

1 **STATE OF WASHINGTON**
2 **DEPARTMENT OF FINANCIAL INSTITUTIONS**
3 **SECURITIES DIVISION**

4 IN THE MATTER OF DETERMINING) Order No. S-17-2288-18-SC01
5 Whether there has been a violation of the)
6 Franchise Investment Protection Act of) STATEMENT OF CHARGES AND NOTICE OF INTENT
7 Washington by:) TO ENTER ORDER TO CEASE AND DESIST
8)
9 Morgan Henning a/k/a Morgan Rothschild; and)
10 Party Princess International, LLC,)

11 Respondents.

12 THE STATE OF WASHINGTON TO: Morgan Henning a/k/a Morgan Rothschild; and Party Princess International,
13 LLC

14 **STATEMENT OF CHARGES**

15 Please take notice that the Securities Administrator for the state of Washington has reason to believe that
16 Respondents Morgan Henning a/k/a Morgan Rothschild and Party Princess International, LLC have each violated the
17 Franchise Investment Protection Act of Washington and that, pursuant to RCW 19.100.248, their violations justify the
18 entry of an order against each to cease and desist from these violations. The Securities Administrator finds the following:

19 **TENTATIVE FINDINGS OF FACT**

20 Respondents

21 1. Party Princess International, LLC is a Colorado limited liability company formed for the purpose of
22 franchising the right to host costumed and themed parties for children. Party Princess International's principal place of
23 business is Orange, California. Party Princess International, LLC used the name Party Princess USA, LLC, through
24 July 2017. Party Princess International does business under the names Party Princess USA and Party Princess
25 Productions.

26 2. Morgan Henning, a California resident, is the sole member and manager of Party Princess International. He
27 further acts as the principal and sole shareholder of Rothchild Enterprises, Inc.¹ Morgan Henning also uses the name
28 Morgan Rothschild.

29 Overview

30 3. A franchise system often provides franchisors with a significant amount of control over the terms of a
31 franchise agreement, the profitability of a franchise, and the operation of a franchise. As an effort to manage this

32 _____
33 ¹ Rothchild Enterprises, a California corporation with a principal place of business in Orange, California, operated a business that,
34 from 2011 to 2017, performed costumed and themed children's birthday parties in Southern California under the name Party
35 Princess Productions Orange County. Rothchild Enterprises currently owns the trademark for Party Princess Productions.

1 imbalance, the Franchise Investment Protection Act provides franchisees with some protections, some of which are
2 administered by the Securities Division. Specifically, unless exempt from registration, franchisors must register their
3 offer with the Securities Division. As part of this registration process, the Securities Division reviews a franchisor's
4 disclosure documents, documents which must be provided to franchisees prior to the sale of a franchise. The Securities
5 Division is also invested with the authority to investigate and charge violations of the Franchise Investment Protection
6 Act.

7 4. Through the sale of a Party Princess International franchises in Washington in 2015 and 2016, Morgan
8 Henning and Party Princess International violated the registration and document disclosure provisions of the Franchise
9 Investment Protection Act. As part of these sales, Morgan Henning and Party Princess International also used
10 dishonest sales tactics by making misleading statements to prospective franchisees about the profitability of owning a
11 Party Princess International franchise in Washington.

12 General Sale of Party Princess Franchises and Registration Status in Washington

13 5. Since 2015, Party Princess International has been engaged in the sale of franchises which provide costumed
14 and themed parties, primarily for children. Neither Morgan Henning, nor Party Princess International registered with
15 the Securities Division in one of their two sales of Party Princess International franchises in Washington.

16 6. In a typical franchise agreement, Party Princess International provides, in part, that for a fee of approximately
17 \$49,500, prospective franchisees have the right, in a specific territory, to host costumed and themed parties using Party
18 Princess International's trademarks. Party Princess International charges prospective franchisees additional initial fees,
19 which include a \$6,000 fee to activate a franchisee's website, a \$45,000 fee for an initial set of 30 costumes, and a
20 \$2,000 fee for opening equipment and supplies. Party Princess International agrees to provide franchisees with an
21 initial training program and an operations manual. Party Princess International also manages the franchise system's
22 national advertising and marketing campaign.

