B.J. (December 2005).

III. UNIDROIT - Guide to Master Franchise Agreements and Model Franchise Disclosure Law

The UNIDROIT Franchising Initiatives (referred to as the Initiatives) are promulgated by the International Institute for Unification of Private Law which is an independent inter-governmental organization based in Rome, Italy. Its purpose is to examine ways of harmonizing and coordinating the private domestic law of member States and prepare for adoption by the States uniform laws of private law. The Institute serves as a group of uniform law commissioners at the international level similar to the National Conference of Commissioners on Uniform State Laws (NCCUSL) on the state level. Formed in 1926, the Institute has promulgated uniform laws on commercial contracts, international leasing, international wills as well as international franchising.

The Initiatives consist of a Guide for the preparation of franchise agreements and a Model Disclosure law. A U.S. franchisor seeking to franchise in other countries can use the Guide to prepare a franchise agreement that will cross legal cultures. The Model Disclosure Act was promulgated in 2002 as an act which could be adopted by countries seeking to establish a disclosure regulatory scheme, see www.unidroit.org.

TAB 9

CONTRACT DRAFTING TECHNIQUES

CONTRACT DRAFTING TECHNIQUES

I. Clear Writing Begins With Clear Thinking

Clear and precise writing will almost inevitably flow from clear and precise thinking. There are no drafting techniques that will make clear on paper a concept that is unclear in the mind of the attorney. Knowledge of the subject matter of the contract, an understanding of the objectives of the parties and an analysis of the practical and logical consequences of each contract provision is essential to a clearly written and precise contract.

Once the thinking is clear and precise, the words used must be clear and precise. As Justice Felix Frankfurter once said: “Exactness in the use of words is the basis of all serious thinking. You will get nowhere without it. Words are clumsy tools, and it is very easy to cut one’s fingers with them, and they need the closest attention in handling; but they are the only tools we have, and imagination itself cannot work without them. You must master the use of them, or you will wander forever guessing at the mercy of mere impulse and unrecognized assumptions and arbitrary associations, carried away with every wind of doctrine.”¹

II. Use of “Shall”, “Must” “May” and “Will”

A. “Shall” or “Must” are the most powerful words available to a drafter. They are imperatives and cause a legal obligation to be imposed or undertaken. They should always be used to the exclusion of “May” or “Will” whenever a provision is meant to impose an affirmative obligation on a party. They should never be used to specify future performance or a future occurrence.

B. “May” is permissive or discretionary in character. It should be used only when a provision is meant to accord discretion, power or a privilege to a party.

¹ The Record, Association of the Bar of the City of New York, 1947, p.29

C. “Will” is predictive in character. It should rarely be used at all in a contract and it should never be used to impose an obligation on a party.

D. Never use “Should” in a contract because, while it can mean “Must”, it can also mean “It Would Be Desirable”, See Ashlodge Ltd. v. Hauser, 163 F.3d 681 (2d Cir.1998).

III. Use of Active Language Rather Than Passive Language and Affirmative Language Rather Than Negative Language

Wherever possible use active language rather than passive language. The active voice is more precise and avoids some of the vagaries inherent in the passive voice.

A. Do not write: *“The royalty shall be paid on the first day of each month.”*

B. Write: *“Franchisee shall pay the royalty on the first day of each month.”*

C. Do not write: *“The failure of Franchisee to pay the royalty on the first day of each month is not an incurable event in default.”*

D. Write: *“The Franchisee may cure an event in default caused by its failure to pay the royalty when due.”*

IV. Use Present Tense

Even though a contract may refer to or describe an event that will happen in the future or at least some time after the contract is executed, the contract language should be phrased in the present tense. A contract is a “living” document in the sense that once it is executed, it continuously governs the parties and has no present or future.

A. Write: *“If a Party dies.....”*

B. Do Not Write: *“If a Party should die.....”*

V. Use of “And” and “Or”

Never use “and” and “or” interchangeably. Items connected by “and” will be treated the same or in the conjunctive. Items connected by “or” will be treated alternatively or in the disjunctive.

VI. Use of “Any”, “Each” and “No”

A. If an obligation is to be imposed, use “Each”: *“Each Party shall pay its assessment on May 1.”*

B. If discretion, a power or privilege is to be accorded, use “Any”: *“Any Party may pay its assessment on May 1.”*

C. If an obligation to refrain from acting is to be imposed or a discretion, power or privilege is being limited or eliminated, use “No”: *“No Party shall pay its assessment after May 1.”*

VII. Use of Number of Days Rather Than Months or Years

Use number of days to measure time rather than calendar periods such as weeks, months or years. Note that “3 months” and “90 days” are different time periods. Also, always specify whether the days are calendar days or business days.

VIII. Use of “Unless” and “As Long As”

Conditions, whether precedent or subsequent, should always be clearly drafted to reflect that they are conditions and not promises. The courts will generally construe a condition that is also a promise to be a promise rather than a condition. The connectors “Unless” or “As Long As” are language of condition and should be used where the parties intend to create a condition to performance or to discharge rather than a promise to perform. The connector “provided” is ambiguous. Depending on the context, it can be construed as either language of condition or as a promise.

A. “The Contractor shall pay Subcontractor when Client pays Contractor.”

Compare to:

B. “Contractor shall not pay Subcontractor unless Client has paid Contractor.”

or

C. “Contractor shall have no obligation to pay Subcontractor unless Client has paid Contractor.”

Also, in drafting express conditions, be aware that courts will imply constructive conditions to assure fairness particularly where the occurrence of an express condition is within the control of one party. For example, if the parties to a real property sales contract have agreed that the performance of the buyer is conditioned on the buyer securing financing for the purchase, the courts will imply a constructive condition that the buyer must exercise its best efforts to secure financing.

IX. Use of “Reasonableness” Clause

Refrain from using a “reasonableness” clause instead of an actual standard to describe the manner in which an obligation should be performed. An exception is where the consent or approval of a party is required before a benefit can flow to or a power can be exercised by the other party. The most common instance is in leases that require the approval of the landlord before the lease can be assigned or the premises sub-leased.

A. “The Tenant shall not assign this Lease or sub-lease the premises unless it has obtained the consent of the landlord.”

Compare to:

B. “The Tenant shall not assign this Lease or sub-lease the premises unless it has obtained the consent of the landlord, *which consent shall not be unreasonably withheld.*”

X. Use of Legal Terms of Art

A legal term of art is a term that is imprecise in its ordinary usage but which has acquired a meaning over years of usage in contracts, briefs and decisions so that it is at least intuitively understood by attorneys and judges. These terms include “*promptly*” and “*best efforts*”. They should be used only when necessary to effect a compromise on language in a “non-deal breaking” provision in a contract. The legal effect of these terms should be explained to the client.

XI. Use of the Particular and the General

As a matter of contract law, a list of particulars is treated as exhaustive and excludes any item not listed in the list of particulars, (referred to as the doctrine of *expressio unius est exclusio alterius* i.e. the expression of one thing is the exclusion of another). Also, as a matter of contract law, a general description includes only those particulars that are similar to or encompassed by the general description, (referred to as the doctrine of *ejusdem generis* i.e. of the same kind). If it is not practical to list all possible particulars, combine the general and the particular by providing a general description and listing representative particulars preceded by the clause *including but not limited to*.

A. “The Athlete shall perform every physical act required by the position of quarterback.”

Compare to:

B. “The Athlete shall perform every physical act required by the position of quarterback *including but not limited to* passing, running and play-calling.”

XII. Time

Contracts often contain a “time is of the essence” clause. This clause means that to the extent that there are times for performance specified in the contract, any failure to strictly comply with any such specified time is a material breach of the contract. The clause negates the common law defense of substantial compliance. The clause is most common in real estate sales contracts and leases.

XIII. No “Whereas”

“Whereas” clauses are neither binding nor enforceable. Do not use them.

XIV. Nunc Pro Tunc

Translated from the Latin, the term means “now for then”. The principle underlying the term is that a legal effect can be made retroactive to a date prior to the date of a current legal instrument. Parties can agree that, even though they execute a contract today, the rights and obligations under the contract took effect on a date before today.

XV. Further Reading

The *Guidelines for Drafting and Editing Court Rules*, found at 169 F.R.D. 176 (January, 1997) contains an excellent discussion of drafting principles and techniques. Although the *Guidelines* is intended for drafting court rules, many of the principles and techniques it discusses are instructive and useful for contract drafting. See also *Adams*, *A Manual of Style for Contract Drafting* (American Bar Association Section of Business Law, 2004); *Burnham*, *Drafting Contracts*, (Michie Second Edition, 1993); *Feldman and Nimmer*, *Drafting Effective Contracts: A Practitioner’s Guide* (Aspen Law & Business, Second Edition 1999) and *Stark*, *Negotiating and Drafting Contract Boilerplate*, (ALM Publishing 2003).

TAB 10

PRINCIPLES OF INTERPRETING CONTRACTS

PRINCIPLES OF INTERPRETING CONTRACTS

I. The Plain Meaning Rule

The fundamental objective of effective contract drafting is to avoid any need for interpreting the contract. The contract should be drafted with sufficient precision so that the intent of the parties with respect to the terms and conditions of the agreement is apparent from the language of the provisions of the contract. This principle is reflected in the primary rule of contract interpretation referred to as the “Plain Meaning Rule”. The Plain Meaning Rule holds that, in the absence of an ambiguity in the language of a contract, the language of the duly executed written contract speaks for itself and binds the parties without resort to any evidence extrinsic to the written document, Hart v. Vermont Inv. Ltd. Partnership, 667 A.2d 578 (D.C.App.1995). The meaning of the plain language of the contract is determined not according to what a party thought the language meant but rather according to what a reasonable person in the position of a party would have thought the language meant, District of Columbia v. C.J. Langenfelder & Son, Inc., 558 A.2d 1155 (D.C.App.1989). That reasonable person is presumed to know all of the circumstances surrounding the making of the contract and bound by the usages of terms that the parties know or have reason to know, Rastall v. CSX Transportation, Inc., 697 A.2d 46 (D.C.App.1997).

A. Words Given Their Ordinary Meaning

The ordinary definition of a term should be given weight in ascertaining the meaning of a term, Obelisk Corp. v. Riggs Bank, 668 A.2d 847 (D.C.App.1995). A term or provision will be accorded a meaning that is consistent with the contract as a whole, BWX Electronics, Inc. v. Control Data Corp., 929 F.2d 707 (CADC.1991).

B. Words Given Particular Meaning in Custom, Trade Usage or Course of Dealing

Words that have particular meaning in the context of the custom, trade usage or course of dealing of the contractual relationship, will be accorded that particular even if it differs from the ordinary meaning, Restatement, 2d §§ 219-223.

C. Ambiguity Exception to Plain Meaning Rule

If an ambiguity is found to exist in the language, then extrinsic evidence may be introduced to demonstrate the intent of the parties. Extrinsic evidence can be in the form of oral testimony about the negotiations, the states of mind of the parties, custom and trade usage in the applicable industry or course of dealing between the parties. A contract provision is ambiguous if it is reasonably susceptible to different constructions, however, it is not ambiguous simply because the parties disagree as to the meaning, Bennett Enterprises, Inc. v. Domino's Pizza, Inc., 45 F.2d 493 (CADC. 1995); Washington Properties, Inc. v. Chin, Inc., 760 A.2d 546 (D.C. App. 2000). Whether or not a term is ambiguous is a question of law to be resolved by the court and not by a trier of fact, Gryce v. Lavine, 675 A.2d 67 (D.C.App.1996).

Under the traditional application of the ambiguity exception (Williston/Holmes), where the meaning of the term is "plain" either in ordinary usage or in a particularized usage, then no ambiguity exists and extrinsic evidence of the meaning of a term is not admissible. Under the modern trend (Corbin/Restatement), if a term is "reasonably susceptible" to the meaning asserted by a party, then extrinsic evidence of the meaning of the term is admissible.

D. Criticism of the Plain Meaning Rule

The Plain Meaning Rule has been criticized by many commentators. They have remarked that, because there are inherent linguistic limits on how precise a writing can be, it is both unconstructive

and unfair to rely exclusively on the written document to determine the intent of the parties. Moreover, determining whether or not an ambiguity exists is so subjective as to be almost arbitrary. Any competent evidence that is reasonably calculated to elucidate the intent of the parties should be considered. Despite the criticism, the Plain Meaning Rule is followed by most jurisdictions in the nation, including the area jurisdictions. Therefore, attorneys must draft contracts not only to avoid ambiguities that are inherent in language but also to avoid ambiguities that may be found by the courts. This is an extremely difficult endeavor because, as one court has pointed out, contract interpretation is largely an individualized process so that to the extent that contractual language from prior cases significantly differs from the contract being interpreted, prior cases cannot control, Rivers & Bryan, Inc. v. HBE Corp., 628 A.2d 631 (D.C.App.1993).

II. Language Construed Against Drafter

In choosing among the various reasonable meanings of a term, the preferred meaning will be the one that operates against the interest of the party that supplied the disputed words or from the disputed language is derived (referred to as the rule of *contra proferentum*) at least where the parties are in equal bargaining positions, Mesa Air Group v. Dept. of Transportation, 87 F.2d 498 (CADC. 1996); American Building Maintenance Co. v. L'Enfant Plaza Properties, Inc., 655 A.2d 858 (D.C.App.1995). This rule is a secondary rule of interpretation and is used only when all other rules of interpretation have failed to resolve the meaning of a disputed term, American Building Maintenance Co. v. L'Enfant Plaza Properties, Inc., *Ibid.*

III. Accord Meaning to All Terms

Parties are assumed to intend legal and practical consequences when they enter into a contract. Where two interpretations of a term are possible in a contract and one such interpretation

would render the term or the contract without legal or practical effect, the interpretation that accords legal or practical effect to the term or contract. Restatement 2d §203(a).

IV. Conflicting Terms

Where two terms conflict with one another, the more specific term will be deemed an exception to the more general term, Restatement 2d § 203(d). Where part of the contract is handwritten or typewritten and part of the contract is printed and the handwritten or typewritten parts conflict with the printed part, the handwritten or typewritten parts will control, Ibid.

V. The Parol Evidence Rule Distinguished from the Plain Meaning Rule

The Plain Meaning Rule should not be confused with the Parol Evidence Rule. The Parol Evidence Rule holds that where a written contract contains an integration clause stating that it is the final and full expression of the agreement between the parties or a fact finder finds that the written contract is the final and full expression of the agreement between the parties, no prior oral or written agreement or negotiation or custom/usage can be admitted into evidence in a legal proceeding that adds or removes any term or provision from an integrated written contract.

The Parol Evidence Rule is a substantive rule of contract law or a rule of evidence but not a rule of interpretation. The Parol Evidence Rule is used to determine the *content* of the contract *i.e.* which terms and provisions are *to be included* in the contract. The Plain Meaning Rule is used to determine the *meaning* or *legal effect* of the terms and provisions of the contract.

VI. Relational Contracts

A relational contract is a contract in which the social or commercial context as well as the relationship of the parties are as significant to interpreting the contract as are the terms of the contract itself. Relational contracts have existed for as long as there has been commercial activity. However,

within the past 20 years, relational contracts have been endowed with a scholarly conceptual framework, (*See 94 Northwestern U Law Rev Symposium on Relational Contract Theory, Spring 2000*). The primary characteristics of a relational contract are:

- A. Extended Duration Rather Than “Spot” or Short Term
- B. Open Terms and Reserved Discretion
- C. Agreed Governance Mechanisms
- D. Benefits and Burdens Shares Rather Than Allocated
- E. Transaction Specific Investments
- F. Overarching Relationship External to Contract

The types of contracts that generally have the characteristics of a relational contract are franchise agreements, employment agreements and long term supply contracts.

TAB 11

SAMPLE FRANCHISE AGREEMENT

ARTICLE II
GRANT OF FRANCHISE, INITIAL FRANCHISE FEE AND TERM OF THE FRANCHISE

2.1. Grant of Franchise. FRANCHISOR grants a Franchise and FRANCHISEE accepts the Franchise to operate a donut store/luncheonette utilizing the TWIN DONUT system upon the terms and conditions set forth in this Agreement.

2.2. No Exclusive Territory. Nothing in the grant of this Franchise shall be construed as obligating FRANCHISOR to refrain from granting other Twin Donut Franchises within any particular geographic area at or about the premises on which the Franchise granted under this Agreement will be operated. The FRANCHISOR may, in its sole discretion, grant Twin Donut Franchises to persons other than FRANCHISEE to operate Twin Donut Stores or Twin Donut Satellites at any location without regard to the geographical proximity or distance that any such location bears to the premises upon which the Franchise granted under this Agreement shall be operated.

2.3. Purchase of Additional Twin Donut Franchises. The FRANCHISOR may require FRANCHISEE to execute an agreement within the 90-day period described in Paragraph 3.1 to purchase one or more Twin Donut Franchises within a defined period of time in addition to the Twin Donut Franchise purchased under this Agreement. If FRANCHISOR makes this requirement, that requirement shall be contained in an Addendum to this Agreement.

