

**STATE OF WASHINGTON
DEPARTMENT OF FINANCIAL INSTITUTIONS
SECURITIES DIVISION**

IN THE MATTER OF DETERMINING
Whether there has been a violation of the
Franchise Investment Protection Act of
Washington by:

NEIGHBORHOOD NETWORKS
PUBLISHING, INC.,
d/b/a N2 Publishing

Respondent

Order No. S-18-2456-18-CO01

CONSENT ORDER

On November 5, 2018, the Securities Administrator of the Securities Division of the Department of Financial Institutions (“Securities Division”) issued a Statement of Charges and Notice of Intent To Enter Order To Cease and Desist (“Statement of Charges”), Order Number S-18-2456-18-SC01, against Respondent Neighborhood Networks Publishing, Inc., d/b/a N2 Publishing, (“N2 Inc.). Pursuant to the Franchise Investment Protection Act of Washington, RCW 19.100, the Securities Division and Respondent N2 Inc., do hereby enter into this Consent Order in settlement of the matters alleged herein. Respondent N2 Inc. neither admits nor denies the Findings of Fact or Conclusions of Law as stated below.

FINDINGS OF FACT

I.

Respondent

1. N2 Inc. is a Delaware corporation that was formed on January 16, 2009.¹ Its principal place of business is in Wilmington, North Carolina. N2 Inc. publishes magazines and/or newsletters for residential communities. Each N2 Inc. publication is specific to a particular residential community. N2 Inc. also sells

¹ N2 Inc. was originally incorporated in Missouri, then became a North Carolina corporation before becoming a Delaware corporation.

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DEPARTMENT OF FINANCIAL INSTITUTIONS
Securities Division
PO Box 9033
Olympia, WA 98507-9033
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1 advertising space within these publications to local businesses. N2 Inc. contracts with local area directors who
2 sell the advertisements and help generate content for the publications.

3 **Related Entity**

4 2. N2 Franchising, LLC d/b/a N2 Publishing (“N2 Franchising”) is a Delaware limited liability
5 company that was formed on October 26, 2016. It has the same principal place of business as N2 Inc. in
6 Wilmington, North Carolina. It is in the business of offering and selling franchises for businesses that are
7 similar to N2 Inc.’s area directorships. N2 Franchising is currently licensed with the Securities Division to
8 sell such franchises, and has been since January 3, 2017. It has a pending application with the Securities
9 Division to register a similar, but separate, franchise that involves publications that focus on the real estate
10 industry. Most of the Washington area directors that are the subject of this Statement of Charges have
11 converted their area director arrangements to franchises.

12 **II.**

13 **Nature of the Conduct**

14 3. Beginning no later than February 2010 to at least July 2017, N2 Inc. offered and sold area
15 director arrangements to at least 30 Washington residents. Area directors sold advertising in N2 Inc.’s
16 publications to local businesses and community members, and offered N2 Inc. services, including N2 Inc.’s
17 advertising design services, to the community. They also provided content to N2 Inc. for publication. N2 Inc.
18 designed, published, printed, and distributed the publication to those within the specific community or
19 industry. N2 Inc. provided area directors with a marketing plan and business system that area directors were
20 to comply with, granted area directors the right to use N2 Inc.’s trademarks in their business, and deducted
21 15% from the advertising payments received from advertisers as part of the calculation of the commission
22 payments paid to area directors.

1 **N2 Inc. Granted Area Directors The Right To Use Its Trademarks**

2 4. N2 Inc. entered into a written agreement with each area director (the “Agreement”), effective
3 for one to three years. In the Agreement, N2 Inc. granted area directors a limited license to use its trademarks,
4 service marks and copyrighted materials to advertise and promote their N2 Inc. publication business. For
5 example, area directors were often provided with their own “n2pub.com” email, a domain that N2 Inc. owns,
6 to use in marketing their N2 Inc. business. N2 Inc.’s logo also appeared on the inside cover of the publications.

