

BEFORE THE
SECURITIES COMMISSIONER OF MARYLAND

IN THE MATTER OF:

Schmidt Baking Distribution, LLC,
d.b.a. Schmidt,

Respondent,

Case No. 2017-0675

* * * * *

CONSENT ORDER

WHEREAS, the Securities Division of the Office of the Attorney General of Maryland (the “Securities Division”) initiated an inquiry into the franchise-related activities of Schmidt Baking Distribution, LLC, d.b.a. Schmidt (“Schmidt”) under the authority granted under the Maryland Franchise Registration and Disclosure Law, MD. BUS. REG. CODE ANN. §14-201 et seq. (2015 Repl. Vol. and Supp. 2017) (the “Maryland Franchise Law”); and

WHEREAS, based on information presented by the Securities Division, the Maryland Securities Commissioner (the “Securities Commissioner”) concluded that grounds existed to allege that Schmidt violated the disclosure and anti-fraud provisions of the Maryland Franchise Law, in relation to offers and sales of Schmidt franchises in Maryland; and

WHEREAS, before the holding of a hearing in this matter, without trial or final adjudication of any issue of fact or law, and without Schmidt admitting or denying any violation of law, the Commissioner and Schmidt have reached an agreement to enter into this Consent Order; and

WHEREAS, Schmidt waives its rights to a hearing and any rights to seek judicial review or otherwise challenge or contest the terms and conditions of this Consent Order; and

WHEREAS, the Securities Commissioner has determined that it is in the public interest to issue this Consent Order;

NOW, THEREFORE, IT IS HEREBY ORDERED AND DECREED:

I. JURISDICTION

1. The Securities Commissioner has jurisdiction in this proceeding pursuant to Section 14-210 (a) of the Maryland Franchise Law.

II. STATEMENT OF FACTS

A. Background

2. Schmidt is a Maryland limited liability company organized in 2010 with a principal business address of 601 South Caroline Street, Baltimore, Maryland 21231.

3. Schmidt offers and sells franchises in the form of distributorships to independent operators who sell and distribute bakery products.

4. Schmidt's distributors operate in the states of Delaware, Maryland, New Jersey, Pennsylvania, Virginia, and West Virginia.

5. Schmidt has been registered with the Securities Division to offer and sell franchises under the Maryland Franchise Law for most periods since June 2011. Schmidt's most recent franchise registration in Maryland was made effective on June 6, 2018.

6. In July 2017, the Securities Division received information suggesting that Schmidt had offered and sold franchises without providing to prospective distributors a copy of the Franchise Disclosure Document ("FDD") required under the Maryland Franchise Law.

7. On July 26, 2017, the Securities Division's wrote Schmidt a letter asking for information regarding its sales of franchises in Maryland, including copies of acknowledgment of receipt forms reflecting that Schmidt had provided copies of FDDs to prospective distributors at

least 14 days before executing any franchise agreements or accepting payment of consideration in relation to the sale of a Schmidt franchise.

8. In response to the Securities Division's July 26, 2017 inquiry, Schmidt provided materials and information regarding offers and sales of Schmidt franchises but was unable to provide copies of any acknowledgment of receipt forms reflecting delivery of FDDs to any prospective Schmidt distributors after April 2013.

9. Schmidt represented to the Securities Division that, prior to April 2013, an outside consultant had provided Franchise Disclosure Documents to prospective Schmidt distributors and that, starting in April 2013, Schmidt took over responsibility from that outside consultant to provide Franchise Disclosure Documents to prospective distributors.

B. Nature of Schmidt's Franchise Offering

10. Under Schmidt's Distribution Agreement, Schmidt charges new distributors an initial franchise fee equal to a multiple of the average weekly net sales of Schmidt products based on historical sales records in the territory sold to the distributor.

11. Schmidt's affiliate, Exeter Financial Services, LLC, and an unaffiliated entity, Distribution Services of America, Inc., offer financing to Schmidt distributors.

12. Schmidt's Distribution Agreement remains in effect until a distributor transfers or sells its distribution rights.

13. Schmidt offers distributors the unconditional right to sell their distribution rights back to Schmidt within one year of purchase at the purchase price the distributor paid for those rights.

14. After the expiration of the one year buy-back agreement, a Schmidt distributor can transfer its distribution rights back to Schmidt, or to a third party, subject to Schmidt's right of first refusal to repurchase distribution rights on the same terms and conditions as the third party's offer.

15. When a Schmidt distributor transfers its distribution rights to a third party, the selling distributor (transferor) is liable for a 2% transfer fee payable to Schmidt.

16. From January 23, 2015 to the date of the Securities Division's inquiry, Schmidt sold approximately 49 Maryland franchises in the form of distribution agreements it entered into with residents of Maryland and to others whose distribution rights under their distribution agreements included territories in Maryland (hereafter "Maryland Distributors").