2.4. Initial Franchise Fee. Upon execution of this Agreement, FRANCHISEE shall pay \$25,000.00 to FRANCHISOR for a Full Service Store Franchise or \$15,000.00 for an Independent Satellite Franchise in a form designated by FRANCHISOR. The Initial Franchise Fee is not a draw or advance against any other payment which FRANCHISEE shall be obligated

to make under this Agreement to FRANCHISOR or any Third Party. The Initial Franchise Fee shall be deemed fully earned upon receipt and non-refundable except as provided in Article III.

2.5. Type of Franchise. The Franchise purchased under this Agreement is a (check one):

Full Service Store Franchise—

The FRANCHISEE shall manufacture baked goods for sale on the Business Premises for consumption on the premises or for take-out.

Independent Satellite Franchise--

The FRANCHISEE shall not manufacture or bake goods for sale on the Business Premises. The FRANCHISEE shall offer for sale baked goods any other foods that have been prepared only in another Twin Donut Store for consumption on premises or for take-out.

2.6.Re-Location. Nothing in this Agreement shall be construed to obligate FRANCHISOR to re-locate or enable FRANCHISEE to re-locate the Franchise to another location for any reason including but not limited to the destruction or condemnation of the business premises.

2.7.Supply of Product to Independent Satellite. If the Franchise is an Independent Satellite Franchise, FRANCHISEE shall purchase baked goods from other Twin Donut Stores and no other source. The FRANCHISOR may assist in facilitating such purchasing relationships. The FRANCHISOR has no obligation to supply the Independent Satellite with baked goods or any other product. The FRANCHISOR does not either directly or indirectly guarantee that the FRANCHISEE shall receive baked goods or any other product from another Twin Donut Store.

2.8. Term of Franchise. The Term of this Franchise shall be 20 years except that if the term of the Primary Lease on the business premises described in Article III is less than 20 years, then the Term of this Franchise shall run as follows:

- a. The Term of this Franchise shall commence on the ____ day of _____, 2006 and shall expire when the term of any Primary Lease or the Franchisee Store Lease expires unless the Primary Lease or the Franchisee Store Lease terminates prior to expiration, in which case, the Term of this Franchise shall expire when the Primary Lease or the Franchisee Store Lease terminates. The FRANCHISEE shall operate the Franchise as of the date of closing and all terms and conditions of this Agreement shall be deemed to run as of that date and be in full force and effect.
- b. If the Primary Lease or Franchisee Store Lease executed by FRANCHISEE extends beyond the expiration date of this Franchise then this Agreement expires on the last day of any such extension.
- c. The Term of this Franchise shall expire if at any time the Twin Donut Store is destroyed, condemned or otherwise rendered uninhabitable and FRANCHISEE does not re-build and re-equip the Twin Donut Store or manifest a bona fide intention, in the opinion of FRANCHISOR, to re-build and re-equip the Twin Donut Store within a reasonable time.

ARTICLE III
SITE SELECTION AND BUSINESS PREMISES OF THE FRANCHISE

3.1. Site Selection by FRANCHISEE. The FRANCHISEE shall identify to FRANCHISOR any site that FRANCHISEE has selected to establish and operate the Twin Donut Store. The FRANCHISOR shall inspect the site and approve or reject the site within 3 business days after the day on which any such inspection is complete. If the FRANCHISOR rejects the site, the FRANCHISOR shall refund the Initial Franchise Fee without deduction or set off of any kind and this Agreement shall expire without further obligation between the Parties. Within 90 calendar days after the day on which FRANCHISOR approves the site, the FRANCHISEE shall:

- a. Submit to FRANCHISOR for its written approval, a bona fide proposed lease (or executed lease if FRANCHISEE has legal possession of the site it identifies to FRANCHISOR) that, in the opinion of FRANCHISOR, would if executed evidence present legal possession, and
- b. Upon receipt of the written approval of FRANCHISOR, obtain legal possession of the site, and

- c. Execute bona fide agreements to construct and equip the Twin Donut Store.

3.2. Site Selection by FRANCHISOR. The FRANCHISOR shall identify to FRANCHISEE one or more sites which sites shall be deemed sites approved by FRANCHISOR. Within 90 calendar days after the day on which FRANCHISOR has identified the last such site to FRANCHISEE, the FRANCHISEE shall:

- a. Choose one of the sites and communicate that choice to FRANCHISOR in a signed writing, and
- b. Submit a bona fide proposed lease (or executed lease or other document if FRANCHISEE has legal possession of a site it identifies to FRANCHISOR under Paragraph 3.1) that, in the opinion of FRANCHISOR, evidences present legal possession to FRANCHISOR for its written approval, and
- c. Upon receipt of the approval of FRANCHISOR, obtain legal possession of the site, and
- d. Execute bona fide agreements to construct and equip the Twin Donut Store.

3.3. Failure to Comply within 90-Day Period. The FRANCHISOR may revoke the Franchise granted under this Agreement when the 90-day period expires, if:

- a. Under Paragraph 3.1, the FRANCHISEE has failed to accomplish each of items a through c of Paragraph 3.1, or
- b. Under Paragraph 3.2, the FRANCHISEE has failed to accomplish each of items a through d of Paragraph 3.2, or
- c. Under either Paragraph 3.1 or 3.2, FRANCHISOR does not approve a proposed lease or an executed lease, or
- d. Under any requirement to execute an agreement to purchase additional Twin Donut Franchises under Paragraph 2.3, the FRANCHISEE failed to execute such agreement.
- e. If FRANCHISOR revokes the Franchise under this Paragraph, then the

Parties shall have no further obligation to one another. The FRANCHISOR shall not be obligated to refund any portion of the Initial Franchise Fee and shall not be liable in any way to FRANCHISEE.

3.4. Approval of Lease by FRANCHISOR. If the lease is a Franchisee Store Lease with TDS Leasing, Inc. or TDS Leasing, LLC as lessor, then the lease shall be deemed approved by FRANCHISOR. If the lease is with any person or entity other than TDS Leasing, LLC as lessor, the FRANCHISOR shall not be obligated to approve any lease that does not contain provisions drafted in form acceptable to FRANCHISOR that provide as follows:

- a. The FRANCHISOR or its designee shall replace FRANCHISEE as tenant under the lease if:
 - (I) the lease expires for any reason other than the chronological expiration of the term of the lease, including any renewal or extension term and the procedure described in sub-paragraph b is fully executed, or
 - (ii) the lease terminates for any reason before the chronological expiration of the term of the Store lease, including any renewal or extension term and the procedure described in sub-paragraph b is fully executed, or
 - (iii) FRANCHISEE ceases for any reason to be a Twin Donut Franchisee or ceases to operate the business of a Twin Donut Franchise on the Demised Premises and the procedure described in sub-paragraph c is fully executed.
- b. If the lease expires or terminates under either a(I) or a(ii), then:
 - (I) Within 3 business days after the day on which the lessor determines that the lease has expired or terminated, the lessor shall notify FRANCHISEE in a signed writing. The writing shall contain the balance of the term, a description of any outstanding default, the means of curing any such default and a copy of the Store Lease then in effect, including each amendment or modification, if any.
 - (ii) No later than 15 business days after the day on which it receives the writing in (I), FRANCHISOR shall cure each default contained in

the writing. Immediately after accomplishing each such cure, FRANCHISOR or its designee shall be entitled to possession of the premises and the lessor shall recognize FRANCHISOR or its designee as the exclusive Tenant under the lease and the FRANCHISOR shall be entitled to all rights and subject to all obligations of the lease.

(iii) If FRANCHISOR fails to cure any default under (ii), then lessor and FRANCHISOR shall have no further obligation to one another including any obligation that may be construed as being incident to the lease or implied in law.

c. If FRANCHISEE ceases for any reason to be a Twin Donut Franchisee or ceases to operate the business of a Twin Donut Franchise on the premises under the lease, then:

(I) Within 3 business days after the day on which FRANCHISOR determines that FRANCHISEE has ceased to be a Twin Donut Franchisee or has ceased to operate the business of a Twin Donut Franchise on the premises, FRANCHISOR shall notify the lessor in a signed writing.

(ii) Within 3 business days after the day on which the lessor receives the writing in (I), the lessor shall notify FRANCHISOR in writing as to the balance of the term and attach a copy of the lease then in effect, including each amendment or modification, if any.

(iii) No later than 7 business days after the day on which it receives the writing in (ii), FRANCHISOR shall either accept or reject the lease. If FRANCHISOR accepts the lease then FRANCHISOR or its designee shall be entitled to possession of the premises and the lessor shall recognize FRANCHISOR or its designee as the exclusive tenant under the lease and the FRANCHISOR or its designee shall be entitled to all rights and subject to all obligations of the lease.

(iv) If FRANCHISOR fails to accept the lease under (iii), then lessor and FRANCHISOR shall have no further obligation to one another including any obligation that may be construed as being incident to the lease or implied in law.

d. If FRANCHISEE contests any legal action necessary to enforce subparagraph c and FRANCHISOR accepts the lease, then FRANCHISEE

shall undertake the prosecution of any such action at its sole cost.

- e. If FRANCHISEE defaults under the lease during the pendency of any legal action described in sub-paragraph d on any payment obligation, FRANCHISOR shall cure any such payment default at any time prior to and as a condition precedent to taking possession of the premises
- f. After FRANCHISOR has approved the lease under this Paragraph, the lessor and FRANCHISEE shall not under any circumstances amend, modify or alter the lease in any way unless FRANCHISOR approves of any such amendment, modification or alteration in a signed writing which approval shall not be unreasonably withheld.

3.5. Binding Lease Prior to Approval. If FRANCHISEE enters into a binding lease before FRANCHISOR has approved any such lease, FRANCHISOR shall not be liable for any loss or damage to FRANCHISEE that arises from or is incident to any such lease by reason of the refusal of FRANCHISOR to approve the lease or other document.

3.6. Definition of Legal Possession. For the purpose of this Agreement, FRANCHISEE has legal possession of a site when it has been granted the use and enjoyment of the site under a written binding lease executed by a person or entity with a possessory right or interest in the site that is superior to the possessory right of FRANCHISEE and which lease is enforceable under the laws of the State in which the site is located.

ARTICLE IV CONSTRUCTION AND EQUIPPING OF TWIN DONUT STORE

4.1. Construction by Affiliate of FRANCHISOR. The FRANCHISEE may, in its sole discretion, contract with Spartan Built, Ltd., an affiliate of FRANCHISOR, to construct the Twin Donut Store. If the Twin Donut Store is constructed under this Paragraph, then the construction shall be deemed to conform to the Twin Donut System and be approved by FRANCHISOR under Paragraph 4.5.

4.2. Equipping by Affiliate of FRANCHISOR . The FRANCHISEE shall contract with Spartan Built, Ltd., an affiliate of FRANCHISOR, to equip the Twin Donut Store for Equipment and Furnishings that FRANCHISOR deems essential to the operation of the Franchise. The FRANCHISEE may contract with a Third Party of its choice to equip or furnish the Twin Donut Store with equipment or furnishings required but deemed non-essential by FRANCHISOR subject to Paragraphs 4.3 through 4.6 of this Article.

4.3. Quality of Construction and Equipment. Unless otherwise permitted by FRANCHISOR in a signed writing, each item of construction and each item of equipment shall be in brand new condition.

4.4. Specifications for Construction and Equipment. The Twin Donut Store shall be constructed according to specifications provided to FRANCHISEE by FRANCHISOR (referred to as the Twin Donut Specifications). The Twin Donut Store shall contain each item of equipment specified by FRANCHISOR.

- a. During construction and equipping, FRANCHISOR may but is not obligated to inspect the Twin Donut Store. If, at any time, FRANCHISOR identifies an item of construction or equipment or any physical condition that fails to comply with the Twin Donut Specifications, FRANCHISEE shall upon oral or written notice from FRANCHISOR immediately rectify any such non-compliance at its sole cost.
- b. If due to a physical condition unique to the site of the Twin Donut Store it is impractical to comply with a Twin Donut Specification, FRANCHISEE shall upon discovery of such condition immediately notify FRANCHISOR. If FRANCHISOR concurs that the physical condition requires a departure from any Twin Donut Specification, then FRANCHISEE shall approve that departure and such departure shall not be deemed non-complying.

4.5. Final Approval of Twin Donut Store. The FRANCHISEE shall notify FRANCHISOR in a signed writing that the Twin Donut Store is fully constructed and equipped

and ready to commence business. When it receives the completion notice FRANCHISOR shall inspect the Twin Donut Store. The FRANCHISOR shall either issue a written final approval or identify to FRANCHISEE any non-complying items. The FRANCHISEE shall cure or rectify any such non-compliance at its sole cost. If FRANCHISEE fails to promptly cure or rectify any such non-compliance, FRANCHISOR may revoke the Franchise granted under this Agreement without any liability whatsoever or any further obligation to FRANCHISEE.

4.6. Time for Commencing Business Operations. The FRANCHISEE shall construct, equip and have the Twin Donut Store ready to commence business no later than 90 calendar days after the date on which FRANCHISEE has obtained legal possession of the site for the Twin Donut Store. If, under Paragraph 3.1 of Article III, FRANCHISEE has legal possession of the site when it identifies the site to FRANCHISOR then the 90-day period shall begin on the date on which FRANCHISOR approves the site.

4.7. Commencement of Business. Under this Article, the Twin Donut Store shall be ready to commence business when the public can avail itself of the products and services offered by the Twin Donut Store on a continuous and systematic basis.

4.8. Government Approvals, Consents and Licenses. The FRANCHISEE must apply for, qualify for and obtain all government and quasi-government approvals, consents and licenses necessary to construct, equip, open and operate a Twin Donut Store. The FRANCHISEE is obligated to perform every legal act necessary to obtain each such approval, consent and license.

4.9. Legal Inability to Obtain Approvals, Consents and Licenses. Nothing in this Agreement shall be construed as a representation by FRANCHISOR that FRANCHISEE shall or will obtain the items described in Paragraph 4.8. If, in the opinion of FRANCHISOR,

FRANCHISEE found to be legally ineligible for or is otherwise unable as a matter of law to obtain any such item, FRANCHISOR may in its sole discretion terminate this Agreement.

ARTICLE V
MATERIALS, PRODUCTS AND SUPPLIES

5.1. Approved Sources. The FRANCHISEE shall purchase all materials, products, and supplies necessary or incident to the business of the Franchise from sources approved by FRANCHISOR or from another Twin Donut Store, subject to Paragraph 5.5.. Such materials, products and supplies shall include but not be limited to doughnut flour, pastry filling, toppings, coffee, tea, chocolate, milk, cream, and other non-alcoholic beverages, ice cream and other dairy products, paper supplies, including coffee containers, cups, paper plates, spoons, doughnut boxes, bags, napkins, doilies, menus, matches, toothpicks, advertising signs or other advertising media, linens and uniforms. The FRANCHISEE shall purchase all equipment and replacement equipment that FRANCHISOR deems necessary to the business of the Franchise only from Approved Sources. Equipment and replacement equipment shall include but not be limited to the items listed in TAB 3 of the current Twin Donut Inc. Franchise Offering Circular. Paragraph 5.5 shall not apply to purchases of equipment or replacements of equipment.

5.2. Holds Harmless. The FRANCHISEE shall hold FRANCHISOR completely harmless and indemnify FRANCHISOR for any loss, damage or injury to FRANCHISEE or any Third Party arising out of or incident to the purchase or delivery of any such material, product or supply.

5.3. Uniform System. The FRANCHISEE acknowledges that the purpose of this Article is to insure that a uniform and high quality standard of operation is maintained for all

stores operating under the Twin Donut system. The FRANCHISEE shall exercise its best efforts to protect and sustain the reputation of FRANCHISOR. The FRANCHISEE further acknowledges that the Twin Donut System is an evolving concept. FRANCHISOR may at any time change components of the Twin Donut system including but not limited to menus, products, services, policies and procedures. FRANCHISEE shall adopt any such changes and bear the reasonable cost of any such change.

5.4. No Affiliate. The FRANCHISOR warrants that neither FRANCHISOR nor any of its affiliates is, in any way, an agent, employee or partner of any approved source.

5.5. Non-Approved Source. The FRANCHISEE may, in its sole discretion, purchase any material, product or supply from a source other than an approved source, as long as:

- a. FRANCHISEE submits a sample of the material, product or supply to FRANCHISOR, and
- b. After FRANCHISOR tests the item or supply for 30 days, the material, product or supply is found in good faith, by FRANCHISOR to be of at least equal quality to the same material, product or supply sold by an approved source.

ARTICLE VI TRADENAME AND TRADEMARKS

6.1. Proprietary Marks. FRANCHISOR grants to FRANCHISEE the non-exclusive right to conduct business under the name "TWIN DONUT" or "TWIN DONUT plus" subject to the terms and conditions of this Article.

