Practice Update

Avoiding New York's Franchise Law: A Look at Key Exemption-Based Strategies

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New York's franchise regulatory regime is among the most expansive in the United States, applying not only to franchises physically located in the state but also to transactions where offers or acceptances occur in New York, regardless of where the parties reside or where the business will operate. The broad definitions and jurisdictional reach of the New York Franchise Sales Act (NYFSA) mean that franchisors can inadvertently fall within its scope, even if they believe their activities are centered elsewhere.

Assuming an arrangement constitutes a "franchise" under the federal FTC Franchise Rule (FTC Franchise Rule) and the NYFSA (which determination is not the focus of this article), registration in New York and disclosure of a Franchise Disclosure Document (FDD) to prospects are required in order to offer and sell franchises in New York, unless both a federal exemption from disclosure and a New York exemption from registration and disclosure apply.

This article outlines strategies for exemption-based franchising in New York, with particular focus on four New York franchise exemptions that arise frequently in practice: (1) fractional franchise; (2) isolated sales; (3) trade show; and (4) discretionary. These exemptions differ from similar exemptions available under the FTC Franchise Rule and the laws

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of other states. A careful, case-by-case analysis is essential, as relying on exemptions can expose franchisors to significant risk if the requirements are not strictly met. Because similar exemptions differ by jurisdiction, franchisors should make sure they satisfy each applicable jurisdictional exemption they claim.

Fractional Franchise Exemption

The fractional franchise exemption provides a useful illustration of how the NYFSA deviates from the FTC Franchise Rule in ways that materially affect regulatory compliance and long-term planning. A fractional franchise exemption permits established business owners to add a complementary, ancillary product or service line without requiring registration or disclosure of the new business. Both federal law and New York law have fractional franchise exemptions, and the rationale for both is similar: regulation of a franchise is not necessary where prior experience and a limitation on expected sales from the fractional franchise are present.

Under the FTC Franchise Rule, 16 C.F.R. §§ 436.1(g) and 436.8(a)(2), fractional franchises are exempt from disclosure. (Note that federal law never requires registration at the federal level.) The FTC Franchise Rule defines "fractional franchise" as a franchise relationship that meets two distinct criteria: (1) the franchisee, any of its current directors or officers, or any current directors or officers of a parent or affiliate have more than two years of experience in the same type of business; and (2) the parties have a reasonable basis to anticipate that the sales arising from the relationship will not exceed 20% of the franchisee's total dollar volume in sales during the first year of operation.

NYFSA's fractional franchise exemption has stricter requirements. First, the two years of experience requirement only considers the experience of directors or officers of the prospective franchisee. Second, the franchised business must be operated

from the same business location as the existing business. This is not an explicit requirement of the federal exemption. Third, the parties must reasonably anticipate the gross sales from the fractional franchise will not exceed 20% of the franchisee's total dollar volume in sales *annually*, not just during the first year of operation.

Because the FTC Franchise Rule is concerned primarily with pre-sale disclosure, the inquiry at the federal level focuses on whether, at the time of the sale, the parties reasonably anticipate that the franchise will be fractional in the short term. By comparison, the annual sales test under the NYFSA suggests that New York wants to ensure the franchise relationship will likely remain truly fractional over time. This annual cap tests the economic reality of the relationship and helps prevent a situation where an ancillary product or service line starts small but quickly becomes the primary business, and no longer qualifies as a fractional franchise. Accordingly, franchisors should treat the NYFSA's annual sales cap as a continuing compliance requirement to maintain a fractional franchise exemption.

Isolated Sales Exemption

Another commonly cited NYFSA exemption is the isolated sales exemption. This exemption is not available under the FTC Franchise Rule; however, a few other registration states, including Indiana, Minnesota, and Washington, have similar statutory isolated sales exemptions. This exemption permits a limited number of franchise sales in New York without registration, typically where a transaction is isolated and not part of a larger franchise sales plan in New York.

In New York, the offer or sale of a franchise is exempt from the NYFSA's registration and disclosure requirements if: (1) the franchisor directs the offer to not more than two persons, (2) the franchisor does not grant the right to subfranchise, (3) the franchisor

does not pay a commission for soliciting a prospective franchisee in New York, and (4) the franchisor is domiciled in New York or has filed with the New York Department of Law its consent to service of process.

The exemption is intended to apply to truly isolated transactions, such as a one-off sale where the franchisor is not engaging in repeated offerings in New York. Use of the exemption requires careful analysis of the franchisor's long-term sales plan, including past and contemplated future sales, marketing efforts, and solicitation activities that may evidence an intent to develop a franchise program in New York.