17. Some of the Maryland Distributors purchased their distribution rights from Schmidt and some from other Maryland Distributors, but all of the Maryland Distributors entered into distribution agreements with Schmidt.

18. When Maryland Distributors transferred their distribution rights, whether to Schmidt or to third parties, those Maryland Distributors ("Maryland Transferors") received a full or partial refund of their initial franchise fee in the form of the selling price they received on the sale of their Schmidt distribution rights.

19. Some Maryland Distributors were existing distributors that previously entered into distribution agreements with Schmidt for franchises that were substantially similar to franchises already owned by the Maryland Distributor ("Existing Distributors") and subsequently purchased additional distribution rights.

C. Representations by Schmidt

20. On September 15, 2017, Schmidt represented to the Securities Division that, in the future, it would furnish all prospective Maryland Distributors with a copy of Schmidt's Maryland-registered FDDs as required under the Maryland Franchise Law, that it would retain copies of acknowledgment of receipt pages confirming delivery of those FDDs within the time required under the Maryland Franchise Law.

21. On September 21, 2017, Schmidt represented to the Securities Division that it would disclose its Maryland-registered FDD to all prospective Maryland distributors that enter into new distribution agreements with Schmidt upon the distributor's purchase of distribution rights from Maryland Transferors.

22. Although Schmidt offered and sold distribution rights to residents of states other than Maryland, Schmidt represents that all offers and sales of distribution rights to distributors other than Maryland Distributors and Maryland Transferors were made from locations outside of Maryland, and those distributors accepted offers to purchase their Schmidt distributorships at locations outside of Maryland.

23. On October 4, 2017, Schmidt required all of its officers and franchise sales personnel to undergo a four hour training class from an attorney experienced in federal and state franchise law about the disclosure requirements of the Maryland Franchise Law.

24. Following a reasonably diligent inquiry, Schmidt represents that, other than offers to sell and sales of distribution rights to Maryland Distributors and Maryland Transferors described in this Consent Order, Schmidt did not offer or sell a Schmidt franchise to a Maryland Distributor from April 2013 to July 26, 2017.

III. CONCLUSIONS OF LAW

25. By engaging in the above activities, the Securities Commissioner has concluded that Schmidt violated §§14-216, 14-223, and 14-229 of the Maryland Franchise Law.

IV. ORDER AND CONSENT

26. THE COMMISSIONER HEREBY ORDERS, AND SCHMIDT REPRESENTS AND CONSENTS THAT:

- A. Schmidt shall immediately and permanently cease and desist from the offer and sale of franchises in violation of the Maryland Franchise Law;
- B. Within forty-five (45) days of its receipt of a fully executed Consent Order of the Securities Commissioner, Schmidt shall send to all Maryland Distributors who currently operate a Schmidt distribution route, and who were not Existing Distributors the following: (i) a copy of the effectively registered or exempt Maryland Franchise Disclosure Document for Schmidt; (ii) a copy of this Consent Order; and (iii) a letter, in substantially the form attached to this letter as Exhibit 1, notifying that Maryland Distributor that it is being offered an opportunity to rescind its Schmidt distributorship under the terms of this Consent Order;
- C. Within thirty (30) days of its receipt of a fully executed Consent Order of the Securities Commissioner, Schmidt shall send to all Maryland Transferors who were not Existing Distributors and who were charged a transfer fee as part of their transfer the following: (i) a copy of this Consent Order and; (ii) a letter, in substantially the form attached to this letter as Exhibit 2, notifying that Maryland Transferor that it will be receiving a refund of the Transfer Fees it paid upon the transfer of its Schmidt distributorship under the terms of this Consent Order;
- D. Schmidt shall pay the Office of the Attorney General the sum of Thirty Two Thousand Five Hundred (\$32,500) as a civil monetary penalty; and
- E. Schmidt acknowledges that this Consent Order is a discloseable order as described under the Maryland Franchise Law, and Item 3 of the NASAA Franchise Registration and Disclosure Guidelines and Amended FTC Franchise Rule.

V. JURISDICTION RETAINED

27. Jurisdiction shall be retained by the Securities Commissioner for such further orders and directions as may be necessary or appropriate for the construction or enforcement of the Consent Order.

VI. CONSEQUENCES OF VIOLATING THIS CONSENT ORDER

28. If Schmidt fails to comply with any term of this Consent Order, the Securities Division may bring administrative or judicial proceedings against it to enforce this Consent Order or to sanction it for violating an order of the Securities Commissioner, and may take any other action authorized under the Maryland Franchise Law or any other applicable law. In any such proceeding in which, after an opportunity for a hearing, the Securities Commissioner or a court

finds that Schmidt has violated this Consent Order, the Statement of Facts and the violations of the Maryland Franchise Law alleged in the Consent Order shall be deemed admitted and may be introduced into evidence against it.

