

Lori Karpman & Associates Ltd.

Franchising 101 or “I’ve bought this book so now what”?

By Lori Karpman

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ongratulations! In purchasing this book, you’ve taken the first and most important step on the road to the self-employment that franchising has to offer. Franchising is a specialized business model that allows thousands of individuals each year to fulfill their dream of owning a business.

While every system may operate a little differently, there are basics that transcend the industry. In this article, my goal is to educate you about this business model allowing you to make an informed decision in selecting the best franchise opportunity for you.

Franchising is a specialty of business, as pediatrics is a specialty of medicine. It is actually a financing model since every business needs money to grow. When a business wants to expand it can either: (a) go to the bank and ask for a loan to finance building corporate stores or, (b) go to individuals, called “franchisees” and have them invest in individual stores. Option (b) is much more attractive as the growth is funded with the money of others and not with corporate debt and hence, the company grows at a quicker rate. It then becomes a Franchisor, and creates a Franchise System. Each unit in the System must then share common goals and methods of operations. It has to appear as if the original business had financed multiple corporate stores.

The success of a franchise system is based upon 2 intangible principals: Consistency and Goodwill. This is true regardless of the product or service. By consistency, I mean that the customer can expect to have the same experience in every unit. A Big Mac is a Big Mac wherever you may be. The second element, goodwill refers to the fact that once the sign goes up above the door, customers will automatically be drawn to your store just by virtue of the fact that they’ve recognized the name and that they know what to expect from the customer experience. These elements must be present in any system you evaluate.

How do you know it’s there? Pretend that you are a mystery shopper, visit several locations. Do they look the same? Is the staff trained in the same way? Did you have basically the same experience at them all? Keep in mind that there will be variations among different outlets to reflect the personalities of the individual trade market area.

The Franchisor is a team of people who create, implement and manage the system for the benefit of the whole. When you buy a franchise you will be given extensive training in that field of expertise. You are expected to follow the rules. Remember, that’s why you bought a franchise in the first place. What you are buying is the system, tried and tested, the tools, and a less risky way to go in to business. The franchisor’s job is to give you the tools and yours is to use them. Inevitably, franchisees forget this and figure out a way to “do it better, cheaper...whatever”. It’s on that day that your results will suffer. Many, many, great ideas have come from franchisees, and franchisors want to hear all of them, but there is a procedure for it. Franchisees cannot unilaterally implement changes at the store level. Most consumers don’t understand franchising, so if they have a bad experience at one unit, it reflects poorly on the entire

system. The upside of franchising however, is huge, the franchisor provides the name and goodwill, the research and development, continuing support and marketing, and that allows you to do what you need to do most, run your business. That's the formula for franchising success.

This is why when investigating a franchise it is so important to meet the franchisor's management team. It's easy to get caught up in investigating the actual business opportunity but don't forget to pay attention to the people behind the opportunity. You are investing your money not only in your particular unit but in the system as a whole. You want to know about the foundation upon which the system is built. The provinces of Ontario and Alberta require prospective franchisees to receive a disclosure document as the first step in the franchise purchase process. However, in all other Provinces, no such documentation is required. In the disclosure document, relevant information regarding the personal and professional backgrounds of all senior members of the management team is provided, as well, various financial and legal information regarding the franchisor. Given that providing this information is not standard procedure in everywhere, it is very important that you be an advocate for yourself and request it. Remember that this management team is the team that will lead your franchise and the system to future growth. Therefore, you want to know about the financial security of the company and its ability to finance future growth, how committed the team is to future growth, and what their development plans and strategies are. One telling question is whether the corporate stores contribute to the royalty and advertising funds. Another important element is whether there are any outstanding actions against the Franchisor by franchisees or suppliers.

One of the biggest indicators of the success of the system is how often units have been re-sold, how many franchisees typically renew or sell their units at the end of the term and how many multi-unit operators there are. This will give you an idea as to whether the present franchisees in the system are committed to growth and whether they foresee a future for the system as a whole. It is important to speak to other franchisees to determine what kind of support they have received. Other franchisees, including those that have left the system are a valuable source of information. The franchisor will furnish you with a list of franchisees to contact. Keep in mind the source of the information though, disgruntled franchisees are not likely to give raving reviews!

Franchisor's, in evaluating prospective franchisees, all look for similar things. Believe it or not, experience in the area of expertise is not high on the list. Good franchisees are "intrapreneurs", they have something of value to add to the system, and will be dedicated to developing their businesses. Their greatest prerequisite skills are in the areas of people and time management.