23 7. Party Princess International relied on third-parties to promote the sale of Party Princess International
24 franchises. After a prospective franchisee made an initial inquiry with Party Princess International, either Party
25 Princess International or a thirty-party would provide the prospective franchisee with written information about the
franchise. This written information typically included a copy of the Party Princess International franchise disclosure
document, as well as financial projection worksheets. The financial projection worksheets provided a series of inputs
for business volume and growth and fixed and variable expenses for prospective franchisees to enter to determine the
profitability of a Party Princess International franchise. As part of the sales process, prospective franchisees were also
encouraged to meet with Morgan Henning and attend a live informational presentation about the franchise.

8. Party Princess International has sold approximately fifteen franchises nationwide since 2015, two of which
were Washington franchises. Party Princess International signed franchise agreements substantially similar to the
franchise agreement described in paragraph six with two Washington franchisees, Franchisee A and Franchisee B.

9. For the sale of a Party Princess International franchise to Franchisee B, neither Morgan Henning, nor Party Princess International were registered to offer or sell franchises in the state of Washington and had not been previously registered to do so. Party Princess International was registered with Washington to offer and sell franchises from January 8, 2016, to April 30, 2017, during which time the sale of a Party Princess International franchise to Franchisee A took place.² In the course of selling franchises to both Franchisee A and Franchisee B, both Morgan Henning and Party Princess International made misleading statements to Franchisee A and Franchisee B about the profitability of owning a Party Princess International franchise.

Offer and Sale of Party Princess International Franchises in Washington

Sale of Party Princess International Franchise to Franchisee A Using Misleading Profit Projections

10. Morgan Henning and Party Princess International misrepresented and omitted material information in representations to Franchisee A about the profitability of owning a Party Princess International franchise and the number of events that Franchisee A could expect to host per month.

11. Through a franchise broker, Franchisee A, a Washington resident, learned of Party Princess International and then reached out to Morgan Henning to learn more about the franchise. In meetings and phone calls with Franchisee A, Morgan Henning emphasized the ability of Party Princess International's search engine optimization efforts to capture demand for costumed and themed parties for children. Morgan Henning represented that through the success of the company's targeted advertising with Google, Franchisee A's phone would constantly be ringing for party bookings and that Franchisee A would not have to invest a lot of time or attention into the franchise to be successful.

12. Morgan Henning reinforced these same representations about the high demand for costumed and themed parties for children in documents that he sent to Franchisee A. In an analysis of Franchisee A's prospective territory in Washington, Party Princess International represented that with an approximately \$6,000 per month advertising budget, Franchisee A could expect to book over 200 parties per month,³ generating large revenues for Franchisee A.⁴ Party Princess International based these representations on the performance of its Orange County franchise, but failed to disclose the bases and assumptions for the company's representation that with a similar advertising budget, Franchisee A's territory would capture a similar level of demand as the Orange County franchise. Party Princess International failed to disclose to Franchisee A whether other Party Princess International franchisees were able to capture similar demand with a similar advertising budget and failed to disclose the risk that Franchisee A may not attain similar

² In September 2017, Party Princess International reapplied to register with Washington to offer and sell franchises in the state, but abandoned its application as a result of this investigation.

³ Franchisees are not expected to personally attend every party. Rather, the Party Princess International franchise business model contemplates that franchisees hire independent contractors to perform at the parties, enabling franchisees to potentially book multiple parties at the same time.

⁴ Party princess International represented that average revenues per event ranged from approximately \$135 to \$185.

1 success with a similar advertising budget. Franchisee A thought that if he could capture a modest amount of the
2 projections of 200 parties, then he could operate a very profitable business.

3 13. On a separate occasion, Party Princess International and Morgan Henning represented to Franchisee A that
4 Franchisee A could expect to host at least 40 parties per month. The Party Princess International franchise agreement
5 provides that Party Princess International can terminate the franchise agreement, if the franchisee fails to host a
6 minimum of 40 parties per month for six or more months. When, prior to the purchase of a franchise, Franchisee A
7 asked Morgan Henning about the feasibility of hosting 40 parties per month, Morgan Henning stated that booking 40
8 parties per month would be easy. Morgan Henning again referred to the ability of Party Princess International's search
9 engine optimization efforts to generate demand for Party Princess International franchisees. Morgan Henning,
10 however, failed to disclose the basis or assumptions underlying his claim that Franchisee A could expect to host at
11 least 40 parties per month and failed to disclose whether and how often other Party Princess International franchisees
12 were able to meet this minimum.