6.2. Name. The name "TWIN DONUT" shall be prominently displayed without any other words or symbols accompanying it on the exterior of the business premises.

6.3. Name Restriction. FRANCHISEE shall not conduct any business under this

Franchise under any name other than "TWIN DONUT" or "TWIN DONUT plus" but the name "TWIN DONUT" shall not form any part of the corporate, partnership or business tradename of FRANCHISEE.

6.4. Manner of Name Display. The name "TWIN DONUT" shall be prominently displayed in a tasteful and attractive manner and always maintained in good repair.

6.5. Location of Name Display. FRANCHISOR may, in its discretion, and at any time, prescribe the location and manner in which the name "TWIN DONUT" shall be displayed.

6.6. Name on Products. The name "TWIN DONUT" and its trademark/symbol (as designated by FRANCHISOR) shall appear on all paper goods, napkins, sippers, containers, bags, spoons, cups, utensils, matches, menus and other articles used for or in connection with the sale or display of doughnuts and other products and merchandise to be sold or distributed under this Franchise.

6.7. Display Costs. All costs of any kind arising out of or incident to the display of the name "TWIN DONUT" or any trademark/symbol shall be borne solely by FRANCHISEE.

6.8. Sole Property. The name "TWIN DONUT" and any trademark/symbol shall, at all times, be the sole property of FRANCHISOR and shall not, in any way, become the property of FRANCHISEE.

6.9. Infringement. FRANCHISOR shall, at its sole expense, defend the trademark/symbol from any interference or infringement.

ARTICLE VII PAYMENTS ON GROSS SALES

7.1. Franchise Fees. In consideration of the rights granted under this Franchise,

FRANCHISEE shall pay to FRANCHISOR a percentage of the weekly gross sales realized by FRANCHISEE according to the terms of this Article. The Franchise Fees are and shall be deemed additional rent under any lease between FRANCHISEE and TDS Leasing, LLC.

7.2. Percentage. In each 12 consecutive calendar month period from the commencement date of this Franchise, FRANCHISEE shall pay:

- a. 6% of the total gross sales of each week.

7.3. Gross Sales. Gross sales shall mean all revenues received in any form from any sales of FRANCHISEE which are derived in any manner from any aspect of the business of the Franchise. Gross sales shall not include gratuities paid to employees by customers or the amount of sales tax imposed by any federal, state, municipal or other government authority directly on sales and collected from patrons as long as the amount of tax is added to the selling price or absorbed in the selling price and actually paid by FRANCHISEE to such governmental authority.

7.4. Week. For the purposes of this Article, a week shall run 7 consecutive days beginning at 12:01 A.M. on Sunday to 12:00 midnight on Saturday. The payments described in paragraph 7.2 of this Article shall be received in a form designated by FRANCHISOR no later than the close of business on each Thursday following the Saturday on which the preceding week ends.

7.5. Observer. The FRANCHISOR may, in its sole discretion and at any time, place an observer in the Twin Donut Store to verify gross sales upon reasonable evidence that the gross sales are not being reported or not being reported accurately. The FRANCHISEE shall cooperate

in good faith with the observer and pay the costs and fees incurred by FRANCHISOR as a result of placing the observer which costs and fees shall be reasonable. The observer shall exercise its best reasonable efforts not to interfere in the business operation of the Twin Donut Store.

7.6. Administrative Expense in Bankruptcy. If this Agreement is terminated for any under Paragraph 20.2 b-e for any reason related to the bankruptcy of FRANCHISEE, the payments due under this Article shall be deemed an administrative expense under 11 U.S.C. §503.

ARTICLE VIII
REPORTS AND CASH RECEIPTS OF GROSS SALES

8.1. Weekly Reports. FRANCHISEE shall submit a weekly written report, on a form to be provided by FRANCHISOR, of gross sales realized by FRANCHISEE for each week during the term of this Franchise. This report shall accompany each weekly payment made under Article VII.

8.2. Execution of Weekly Reports. Each weekly report shall be signed by an officer of FRANCHISEE and shall execute a sworn statement attesting to the accuracy of the weekly report on behalf of FRANCHISEE. This statement shall be duly notarized.

8.3. Cash Register. FRANCHISEE shall, at all times, record every sale made under this Franchise on cash registers which record on tape each sale made by FRANCHISEE and such cash registers shall not have any resetting device of any kind. The tapes for each week shall accompany each payment made under Article VII.

8.4. Cash Register Tapes. Any payment made under Article VII which is not accompanied by the weekly report and the cash register tapes for the week shall not be deemed

duly received even if FRANCHISOR accepts the payment.

- a. FRANCHISOR may, at any time and in its sole discretion require FRANCHISEE, to replace any cash register in the Twin Donut Store with a cash register specified by FRANCHISOR.
- b. Upon receipt of notice of replacement from FRANCHISOR, FRANCHISEE shall immediately install any new cash register and cease using any prior cash register.

8.5. Right to Estimate Gross Sales. If FRANCHISEE fails to submit the documentation described in this Article with each payment or fails to create or maintain the documentation and records described in Article X, FRANCHISOR shall estimate the gross sales for any period for which FRANCHISEE has failed to submit, create or maintain the foregoing records and documentation. The FRANCHISEE shall be bound by the estimate of FRANCHISOR unless it produces the foregoing records and documentation and those records and documentation demonstrate that the actual gross sales were lower than the estimate of FRANCHISOR.

ARTICLE IX ADVERTISING ASSESSMENT

9.1. Advertising Assessment. In addition to the payments due under Article VI and VII, FRANCHISEE shall pay an advertising assessment of 2% of its annual total gross sales as gross sales are defined in paragraph 7.3 at times and in a manner to be specified by FRANCHISOR.

9.2. Use of Assessment. Such assessment shall be used by FRANCHISOR for media advertising including but not limited to print, electronic and direct mail according to a plan developed by FRANCHISOR.

9.3. Advertising Fund. The assessment shall be deposited into and maintained in a

separate account entitled the “Twin Donut Advertising Fund”. The Fund shall be administered by FRANCHISOR.

ARTICLE X
ACCOUNTING AND BUSINESS RECORDS

10.1. Bookkeeping and Accounting. FRANCHISEE shall maintain a bookkeeping and accounting system which shall be in accord with the TWIN DONUT system and approved by FRANCHISOR.

10.2. Financial Statements. FRANCHISEE shall maintain and submit to FRANCHISOR a profit and loss statement and a balance sheet in forms acceptable to FRANCHISOR no later than 30 calendar days after the end of each 6 month period of operations. Both documents shall be certified by an independent Certified Public Accountant engaged by FRANCHISEE at its sole expense.

10.3. Required Documentation. FRANCHISEE shall maintain all forms, documents, records or reports which relate in any way to the business or financial operation of the Franchise including but not limited to:

- a. daily cash reports, and
- b. cash receipts journal and general ledger, and
- c. cash disbursements journal and weekly payroll register, and
- d. monthly bank statements, daily deposit slips and canceled checks, and
- e. all tax returns (federal, state and local) including sales tax returns, and
- f. invoices from suppliers (paid and unpaid), and

- g. daily production, throwaway and finishing records and weekly inventories, and
- h. such other records as FRANCHISOR may from time to time request.

10.4. Other Documentation. FRANCHISEE shall submit to FRANCHISOR any record, report or supporting documentation which FRANCHISOR may, in its sole discretion, request from time to time.

10.5. Inspection. FRANCHISOR may, in its sole discretion and at any time, inspect and copy any record, report or supporting documentation which relate in any way to the business or financial operation of the Franchise. FRANCHISEE shall fully and promptly cooperate with FRANCHISOR when FRANCHISOR exercises its right under this Paragraph.

10.6. Preservation of Records. FRANCHISEE shall preserve for a period of not less than 3 years during this Agreement and not less than 3 years after the expiration or termination of this Agreement all accounting records and supporting documentation described in this Agreement.

10.7. English Language. All records, reports and supporting documentation under this Agreement shall be written in the English language.

ARTICLE XI TRAINING OF PERSONNEL

11.1. Training. Prior to the commencement of business operations but as soon as possible after all agreements have been executed, FRANCHISEE shall attend a two-week Training Session at a Twin Donut Store which is currently being operated by FRANCHISOR. During the training session, FRANCHISEE shall observe and participate in all aspects of the actual operation of a Twin Donut Store including but not limited to baking and cooking methods, equipment use and maintenance and record keeping. If FRANCHISEE is a legal entity or a partnership, any person

designated by the FRANCHISEE to manage the daily operations shall be trained as well as at least one person who is a holder of shares or an ownership interest in the legal entity or partnership.

11.2. Manual. FRANCHISEE shall receive from FRANCHISOR a manual entitled Managerial Duties and Control and any other written instructional material which FRANCHISOR may issue from time to time. The Manual, including any additions, deletions, revisions or supplements, shall not materially alter FRANCHISEE's rights and obligations under this Agreement or place an excessive economic burden on FRANCHISEE's operations.

11.3. Experienced Store Manager. When FRANCHISEE assumes control of the operation or commences business, FRANCHISOR may, in its sole discretion and at its sole expense, place an experienced store manager in the Twin Donut Store to assist FRANCHISEE in the initial stages of the operation.

11.4. No Fees. FRANCHISEE shall not pay any fees for the Training Session or for any manuals or written instructional material it receives from FRANCHISOR except that FRANCHISEE shall pay for any travel and living expenses it incurs in connection with the Training Session.

ARTICLE XII REMODELING, RENOVATION AND COMPLIANCE WITH STANDARDS

12.1. Remodeling and Renovation. The FRANCHISOR may periodically require FRANCHISEE to remodel, renovate, update or re-equip the Twin Donut Store to ensure that it conforms with the current Twin Donut design and equipment standards. FRANCHISEE shall, at its sole cost, re-model, renovate and re-equip according to specifications provided by

FRANCHISOR. The total cost of such re-modeling, renovations, updating and re-equipping shall not exceed 50% of the original total cost of construction and equipment in any period of 24 consecutive calendar months during the term of this Franchise.

12.2. Standards Compliance Inspection. To insure compliance with the terms and conditions of this Agreement, FRANCHISOR may, in its sole discretion and at any time, enter the business premises and inspect any aspect of the business operation and confer with employees of FRANCHISEE in connection with any aspect of the business or financial operation.

12.3. Remedies on Non-Compliance. If FRANCHISEE fails, in any way, to observe any of its obligations or conform to the standards of quality of the TWIN DONUT system, FRANCHISOR may in its sole discretion and upon a 5-day prior notice to FRANCHISEE to cure, either:

- a. Correct any deficient or non-conforming condition and charge the expense of such correction to FRANCHISEE, or
- b. Place a representative in the business premises who shall have the power to require FRANCHISEE to correct any deficient or non-conforming condition until FRANCHISOR is satisfied that FRANCHISEE is in compliance.
- c. FRANCHISEE shall pay the costs and expenses incurred by FRANCHISOR incident to the placing of the representative.

12.4. No Liability. FRANCHISOR shall not be liable for or guilty of any tort or trespass if it chooses to exercise its rights under this Article.

ARTICLE XIII INSURANCE

13.1. Insurance Policies. FRANCHISEE shall procure and maintain in full force and effect at its sole expense and during the entire term of this Franchise, insurance policies protecting

FRANCHISEE and FRANCHISOR and the directors, officers and employees of FRANCHISOR against any loss, liability or expense from fire, personal injury, property damage or other casualty which arises out of or is incident to the use of the business premises or the business operation of the Franchise. FRANCHISOR shall be named as an additional insured on all of these insurance policies. FRANCHISOR may, in its sole discretion, require FRANCHISEE to deposit with FRANCHISOR a total of premium payments in an amount equal to 12 months of premium payments.

13.2. Policy Limits. Such policies shall be written by an insurance company which is acceptable to FRANCHISOR and shall be consistent with the coverage required under any Primary Lease on the premises or provide for:

- a. \$2,000,000 for injury to 1 or more persons per occurrence, and
- b. \$ 500,000 for property damage coverage
- c. Employer's Liability and Workers' Compensation as required by law.

13.3. FRANCHISOR'S Policy. The insurance coverage afforded by any policy procured under this Article shall not be limited in any way by reason of any insurance policy procured and maintained by FRANCHISOR.

13.4. Certificates. FRANCHISEE shall promptly provide certificates of insurance evidencing compliance with this Article upon request by FRANCHISOR. The certificate shall include a statement that the policies shall not be canceled or altered unless FRANCHISOR receives at least 10 days notice of such cancellation or alteration. If FRANCHISEE fails to provide certificates under this Paragraph, FRANCHISOR may, in its sole discretion, obtain insurance and charge the premium payments to FRANCHISEE against any franchise fees paid

under this Agreement.

13.5. Effect of Full Compliance. Full compliance with this Article shall not, in any way, relieve FRANCHISEE of any liability under Article XIV.

ARTICLE XIV
HOLDS HARMLESS AND INDEMNIFICATION

14.1. FRANCHISEE's Holds Harmless. FRANCHISEE shall hold FRANCHISOR completely harmless and indemnify FRANCHISOR for any injury to persons, any damage to property and any contractual liabilities to Third Parties including any costs or attorneys' fees which arise out of or are incident to the construction and equipping of the Twin Donut Store, the use of the business premises or the business operation of this Franchise.

14.2. Party to Cause of Action. If FRANCHISOR is made a party to any litigation by or against FRANCHISEE, FRANCHISEE shall pay all penalties, judgments, contributions or costs (including reasonable attorneys' fees) imposed on or incurred by FRANCHISOR as a result of such litigation.

14.3. No Application. Paragraph 14.2 of this Article shall not apply to litigation which is commenced by one Party to this Agreement against the other Party.

ARTICLE XV
COVENANTS AND WARRANTS OF FRANCHISEE

15.1. Maintenance. FRANCHISEE shall at all times maintain at its sole expense the interior and exterior of the business premises including all equipment and bathroom facilities and fixtures in the highest degree of cleanliness, healthfulness, orderliness, sanitation and in good

repair. FRANCHISEE acknowledges that it is essential to the public image of Twin Donut, Inc. that the Twin Donut Store be maintained as set forth in this Paragraph.

15.2. No Alteration. FRANCHISEE shall not alter the interior or exterior of the business premises in any way unless it receives the written consent of FRANCHISOR.

15.3. Operation. FRANCHISEE shall operate the business of the Franchise on such days and during such hours as FRANCHISOR shall determine in its sole discretion.

15.4. Approval of Advertising. FRANCHISEE shall not employ any advertising or promotional methods or copy unless FRANCHISOR has approved of such methods or copy in a signed writing.

15.5. Sales. FRANCHISEE shall exercise its best efforts to establish, maintain and increase sales of all products and merchandise under this Franchise.

15.6. Financial Records. FRANCHISEE shall maintain all financial records in accordance with this Agreement and generally accepted accounting principles.

15.7. Approved Products and Sources. FRANCHISEE shall offer for sale only donuts or pastries which are baked in the Twin Donut Store with equipment and materials purchased from sources designated or approved by FRANCHISOR. FRANCHISEE shall offer for sale luncheonette type food prepared in the Twin Donut Store with equipment and materials purchased from sources designated or approved by FRANCHISOR.

15.8. No Vending Machines. FRANCHISEE shall not place any vending machine or entertainment device nor sell any product (other than approved products) on the business premises unless FRANCHISEE has received the written consent of FRANCHISOR.

15.9. No Diversion. FRANCHISEE shall not, in any way, divert or attempt to divert

customers to any other competitive establishment from the Twin Donut Store of this Franchise or from any other Twin Donut Store.

15.10. Personal Operation. FRANCHISEE shall personally operate and manage the business of the Franchise or, if FRANCHISEE is a limited liability company, corporation or partnership, an individual shareholder or partner who owns 50% or more of the shares or ownership interests, whichever applies, shall personally operate and manage the business of the Franchise.

15.11. No Litigation. FRANCHISEE warrants that it or, if a corporation, partnership or limited liability company, any individual who owns 50% or more of the shares, ownership interests or membership interests of FRANCHISEE does not or do not have any civil, administrative or other legal or equitable causes of action pending against it in any court or administrative agency in the United States which could, in any way, adversely affect its ability to perform its duties under this Agreement.

15.12. Capability. FRANCHISEE warrants that it or, if a corporation or partnership or limited liability company, any individual who owns 50% or more of the shares or ownership interests of FRANCHISEE has or have the financial and technical capability to perform all of its duties under this Agreement and has no actual or constructive knowledge of any fact or condition which could adversely affect its ability to perform its duties under this Agreement.

15.13. Compliance with Lease. FRANCHISEE covenants that it shall comply with each obligation and satisfy each condition of any lease and sub-lease on the Demised Premises. FRANCHISEE shall not commit any act or fail to perform any act which would cause the lease or sub-lease to expire or terminate.