When deciding what to purchase most people first consider the amount they have to invest. WRONG! You first have to make a quality of life choice. Franchisees have to be totally committed to working their business. If you don't want to be up at 4 am, don't buy a breakfast franchise! Evaluate all of the aspects of the franchise including: hours per week, training and ongoing training, amount of networking required, etc. Most of all, make sure it is a business you will enjoy. You have to get up every morning and go there. Once these factors have been established, review what options are available in your financial range.

To best educate yourself on the franchise industry and your individual choices there are great publications and resources. This Handbook is my go-to-book for any information I need on the Canadian franchise industry. In fact, I give my clients this book or the Canadian Business Franchise Annual Directory as homework and I ask them to narrow down their choices to 5-10 franchises and then we investigate the

“fit” of each opportunity. Canadian Business Franchise Magazine keeps me up to date during the year. The Canadian Franchise Association (www.cfa.ca) website is chock full of information on franchising, and is the voice of franchising in Canada. In Quebec, the Conseil Quebecois de la franchise (www.cqf.ca) keeps tabs on the industry there.

Once you have made some selections, you are now at a critical point in the buying process. This is the point at which emotion comes out of the process entirely. Now you must investigate each opportunity purely on the basis of “dollars and cents”. You are making a large investment and you must continue in this frame of mind “Cousin Henry asked me to invest his money in a business, which one should I buy for him and why?” You may love the franchise but if it doesn’t meet your financial needs then don’t buy it.

I can’t stress enough the importance of doing your homework. Remember consistency and goodwill? Now is the time to investigate the systems on your list? Visit units, be mystery shoppers, speak to franchisees, and meet the management team. Don’t be shy about asking questions. A good franchisor understands the value of finding just the right “fit” between the franchisor and franchisee. Just like people have personalities, so do systems. It’s important for there to be a match. You should be looking for it too. Make sure when you sign that you are taking a level of risk that you are comfortable with and that you understand all your rights and obligations.

The buying process begins with the completion of an Application Form and often, the remittance of a fully-refundable deposit. This deposit shows your good faith that if you are accepted, you will continue with the buying process and ultimately, buy. There is then a personal meeting, and depending on the province, remittance of a Disclosure Document. If a deposit has not been given, it will likely be requested 14 days after delivery of the Disclosure Document. If the parties still like each other, the next step is the signing of the Franchise Agreement and the payment of the balance of the Franchise Fee. If the Application is not accepted and a deposit has been given, it will be refunded immediately. At this point if there is a location to be selected, it will likely be done simultaneously with the negotiation of the franchise agreement. If you are buying a service business, it is not likely that any training will begin until the Franchise Agreement has been executed. In retail, including restaurant, you usually train (at a corporate centre) while your unit is under construction. You then get onsite training from pre-opening until sometime after opening, depending on the system. From then on you are a “franchisee” and will receive all the services and support you contracted for in the Franchise Agreement. Although this is a simplified view of the process, it should follow this general path.

If the process sounds scary, (it’s not really!), there are a bevy of professionals in the franchise industry who are willing to help out. I do recommend that you use “franchise” professionals as franchising is a specialty. An investment in professional legal and financial advice will be the smartest investment you will ever make. It may cost you a couple of thousand dollars but it could save you a couple of *hundreds* of thousands of dollars!

The franchise selection process can be long and is often trial and error. Don’t get discouraged. It can take a while to find the “right” opportunity but you will know it when you find it. It will excite you. Wait for that “right” one and don’t feel obligated to anyone. Remember it’s *your money*, and *you* are in the driver’s seat-no matter what sales pitch you are given. Take your time and finish your homework dear!

Franchising is my favorite business model and I have been working with it for 15 years now. I have seen systems and franchisees come and go. The successful franchisors are those who recognize that to be successful, the franchisees must be successful. They realize that prospects will ask franchisees 2 questions (1) are you making money? and (2) are you getting support? If the answers are yes to both,

then the franchisees become their best salesmen and vehicle for growth. Successful franchisees are committed to following the system and they actively work and promote their business. A solid franchisor has a committed management team and a committed network of franchisees.

Franchising has had a bad rap on occasion, and it is wholly undeserving. In fact, it is a brilliant way to get into business. Industry Canada Statistics show that independent business owners over a 5 yr period go bankrupt at a rate of 85%; however, of those in a franchised business, at a 5 yr. term, over 85% are still in business. The numbers speak for themselves.

I have had the joy of seeing many people flourish in business with this model and to realize dreams beyond their wildest imagination. To each of you I wish the same success.

Sincerely,

Lori Karpman

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