VII. MODIFICATION OF CONSENT ORDER

29. The terms of this Consent Order may be modified only by a subsequent order issued by the Securities Commissioner.

DATE OF THIS ORDER

January 28, 2019

SO ORDERED:

**Commissioner's Signature on File
w/Original Order**

Melanie Senter Lubin
Securities Commissioner

BY CONSENT:

Schmidt Baking Distribution, LLC

By: Stephen J. Paterakis, President

FORM
(On Company Letterhead)

Certified Mail
Return Receipt Requested

Re: Rescission Offer

Dear :

In accordance with discussions our attorneys have had with the Securities Division of the Office of the Attorney General of Maryland (the "Securities Division") and the enclosed Consent Order, Schmidt Baking Distribution, LLC, d.b.a. Schmidt ("Schmidt" or "we") have agreed to offer rescission to certain Maryland distributors who entered into franchises with us in the form of Schmidt Distribution Agreements after January 23, 2015. The Securities Division is requiring us to make this rescission offer under the enclosed Consent Order to Schmidt distributors who did not receive a copy of a Franchise Disclosure Document required under the Maryland Franchise Law at the time they purchased their initial Schmidt franchise. This offer of rescission is made in settlement of the administrative proceeding that the Securities Division may bring for the sale of a franchise in violation of the Maryland Franchise Law and does not affect any civil liability for which we may be responsible.

If you are a current distributor, if you choose to rescind and terminate your franchise, we agree to return to you all initial fees you paid, including loan fees and interest payments you made to Exeter Financial Services, LLC ("Exeter") and Distribution Services of America, Inc. ("DSA") during the term of your franchise, less the balance outstanding at the time of rescission of any loans that you obtained from Exeter and DSA to finance your franchise purchase. We will also cause to be canceled the outstanding amount of any such loans.

In the event you elect to rescind, you will give up your Schmidt Distribution Agreement effective thirty (30) days after we receive your Acceptance of Offer to Rescind. You also will give up any rights to use our trademarks and system and be obligated to refrain from using and disclosing any of our trade secrets and any of our confidential and proprietary information. We will make payments and cause Exeter and DSA to cancel any applicable loans on the effective date of termination of your Schmidt Distribution Agreement, and make any payments within twenty-one (21) days after the effective date of termination of your Schmidt Distribution Agreement. Any such payment will reflect a final reconciliation of expenses owed to Schmidt for inventory you have purchased from Schmidt and any other operational expenses you may owe Schmidt.

Please check the appropriate place below and return a signed copy of this letter to the undersigned. This offer will remain open for thirty (30) days from the date you receive this letter. If you do not respond within those 30 days, the offer expires, and we assume you have rejected this offer of rescission. If you have any questions, please contact Dale E. Cantone, Assistant Attorney General, at the Securities Division (410-576-6368).

Sincerely,

Schmidt Baking Distribution, LLC

Enclosure (Consent Order)

ACCEPTANCE OR REFUSAL OF OFFER TO RESCIND FRANCHISE

1. I, the undersigned, acknowledge that I have read the preceding Rescission Offer and understand its contents.
2. I understand that I have not waived my rights under the Maryland Franchise and Disclosure Law by signing this document.

CHECK ONE

_____ I hereby **accept** your offer of rescission. I agree to not use your trademarks and system and to not use or disclose to anyone the trade secrets, and confidential and proprietary information that we obtained from you.

_____ **I do not wish to accept your offer of rescission.** I wish to remain a distributor under my current Schmidt Distribution Agreement.

Date: _____

Distributor

FORM
(On Company Letterhead)

Certified Mail
Return Receipt Requested

Re: Refund Notice

Dear :

In accordance with discussions our attorneys have had with the Securities Division of the Office of the Attorney General of Maryland (the "Securities Division") and the enclosed Consent Order, Schmidt Baking Distribution, LLC, d.b.a. Schmidt ("Schmidt" or "we") have agreed to issue a refund of the transfer fees paid by certain Maryland distributors who entered into franchises with us in the form of Schmidt Distribution Agreements after January 23, 2015 who transferred their distribution rights. The Securities Division is requiring us to issue this refund under the enclosed Consent Order to Schmidt distributors who did not receive a copy of a Franchise Disclosure Document required under the Maryland Franchise Law. This refund is made in settlement of the administrative proceeding that the Securities Division may bring for the sale of a franchise in violation of the Maryland Franchise Law and does not affect any civil liability for which we may be responsible.

If you have previously terminated your Schmidt franchise because of a transfer of your distribution rights to a third party, we agree to return to you the transfer fees you paid to us. Based on our records, the refund you will receive is _____. We will make payments to you within thirty (30) days of the date of this letter. We will also void any general release you were required to sign in connection with the sale or transfer of your franchise agreement.

If you have any questions, please contact Dale E. Cantone, Assistant Attorney General, at the Securities Division (410-576-6368).

Sincerely,

Schmidt Baking Distribution, LLC

Enclosure (Consent Order)

Exhibit 2