ARTICLE XVI
EMPLOYEES OF FRANCHISEE

16.1. Employees. FRANCHISEE shall employ at its sole expense a sufficient number of qualified persons to meet public demand.

16.2. Skill and Appearance. Each employee shall conform to such standards of skill, personal hygiene and demeanor as FRANCHISOR shall prescribe. Each employee shall wear uniforms or other dress prescribed by FRANCHISOR at all times during which he or she performs any duty as an employee or any function within the scope of his or her employment.

16.3. Managers. Any employee who performs a managerial function or receives training from FRANCHISOR shall execute a covenant of non-competition which is the same as the covenant set forth in Article XVII.

16.4. Special Training. If any employee performs any work or function which FRANCHISOR deems to require special training or certification, such employee shall receive such training or certification at the sole expense of FRANCHISEE.

ARTICLE XVII
COVENANT OF NON-COMPETITION AND CONFIDENTIALITY

17.1. No Competition During the Term. During the term of this Agreement, FRANCHISEE shall not in any capacity, except with the written consent of FRANCHISOR, engage at any other place in any business which is the same as, competitive with or substantially similar to the business of a Twin Donut Franchise. FRANCHISEE shall not knowingly employ or seek to employ any person who is employed by any other business operated under the name of TWIN DONUT and shall not, directly or indirectly, induce any such person to leave his or her employment.

17.2. No Competition After the Term. For a period of 24 consecutive calendar months after the month in which this Agreement expires or terminates, FRANCHISEE shall not directly or indirectly, own, enter the employment of, or render services to any person, legal entity or association engaged in a business that is the same as, competitive with or substantially similar to the business of a Twin Donut Franchise and which is located either on the Approved Site or within a 25 mile radius of any of FRANCHISEE's places of business, the place of business of any company-owned Twin Donut Store or any place of business of any other Twin Donut Franchisee. During such period of time, FRANCHISEE shall not within such territory engage in such business on its own account, or become interested directly or indirectly, as an individual, partner, shareholder, member, manager, director, officer, clerk, principal, agent, employee, trustee, or in any relation or capacity whatsoever.

17.3. No Successor Lease Term on Demised Premises. For a period of 24 consecutive calendar months after the month in which this Agreement expires or terminates, FRANCHISEE shall not directly or indirectly, own, enter the employment of, or render services to any person, legal entity or association who so that engages in a business that is the same as, competitive with or substantially similar to the business of a Twin Donut Franchise on the Demised Premises.

17.4. Lesser Included Covenants Enforceable. If all or any part of the covenants set forth under this Article are found to be unreasonable or unenforceable for any reason by an arbitrator or a court, the arbitrator or court is empowered to revise or construe this Article so that it conforms to the then applicable law governing noncompete covenants and is not obligated to find this Article per se unenforceable. FRANCHISEE shall be bound by any such revision or construction as if it was an original term of this Agreement.

17.5. Confidentiality. FRANCHISEE shall not communicate or divulge to, or use for the benefit of, any other person, legal entity or association any information or knowledge concerning the methods of manufacture, promotion, sale, or distribution used or employed by FRANCHISOR in and about its business which may be communicated to FRANCHISEE or which FRANCHISEE may acquire by virtue of its operation under the terms of this Agreement. FRANCHISEE shall not do any act prejudicial or injurious to the business or goodwill of FRANCHISOR.

17.6. Enforcement. The FRANCHISEE acknowledges that if FRANCHISEE violates this Article that FRANCHISOR shall suffer immediate and irreparable harm and lack an adequate remedy at law. In any cause of action by FRANCHISOR to enforce the covenants under this Article, FRANCHISEE waives the equitable defenses of no irreparable harm and existence of an adequate remedy at law.

17.7. Independent Covenants. The covenants set forth in this Article shall be construed as independent of any other provision of this Agreement unless otherwise stated, and the existence of any claim or cause of action of FRANCHISEE against FRANCHISOR, whether predicated on this Agreement or otherwise, shall not constitute a defense to the enforcement by FRANCHISOR of such covenants.

17.8. Definitions. For the purposes of this Article, if FRANCHISEE is a partnership, corporation or limited liability company, the term "FRANCHISEE" shall include but not be limited to any individual partner, officer, director, shareholder, manager, member, agent or employee of any such partnership, corporation or limited liability company and any relative of the first degree by blood or marriage of any such individual.

17.9. Waiver of Defense. On behalf of any person within the definition under Paragraph

17.7, the signatory for FRANCHISEE waives any defense to an action to enforce this Article at law or in equity which defense is asserts that a person within that definition is not obligated under this Article because such person did not execute this Agreement or otherwise personally agree to be bound by this Article.

17.10. Survival. The covenants and terms of this Article shall survive the expiration or termination of this Agreement.

ARTICLE XVIII
ASSIGNMENT AND TRANSFER

18.1. No Assignment. Neither FRANCHISEE nor any partner of FRANCHISEE, if FRANCHISEE is a partnership, nor any shareholder of FRANCHISEE, if FRANCHISEE is a corporation nor any member of FRANCHISEE if FRANCHISEE is a limited liability company, shall assign any benefit or transfer any right nor attempt to make any such assignment or transfer in connection with any interest which arises out of or is incident to the Franchise or assign any benefit or transfer any right in the entity to which FRANCHISOR has granted the Franchise except as otherwise set forth in this Article.

18.2. Procedure. If FRANCHISEE desires to assign any benefit or transfer any right in any interest or asset described in Paragraph 18.1, FRANCHISEE shall inform FRANCHISOR in writing of such desire and shall offer to assign or transfer any such benefit or right to FRANCHISOR before making any such offer to a Third Party or accepting any such offer from a Third Party.

- a. The terms of any such offer shall be the same as the best bona fide offer, if any, received by FRANCHISEE from any Third Party.
- b. FRANCHISEE shall, in the same writing, fully disclose to FRANCHISOR

the actual identity of the Third Party, including the shareholders, directors, officers, partners, members and managers, if any.

18.3. First Refusal. Within 30 calendar days after either the date on which FRANCHISOR receives from FRANCHISEE the terms of an offer or the date on which FRANCHISOR receives from FRANCHISEE the terms of the best bona fide offer made by a Third Party and the identity of the Third Party whichever date is later, FRANCHISOR may, to the exclusion of any other person or entity, accept or reject the offer or submit counteroffers to FRANCHISEE.

18.4. Assignment to Third Party. If, at the end of the 30 day period, FRANCHISOR does not accept such offer or the Parties are otherwise unable to agree on terms, then FRANCHISEE may assign or transfer any benefits or rights under this Franchise to a Third Party, as long as:

- a. The Third Party executes the Franchise Agreement of FRANCHISOR contained in the Franchise Offering Circular for the year in which the assignment or transfer is made, a sworn closing and estoppel certificate and any other contract or document required by FRANCHISOR or any of its affiliates.
 - (I) If the Third Party is a corporation, then all officers and shareholders shall execute the affidavit on behalf of the corporation and not as individuals, or
 - (ii) If the Third Party is a partnership then all partners shall execute the affidavit, or
 - (iii) If the Third Party is a limited liability company then all members and managers shall execute the affidavit on behalf of the limited liability company and not as individuals, and
- b. The Third Party demonstrates at least the same level of business qualifications, credit rating and moral character possessed by FRANCHISEE,
 - (I) If the Third Party is a corporation then the shareholder(s) who will substantially operate and participate in the business shall so demonstrate, or

- (ii) If the Third Party is a partnership then the partner(s) who will substantially operate and participate in the business shall so demonstrate, or
 - (iii) If the Third Party is a limited liability company then the member who will substantially operate and participate in the business shall so demonstrate, and
- c. Any document of sale or stock certificate shall state prominently on its face that any assignment or transfer is subject to the terms of this Agreement, the Franchisee Store Lease and any other contract, and
- d. FRANCHISEE has fully performed all of its payment and other obligations under this Agreement, the Franchise Store Lease, the Security Agreement and other contract, and
- e. FRANCHISEE pays to FRANCHISOR a transfer fee equal to the dollar amount of the Initial Franchise Fee charged by FRANCHISOR for new Franchises at the time the assignment or transfer occurs, and
- f. FRANCHISEE and other affiliated persons execute a sworn affidavit affirming to be to be bound by Article XVII, and
 - (I) If the Third Party is a corporation, then all officers and shareholders shall execute the affidavit, or
 - (ii) If the Third Party is a partnership, then all partners shall execute the affidavit, or
 - (iii) If the Third Party is a limited liability company, then all members and managers shall execute the affidavit, and
- g. FRANCHISOR approves of the Third Party in a signed writing which approval shall not be unreasonably withheld or delayed.
- h. The Third Party is not a limited partnership.

18.5. Transfer of Shares. The sale, transfer or exchange of 50% or more of the shares of FRANCHISEE if it is a corporation or 50% or more of the ownership interests of FRANCHISEE

if it is a partnership or a limited liability company shall be deemed an assignment and subject to the terms of this Article.

18.6. Assignment by FRANCHISOR. FRANCHISOR may assign any benefit or transfer any right as long as the assignee or transferee agrees in writing to assume all obligations of FRANCHISOR under this Agreement except for any accrued liabilities. Any assignee or transferee shall agree not to substantially vary the obligations of FRANCHISEE or the risks to FRANCHISEE from those contemplated under this Agreement.

ARTICLE XIX EVENTS IN DEFAULT

19.1. Events in Default. An Event in Default shall be deemed to have occurred if:

- a. FRANCHISEE fails to forward monies due under this Agreement along with the specified documentation on the specified dates or breaches any other agreement or contract with FRANCHISOR, or
- b. FRANCHISEE fails to procure and maintain the specified insurance coverage and provide certificates of insurance, or
- c. FRANCHISEE fails to maintain the financial and accounting system under this Agreement, or
- d. FRANCHISEE fails to report accurately and in good faith any gross sales, or
- e. FRANCHISEE violates any provision of the lease on the Demised Premises and thereby causes the lease to expire or terminate, or
- f. FRANCHISEE fails to maintain all records and documentation required under this Agreement or fails to provide any record or document requested by FRANCHISOR under this Agreement, or
- g. FRANCHISEE fails to comply with any other obligation or duty set forth in this Agreement, or

- h. FRANCHISEE violates any provision of the Franchisee Store Lease with any membership series of TDS Leasing, LLC, the Security Agreement (if any) and the Promissory Note (if any) with Spartan Built, Ltd. or any other agreement or contract either with FRANCHISOR or with an affiliate of FRANCHISOR, respectively,
- I. FRANCHISEE fails to promptly apply for or perform every legal act necessary to obtain each government and quasi-government approval, consent and license necessary to construct, equip, open and operate a Twin Donut Store, or
- j. FRANCHISEE fails to maintain the Twin Donut Store as provided in Paragraph 15.1.

19.2. Cure of Default. If an Event in Default occurs other than an Event in Default under Paragraph 19.1(e), FRANCHISEE shall have 5 calendar days after the date upon which it receives written Notice to Cure from FRANCHISOR to cure any such Default. If FRANCHISEE fails to cure within the 5-day period, then the Franchise granted under this Agreement shall expire under Paragraph 20.1 of Article XX. If the Event in Default does not involve the payment of money, then the Default shall be deemed cured if, within the 5-day period, FRANCHISEE takes deliberate action that is calculated to promptly cure the Default even though the Default is not actually cured within the 5-day period.

19.3. Cure of Default under Paragraph 19.1(e). If an Event in Default occurs under Paragraph 19.1(e), then the method of cure and the cure period shall be the method and period specified in whichever agreement, lease or contract has been breached.

19.4. Persistent Default. If FRANCHISEE consistently fails to perform any payment obligation under this Agreement, then an Event in Default shall be deemed to have occurred even though FRANCHISEE may have cured each failure to pay in each individual instance.

19.5. Abandonment. If FRANCHISEE fails to transact the business of the Franchise for 5

consecutive calendar days in any one calendar month or for a total of 7 days that need not be consecutive days in any one calendar month, FRANCHISEE shall be deemed to have abandoned the Franchise and FRANCHISOR may terminate this Agreement. A force majeure shall toll the running of any time period under this Paragraph.

ARTICLE XX
EXPIRATION OR TERMINATION

20.1. Immediate Expiration. This Agreement and the Franchise granted under this Agreement shall immediately expire as if the chronological term of the Franchise had expired if FRANCHISEE fails to cure an Event in Default under Paragraph 19.2 and 19.3 of Article XIX.

20.2. Discretionary Termination. FRANCHISOR may, in its sole discretion, terminate this Agreement prior to the expiration of its term if:

- a. Any individual signatory to this Agreement dies subject to Article XXI or any legal entity which is a signatory to this Agreement is dissolved or otherwise ceases to exist, or
- b. FRANCHISOR becomes insolvent or makes an assignment for the benefit of creditors, or
- c. A petition in bankruptcy is filed by or against FRANCHISEE or FRANCHISEE is adjudicated a bankrupt, or
- d. A receiver or other custodian is appointed either with or without the consent of FRANCHISOR, or
- e. The real or personal property of FRANCHISEE is sold after levy by a duly appointed authority.

20.3. Events Upon Expiration or Termination. Upon expiration or termination of this Agreement, FRANCHISEE shall immediately:

- a. Pay all monies due and owing under this Agreement and any other contract or lease with FRANCHISOR and any damages or costs including attorneys' fees incurred by FRANCHISOR as a result of default by FRANCHISEE,

and

- b. Deliver possession of the business premises to FRANCHISOR according to any lease obligation or lease with FRANCHISOR, and
- c. Discontinue the use of all trade names, trademarks, signs, structures, and forms of advertising indicative of TWIN DONUT or its business or products and shall make or cause to be made such changes in signs, buildings, and structures as FRANCHISOR shall reasonably direct so as to effectively distinguish the same from its former appearance and from any other TWIN DONUT place of business. If FRANCHISEE shall upon request fail or omit to make such changes or cause them to be made, then FRANCHISOR shall have the right to enter upon the premises upon which such business is being conducted without being liable for or guilty of trespass or any other tort, and shall have the right to make such changes or cause them to be made at the expense of FRANCHISEE, which expense FRANCHISEE shall pay on demand. FRANCHISEE shall also on request of FRANCHISOR, and upon the payment of the reasonable market value, deliver to FRANCHISOR all items and things bearing the trademark or trade name of TWIN DONUT and,
- d. Return all manuals or other written operating information supplied by FRANCHISOR.

ARTICLE XXI
DEATH OR INCAPACITY OF FRANCHISEE

21.1. Death or Incapacity. If FRANCHISEE or any partner or shareholder or member of FRANCHISEE who substantially manages and operates the business of the Franchise dies or is rendered incapable of operating the Franchise, then the legal representative of the decedent or incompetent and all surviving shareholders and partners, if any, shall apply in writing to FRANCHISOR for the right to transfer the Franchise or the interest of the decedent or incompetent to the person(s) set forth in the written application.

21.2. Application. The written application shall be received by FRANCHISOR within 30 days after the death or incapacity and it shall demonstrate that the proposed transfer and transferees shall satisfy paragraph 18.4 of Article XVIII.

21.3. Consent. If all conditions in paragraph 18.4 of Article XVIII are satisfied, then FRANCHISOR shall consent to the proposed transfer.

21.4. Rights of Estate. If no application is made during the 30 day period or the conditions in paragraph 18.4 are not satisfied, then the legal representative and any surviving shareholders or partners or members shall have only those rights in the Franchise which FRANCHISEE would have upon termination of the Franchise.

ARTICLE XXII ARBITRATION

22.1. Arbitration. Subject to Paragraph 22.4, if a dispute arises between the Parties which arises out of any provision of this Agreement or in connection with this Agreement, then FRANCHISOR shall have the option of submitting the dispute to arbitration in the State of New York according to the rules of the American Arbitration Association (AAA).

- a. If FRANCHISOR is the claimant, then FRANCHISOR shall exercise its option to arbitrate at any time prior to commencing judicial proceedings against FRANCHISEE.
- b. If FRANCHISEE commences judicial proceedings, then FRANCHISOR shall exercise its option to arbitrate at any time before the last day of the time period within which FRANCHISOR must respond to a summons/complaint or, if the judicial proceedings are commenced by any motion or order to show cause, the last day before the actual return date of any such motion or order to show cause.

22.2. Binding Effect. The decision/award of the AAA shall be final and binding on the

Parties and either Party may docket the decision/award as a final judgment in the courts of the State of New York.

22.3. Discovery. If FRANCHISOR exercises its option to arbitrate under this Article, then FRANCHISEE shall provide to FRANCHISOR any record, report or supporting documentation which FRANCHISEE is required to maintain under this Agreement or any record, report or supporting documentation which FRANCHISEE would be required to provide to FRANCHISOR under the Disclosure provisions of the Civil Practice Laws and Rules of New York or under the Discovery provisions of the Federal Rules of Civil Procedure. The FRANCHISEE shall have the same discovery as FRANCHISOR under this Paragraph.