13 14. Through a financial projection worksheet that Party Princess International sent Franchisee A prior to the
14 purchase of a franchise, the company further represented that Franchisee A's business would be profitable. The
15 worksheet provides a series of inputs for Franchisee A to complete to determine the net income of a Party Princess
16 International franchise.⁵ Many of the inputs asked for projections of fixed and variable operating expenses, such as
17 employment, technology, supplies, and marketing. The worksheet's biggest driver of a franchise's profitability,
18 however, is the market demand for a franchise, and Party Princess International identifies only four factors for a
19 franchisee to consider about a territory's market demand: the territory's population, the percentage of children ages
20 zero to nine in the territory, the percentage of parents whom a franchisee knows that would search for costumed or
21 themed parties for their children, and of this percentage, the percentage of parents that a franchisee thinks would book
22 a costumed or themed party. Franchisee A entered conservative number for many of the worksheet's inputs, yet Party
23 Princess International projected an incredibly profitable business for Franchisee A. Franchisee A then entered a series
24 of even more conservative numbers for the inputs, yet each time Party Princess International projected a very
25 profitable business for Franchisee A. Through the worksheet, Party Princess International misrepresented to Franchisee
A that those four factors were sufficient to determine the demand for a Party Princess franchise and failed to disclose
to Franchisee A that Party Princess International had not tested whether prospective franchisees could rely on the
financial projection worksheet to assess the profitability of a Party Princess International franchise.

15. Franchisee A felt that he could not pass on the opportunity to purchase a Party Princess International franchise
based on the high net income projections provided by Party Princess International. Based on the worksheet and
Morgan Henning's and Party Princess International's other representations described above about the profitability of a

⁵ In at least one instance, Party Princess International supplied a prospective franchisee with figures to enter into the financial
projection worksheet to demonstrate the profitability of a Party Princess International franchise.

1 Party Princess International franchise, in 2016, Franchisee A purchased multiple Party Princess International franchise
2 territories in Washington, at an initial franchise fee cost of \$325,000, giving Franchisee A one of the largest footprints
3 of hosting 40 parties per month, this is because he owns multiple territories and can aggregate parties from each
4 territory to meet the minimum requirement.

5 *Sale of Party Princess International Franchise to Franchisee B Using Misleading Profit Projections*

6 16. Morgan Henning and Party Princess International similarly misrepresented and omitted material information in
7 representations to Franchisee B about the profitability of owning a Party Princess in Washington franchise and the
8 number of events that Franchisee B could expect to host per month.

9 17. In 2015, a franchise broker discussed with Franchisee B the possibility of opening a Party Princess
10 International franchise in Washington and then arranged for Morgan Henning to speak with Franchisee B.

11 18. During their initial phone call, Morgan Henning explained to Franchisee B the business model for Party
12 Princess International franchisees. Morgan Henning also explained that through years of practice, Party Princess
13 International had developed a system to advertise through Google to capture a portion of the Google search results for
14 costumed and themed birthday parties. Morgan Henning represented that this marketing method could easily provide
15 franchisees with over \$100,000 per year in revenue, and possibly up to \$200,000 in revenue. Morgan Henning failed to
16 provide Franchisee B with the basis or assumptions for these representations and failed to disclose the risk that
17 Franchisee B may not achieve these revenues.

18 19. In subsequent conversations, Morgan Henning continued to emphasize the strength of Party Princess
19 International's marketing campaign through Google, representing that Party Princess International could duplicate
20 these efforts within a franchisee's territory and that through these marketing efforts, the franchisee would be
21 successful. Morgan Henning explained that Party Princess International's marketing campaign enabled the success of
22 Party Princess International franchisees. A Party Princess International representative further claimed to Franchisee B
23 that through years of research, Party Princess International could predictably determine the demand for costumed and
24 themed children's parties in a franchisee's territory. Morgan Henning, however, failed to disclose whether Party
25 Princess International has explored the possibility of the success of its marketing campaign in Franchisee B's
prospective territory and failed to disclose the risk to Franchisee B that Party Princess International's marketing efforts
in Franchisee B's territory may not generate sufficient demand for Franchisee B to run a profitable business.

