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The following is a contribution to the « Leaders of Kingston » section in the www.randycleary.com website.

Question:

After years of working in business law in Quebec City and Toronto you have moved your practice to Kingston and one of your areas of focus will be helping small business owners. Can you tell me some of the ways you do this, and also discuss the pros and cons of being involved in a franchise vs. staying independent?

Answer:

Randy,

I have practiced law for more than 30 years with a constant focus on serving the needs of businesses. I was a partner in my own firm and for more than 10 years I practiced law in-house with a large multi-national corporation where I was a senior executive. Since opening my own law office in Kingston, I have not only been practicing business law but I have been in the business of practicing law. I am no stranger to the challenges of the business world and am now experiencing first hand the challenges of being a small business owner.

My philosophy is that I am not solely a provider of legal services. I provide to my clients the services of a counsellor in Business Law by offering them strategic advice and solutions that are tailored to their needs while protecting their interests. This can only be achieved by trying to understand the business problems faced by my clients and looking beyond the legal issues for which they seek the services of a lawyer.

The second part of your question goes to the heart of an area of law in which I have practiced extensively during the past 6 years. Over that period of time the law regulating franchises has evolved considerably in Ontario and it can now be said that franchising has become a regulated industry. Lawyers advising clients in that field need to have a greater familiarity with the various aspects of the franchise industry and its regulatory framework.

Clearly, being involved in a franchise is not for everyone. Likewise, the benefits of being involved in a franchise are only as good as the franchise system itself. Before discussing the pros and cons, we need to understand a few basic facts. In many cases, buying a franchise can be more expensive than starting as an independent. The franchisee will generally not have a choice of how small or big the initial investment will be as these issues are determined by the franchisor. Although there is very little scientific data on this issue, it is generally accepted that the success rate for a franchised business is higher than for independent start-ups. This empirical evidence would be supported when a franchisee is investing in a concept that has a proven track record and is doing business with a franchisor that

provides training, marketing support, management and operational support and other services to the franchisee.

Another general concept to keep in mind is that when investing in a franchise, the franchisee is not really buying the business. What the franchisee receives is the right to conduct the business pursuant to a franchise agreement which has a limited time frame, usually 5 to 20 years, including renewal options. There is no guarantee that the franchisee will be able to renew the franchise at the end of the agreement and the renewal terms. This may also have an impact on the franchisee's ability to sell the franchised business.

Establishing a list of pros and cons is tricky since many of the "pros" are not necessarily provided uniformly by all franchisors and their absence may turn into a warning sign that a specific franchise system is not offering value for money. Among the "**pros**" we could list the following elements:

Proven concept: This is the backbone of what the franchise system has to offer. The system should be offering some established goodwill as well as products and methods that have been tested and proven to be successful. Investing in a proven concept can help reduce the business risk.

Training: The franchisor should be offering thorough and complete training on all aspects of the operations of the franchise. Good training should give a potential franchisee a head start in terms of knowledge of the business which otherwise could only be obtained by years of experience in the field.

Supervision and Consulting: A good franchise system should offer ongoing advice in the management of the business, plus ongoing training to help its franchisees improve their skills.

Site Selection: The franchisor should provide assistance in the site selection. In many cases, a franchisor will rent the location and sublet it to the franchisee. This "pro" can rapidly turn into a disadvantage if the franchisor has done a poor job in selecting the site. As the old saying goes, everything is location, location, location. Statistics show that the number one reason for business failure in general (whether the business is franchised or not) is poor location.

Buying Power: A franchisor can in the right circumstances enjoy a significant buying power. In many cases, the economies of scale generated by the franchisor's buying power are not passed directly to the franchisees. In certain cases, however, franchisors will use their buying power to obtain contributions from suppliers that will help fund national and regional advertising campaigns.

Research and Development: No one would expect a business not to improve its products and systems over a long period of time. A franchisee can expect that the franchisor will constantly try to improve the system and that the benefit of those improvements will be passed on to the franchisees.

These "**pros**" will not come without a certain number of negative points which must also be taken into consideration. Among those negatives or "**cons**", we can note the following:

Fees: These can be substantial. In addition to the initial franchise fee, there will generally be a royalty payable on a weekly or monthly basis, a contribution to the advertising fund, and other fees that may be charged to the franchisees for various services. In other words the “pros” come with a price tag and the franchisee must be certain that value for money will be received. A good franchise system will allow its franchisees to make a reasonable profit and reward the management and business skills of the franchisees. If these factors are not present, the loss of independence (discussed below) will become a greater negative.

Loss of independence: This is, by far, one of the greatest negatives. The franchisee must be prepared to work within a system. The franchisee may have made a sizable investment but still does not hold all the rights to the business. As mentioned in the discussion on the fees, this loss of independence can become a serious point of contention if the franchisee merely becomes a glorified store manager who is not given the opportunity to make a reasonable profit or the possibility to enjoy the independence that generally comes with being in business for oneself.

The franchisor may not enforce the standards uniformly across the system: A franchisee can be seriously hurt if its efforts are negated by a perception in the marketplace that the quality of products or services is not uniform across the system. This will be particularly true in industries that cater to a transient clientele, such as the tourism and hospitality sector. People may stay away from an otherwise well run franchised business because of a bad experience in another location of the same system.

The franchisee will suffer from the image problems of the system: In this age of communications, a negative development in one part of the system will have an impact on all other members of the system. While the franchisee will benefit from the franchisor’s goodwill, it will also suffer if for whatever reason the franchisor’s goodwill is impaired during the term of the franchise.

There is a lot more that can be said about the franchise relationship. This is how some authors wrote books on the topic. We will certainly come back to some of those points in the future as we continue our dialogue. In closing, I would like to leave one final thought: The first question to ask when considering a franchise opportunity is: Is this a business where I would want to be if I was going as an independent? The investment will be the same if not more and the hours will certainly be no less. Secondly, a prospective franchisee should make sure that the pros discussed in my answer to your question are there when they consider a franchise opportunity. The best advice that I could give to anyone contemplating the purchase of a franchise is: Do your homework, do your homework, and do your homework.

A Word of Caution

This document is intended to provide general information and should not be relied upon as legal advice. If you require legal advice we would be pleased to assist you.