22.4. Rights, Actions or Remedies under Franchisee Store Lease with Leasing Affiliate. . If FRANCHISEE leases the business premises from a Leasing Affiliate of FRANCHISOR, the FRANCHISOR may, in its sole discretion, authorize the Leasing Affiliate to pursue any rights, actions or remedies available under any such Lease for non-payment of franchise fees. If the FRANCHISOR makes that authorization, then this Article shall not apply to any action or proceeding brought by the Leasing Affiliate pursuant to that authorization and under the Lease.

ARTICLE XXIII GOVERNANCE PROVISIONS

23.1. Independent Contractors. FRANCHISOR and FRANCHISEE are strictly independent contractors. FRANCHISEE is not, in any way, an employee, partner, joint venturer or agent of FRANCHISOR. FRANCHISEE shall not, in any way, bind FRANCHISOR to any person unless FRANCHISEE has received the written consent of FRANCHISOR.

FRANCHISEE shall undertake all reasonable measures in its operation to inform Third Parties that FRANCHISOR has no direct or indirect liability for any act or agreement taken by FRANCHISEE and that FRANCHISOR does not control the performance of FRANCHISEE.

23.2. Strict Compliance. No failure of FRANCHISOR to exercise any right or to insist upon strict compliance by FRANCHISEE with any obligation and no custom or practice of the Parties at variance with this Agreement shall constitute a waiver of FRANCHISOR's rights to demand exact compliance. Waiver by FRANCHISOR of any particular default by FRANCHISEE shall not affect or impair FRANCHISOR's rights in respect to any subsequent default of the same or of a different nature, nor shall any delay or omission of FRANCHISOR to exercise any rights arising from such default affect or impair FRANCHISOR's rights as to such default or any subsequent default.

23.3. Severability and Independent Covenants. If any term, condition, covenant, provision or any part thereof of this Agreement is invalid, illegal or incapable of being enforced, by reason of any rule of law, administrative order, judicial decision or public policy, all other terms, conditions, covenants and provisions or parts thereof shall remain in full force and effect. No covenant, obligation or provision shall be deemed dependent upon any other covenant, obligation or provision unless so expressed in this Agreement.

23.4. Governing Law. This Agreement shall be governed exclusively by the Laws of the State of New York not including the conflicts of laws principles of New York. Any dispute arising from this Agreement that is not resolved by arbitration (Article XXII) shall be resolved only in the Courts of or in the State of New York.

23.5. Full Agreement. The terms and conditions of this Agreement constitute the full and

complete agreement between the Parties. No other verbal or written agreement shall, in any way, vary or alter any provision of this Agreement unless both Parties consent to vary or alter any provision of this Agreement in a signed writing. Each Party waives the application of any exception to the Statute of Frauds enacted under New York law that may render an oral modification effective and binding on the Parties.

23.6. Integration. This Agreement is intended to be an integrated writing and any prior oral or written agreements between the Parties are merged into this Agreement and extinguished. No custom, industry standard or course of dealing between the Parties shall in any way vary or alter the terms and conditions of this Agreement.

23.7. Jointly Drafted. The Parties waive the defense of *contra proferentum* so that, in the event of a dispute, this Agreement shall not be construed against either party.

23.8. Waiver of Equitable Remedies. The FRANCHISEE waives all equitable remedies including equitable rescission and rescission at law.

23.9. Further Assurances. If requested by FRANCHISOR, FRANCHISEE shall execute and deliver such other documents and take such other action as may be necessary to effect the terms of this Agreement and the terms of any other agreement or lease made by FRANCHISEE with any affiliate of FRANCHISOR in connection with the Franchise.

23.10. Assignment to Corporation or Limited Liability Company. If an individual or a general partnership that is not a limited liability partnership executes this Agreement, FRANCHISOR shall approve an assignment of the Franchise and this Agreement to a corporation or limited liability company as long as 51% or more of the common shares or membership interests of any such corporation or limited liability company are owned by at least one of the

individuals who executed this Agreement as FRANCHISEE and the corporation or limited liability company assumes all of the obligations of FRANCHISEE in a written assignment prepared by FRANCHISOR. Nothing in this Paragraph shall be construed to relieve, alter or modify any obligation of any individual who has executed any personal guaranty in connection with this Franchise.

23.11. Limitation on Actions. The statute of limitations on any claim or cause of action by FRANCHISEE arising from or incident to any violation of any franchise law or regulation shall be 365 consecutive calendar days from the date on which the violation occurred or should have been discovered.

23.12. Benefit and Binding Effect. All rights and obligations of this Agreement shall benefit and bind all successors in interest, assigns, transferees or heirs of each Party to this Lease.

23.13. Nature of Obligations. All obligations of FRANCHISOR under this Agreement run only to FRANCHISEE. No other person may rely on or enforce any obligation of FRANCHISOR or obtain redress for any breach of any such obligation either directly or by subrogation.

23.14. Notices. All notices shall be sent by the most expeditious means available including but not limited to facsimile, overnight courier or certified or registered mail to the addresses set forth below the signatures or to the address of the Twin Donut Store set forth in Article III. Any such notice shall be deemed delivered when received. FRANCHISEE acknowledges that its attorney or other designated corporate agent is authorized to issue any notice due or permitted

under this Agreement.

INTENDING TO BE LEGALLY BOUND, the undersigned Parties, have duly caused this Agreement to be executed and any individual signatory(ies) executing on behalf of a corporation or limited liability company are duly authorized by their respective corporations or limited liability company to execute this Agreement.

Signature

By: George P. Psathas, President
for Twin Donut, Inc.

FRANCHISOR

Signature

Print Name:
Title:
For:

FRANCHISEE

By executing this Agreement, the undersigned shareholder(s) of the corporate Franchisee or members of the limited liability company Franchisee or partners of the partnership Franchisee or individual Franchisee personally accepts and shall comply with Article XVII of this Agreement. The undersigned shall cause any person described in Paragraph 17.7 to execute and be bound by Article XVII and acknowledges that the Franchisor has executed this Agreement in reliance upon the commitments contained in Article XVII.

Signature

Print Name:

PERSONAL GUARANTY

DATED: _____, 2006
PERSONAL GUARANTOR(S):
FRANCHISEE:
FRANCHISOR: Twin Donut, Inc.
LOCATION:

In consideration of and as an inducement to the execution of the foregoing Franchise Agreement of Twin Donut, Inc., each of the undersigned unconditionally guarantees to FRANCHISOR that FRANCHISEE or any assignee-entity formed by him under Article XXIII, Paragraph 23.9 (referred to as FRANCHISEE) shall timely make all payments, perform all duties and comply with all obligations set forth in the foregoing Agreement.

If FRANCHISEE fails to make any payment, perform any duty or comply with any obligation, the undersigned shall personally make any such payment, perform or cause to be performed any such duty or comply or cause compliance with any such obligation. The undersigned shall be primarily liable under this guaranty and waives any notices or demands as a condition to liability. The undersigned shall be jointly and severally liable on this guaranty.

The undersigned shall not be liable under this Guaranty if FRANCHISEE simultaneously vacates and surrenders the Demised Premises to the lessor and unconditionally releases the Twin Donut Franchise to Twin Donut, Inc. However, the undersigned individual shall remain liable for any payment or obligation that accrues between the date that FRANCHISEE fails to pay or perform and the date on which vacates and surrenders the Demised Premises.

The obligations of GUARANTOR are unconditional and independent from any claim or

cause of action GUARANTOR has or may have against FRANCHISOR or any subsidiary or affiliate of FRANCHISOR. The GUARANTOR shall not interpose any set off or defense that arises from or is incident to any such claim or cause of action to limit or avoid its obligations under this Guaranty. The rights of FRANCHISOR under this Guaranty are fully vested and shall not be modified or altered by implication. This Guaranty shall remain in full force and effect without regard to any change in the circumstances that existed when this Guaranty was executed or the occurrence of any condition, whether contemplated or not contemplated by the Parties at the time of execution.

I/We, the undersigned, have read the foregoing Guaranty and consulted with an attorney of my choosing as to the legal nature and effect of the Guaranty.

Signature

Print Name: an individual PERSONAL GUARANTOR

Street Address: _____

County: _____ City: _____ Zip: _____

State: _____ Tel. () _____

TAB 12
SAMPLE UFOC

SAMPLE UFOC
NOT FOR FILING OR DISTRIBUTION

"TWIN DONUT"
"TWIN DONUT plus"
Trade Name
Trade Service Mark

INFORMATION FOR PROSPECTIVE FRANCHISEES
REQUIRED BY THE FEDERAL TRADE COMMISSION

* * *

To protect you, we have required your franchisor to give you this information. We have not checked it, and do not know if it is correct. It should help you make up your mind. Study it carefully. While it includes some information about your contract, do not rely on it alone to understand your contract. Read all of your contracts carefully. Buying a franchise is a complicated investment. Take your time to decide. If possible, show your contract and this information to an advisor, such as a lawyer or an accountant. If you find anything you think may be wrong or anything important that has been left out, you should let us know about it. It may be against the law.

There may also be laws on franchising in your state. Ask your state agencies about them.

2006 Franchise Offering Circular
Twin Donut, Inc.

"TWIN DONUT"
"TWIN DONUT plus"
Trade Name
Trade Service Mark

FRANCHISE OFFERING CIRCULAR

OF

TWIN DONUT, INC.
35 EAST GRASSY SPRAIN ROAD
SUITE 500
YONKERS, NEW YORK 10710
Telephone: (914) 779-7100
Facsimile: (914) 779-2426
E-mail:twdonut@mindspring.com

The Franchise offered is a Twin Donut Store for the operation of a retail donut/luncheonette store and a facility for baking donuts in the Twin Donut Store, a satellite Twin Donut Store from which baked goods are sold but are not produced and a concession counter from which baked goods are sold but not produced.

The Initial Franchise Fee and the estimated Initial Investment are as follows:

A. Initial Franchise Fee

1. Under Full Service Store Franchise Plan..... \$25,000 for grant of franchise and legal and administrative expense.
2. Under the Independent Satellite Franchise Plan...\$15,000 for grant of franchise and legal and administrative expenses.
3. Under the Concession Franchise Plan.....\$5,000 for grant of franchise and legal and administrative expenses
4. \$0 to \$500,000 for goodwill and business reputation depending on the location and, if a pre-existing Store, the length of time

the Twin Donut Store has been operating.

B. Initial Investment Under Full Service Store Plan:

1. Real Property...\$3,900-\$14,000 per month; Requires approx. 1800-4000 sq.ft. in high commercial traffic area.
2. Construction/Equipment...\$250,000-\$500,000.
3. Inventory...\$5,000.
4. Working Capital...\$10,000.
5. Statutory Licenses...\$300-\$500.
6. Insurance Premiums...\$5,000-\$18,000.

C. Initial Investment Under Independent Satellite Franchise Plan

1. Real Property...\$2,900-\$11,000; Requires approx. 800-1500 sq.ft. in high commercial traffic area.
2. Construction/Equipment...\$175,000-\$250,000.
3. Inventory...\$5,000.
4. Working Capital...\$10,000.
5. Statutory Licenses...\$300-\$500.
6. Insurance Premiums...\$3000-\$15,000.

D. Initial Investment Under Concession Franchise Plan

1. Real Property...Requires approx. 400-800 sq. ft.
2. Construction/Equipment...\$15,000-\$30,000.

3. Inventory....\$1,000.
4. Working Capital...N/A
5. Statutory Licenses...\$300-\$500.
6. Insurance Premiums...Cost of Additional Operation

SPECIAL RISK FACTORS

1. THE TERM OF THIS FRANCHISE IS THE ONLY TERM BEING OFFERED. THE FRANCHISOR IS NOT OBLIGATED UNDER ANY CIRCUMSTANCES TO RENEW THE FRANCHISE AGREEMENT UPON THE EXPIRATION OF THE FRANCHISE TERM.

2. THE BUSINESS OF A TWIN DONUT STORE/CONCESSION DEPENDS DIRECTLY ON THE VOLUME OF PEDESTRIAN AND STREET TRAFFIC THAT PASSES BY OR IN THE VICINITY OF THE TWIN DONUT STORE. SHOULD THE DEMOGRAPHY OF THE AREA IN WHICH THE TWIN DONUT STORE IS LOCATED CHANGE IN A WAY THAT REDUCES THAT VOLUME OF TRAFFIC, THEN THE TWIN DONUT STORE WILL EXPERIENCE A REDUCTION IN REVENUES.

INFORMATION COMPARING FRANCHISORS IS AVAILABLE. CALL THE STATE ADMINISTRATORS OR YOUR PUBLIC LIBRARY FOR SOURCES OF INFORMATION. REGISTRATION OF THIS FRANCHISE BY NEW YORK STATE DOES NOT MEAN THAT NEW YORK STATE RECOMMENDS OR HAS VERIFIED THE INFORMATION IN THIS OFFERING CIRCULAR. IF YOU LEARN THAT ANYTHING IN THE OFFERING CIRCULAR IS UNTRUE, CONTACT THE FEDERAL TRADE COMMISSION AND NEW YORK STATE DEPARTMENT OF LAW BUREAU OF INVESTOR PROTECTION AND SECURITIES, 120 BROADWAY, 23RD FLOOR NEW YORK, N.Y. 10271.

The effective date of this Franchise Offering Circular is September 29, 1986.

Amended: _____ (Amendment 19)

THE FRANCHISOR MAY, IF IT CHOOSES, NEGOTIATE WITH YOU ABOUT ITEMS COVERED IN THE PROSPECTUS. HOWEVER, THE FRANCHISOR CANNOT USE THE NEGOTIATING PROCESS TO PREVAIL UPON A PROSPECTIVE FRANCHISEE TO ACCEPT TERMS WHICH ARE LESS FAVORABLE THAN THOSE SET FORTH IN THIS PROSPECTUS.

TABLE OF CONTENTS

	<u>Page</u>
ITEM 1. FRANCHISOR AND ITS PREDECESSORS.	9
ITEM 2. IDENTITY AND BUSINESS EXPERIENCE OF PERSONS AND COMPANIES AFFILIATED WITH FRANCHISOR.....	11
ITEM 3. LITIGATION.	12
ITEM 4. BANKRUPTCY.	14
ITEM 5. INITIAL FRANCHISE FEE.	14
ITEM 6. OTHER FEES.....	15
ITEM 7. INITIAL INVESTMENT.	18
ITEM 8. RESTRICTIONS ON SOURCES OF PRODUCTS AND SERVICES.....	22
ITEM 9. FRANCHISEE'S OBLIGATIONS.....	27
ITEM 10. FINANCING.	30
ITEM 11. FRANCHISOR'S OBLIGATIONS.	31

ITEM 12. TERRITORY.....	34
ITEM 13. TRADEMARKS.....	35
ITEM 14. PATENTS, COPYRIGHTS AND PROPRIETARY INFORMATION.	36
ITEM 15. OBLIGATION OF FRANCHISEE TO PARTICIPATE IN THE ACTUAL OPERATION OF FRANCHISE.	36
ITEM 16. RESTRICTIONS ON WHAT THE FRANCHISEE MAY SELL.	37
ITEM 17. RENEWAL, TERMINATION TRANSFER AND DISPUTE RESOLUTION.	37
ITEM 18. PUBLIC FIGURES.	39
ITEM 19. EARNINGS CLAIMS.	40
ITEM 20. INFORMATION REGARDING FRANCHISES OF FRANCHISOR.	40

APPENDICES

TAB 1 LIST OF FRANCHISES UNDER AGREEMENT.....	43
TAB 2 APPROVED SOURCES.	44
TAB 3 SAMPLE EQUIPMENT LIST.	45

TAB 4 AUDITED FINANCIAL STATEMENTS.....	46
TAB 5 FORM FRANCHISE AGREEMENT FORM EXTENSION SATELLITE AGREEMENT.....	47
TAB 6 FORM FRANCHISEE STORE LEASE.....	48
TAB 7 FORM PROMISSORY NOTE FORM SECURITY AGREEMENT FORM AFFIDAVIT OF CONFESSION OF JUDGMENT	49
TAB 8 FORM SUBFRANCHISOR AGREEMENT.....	50
TAB 9 FORM FRANCHISE OPTION AGREEMENT.....	51
TAB 10 FORM CONCESSION FRANCHISE AGREEMENT (Host and Non Host Franchisor).....	52
RECEIPT.....	53

ITEM 1. FRANCHISOR AND ITS PREDECESSORS

A. Twin Donut, Inc.

Twin Donut Inc. is a New York corporation and was incorporated on December 30, 1959. It does business under that name. Its principal place of business is 35 East Grassy Sprain Road Suite 500 Yonkers, New York. George P. Psathas, located at the foregoing address, is the agent of the Twin Donut, Inc. for service of process. There are no predecessors to Twin Donut, Inc.