20. As Franchisee B wavered about the purchase of a Party Princess International territory, he asked Morgan
Henning what revenues Morgan Henning and Party Princess Productions projected for Franchisee B's prospective
territory. Morgan Henning stated that a Google advertising campaign alone in Franchisee B's prospective territory
would generate Franchisee B a minimum of \$100,000 per year. Morgan Henning failed to provide Franchisee B with
the basis or assumptions for these representations and failed to disclose the risk that Franchisee B's Party Princess

1 International franchise may not generate a minimum of \$100,000 per year. Morgan Henning noted that he could not
2 put this projection in writing due to regulatory prohibitions.

3 21. Prior to purchase, Franchisee B read through the Party Princess International franchise agreement and noted
4 that Party Princess International can terminate a franchise agreement if the franchisee does not host a minimum of 40
5 parties during a calendar month. Franchisee B asked Morgan Henning about this provision, and Morgan Henning
6 replied that hosting 40 parties per month would be easily achievable. Morgan Henning failed to provide Franchisee B
7 with the basis or assumptions for this representation. Morgan Henning further failed to disclose whether and how often
8 other Party Princess International franchisees were able to host at least 40 parties per month.

9 22. Convinced of the profitability of a Party Princess International franchise based on Morgan Henning's
10 representations, in December 2015, Franchisee B purchased a Party Princess International franchise located in
11 Washington. Months later, Party Princess International reaffirmed many of Morgan Henning's representations to
12 Franchisee B described above about the profitability of Party Princess International franchises. Party Princess
13 International sent Franchisee B a document, in which the company provided Franchisee B with "predictive analysis"
14 about the "worst-case-scenario revenue data" for Franchisee B. In this analysis, Party Princess International
15 represented that, if Franchisee B did not take any steps to attract business, other than the funding of an approximate
16 \$2,000 per month advertising campaign through Google, then Franchisee B's Washington franchise could expect to
17 meet the 40 party per month minimum and provide Franchisee B with approximately \$90,000 in gross revenue per
18 year.

19 23. Franchisee B, however, faced a significant lack of demand for costumed and themed birthday parties for
20 children soon after opening his franchise. Through Party Princess International's marketing team, Franchisee B fully
21 funded an advertising campaign through Google each month to capture the maximum amount of search results for
22 costumed and themed birthday parties for children. Despite these and other efforts, the demand never approached what
23 Morgan Henning and Party Princess International had represented.⁶ At one point, Morgan Henning explained to
24 Franchisee B that Party Princess International was "trying to figure out" why the demand for Franchisee B was so low,
25 even though Franchisee B was sold a franchise, for which Party Princess International and Morgan Henning
represented that there was full demand. Over the course of 15 months, Franchisee B hosted an average of 16 parties per
month, never hosting more than 30 parties in a given month, and failing to host 40 parties for every month.

21 24. After Franchisee B filed a complaint with the Securities Division related to Party Princess International's sales
22 tactics, in October 2017, Party Princess International filed an arbitration claim seeking to terminate its franchise
23 agreement with Franchisee B, effectively erasing all of Franchisee B's substantial investments in the purchase and

24 ⁶ When Franchisee B later brought up this issue with one of the marketing companies for Party Princess International, the
25 representative admitted that he had relied on data from Party Princess International's Los Angeles and Orange County franchises
to project Franchisee B's "worst-case scenario revenue data."

1 operation of his business. To date, Party Princess International's arbitration claim against Franchisee B is still pending.
2 The site of the arbitration is in Denver, Colorado, however, had Party Princess International properly registered this
3 franchise sale in Washington, the Securities Division would have required that any arbitration take place in
4 Washington.

5 25. In addition to Franchisee B, other franchisees have struggled to run profitable Party Princess International
6 franchises.