Because there is no corresponding isolated sales exemption under the FTC Franchise Rule, a franchisor must rely on another applicable federal exemption to offer or sell a franchise in New York under the isolated sales exemption without disclosing an FDD to a prospect.

Trade Show Exemption

In perhaps a nod to franchisors' desire to promote and market their concepts in New York, New York will grant an unregistered franchisor a temporary exemption from the NYFSA's registration requirements to exhibit, for example, at the International Franchise Expo (IFE) trade show, which takes place in New York every year in June. New York requires every franchisor that exhibits at IFE to either be registered or to have a temporary exemption. The New York Department of Law grants temporary exemptions from registration for unregistered IFE exhibitors pursuant to its discretionary authority, as further discussed below. A franchisor must fill out the application form available on the New York State Attorney General's website. Even if the franchisor's application is granted, the exemption does not permit the franchisor to (1) sell franchises from or in New York; (2) sell franchises at IFE; or (3) disclose its FDD in

New York, regardless of whether the franchisor is registered in other states or only sells franchises in non-registration states.

Discretionary Exemption

The NYFSA, unlike the FTC Franchise Rule, also permits the New York Department of Law to grant discretionary exemptions from registration and/or disclosure on a case-by-case basis where doing so is "not inconsistent with the public interest or the protection of prospective franchisees." N.Y. Gen. Bus. Law § 684(1). In practice, franchisors sometimes seek this discretionary relief when a proposed New York franchisee is unusually sophisticated or otherwise does not present the investor-protection concerns that the NYFSA is designed to address (for example, where the franchisee has significant business experience, substantial resources, and negotiating leverage). Other states, including Indiana, Maryland, Minnesota, and Rhode Island, have comparable discretionary exemptions from registration and/or disclosure based on similar rationale. Although the mechanics of these discretionary exemptions vary by state, New York's process is often viewed as a potential pathway for a franchisor to make a limited New York offer or sale without undertaking full NYFSA compliance.

Case Study – TwistedSipster

Consider the following fictional case study, which underscores the complexity of exemption-based franchising in New York, particularly for emerging franchisors whose business models and plans for growth are still changing:

TwistedSipster is an early-stage franchised beverage concept offering customizable "dirty sodas" through drive-thru kiosks. It currently operates ten company-owned locations in Colorado and Arizona and has sold two franchises in its home states. TwistedSipster has not registered its FDD in any franchise registration state. In 2025, TwistedSipster attended the IFE in New York and applied for and

obtained a temporary exemption to exhibit at the trade show. At the IFE, TwistedSipster met a representative of a private New York university, collected contact information, and provided general information regarding its franchise model, including franchise fees and estimated investment costs. No FDD was disclosed, no franchise agreement was signed, and no consideration was paid.

Several months later, the university contacted TwistedSipster to explore placing a TwistedSipster kiosk inside a food court operated by the university as part of its existing food and beverage services. The parties discussed an arrangement that constitutes a franchise under both the FTC Franchise Rule and the NYFSA. TwistedSipster believes it may qualify for one or more exemptions from registration and disclosure to proceed with this transaction.

At the federal level, TwistedSipster considers the fractional franchise exemption, given the university's extensive experience operating food and beverage services and the parties' reasonable expectation that kiosk sales will represent approximately 10% of overall dining revenues in the first year. Depending on the structure of the transaction, other federal exemptions, such as the large franchisee exemption (which exemption the NYFSA does not have), may also warrant consideration.

At the New York level, TwistedSipster evaluates whether it may rely on the fractional franchise exemption, bearing in mind that New York measures the 20% sales cap on an annual basis. If TwistedSipster proves popular, the parties may want to expand the concept to other locations on campus, and revenues from TwistedSipster may eventually exceed the 20% sales cap. TwistedSipster also considers whether the transaction may qualify for the isolated sales exemption, given that it would be the franchisor's first franchise sale in New York. Plus, TwistedSipster is targeting markets in

Pennsylvania, New Jersey, and Delaware, none of which are franchise registration states. However, given TwistedSipster's prior marketing efforts and projections and plans for growth along the East Coast, TwistedSipster is not confident that this transaction will be a true one-off in the Empire State. Lastly, TwistedSipster considers seeking a discretionary exemption and outlines the facts and basis for the request for its counsel to write a letter to the New York Law Department.

New York's franchise exemptions differ in meaningful ways from those available under federal law and in other states. Fractional franchises, isolated sales, exhibiting at the IFE, and seeking a discretionary exemption each present opportunities for exemption-based franchising strategies, but only when analyzed carefully and applied narrowly. For franchisors and their counsel, effective compliance requires a layered understanding of jurisdictional reach, exemption scope, and the evolving economic realities of the particular franchise relationship.

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