B. Business of Franchisor

The Franchisor is engaged exclusively in the business of selling Franchises to operate Twin Donut Stores. From time to time Franchisor operates Twin Donut Stores for its own account but intends to sell them as Twin Donut Franchises.

C. Description of Franchise

A Twin Donut Franchise is a retail food service establishment. The Franchisor offers following types of Twin Donut Franchises:

1. Twin Donut Store - There are three phases to the operation:
 - a. Donuts are baked on the premises and sold at the lunch counter or for carry out to the public.
 - b. Luncheonette type meals, including sandwiches and submarine sandwiches are sold either at the lunch counter or cafeteria-style.
 - c. For Franchisees who, in the opinion of Franchisor, have successfully operated the Twin Donut Store, Franchisor may grant the right to expand the Franchise and open an Extension Satellite Franchise. The location of and the lease for the Extension Satellite Store must be approved by Franchisor. The Franchisee shall pay a

\$10,000 fee to Franchisor in exchange for the grant of the Extension Satellite Franchise. All other terms and conditions of the Franchise Agreement and any other agreement that Franchisee has executed with any Twin Donut affiliate shall apply to the Extension Satellite Franchise. The Franchisee is not obligated to open an Extension Satellite Franchise.

2. Twin Donut Independent or Extension Satellite - There is one phase to the operation which is the retail sale of baked goods that have been prepared in a Full Service Twin Donut Store. The Franchisor attempts to facilitate contracts and relationships between existing Twin Donut Franchisees and the Independent Satellite. However, the Franchisor cannot compel a Twin Donut Franchisee to sell product to an Independent Satellite nor does the Franchisor guarantee any supply of product. Baking is not done on the premises of the Satellite. Unlike an Extension Satellite Store, the Independent Satellite is not associated with a Twin Donut Store. The Franchisee pays a \$15,000.00 fee in exchange for the grant of the Independent Satellite Store.

3. Twin Donut Concession Franchise - There is one phase to the operation which is the retail sale of baked goods that have been prepared in a Twin Donut Store. Baking is not done on within the Concession Area. A Concession Franchise may be granted to a person or entity who or that is operating another franchise (referred to as the Host Franchise) on premises in which the Concession Franchise will operate such as a gasoline station, food court or retail grocery outlet. A Concession Franchise may also be granted to a person or entity who or that is operating a business without a Host Franchise.

The general market for the products and services is general pedestrian and vehicle street

traffic that passes by or in the vicinity of the Twin Donut Franchise. Because Twin Donut Franchises are restaurants, they are required to comply with health and sanitation regulations promulgated by the city or county in which the Twin Donut Franchise is located. Twin Donut Franchises must obtain and maintain health permits and are inspected by the relevant government health authority. A Twin Donut Franchise that fails to comply with the prevailing health and cleanliness standards risks incurring fines or being closed by the government health authority until the deficiency is corrected.

A Twin Donut Franchise is classified by the retail food industry as a "fast food restaurant" or a "quick service restaurant". The direct competition for Twin Donut Stores is franchises that offer baked goods and grill food such as Dunkin' Donuts. Local coffee shops and delicatessens also compete with Twin Donut Stores. The effect of the competition will depend on the proximity of any such competing establishment to the particular location of each Twin Donut Store.

D. Prior Business Experience

The Franchisor has operated Twin Donut Stores since December 30, 1959 and Franchisor has offered franchises for Twin Donut Stores since 1960. The Franchisor has not offered franchises in any line of business other than retail donut store/luncheonette.

ITEM 2. IDENTITY AND BUSINESS EXPERIENCE OF PERSONS AND COMPANIES

AFFILIATED WITH FRANCHISOR

A. George P. Psathas

Mr. Psathas is the sole Director and President of Twin Donut, Inc. He founded and incorporated Twin Donut, Inc. in 1959 and has personally directed all phases of the franchising operation since that time. Mr. Psathas conducts all franchise marketing activities and generally does not employ franchise brokers or agents.

From 1951 to 1958, Mr. Psathas was employed by Dunkin' Donuts of Randolph, Massachusetts. During that time, he rose from a Store Manager to a Division Supervisor. From 1960 to 1963, he was a Division Supervisor for Mr. Donuts. He left Mr. Donuts to develop Twin Donut, Inc.

B. TDS Leasing, LLC

TDS Leasing, LLC is a Delaware limited liability company formed in 2001 which has taken over the functions of TDS Leasing, Inc. The business purpose of the LLC is to lease to Twin Donut Franchisees the premises on which the Twin Donut Stores are located and operated. It does business under that name. Its principal place of business is 35 East Grassy Sprain Road Suite 500, Yonkers, New York. Mr. Psathas is the Manager of TDS Leasing, LLC. TDS Leasing, Inc. is no longer an active business entity and has no business operations.

C. Spartan Built, Ltd.

Spartan Built, Ltd. is a New York corporation that was incorporated on January 26, 1968. It does business under that name. Its principal place of business is 35 East Grassy Sprain Road Suite 500, Yonkers, New York 10710. The business purpose of the corporation is to sell

construction materials, services and equipment to Franchisees for the establishment and operation of Twin Donut Stores. Mr. Psathas is the President and sole Director of Spartan Built, Ltd.

ITEM 3. LITIGATION

A. General Disclosure

Neither Twin Donut, Inc. nor any person identified in Item II of this Offering Prospectus has pending against it or him any administrative, criminal or material civil action (or a significant number of civil actions irrespective of materiality) alleging a violation of any franchise law, securities law, fraud, embezzlement, fraudulent conversion, restraint of trade, unfair or deceptive practices, misappropriation of property or comparable allegations.

Neither Twin Donut, Inc. nor any person identified in Item II of this Offering Prospectus has been convicted of a felony or pleaded nolo contendere or, within the 10 year period immediately preceding this offering, been convicted of a misdemeanor charge or been held liable in a civil action by final judgment or been the subject of a material complaint or other legal proceeding which involved violation of any franchise law, fraudulent conversion, restraint of trade, unfair or deceptive practices, misappropriation of property or comparable allegations.

Neither Twin Donut, Inc. nor any person identified in Item II of this Offering Prospectus is subject to any injunctive or restrictive order or decree relating to franchises under any Federal, State or Canadian Franchise, securities, anti-trust, trade regulation or trade practice law as a result of a concluded or pending action or proceeding brought by a public agency.

B. Franchisee Litigation

1. Mathura et al. v. Twin Donut, Inc. et al. Index No. 5247-04
Supreme Court of the State of New York for Westchester County

The Plaintiffs Kadar Mathura and Loretta Mathura, each of whom is a individual, purchased a Twin Donut Franchise to operate a Twin Donut Store at 102 East Post Road in White Plains, N.Y. 10601 on June 13, 2002. The Plaintiffs claim that the Franchisor misrepresented the status of the Primary Lease on the business premises and that equipment purchased to operate the business was either not new or defective. While it is unclear from the Complaint, the Plaintiffs appeared to seek \$500,000 in actual damages and \$500,000 in punitive damages. Management interposed a timely answer that specifically denied the allegations and asserted counterclaims.

On January 11, 2005, the Plaintiffs filed a petition in bankruptcy under Chapter 7 of the U.S. Bankruptcy laws. Spartan Built, Ltd. filed a proof of claim for \$180,000.00. By Order dated August 18, 2005, a discharge was granted to the Plaintiffs and the case was closed on August 26, 2005. The Trustee did not pursue this cause of action during the pendency of the bankruptcy proceeding so that it is deemed dismissed.

2. Daniil et al. v. Twin Donut, Inc. et al. Index No. 117287-04
Supreme Court of the State of New York for New York County

The Plaintiff purchased a Twin Donut Franchise to operate a Twin Donut Store at 300 West 40th Street in New York County on December 16, 1999. While it is unclear from the Complaint, the allegations appear to be against TDS Leasing, Inc. in connection with the status of the Primary Lease on the business premises. TDS Leasing, Inc. is no longer an operating entity. The only allegation against Twin Donut Inc. is that it did not provide training as set forth in the Franchise Agreement. The Plaintiff seeks \$249,000 in damages.

Management interposed an answer and is vigorously litigating this matter. The parties are in discovery.

ITEM 4. BANKRUPTCY

During the 10-year period immediately before the date of the Offering Circular, neither Twin Donut, Inc. nor any affiliate, nor any predecessor, nor any officer or general partner has: (a) filed as a debtor (or had filed against it) a petition to start an action under the U.S. Bankruptcy

Code; (b) obtained a discharge of its debts under the bankruptcy code; or ©) was a principal officer of a company or general partner in a partnership that either filed as a debtor (or had filed against it) a petition to start an action under the U.S. Bankruptcy Code or that obtained a discharge of its debts under the U.S. Bankruptcy Code during or within 1 year after the officer or general partner of the Franchisor held this position in the company or partnership.

ITEM 5. INITIAL FRANCHISE FEE

The Franchisee shall pay to Franchisor an initial Franchise Fee in one lump sum at the time the Franchise Agreement is executed. The initial Franchise Fee is non-refundable and shall consist of:

A. Full Service Store Franchise Plan:

\$25,000.00 for the grant of the Franchise and legal and administrative expenses incurred by Franchisor in negotiating and concluding the Franchise Agreement, and

B. Independent Satellite Franchise Plan:

\$15,000.00 for the grant of the Franchise and legal and administrative expenses incurred by Franchisor in negotiating and concluding the Franchise Agreement.

C. Concession Franchise Plan

\$5,000.00 for the grant of the Franchise and legal and administrative expenses incurred by Franchisor in negotiating and concluding the Franchise Agreement.

ITEM 6. OTHER FEES

A. Recurring Payments

1. Full Service Twin Donut Store and Independent Satellite Franchises

The Franchisee shall pay to Franchisor a percentage of the Gross Sales realized by the Franchisee in each week. The percentage figure is based on the cumulative weekly gross sales realized by Franchisee in each Franchise Year. A Franchise Year means the period between the date on which the Franchisee takes possession of the Twin Donut Store and the date that is 12 consecutive calendar months after the month of the date of possession. The percentage is 6%. The Franchisee pays to Franchisor 6% of its gross sales for each week.

At selected locations or sites, Franchisor may waive the payment on Gross Sales and instead authorize TDS Leasing, LLC to collect the percentages on the terms set forth in 1 through 3, supra, in the form of rent or additional rent.

If Franchisee is a corporation, limited liability company or limited liability partnership, Franchisor may, in its sole discretion, require that the shareholders, members or partners personally guarantee the payment of the percentages on Gross Sales.

2. Concession Franchises

The Concession Franchisee shall pay to Franchisor a percentage of the Gross Sales realized by the Franchisee in each week on the sale of products from the Twin Donut Concession. The percentage figure is 6% on the cumulative gross sales realized by Franchisee in each week of each Franchise Year. A Franchise Year means the period between the date on which the

Franchisee takes possession of the Twin Donut Store and the date that is 12 consecutive calendar months after the date of possession.

B. Lease Payments

Except in circumstances under which the Franchisor has approved the terms and conditions of a lease directly between the Franchisee and a lessor, the Franchisee shall lease from TDS Leasing, LLC the premises on which the Twin Donut Store will be operated. The lease payments will vary depending on the location and actual square footage of the Twin Donut Store. The Franchisee Store Lease shall be subject to the Primary Lease, if any, on the premises. The lease payments under the Franchisee Store Lease may be higher than the lease payments under the Primary Lease. Any such Primary Lease shall be incorporated into the Franchisee Store Lease and Franchisee shall assume all obligations in the Primary Lease as if Franchisee were the tenant under the Primary Lease.

The Franchisee may obtain its own primary lease on the premises. Before the Franchisee executes any such lease, Franchisor must approve the location of the premises and the terms of the primary lease. The Franchisor may also require that the Franchisee and the landlord execute a conditional assignment of the primary lease and leasehold to Franchisor or its designee if the Franchise is terminated for any reason under the Franchise Agreement or any other agreement between the Franchisor or its affiliate(s).

At selected locations and sites, Franchisor may authorize TDS Leasing, LLC to collect the payment on Gross Sales set forth in A, supra, in the form of rent or additional rent. Under such

circumstances, the lease payment to may consist of a fixed base monthly rent plus a percentage of Gross Sales calculated on the terms set forth in A, 1-3, supra.

If Franchisee is a corporation or a limited liability company, TDS Leasing, LLC or TDS Leasing, Inc. may, in its sole discretion, require that the shareholders or the members personally guarantee the lease payments including any payments on percentages of Gross Sales.

C. Transfer Fee

If Franchisee assigns any benefit or transfers any right in the Franchise or Assets to a Third Party, then Franchisee shall pay to Franchisor a transfer fee of which shall be the same dollar amount as the Initial Franchise Fee charged by Franchisor for franchises at the time at which the transfer occurs, (see Item 17, G).

D. Legal and Audit Fees

If Franchisor incurs legal fees or costs in connection with enforcing any provision of any agreement concluded in connection with the Franchise, Franchisee shall reimburse Franchisor for such fees and costs. Similarly, if, due to any act or failure to act by Franchisee, Franchisor must undertake an audit of the business of Franchisee, Franchisee shall pay the costs of such audit or, if Franchisor advances such costs, reimburse Franchisor for the costs of the audit.

G. Refunds

No fee described under this Section is refundable.

ITEM 7. INITIAL INVESTMENT OF FRANCHISE

A. Three Types of Franchise Plans Offered

The Franchisor offers three Franchise Plans to prospective Franchisees - the Full Service Franchise Plan , the Independent Satellite Franchise Plan, and Concession Franchise Plan. Under the Full Service and Independent Satellite Plan, the Franchise consists of either a fully constructed and equipped Twin Donut Store or a Twin Donut to be constructed and equipped according to the specifications of Franchisor on a site which is either identified by Franchisor or approved by Franchisor. Under each Plan, Franchisor requires that Franchisee obtain comprehensive insurance coverage of at least \$2,000,000 per person for general liability, at least \$100,000 per incident for general liability and at least \$500,000 for property damage.

B. Initial Investment Under the Full Service Franchise Plan

	AMOUNT	TO WHOM PAID	WHEN AMOUNT DETERMINED	REFUNDABLE
Real Property	\$3,900-\$14,000/mo	TDS Leasing, LLC	Before Execution	No
Security Deposit	3-6 months rent	TDS Leasing, LLC	Before Execution	Yes
Construction/ Equipment	\$250,000 - \$500,000	Spartan Built, Inc.	Before Execution	No
Inventory	\$5,000	Suppliers	Before Execution	No
Working Capital	\$10,000	Retained	Before Execution	No

	AMOUNT	TO WHOM PAID	WHEN AMOUNT DETERMINED	REFUNDABLE
Licenses	\$300-\$500	Government	Determined by Law	By Law
Insurance	\$5000-\$18,000	Carriers	Before Execution	Carriers
Estimated Total: \$274,200 - \$537,500				

	FINANCED BY FRANCHISOR	ESTIMATE OF LOAN PAYMENTS
Real Property	No	N/A
Construction Equipment	Yes	See Item 10
Inventory	No	N/A
Working Capital	No	N/A
Statutory Licenses	No	N/A
Insurance Premiums	No	N/A

C. Initial Investment Under the Independent Satellite Franchise Plan

	AMOUNT	TO WHOM PAID	WHEN AMOUNT DETERMINED	REFUNDABLE
Real Property	\$2,900-\$11,000/mo	TDS Leasing LLC	Before Execution	No
Security Deposit	3-6 months rent	TDS Leasing LLC	Before Execution	Yes
Construction/ Equipment	\$175,000 - \$250,000	Spartan Built, Inc. or Own Selection	Before Execution	No

	AMOUNT	TO WHOM PAID	WHEN AMOUNT DETERMINED	REFUNDABLE
Inventory	\$5,000	Suppliers	Before Execution	No
Working Capital	\$10,000	Retained	Before Execution	No
Licenses	\$300-\$500	Government	Determined by Law	By Law
Insurance	\$3000-\$15,000	Carriers	Before Execution	As Per Carrier
Estimated Total: \$196,200 - \$291,500				

	FINANCED BY FRANCHISOR	ESTIMATE OF LOAN PAYMENTS
Real Property	No	N/A
Construction Equipment	Yes	See Item 10
Inventory	No	N/A
Working Capital	No	N/A
Statutory Licenses	No	N/A
Insurance Premiums	No	N/A

D. Initial Investment Under the Concession Franchise Plan

	AMOUNT	TO WHOM PAID	WHEN AMOUNT DETERMINED	REFUNDABLE
Real Property	N/A	N/A	N/A	N/A
Security Deposit	N/A	N/A	N/A	N/A

	AMOUNT	TO WHOM PAID	WHEN AMOUNT DETERMINED	REFUNDABLE
Construction/ Equipment	\$15,000 - \$30,000	Spartan Built, Inc. or Own Selection	Before Execution	No
Inventory	\$1,000	Twin Donut Store Suppliers	After Execution	No
Working Capital	\$1,000	Retained	Before Execution	No
Licenses	\$300-\$500	Government	Determined by Law	By Law
Insurance	Cost of Additional Operation	Carriers	Before Execution	As Per Carrier
Estimated Total: \$18,000 - \$32,500				

	FINANCED BY FRANCHISOR	ESTIMATE OF LOAN PAYMENTS
Real Property	No	N/A
Construction Equipment	No	N/A
Inventory	No	N/A
Working Capital	No	N/A
Statutory Licenses	No	N/A
Insurance Premiums	No	N/A

ITEM 8. RESTRICTIONS ON SOURCES OF PRODUCTS AND SERVICES

A. Twin Donut Store Premises and Concession Franchise Premises

Under the Full Service Franchise Plan and the Independent Satellite Franchise Plan, the Franchisee usually shall lease the Twin Donut Store from TDS Leasing, LLC. TDS Leasing, LLC derives revenue of between \$0 to \$2,000 per month on each lease payment in excess of the lease payment set forth under any Primary Lease on the Twin Donut Store Premises.