7 **N2 Inc. Provided Area Directors With A Marketing Plan**

8 5. N2 Inc. established a marketing plan that provided guidance to area directors and a system
9 within which area directors were to operate. N2 Inc. provided its area directors with a multi-day training and
10 held periodic conference calls with area directors to provide sales tips and consultation. Area directors were
11 only allowed to sell products and services approved by N2 Inc., under the terms and pricing set by N2 Inc.
12 N2 Inc. required its area directors to use its form contracts when selling advertisements to local businesses,
13 and area directors had to send the contracts to N2 Inc. for approval and execution. N2 Inc. also required area
14 directors to obtain its prior approval if the area director wanted to use their own marketing materials. More
15 generally, N2 Inc. required its area directors follow its standards and procedures in operating their businesses.
16 N2 Inc. had the right to terminate any area director arrangement if an area director failed to follow N2 Inc.’s
17 standards and procedures, or failed to follow any other provision of the Agreement after an opportunity to
18 cure.

19 **N2 Inc. Required Area Directors To Pay An Indirect Franchise Fee**

20 6. N2 Inc. charged and collected an indirect franchise fee from area directors in the form of a
21 15% deduction from the area directors’ commission payments called the “N2 Cost.”² In the Agreement, N2
22

23 ² In the most recent franchise disclosure document that N2 Inc.’s affiliate, N2 Franchising, filed with the Securities Division as part of its pending application to franchise a business substantially similar to the area directorships (see Paragraph 2), N2 Franchising

1 Inc. defined the N2 Cost as 15% of the “Advertising Value of each N2 Publication, whether or not N2 actually
2 receives payment for the advertisements.” The Agreement defined “Advertising Value” as “the value of the
3 advertising in each N2 Publication, as determined by N2 Inc. in its discretion.”

4 7. N2 Inc. deducted the 15% N2 Cost from the area director’s monthly commission payment. N2
5 Inc. compensated the area directors in this manner because ad purchasers were required to pay for their
6 advertisements by remitting payment directly to N2 Inc. N2 Inc. then deducted the N2 Cost, the actual
7 publication cost, and other miscellaneous costs and fees from the revenue that it received before paying the
8 remainder to the area director as a monthly commission.

9 8. If an area director’s advertisement sales did not generate enough actual revenue to N2 Inc. in
10 any month to cover the area director’s deductions, including the N2 Cost, then the area director did not receive
11 a commission payment for that month. N2 Inc. then deducted the uncovered portion of the N2 Cost and other
12 deductions from the area director’s commission payment for the following month. If an area director did not
13 bring in enough actual revenue to cover the N2 Cost and other deductions for more than two consecutive
14 months, then N2 Inc. had the right to terminate the Agreement.

15 III.

16 Misrepresentations and Omissions

17 9. N2 Inc. did not provide any of the Washington area directors with a franchise disclosure
18 document (“FDD”) prior to the sale of the area director arrangements. The FDD provides a potential
19 franchisee with information such as the cost of the franchise, the business and litigation background of the
20 company’s principals, and the number of opened and closed franchises over the past three years. The FDD
21 must be prepared in accordance with separate guidelines promulgated by the Federal Trade Commission and

22 lists an “N2 Royalty” that it charges to franchisees via a deduction from the franchisee’s commission. N2 Franchising described the
23 N2 Royalty as “15% of the advertising value of each publication.” The N2 Royalty was previously called “N2 Cost” in an earlier
version of the franchise disclosure document.

1 the North American Securities Administrators Association, Inc. A franchisor who chooses to make financial
2 performance representations in its FDD must provide certain information, in accordance with the guidelines,
3 so that the representations are not misleading.

4 10. Instead of making financial performance representations within an FDD and in accordance
5 with regulatory guidelines, N2 Inc. made these representations in advertisements and online videos that it
6 used to sell area director arrangements. N2 Inc. made the financial performance representations in a manner
7 that was misleading because it failed to provide material information regarding the representations. For
8 example, in a 2015 advertisement, N2 Inc. represented that “[t]he average Area Director earns between \$70k-
9 \$100k and top performers earn in excess of \$200k+ annually.” N2 Inc. made a similar statement in an
10 advertisement the following year. Neither advertisement contained any other information that would provide
11 context for these figures, such as the sample size that was used to determine the average, the geographic
12 location of the area directors that formed the basis for these figures, or the length of time the area directors
13 had been with N2 Inc.