7 Respondents Have Been Sued by Other Franchisees for Making Misleading Profit Projections

8 26. In September 2017, a Montana Party Princess International franchisee sued Party Princess International for
9 breach of the implied covenant of good faith and fair dealing, negligent misrepresentation, and fraud in the
10 inducement. Specifically, in the complaint, the plaintiffs alleged that Party Princess International had made the
11 following misrepresentations to the plaintiffs: that the franchise business model was adaptable to Southwest Montana,
12 that Party Princess International had determined that there was sufficient demand for Party Princess International
13 events in Southwest Montana, and that the franchisee would be able to meet the minimum requirement of 40 parties
14 per month. The plaintiffs further alleged that the market demand for Party Princess International events in Southwest
15 Montana did not remotely approach what would be required to meet the 40 party minimum requirement, to break even
16 on the initial investments in the franchise, or to meaningfully offset the initial investments in the franchise. The parties
17 settled the case in October 2017.

18 27. In November 2017, an Ohio Party Princess International franchisee sued party Princess International and
19 Morgan Henning for violations of the Ohio Business Opportunity Purchasers Protection Act, violations of the Ohio
20 Deceptive Sales Practices Act, fraud, negligent misrepresentation, and fraud by omission. The plaintiff alleged that
21 Morgan Henning and Party Princess International represented that they had researched the plaintiff's prospective
22 market, that there was sufficient demand for Party Princess International events in the prospective market, and that the
23 prospective market could support a profitable franchise. The plaintiff further alleged that Party Princess International
24 provided the franchisee with documents projecting profits for the Ohio franchisee from years one through five. Instead,
25 the Ohio franchisee never had a profitable month and has incurred significant losses. This lawsuit is still pending as of
this writing.

Failure to Provide Compliant Disclosure Documents

26 28. Although both Franchisee A and Franchisee B were both provided with copies of the Party Princess franchise
27 disclosure document,⁷ these franchise disclosure documents did not comply with the Franchise Investment Protection
28 Act. The Franchise Investment Protection Act provides that all financial performance representations specific to the
29 offer or sale of a franchise must be included in the franchise disclosure document. The financial performance
30 representations made by Morgan Henning and Party Princess International to Franchisee A and Franchisee B, as

⁷ The franchise disclosure document provided to Franchisee B was not filed with the Securities Division.

described above, were not included in the respective franchise disclosure documents that Franchisee A and Franchisee B received.

Based upon the above findings of fact, the following conclusions of law are made:

CONCLUSIONS OF LAW

1. Morgan Henning’s and Party Princess International’s offer and sale of Party Princess International businesses in Washington constitutes the offer and sale of a franchise as defined in RCW 19.100.010(6), RCW 19.100.010(12), and RCW 19.100.010(17).
2. Morgan Henning and Party Princess International violated RCW 19.100.180 in connection with the offer and sale of franchises to Franchisee A and Franchisee B by making untrue statements of material fact or omitting to state material facts necessary to make the statements made, in light of the circumstanced under which they were made, not misleading.
3. Morgan Henning and Party Princess International violated RCW 19.100.020 by offering and selling a Party Princess International franchise to Franchisee B without being registered with the state to do so.
4. Morgan Henning and Party Princess International violated RCW 19.100.080 by failing to provide Franchisee A and Franchisee B with a franchise disclosure document, which met the requirements of RCW 19.100.040, prior to their respective franchise purchases.

NOTICE OF INTENT TO ORDER THE RESPONDENT TO CEASE AND DESIST

Based upon the above Tentative Findings of Fact and Conclusions of Law, the Securities Administrator intends to order that Morgan Henning and Party Princess International each shall cease and desist from violations of RCW 19.100.180, RCW 19.100.020, and RCW 19.100.080.

AUTHORITY AND PROCEDURE

This Order is entered pursuant to the provisions of RCW 19.100.248 and is subject to the provisions of Chapter 34.05 RCW. Morgan Henning and Party Princess International may each make a written request for a hearing as set forth in the NOTICE OF OPPORTUNITY TO DEFEND AND OPPORTUNITY FOR HEARING accompanying this order. If a respondent does not request a hearing within the time allowed, the Securities Administrator intends to adopt the above Tentative Findings of Fact and Conclusions of Law as final and enter an order to permanent cease and desist as to that respondent.

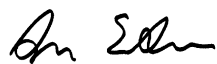
Signed and Entered this 20th day of April 2018.

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