The Franchisee may lease the Twin Donut Store Premises from the primary lessor of the those Premises. Neither the Franchisor nor any affiliate of the Franchisor shall derive any revenue from any lease on which TDS Leasing, LLC is not the lessor. The Franchisor must approve the location and the terms of any lease on which TDS Leasing, LLC is not the lessor. The Franchisor is not obligated to approve any lease that does not contain the following provisions drafted in a form acceptable to Franchisor:

- a. The Franchisor or its designee shall replace Franchisee as tenant under the lease if:
 - (I) the lease expires for any reason other than the chronological expiration of the term of the lease, including any renewal or extension term and the procedure described in sub-paragraph b is fully executed, or
 - (ii) the lease terminates for any reason before the chronological expiration of the term of the Store lease, including any renewal or extension term and the procedure described in sub-paragraph b is fully executed, or
 - (iii) Franchisee ceases for any reason to be a Twin Donut Franchisee or ceases to operate the business of a Twin Donut Franchise on the Demised Premises and the procedure described in sub-paragraph c is fully executed.

- b. If the lease expires or terminates under either a(I) or a(ii), then:
- (I) Within 3 business days after the day on which the lessor determines that the lease has expired or terminated, the lessor shall notify Franchisee in a signed writing. The writing shall contain the balance of the term, a description of any outstanding default, the means of curing any such default and a copy of the Store Lease then in effect, including each amendment or modification, if any.
 - (ii) No later than 15 business days after the day on which it receives the writing in (I), Franchisor shall cure each default contained in the writing. Immediately after accomplishing each such cure, Franchisor or its designee shall be entitled to possession of the premises and the lessor shall recognize Franchisor or its designee as the exclusive Tenant under the lease and the Franchisor shall be entitled to all rights and subject to all obligations of the lease.
 - (iii) If Franchisor fails to cure any default under (ii), then lessor and Franchisor shall have no further obligation to one another including any obligation that may be construed as being incident to the lease or implied in law.
- c. If Franchisee ceases for any reason to be a Twin Donut Franchisee or ceases to operate the business of a Twin Donut Franchise on the premises under the lease, then:
- (I) Within 3 business days after the day on which Franchisor determines that Franchisee has ceased to be a Twin Donut Franchisee or has ceased to operate the business of a Twin Donut Franchise on the premises, Franchisor shall notify the lessor in a signed writing.
 - (ii) Within 3 business days after the day on which the lessor receives the writing in (I), the lessor shall notify Franchisor in writing as to the balance of the term and attach a copy of the lease then in effect, including each amendment or modification, if any.
 - (iii) No later than 7 business days after the day on which it receives the writing in (ii), Franchisor shall either accept or reject the lease. If

Franchisor accepts the lease then Franchisor or its designee shall be entitled to possession of the premises and the lessor shall recognize Franchisor or its designee as the exclusive tenant under the lease and the Franchisor or its designee shall be entitled to all rights and subject to all obligations of the lease.

- (iv) If Franchisor fails to accept the lease under (iii), then lessor and Franchisor shall have no further obligation to one another including any obligation that may be construed as being incident to the lease or implied in law.
- d. If Franchisee contests any legal action necessary to enforce sub-paragraph c and Franchisor accepts the lease, then Franchisee shall undertake the prosecution of any such action at its sole cost.
- e. If Franchisee defaults under the lease during the pendency of any legal action described in sub-paragraph d on any payment obligation, Franchisor shall cure any such payment default at any time prior to and as a condition precedent to taking possession of the premises
- f. After Franchisor has approved the lease under this Paragraph, the lessor and Franchisee shall not under any circumstances amend, modify or alter the lease in any way unless Franchisor approves of any such amendment, modification or alteration in a signed writing which approval shall not be unreasonably withheld.

Under the Concession Franchise Plan, the Franchisee must have legal possession of the premises in which the Twin Donut Concession is to be placed. The Franchisor must approve the Business Premises and the physical placement of the Twin Donut Concession within those Business Premises.

B. Construction and Equipment

Under each of the Franchise Plans, the Franchisee is encouraged to purchase the Construction and Equipment from Spartan Built, Ltd. Spartan Built, Ltd. derives income based

on the difference between the cost to Spartan Built, Ltd. when the Twin Donut Store was built and the cost, as determined by Franchisor, to Franchisee if the same Twin Donut Store were built and equipped on or about the date of sale of the Franchise. Depending on the location of the Twin Donut Store, the difference may also include a factor based on the value and desirability of the particular site.

The Franchisee may obtain its own construction services for the Twin Donut Store. If Franchisee does not purchase the Construction and Equipment from Spartan Built, Ltd., it must satisfy the following requirements:

1. Specifications. The Twin Store shall be constructed according to specifications provided by Franchisor so that the design, layout, colors, signage and decorations of the Twin Donut Store is the same as all other existing Twin Donut Store.
2. Time for Construction . The Twin Donut Store shall commence business no later than 90 days after the date on which the Franchise Agreement is executed.
3. Contractor. The Franchisee shall submit the name, address, resume and business information of its duly licensed Contractor to Franchisee for approval. The Franchisee shall also submit a construction contract executed by the parties to Franchisor for approval. The Franchisor may require changes in the contract as a condition of its approval of the Contractor.
4. Architect's Plans: The Franchisee shall submit to Franchisor plans of the Twin Donut Store that have been prepared by a duly licensed architect in and for the jurisdiction in which the Twin Donut Store is located. The plans shall be in a form that satisfies the requirements of any governmental authority from which any permit or approval must be obtained to construct the Twin Donut Store.
5. Approval by Franchisor: After Franchisor has reviewed the plans, it shall either approve the plans or reject them. If Franchisor approves the plans then the Franchisee shall submit the plans to the relevant government authority to obtain any necessary permits or approvals. If Franchisor rejects the plans, it shall inform

the Franchisee as to the deficiencies in the plans and Franchisee shall submit corrected plans to Franchisor.

6. Insurance: The Franchisee shall procure and maintain all insurances including but not limited to worker's compensation that are necessary or appropriate in the opinion of Franchisor to the construction of the Twin Donut Store. The Franchisee shall provide evidence satisfactory to Franchisor that the Franchisee has obtained such insurance before commencing construction.
7. Completion Bond: The Franchisee shall obtain and maintain a completion bond to the benefit of Franchisor in an amount determined by Franchisor. Unless otherwise agreed by Franchisor, the Franchisee shall provide evidence satisfactory to SBL that the Franchisee has obtained the completion bond before commencing construction.
8. Quality of Materials and Workmanship: The Franchisee shall use only new materials of a high quality in the construction of the Twin Donut Store. All labor, skilled labor and crafting shall be performed according to the highest standards of workmanship and craftsmanship.
9. Holds Harmless and Indemnification: The Franchisee shall hold Twin Donut, Inc., TDS Leasing, Inc. and Spartan Built, Ltd and their employees and agents completely harmless and indemnify each of them for any loss or damage incurred by all of them or any of them including reasonable attorneys' that arises out of or is incident to the construction of the Twin Donut Store.
10. Final Approval: The Franchisee shall not commence business until SBL has issued a final approval of the Twin Donut Store. The Franchisor is not obligated to approve the Twin Donut Store as long as any item of construction or work deviates from the specifications of Franchisor. The Franchisee shall correct any deficiency noted by Franchisor at the sole cost of the Franchisee. The Franchisee waives any claims or causes of action it has or may have against Twin Donut, Inc., TDS Leasing, Inc. and Spartan Built, Ltd or any of their employees and agents that arises from or is incident to the refusal of BBL to issue a final approval.

The Equipment required for the Twin Donut Store is only available from certain vendors who usually sell only to substantial purchasers in the industry. Consequently, the Franchisee will

be required to purchase the Equipment from Spartan Built, Ltd. unless it can demonstrate to the satisfaction of Franchisor that it has the capability to purchase the Equipment from the relevant vendors.

C. Inventory and Supplies

The Franchisee is encouraged though not required to purchase from Approved sources all inventory and supplies (see TAB 2 for Approved Sources). The Franchisee may purchase from a source other than an Approved Source as long as the Franchisee submits a sample of the item or supply to Franchisor and, after testing the item or supply for 30 days, the Franchisor finds that item or supply to be of at least equal quality to the same item or supply sold by an Approved Source. The Franchisor shall not derive any income from any purchase from Approved Sources.

D. Estimate Proportion

The proportion of required purchases and leases to all purchases and leases by Franchisee of goods and services in establishing and operating the franchised business is 100% to 0.

E. Cooperatives

The Franchisor is not aware of any purchasing or distribution cooperatives for the goods and services necessary to establish and operate the franchised business.

F. Leases and Purchases

Under each Plan, Franchisee is encouraged, though not required, to lease or purchase real property, construction or equipment from any affiliate of Franchisor or from any approved source, (See B, supra).

G. Independent Satellite Franchise Plan

The Franchisee must sell only baked goods that have been prepared in a Full Service Twin Donut Store and beverages from approved sources.

H. Concession Franchise Plan

Under the Concession Franchise Plan, the Franchisee must have legal possession of the Business Premises in which the Twin Donut Concession is to be placed. The Franchisee is required to sell only baked goods that have been prepared in another Twin Donut Store and beverages from approved sources.

ITEM 9. FRANCHISEE'S OBLIGATIONS

THIS TABLE LISTS YOUR PRINCIPAL OBLIGATIONS UNDER THE FRANCHISE AND OTHER AGREEMENTS. IT WILL HELP YOU FIND MORE DETAILED INFORMATION ABOUT YOUR OBLIGATIONS IN THESE AGREEMENTS AND IN OTHER ITEMS OF THIS OFFERING CIRCULAR.

NOTE THE FOLLOWING FOR THE PURPOSE OF THE CHART

FRA refers to each of the Turn Key Franchise Agreement, the Site Construction Franchise Agreement and Concession Franchise Agreement

TFRA refers to the Turn Key Franchise Agreement only

SFRA refers to the Site Construction Franchise Agreement only

LEA refers to Franchisee Store Lease with TDS Leasing, Inc.

SEC refers to Security Agreement with Spartan Built, Ltd.

FOC refers to this Franchise Offering Circular

NOTE refers to any Promissory Note for Financing with Spartan Built, Ltd.

OBLIGATION	OBLIGATED	CITE
Site selection/lease	Yes	FRA-III
Pre-Opening purchases/leases	No	----
Site Development; other pre-opening requirements	No	----
Initial and Ongoing Training	Yes	FRA-XI FOC-11
Opening	No	----
Fees	Yes	FRA-VII FOC-7
Compliance with Standards	Yes	FRA-XII
Trademarks/Proprietary Information	Yes	FRA-VI FOC-13
Restrictions on products/services offered	Yes	FRA-V FOP-16
Warranty/customer service requirements	No	----
Territorial development/sales quotas	Yes	FRA-II FRA-ADDM
On-going product/service purchases	Yes	FRA-V
Maintenance, appearance, re-modeling	Yes	TFRA-XII SFRA-IV, XII
Insurance	Yes	FRA-XIII

OBLIGATION	OBLIGATED	CITE
Advertising	Yes	FRA-IX
Indemnification	Yes	FRA-XIV
Owner's Participation/management/staffing	Yes	FRA-XV, XVI, XXI FOC-15
Records and Reports	Yes	FRA-XIII, X
Inspections and Audits	Yes	FRA-VIII, XIII
Transfer	Yes	FRA-XVIII FOC-17
Renewal	No	----
Post-Termination Obligations	No	----
Dispute Resolution	Arbitration	FRA-XXII
Lease Payments	Yes	LEA-IV
Personal Guaranty	Yes	FRA-GUA LEA-GUA SEC-GUA NOTE-GUA
Note Payments	Yes, if purchase is financed	SEC-III, NOTE

ITEM 10. FINANCING

A. Financing Obtained by FRANCHISEE

The Franchisor desires that Franchisee obtain its own financing for the Initial Investment.

If Franchisee obtains its own financing, Franchisee must fully disclose to Franchisor all aspects of

any financing arrangement and submit copies of all financing documents to Franchisor for approval prior to executing any agreement in connection with financing the Franchise. The Franchisor may, in its sole discretion, reject any financing arrangement which it deems unsuitable for the business operation of the Franchise. The Franchisor does not offer financing for franchises under the Concession Franchise Plan.

B. Financing Available from Franchisor

The Franchisor, through its affiliated company, Spartan Built, Ltd., offers financing for the purchase of Construction and Equipment. The Franchisor does not offer financing for Inventory, Working Capital or any Recurring Payments.

The terms of the financing are as follows:

1. One-Third to One-Half of the gross sum financed must be paid in cash to Spartan Built, Ltd.
2. Interest at 10%-12% per year over a 4 year (48 month) period, a 5 year (60 month) period, a 7.5 (90 month) period or for the term of any lease of the premises on which the Twin Donut Store is located.
3. Payments of principal and interest are due monthly during the financing period and evidenced by a Promissory Note with monthly vouchers and a Security Agreement.
4. The principals, shareholders or members of a Franchisee-corporation or a Franchisee-limited liability company shall be required to either personally guarantee the obligation or execute an Affidavit of Confession of Judgment or both. The Franchisor may, in its sole discretion, dispense with this requirement.
5. Upon 30 days written notice to Franchisor the Franchisee may pre-pay the balance of the principal and interest by paying the remaining Promissory

Notes in inverse order so that the last Note is paid first. The Franchisor may sell the Promissory Notes back to Franchisee at a discounted purchase price.

6. Upon transfer of the Franchise or of an interest in any Franchisee-corporation, Franchisee-limited liability company or Franchisee-limited liability company, Franchisee shall pay the principal and interest due and owing at the time of any such transfer. The Franchisor may, in its sole discretion, waive this provision in whole or in part.
7. The Franchisor may discount or assign any note or financing instrument to a Third Party.
8. The Franchisor does not receive any payments from any person for placing financing with any such person.
9. If Franchisee defaults under any financing arrangement, Franchisee shall be liable to Franchisor for all installment payments in arrears, the sum total of the balance of principal and interest remaining, the expenses of retaking possession of the Equipment or the Twin Donut Store, attorneys' fees and court costs.

C. Other Financing Sources

[RESERVED]

ITEM 11. FRANCHISOR'S OBLIGATIONS

A. Obligations Prior to Commencement of Operations

If the Twin Donut Store at which the business of the Franchise is to be operated is fully constructed and equipped, then Franchisor is obligated only to cause the Twin Donut Store to be ready to commence business unless otherwise agreed. (see Article III, page 3-6 of the Franchise Agreement.)

If the Twin Donut Store at which the business of the Franchise is to be operated is not fully constructed and equipped, then the Franchisee may propose a site to Franchisor. The Franchisor may, in its sole discretion, reject the proposed site and designate the premises on which the Twin Donut Store or Concession will be operated. Site selection shall occur prior to the execution of any agreements in connection with the Franchise. The Franchisor shall also submit to Franchisee written specifications for constructing and equipping the Twin Donut Store. The Franchisee shall accept these specifications prior to executing any agreements in connection with the Franchise (see Articles III and IV pages 3-8 of the Franchise Agreement and Concession Franchise Agreement).

B. Supervision, Assistance or Services

The Franchisee shall receive a manual prepared by Franchisor entitled Managerial Duties and Control. The manual sets forth the method of operation, quality control, managerial duties, maintenance of equipment and personnel policies (see Article XI, pages 14-15 of the Franchise Agreement.)

When Franchisee assumes control of the operation or commences business, Franchisor may place an experienced store manager in the Twin Donut Store to assist Franchisee in the initial stages of the operation. The Franchisor is not obligated to do so under the Franchise Agreement (see Article XI, pages 14-15 of the Franchise Agreement.)