14 11. Similarly, in a 15 minute video that N2 Inc. posted on its website (www.n2pub.com), designed
15 to help area directors decide “whether or not N2 is a good fit,” N2 Inc. provided earnings examples for three
16 area directors that were misleading. N2 Inc. showed the area directors’ cash received, expenses, and take-
17 home earnings for the startup phase (typically the first 12-15 months of operations) or for the second year of
18 operations. N2 Inc.’s example showed those in the startup phase earned no income during the first few months
19 of ramping up, but thereafter earned income that increased overall by the end of the period. One of these area
20 directors earned over \$10,000 in one month towards the end of the startup phase. In the example for an area
21 director’s second year of operations, N2 Inc. showed that the area director earned over \$185,000 total after
22 expenses were deducted. In none of these examples did N2 Inc. include any information that would provide
23 more context for these earnings figures, including the area directors’ geographic location, how many

1 publications each area director owned, how many hours the area directors worked to achieve these results, or
2 how typical the results were.

3 **IV.**

4 **Registration Status**

5 12. Respondent N2 Inc. is not currently registered to sell its franchises in the state of Washington
6 and has not previously been so registered. There is no notification of exemption on file with the state of
7 Washington.

8 Based upon the above Findings of Fact, the following Conclusions of Law are made:

9 **CONCLUSIONS OF LAW**

10 **I.**

11 The offer and sale of the N2 Inc. area director arrangements as described above constitutes the offer
12 or sale of a franchise as defined in RCW 19.100.010(6), RCW 19.100.010(12), and RCW 19.100.010(17).

13 **II.**

14 The offer or sale of said franchise was in violation of RCW 19.100.020 because no registration for
15 such offer or sale is on file with the Washington Securities Administrator for the time period when offers
16 and/or sales occurred.

17 **III.**

18 The offers and/or sale of said franchises were in violation of RCW 19.100.080, the disclosure
19 document requirement provision of the Franchise Investment Protection Act, because Respondent N2 Inc.
20 failed to provide prospective purchasers with a current disclosure document that contained all material
21 information about the franchise including, but not necessarily limited to, information related to earnings
22 claims or financial performance representations that would make such claims or representations not
23 misleading.

1 **IV.**

2 The offers and/or sale of said franchises were made in violation of RCW 19.100.170 because, in
3 offering and/or selling franchises to Washington residents, N2 Inc. omitted material facts regarding its
4 financial performance representations that were necessary for the representations to not be misleading.

5 **CONSENT ORDER**

6 Based upon the foregoing and finding it in the public interest:

7 IT IS AGREED AND ORDERED that Respondent N2 Inc. and its agents and employees shall each
8 cease and desist from offering or selling franchises in violation of RCW 19.100.020, the registration section
9 of the Franchise Investment Protection Act of the state of Washington.

10 IT IS FURTHER AGREED AND ORDERED that Respondent N2 Inc., and its agents and employees
11 shall each cease and desist from any violation of RCW 19.100.080, the franchise disclosure document section
12 of the Franchise Investment Protection Act of the state of Washington.

13 IT IS FURTHER AGREED AND ORDERED that Respondent N2 Inc., and its agents and employees
14 shall each cease and desist from any violation of RCW 19.100.170, the violations section of the Franchise
15 Investment Protection Act of the state of Washington.

16 IT IS FURTHER AGREED that the Respondent N2 Inc. shall be liable for and shall pay investigative
17 costs of \$4,000 prior to the entry of this Consent Order.

18 IT IS FURTHER AGREED that the Securities Division has jurisdiction to enter this Consent Order.

19 IT IS FURTHER AGREED that Respondent N2 Inc. enters into this Consent Order freely and
20 voluntarily and, having been represented by counsel, with a full understanding of its terms and significance.

21 IT IS FURTHER AGREED that in consideration of the foregoing, Respondent N2 Inc. waives its
22
23

right to a hearing and to judicial review of this matter.

Signed this 16th day of April, 2019.

Signed by:

Approved as to form by:

Neighborhood Networks Publishing, Inc.

By /s/
DUANE HIXON
C.E.O.

/s/
CAROLINE FICHTER
WSBA# 42554

SIGNED and ENTERED this 22nd day of April, 2019.



WILLIAM M. BEATTY
Securities Administrator

Approved by:

Presented by:



SUZANNE SARASON
Chief of Enforcement



/s/
MARTIN CORDELL
Financial Legal Examiner

Reviewed by:

JACK MCCLELLAN
Financial Legal Examiner Supervisor

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