

Understanding the FDD and Franchise Agreement Before You Invest

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Franchise Agreements Are Binding and Often One-Sided

Franchise Agreements are typically drafted by the franchisor and presented on a “take it or leave it” basis. These contracts often impose strict controls over how you operate your business — from approved vendors and marketing strategies to pricing, hours of operation, and technology platforms. They also frequently include provisions that:

- Limit your ability to exit the business without penalties
- Impose personal guarantees and long-term non-competes
- Allow the franchisor to raise fees or change system rules unilaterally
- Require extensive marketing spend and recurring royalty payments, regardless of profitability

Once signed, these agreements are legally binding, and courts generally enforce them as written. That's why it's critical to understand every term, especially the financial and operational obligations that can continue even if your business underperforms.

The FDD Reveals More Than You Think—If You Know Where to Look

Federal law requires all franchisors to provide an FDD at least 14 days before you commit to purchasing a franchise. This document includes 23 mandatory items covering everything from fees and restrictions to litigation history and franchisee turnover. Key areas to focus on include:

- Item Seven (Estimated Initial Investment): Are the start-up costs realistic? Do they include real estate, equipment, training, and working capital
- Item 19 (Financial Performance Representations): Does the franchisor provide actual revenue or profit data? If not, you'll need to speak directly with current and former franchisees to assess performance
- Item 20 (System Growth and Turnover): How many outlets have closed, transferred, or terminated in the past three years? A high rate of turnover may signal problems in the system

Location, Location, Location: Real Estate Considerations Matter

For brick-and-mortar franchises, securing the appropriate location is mission-critical. But many prospective franchisees underestimate just how complex and time-consuming the real estate process can be. Questions to ask include:

- Will the franchisor assist with site selection and lease negotiations
- Does your market have sufficient demand for the service you're offering
- Have you accounted for construction costs, permitting delays, or the need for tenant improvements

Before signing a lease, make sure your site is approved by the franchisor, zoned appropriately, and competitively situated within your target market. Poor location decisions can be fatal, even with a strong brand behind you.

Due Diligence Is Not Optional — It's Essential

Even if a franchise system seems successful from the outside, the only way to know whether it's viable for you is through diligent research. This includes:

- Contacting five to seven current and former franchisees in similar markets to ask about actual revenue, marketing effectiveness, franchisor support, and break-even timelines
- Building a financial model that includes royalties, fees, payroll, rent, and realistic revenue assumptions
- Consulting experienced franchise counsel to identify red flags or possible negotiation points (such as non-compete terms,

marketing obligations, or transfer fees)

Understand the Fine Print: Non-Competes and Post-Termination Restrictions

One of the most overlooked — but potentially harmful — aspects of franchise agreements is the restrictive covenants that survive after your business ends. Most franchise agreements include:

- In-term and post-term non-compete clauses that prevent you from operating a similar business for up to two years within a certain geographic radius
- Non-solicitation provisions that restrict contact with former clients, employees, or vendors
- Injunctive relief and fee-shifting clauses that give the franchisor significant enforcement rights if they believe you've violated these obligations

These provisions can limit your ability to earn a living in your field if things don't work out. You must understand exactly what you are agreeing to before committing to the franchise.

Franchise Investment Is a Long-Term Commitment

Most franchise agreements last between five and 10 years, and renewal isn't guaranteed. Even if renewal is offered, it often requires signing a new agreement that may include higher fees or stricter obligations. If your situation changes, selling or transferring your franchise may trigger high administrative fees or require franchisor approval. Some agreements even prohibit termination unless certain financial benchmarks are met.

No Guarantees of Success

Finally, it's important to remember — buying a franchise is not a guarantee of success. Many franchisors explicitly disclaim responsibility for your profitability, and even those that provide financial data often include broad disclaimers. You bear the operational risk, and in many cases, personal financial risk.

Bottom Line: Don't Buy Blind

The decision to invest in a franchise should be driven by facts — not hope, hype, or brand appeal. Review the FDD and Franchise Agreement in full. Speak to other franchisees. Build your own financial model. And don't move forward until you've consulted an attorney who specializes in franchise law. The costs of skipping this step — both financial and emotional — can be far greater than you think.