Beyond the initial stages of the operation, Franchisor does not, on its own initiative, provide continuing supervision or assistance to Franchisee. However, Franchisor shall be available

when called on by Franchisee and shall exercise its best efforts to respond to all reasonable requests for assistance and advice from Franchisee.

C. Obligations of Franchisor During Operation

The Franchisor is not obligated to provide any assistance other B.3, supra., during the Franchise Term.

D. Other Supervision, Assistance or Services

The Franchisor is not obligated to provide any supervision, assistance or services other than B.3, supra.

E. Methods of Site Selection

The Franchisor endeavors to locate Twin Donut Stores in urban and suburban markets which, on the basis of commercial activity and demography, indicate that new Twin Donut Stores can be supported. Real property costs, competition, proximity of major rental activity such as shopping centers, visibility, accessibility, traffic speed and density of population are the principal criteria used in site selection.

F. Time for Commencing Business Operations

If the Twin Donut Store at which the business of the Franchise is to be operated is fully constructed and equipped is either substantially prepared for business or already in operation, then Franchisee may commence business as soon as is practical after the execution of agreements and completion of the training session.

If the Twin Donut Store at which the business of the Franchise is to be operated is not fully constructed and equipped, the Twin Donut Store should be prepared for business operations no less than 90 days and no more than 180 days after the execution of all agreements.

G. Training Offered by Franchisor

1. The Franchisee or its designee shall attend a two-week training session at a Twin Donut Store which is currently being operated by Franchisor. During the training session, Franchisee shall observe and participate in all aspects of the actual operation of a Twin Donut Store including baking and cooking methods, equipment use and maintenance and record keeping.
2. The training session shall be conducted as soon as possible after all agreements have been executed. The training session may be conducted before the agreements are executed where the Twin Donut Store that is the subject of the Franchise is being operated by Franchisor.
3. The instructors are managers employed by Franchisor who are experienced in operating a Twin Donut Store.
4. No fee is charged for the training session and Franchisee shall pay directly all travel and living expenses in connection with the training session.
5. The training session is mandatory but Franchisor may waive the training requirement.
6. No additional training or refresher courses are available from Franchisor.
7. Concession Franchisees are not required to attend training.

ITEM 12. TERRITORY

A. The Franchisor does not grant exclusive territorial rights in any urban area as an urban area is determined in the sole discretion of Franchisor.

B. In a suburban area or rural area as such areas are determined in the sole discretion of

Franchisor, Franchisor shall not grant a new Franchise for a Full Service Twin Donut Store Franchise within 1 ½ miles in either direction on the road or highway which runs in front of a Franchisee's Full Service Twin Donut Store and only on the side of the road or highway on which that Store is located. The exclusive territory shall not under any circumstances be measured as a radius.

The exclusive territorial rights are granted only to Full Service Twin Donut Store Franchises. Exclusive territorial rights are not granted to any of an Independent Satellite Franchise, Extension Satellite Franchise or Concession Franchise. There are other Franchises currently established and operating within the limits described in this sub-Item.

C. The Franchisor shall not establish a new Franchise within the limits described in B, supra.

D. The Franchisor may have company owned outlets currently operating within the limits described in B, supra. The Franchisor shall not establish a new company owned outlet within the limits described in B, supra.

E. The Franchisor does not and shall not establish other Franchises or company owned outlets selling or leasing similar products or services under a different name or trademark.

F. Continuation of the exclusive territorial rights does not depend on the attainment of a certain sales volume, or revenues or market penetration or other contingency. The exclusive territorial rights may be altered only by an express agreement between Franchisor and Franchisee. However, any such agreement shall be consistent with the formula set forth in B, supra.

G. The Franchisor shall decide in its sole discretion whether a particular location is an urban area or a suburban area or a rural area.

ITEM 13. TRADEMARKS

A. License to Use Tradename

Under the Franchise Agreement, Franchisor grants to the Franchisee the right to use the name "Twin Donut" or "Twin Donut Plus" and any logotype. The following tradename is registered with the Patent and Trademark Office of the U.S. Department of Commerce on the Principal Register:

"Twin Donut"
Reg. No. 1783085
New Reg No. 78442297

No trademark, logotype or other mark is registered in the State of New York or any other state.

B. Interference and Infringements on Use

There is no pending litigation or pending interference in connection with the tradename or logotype in any court or administrative proceeding. There are no infringing uses actually known to Franchisor. The Franchisor shall, at its sole expense, protect the tradename and logotype from any interference or infringements.

C. Limitations on Use

1. The tradename shall be prominently displayed without any other words or symbols accompanying it on the exterior of the business premises.

2. The tradename shall appear on all paper goods and any other items used for or in connection with the sales of the Franchise.
3. The tradename shall be prominently displayed in a tasteful and attractive manner and always maintained in good repair.

ITEM 14. PATENTS, COPYRIGHTS AND PROPRIETARY INFORMATION

The Franchisor does not own any rights in or to any patents or copyrights which are material to this Franchise.

ITEM 15. OBLIGATION OF FRANCHISEE TO PARTICIPATE IN THE ACTUAL OPERATION OF THE BUSINESS

Under the Franchise Agreement, Franchisee shall personally direct the business operations. If Franchisee is a corporation or a limited liability company, then a shareholder or a member who owns 50% or more of the outstanding shares or total interests shall personally direct the business operations. If Franchisee is a partnership, then a partner who owns at least 50% of the Ownership Interests shall personally direct the business operations. The Franchisee may employ store managers to assist in the day to day operations of the Franchise. However, the Franchisor deems the personal and direct participation of the Franchisee or principal owners of any Franchisee entity to be essential to the profitable operation of the Franchise. The Franchisee is ultimately responsible for the operation of the Franchise and for complying with all agreements.

ITEM 16. RESTRICTIONS ON WHAT THE FRANCHISEE MAY SELL

Under the Franchise Agreement, Franchisee shall offer for sale only donuts or pastries baked in a Twin Donut Store with equipment and supplies purchased from Approved Sources or approved by Franchisor. The Franchisee shall offer for sale luncheonette-type food prepared in a Twin Donut Store with equipment and supplies purchased from Designated Sources or approved by Franchisor. The Franchisee shall not place any vending machines or entertainment devices in the Twin Donut Store unless Franchisor consents in writing to such machine or device.

ITEM 17. RENEWAL, TERMINATION, TRANSFER AND DISPUTE RESOLUTION

THIS TABLE LISTS CERTAIN IMPORTANT PROVISIONS OF THE FRANCHISE AND RELATED AGREEMENTS PERTAINING TO RENEWAL, TERMINATION, TRANSFER AND DISPUTE RESOLUTION. YOU SHOULD READ THESE PROVISIONS IN THE AGREEMENTS ATTACHED TO THIS OFFERING CIRCULAR.

NOTE THE FOLLOWING FOR THE PURPOSE OF THE CHART

FRA refers to each of the Turn Key Franchise Agreement, the Site Construction Franchise Agreement and the Concession Franchise Agreement

LEA refers to Franchisee Store Lease with TDS Leasing, LLC

SEC refers to Security Agreement with Spartan Built, Ltd.

NOTE refers to any Promissory Note for Financing with Spartan Built, Ltd.

PROVISION	SUMMARY OF PROVISION	CITE
Length of term of franchise	20 years or co-extensive with lease term	FRA-II

PROVISION	SUMMARY OF PROVISION	CITE
Renewal or extension of term of franchise	No automatic renewal or extension ²	----
Requirements for franchisee to renew or extend	See Footnote 1	----
Termination by franchisee	Franchisee may terminate upon any grounds available under law	----
Termination by franchisor w/o cause	No such right	----
Termination by franchisor w/ cause	Failure to pay fees, rent, note; consistent failure to comply with system; failure to operate	FRA-XIX, XX LEA-VII, VIII SEC-VI
“Cause” defined-curable defaults	All payment defaults	FRA-XIX, XX LEA-VII, VIII SEC-VI
“Cause” defined-defaults that cannot be cured	Consistent failure to pay, comply or operate, failure to commence business within specified time, direct communications with primary landlord	FRA-XIX, XX LEA-VII, VIII SEC-VI
Franchisee’s obligations on termination/non-renewal	Vacate premises; cease using marks and proprietary information	FRA-XX LEA-VII
Assignment of contract by franchisor	Yes, as long as assignee assumes obligations; however no assignment will be made except to an assignee who, in the good faith and judgement of the Franchisor, is willing and able to assume the Franchisor’s obligations under the Franchise Agreement	FRA-XVIII
“Transfer” by franchisee - defined	Sale of assets; sale of 50% or more of interests in Franchise entity	FRA-XVIII
Franchisor approval of transfer by Franchisee	Yes	FRA-XVIII

² If the primary lease on the business premises is renewed or extended, Franchise Term will generally be to a term that is co-extensive with the term of the renewed primary lease or extension as long as Franchisee is in full compliance under the Franchise Agreement and all related agreements.

PROVISION	SUMMARY OF PROVISION	CITE
Conditions for Franchisor approval of transfer	Payment of outstanding fees, rent or notes; transferee of same or better financial condition and experience a transferring Franchisor	FRA-XVIII
Franchisor's right of first refusal to acquire business	Yes	FRA-XVIII
Franshisor's option to purchase franchisee's business	None	----
Death or disability of franchisee	Not Relevant ³	----
Non-competition covenant during the term of franchise	Yes	FRA-XVII
Non-competition covenant after franchise terminates or expires	Yes; 2 years	FRA-XVII
Modification of agreement	In writing by mutual consent only	FRA-XXIII
Integration/merger clause	Yes	FRA-XXIII
Dispute resolution by arbitration or mediation	Yes	FRA-XXII
Choice of forum	American Arbitration Association	FRA-XXII
Choice of law	New York	FRA-XXIII

ITEM 18. PUBLIC FIGURES

There are no arrangements with public figures for endorsements or recommendations of the products sold by Franchisee.

³ Except in very special circumstances, the Franchisor does not sell Franchises to individuals. If the majority equity holder of a corporation, partnership or limited liability company dies or becomes disabled, the Franchisor will treat the surviving equity holder(s) as transferees, (See FRA-XXI).

ITEM 19. EARNINGS CLAIMS

TWIN DONUT, INC. DOES NOT FURNISH OR AUTHORIZE ITS SALES PERSONS TO FURNISH ANY ORAL OR WRITTEN INFORMATION CONCERNING THE ACTUAL OR POTENTIAL SALES, COSTS, INCOME OR PROFITS OF A TWIN DONUT STORE FRANCHISE. ACTUAL RESULTS VARY FROM UNIT TO UNIT AND TWIN DONUT CANNOT ESTIMATE THE EARNINGS OF ANY PARTICULAR FRANCHISE.

The Franchisor may provide actual sales and cost information it has received from currently operating Twin Donut Stores which is based on reports from the Franchisees of any such Twin Donut Stores. The Franchisee does not represent or imply to any potential franchisee that its proposed Twin Donut Store shall or may experience the same or similar sales and costs.

ITEM 20. INFORMATION REGARDING THE FRANCHISES OF FRANCHISOR

A. Total Number of Franchises in Operation from January 1, 2003 through December 31, 2005

I. As Of December 31, 2003

New York.	22
New Jersey.	2

ii. As Of December 31, 2004

New York.	26
New Jersey.	2

ii. As Of December 31, 2005

New York.	19
-------------------	----

New Jersey.	0
---------------------	---

B. Names, Addresses and Telephone Numbers of all Franchises
Under Franchise Agreement

See TAB 1

C. Estimated Number of Franchises to be Sold in Current Fiscal
Year

New York.	6
New Jersey.	2

D. Transferred, Cancelled, Termination, Non-Renewal and Reacquisition of
Franchises from January 1, 2003 to December 31, 2005

1. Transferred controlling ownership.	15
2. Canceled or Terminated by Franchisor.	6
3. Not Renewed by Franchisor.	0
4. Reacquired by Franchisor.	3
5. Known to have otherwise ceased doing business in the system.	2

E. Last Known Address and Telephone Number of Franchisees in New
York State Whose Franchise has been Terminated, Cancelled, Not Renewed or
Voluntarily or Involuntarily Ceased Doing Business Between January 1, 2005 and

December 31, 2005 or Who Has Not Communicated with Franchisor Within 10 Weeks of the Application Date.

(LIST INDIVIDUAL NAME AND INDIVIDUAL ADDRESS)

TAB 1

LIST OF FRANCHISES UNDER AGREEMENT

TAB 2

APPROVED SOURCES

TAB 3

SAMPLE EQUIPMENT LIST

The Equipment and number of items will vary depending on the location and size of the particular Twin Donut Store.

TAB 4

AUDITED FINANCIAL STATEMENTS

TAB 5

FORM FRANCHISE AGREEMENT
FORM EXTENSION SATELLITE FRANCHISE AGREEMENT

TAB 6

FORM SUB FRANCHISOR AGREEMENT

TAB 7

FORM FRANCHISEE STORE LEASE

The Franchisee Store Lease is a sub-lease which is subject to a Primary Lease on the premises held by TDS Leasing, Inc. Therefore, this form Franchisee Store Lease will vary considerably from Twin Donut Store to Twin Donut Store depending on the location and the terms of the Primary Lease.

TAB 8

FORM PROMISSORY NOTE
FORM SECURITY AGREEMENT
FORM AFFIDAVIT OF CONFESSION OF JUDGMENT

TAB 9

FORM FRANCHISE OPTION AGREEMENT

TAB 10

CONCESSION FRANCHISE AGREEMENT
(Host Franchisor and Non-Host Franchisor)

ACKNOWLEDGMENT OF RECEIPT OF TWIN DONUT, INC.
FRANCHISE OFFERING CIRCULAR FOR 200

THIS OFFERING CIRCULAR SUMMARIZES CERTAIN PROVISIONS OF THE FRANCHISE AGREEMENT AND OTHER INFORMATION IN PLAIN LANGUAGE. READ THIS OFFERING CIRCULAR AND ALL AGREEMENTS CAREFULLY. IF WE OFFER YOU A FRANCHISE, WE MUST PROVIDE THIS OFFERING CIRCULAR TO YOU BY THE EARLIEST OF:

(1) THE FIRST PERSONAL MEETING BETWEEN THE FRANCHISOR OR ITS AGENT AND THE PROSPECTIVE FRANCHISEE, OR

(2) TEN BUSINESS DAYS PRIOR TO THE SIGNING OF A BINDING FRANCHISE AGREEMENT, OR

(3) TEN DAYS BEFORE A PAYMENT TO FRANCHISOR OR ITS AGENT.

YOU MUST ALSO RECEIVE A FRANCHISE AGREEMENT CONTAINING ALL MATERIAL TERMS AT LEAST FIVE BUSINESS DAYS BEFORE YOU SIGN A FRANCHISE AGREEMENT. IF WE DO NOT DELIVER THIS OFFERING CIRCULAR ON TIME OR IF IT CONTAINS A FALSE OR MISLEADING STATEMENT OR A MATERIAL OMISSION, A VIOLATION OR FEDERAL AND STATE LAW MAY HAVE OCCURRED AND SHOULD BE REPORTED TO THE FEDERAL TRADE COMMISSION, WASHINGTON, D.C. 20580 AND TO THE NEW YORK STATE DEPARTMENT OF LAW 120 BROADWAY 23RD FLOOR NEW YORK,

N.Y. 10271.

No sub-franchisors or franchise brokers are authorized to offer franchises in the State of
New York. Initial _____

RECEIPT (continued)

List of Appendices attached to this Franchise Offering Circular:

TAB 1	LIST OF FRANCHISES UNDER AGREEMENT
TAB 2	APPROVED SOURCES
TAB 3	SAMPLE EQUIPMENT LIST
TAB 4	AUDITED FINANCIAL STATEMENTS
TAB 5	FORM TURN KEY FRANCHISE AGREEMENT FORM EXTENSION SATELLITE AGREEMENT
TAB 6	FORM SUB FRANCHISE AGREEMENT
TAB 7	FORM FRANCHISEE STORE LEASE
TAB 8	FORM PROMISSORY NOTE FORM SECURITY AGREEMENT FORM AFFIDAVIT OF CONFESSION OF JUDGMENT
TAB 9	FORM FRANCHISE OPTION AGREEMENT
TAB 10	FORM CONCESSION FRANCHISE AGREEMENT (Host Franchisor and Non-Host)

Effective Date: September 29, 1986. Amended: _____

The undersigned, personally or as an officer or partner or member of the proposed Franchisee does acknowledge receipt of the Franchise Offering Circular required by the State of New York, including all appendices on _____, 200__.

[continued on next page]

Initial _____

RECEIPT (continued)

Print name and address of signatory

Name

Number and Street

City

State

Zip

Signature

individually and as an officer or
partner or member of

a corporation formed under the laws
of _____

a general partnership formed under
the laws of _____

a limited liability company formed
under the laws of _____

a sole proprietorship under the laws

of _____.

Subscribed and sworn before me this ____ day of _____,

200__.

Notary Public