

# A Franchising Checklist

*Expert knowledge means success*

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Note: This publication has not been updated since it was last published. Some of the hyperlinks may have changed and may need updating. In addition, some of the information in this publication may be out of date.

## Introduction

With Business Format Franchising (generally simply called "Franchising"), the franchisor company grants you, the franchisee, a licence to operate your business using their name, products and services for a specific period of time.

Franchise agreements vary from franchise to franchise. It would be impossible to identify every term and issue that should be considered in every situation. However, this checklist should be a valuable tool if you're interested in buying a franchise.

The checklist in this publication shouldn't be used in isolation. Instead, read through it in conjunction with the franchise agreement and the franchise operations manual. These are the documents that are issued by the franchisor and they will set out all the terms and conditions that will govern your ownership of the franchise. Although you can use the checklist to understand and review a franchise agreement and manual, you definitely shouldn't sign the agreement until you've discussed your options with an accountant or lawyer with experience in this field.

Don't forget that the checklist in this publication is not exhaustive and should be related to your specific business circumstances.

If you wish, you can obtain further information from:

The British Franchise Association  
85f Milton Park, Abingdon, OX14 4RY, UK  
Tel: +44 (0) 1235 820 470  
Web: <http://www.thebfa.org/>

## What is Franchising?

Let's start with defining what a franchise is - Franchising is an arrangement whereby an existing business agrees to allow another to sell its goods or services or use its name within a specific area.

Put simply, an existing business (the

franchisor) will grant a 'franchisee', or the third party retailer, the right to operate under the franchisor's trade name and use its proven method of doing business. In return, the franchisor will usually receive a fee from the franchisee, as well as a continuing income from it based on the fledgling business' turnover, the materials and services supplied to it by the franchisor, or some other method related to the size of the franchisee's business.

One of the first real franchising operations was that of Macdonald's - Ray Kroc, who bought the business from the Macdonald brothers in the 1950s, identified the advantages of a business that could be replicated a hundred, a thousand and even ten thousand times. And we all know how many hamburgers have been sold since then - so the idea clearly worked!

Not surprisingly, this 'business concept' form of franchise has proved immensely popular, since not only does it provide an opportunity for others to take an existing business idea and run it along proven, successful lines, but also enables the owners of the original business concept to increase their income considerably, with very little risk.

Almost any business can be franchised. But with each, care must be taken to provide the franchise with every opportunity to succeed, and that means careful planning.

From the franchisor's point of view, having the right franchisees for his business are a key factor, as are how the relationships between the two are handled.

Good communications are essential to ensure the relationship is a happy one, while there is no better advertisement for prospective franchisees than a number of well-established existing sites already operating successfully.

## Important questions

Anyone thinking of establishing a franchise should ask themselves several important questions first:

- Is there sufficient wide-scale market demand?
- Is the product or service competitive and able to be duplicated by others in a number of different locations?



- Does it have staying power, or is it just a passing fad?
- Can a distinctive image be created to attract customers (perhaps a simple and memorable name)?
- Can a simple manageable framework be established?
- Can effective controls be established?
- Is there sufficient depth of management in the business to recruit franchisees and lead and develop the franchise network?

**When you take on a franchise, you own and operate your outlet yourself, but the franchisor retains control over the way in which their products and services are produced and marketed.**

**Franchising reduces the risks of self-employment. You benefit from a recognised brand name and proven goods and services. You also receive training, help and support from the franchisor company.**

**You will have to pay a fee to the franchisor company, in addition to running your business in strict compliance with the terms laid down by the franchise contract.**

## Choosing the right franchise - A Checklist for Success

**Choosing the right franchise is key to your success. Here are the main things to consider:**

### Assessing your own capabilities

- Do you have the necessary personal commitment?
- Do you have the support of your family?
- Are you fit and healthy?
- Do you have the required skills and experience?
- Do you know what it takes to run your own business?
- Are you naturally a team player?
- Will you be prepared to comply with the franchisor's system and rules?

### The Franchise Cost

- What does the initial franchise fee cover?
- Does it include an "opening" stock of

products and supplies?

- How much of the initial cost can be met from your own resources? How much will you need to borrow to cover start-up and working capital costs? Do you own anything that could be offered to the Bank as security? For example, your property, Life Policy, Guarantees etc.;
- What are the payment terms to the franchisor - amount, time of payment, lump sum or instalment, financing arrangements, etc.?
- Does the franchisor offer any financing, or offer help in sourcing financing?
- Is there any deferred balance? If so, who finances it and at what rate of interest?
- Is any part of the initial fee refundable?
- Does the contract clearly distinguish between "total cost", "initial fee", "initial cash required", and/or "initial costs" etc.?
- Are there periodic royalties? If so, how much are they and how are they calculated and payable?
- How and when are sales and royalties reported, and how are royalties paid or collected?
- If royalty payments are in whole or part payment for services by the franchisor, what services will be provided?
- Are accounting/bookkeeping services included or available?
- How are advertising and promotion costs shared?
- Are there any other supplies (e.g. stationery, point of sale materials, etc.) that must be purchased from the franchisor?
- Is a specified amount of working capital required of the franchisee to cover operating costs until profits can be made?
- Must premises be purchased or rented, and are there further conditions on either of these (from franchisor, selected site, etc.)?
- How and by whom will the building be financed, if purchased?
- Does the franchisee have to make a down payment for construction and/or equipment?
- Is the cash flow and profit forecast provided by the franchisor feasible - what level of income will be required to support the outlet and repay borrowing?
- Do the franchisor's figures allow for taxation, depreciation etc.?
- Does projected income cover not only commitments but also an acceptable standard of living?



# A Franchising Checklist

- If sales/profit projections are not met, could you borrow more or use your own resources?
- Are goods supplied at cost or at a marked-up price as part of your fees?
- Have you discussed your Business Plan with a franchise specialist accountant?

## The Franchise Contract

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- Obtain a copy of the franchise contract and have it assessed by an accountant experienced in these matters and by a solicitor;
- What is the term of the contract and your right to renew it?
- Is there a renewal charge?
- Does the contract guarantee exclusive territory to each franchisee?
- Does it confirm the franchisor's provision of training and support?
- Does it impose restrictions on things such as equipment and suppliers?
- Does it state whether the business can be sold? Under what terms and conditions can this happen?
- Are minimum performance requirements included and what are the consequences of failure to meet them?
- In what circumstances can the contract be terminated?
- Does the contract state who's responsible for providing advertising and promotional support?
- What would happen in the event of your death?

## The Franchisor Company

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- How stable is the company's record as a franchisor?
- Access the franchisor's financial stability by obtaining a bank reference/audited accounts;
- Is the franchisor a member of the British Franchise Association?
- Does the franchisor help with site location, preparation of Business Plans and market research?
- How many outlets are owned by the franchisor?

## The Franchise Network

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- How many franchisees are there? Obtain a list and contact a selection to secure first-hand information. Try to contact some franchisees in areas similar to your own;
- Have any failed? If so, why?
- Has the company run a successful pilot franchise operation?
- Do any franchisees own more than one outlet?

- Do the franchisees seem happy with their businesses?
- Do the franchisees consider the franchisor provides the goods and services (including support and training) required by the franchise agreement?
- Do the franchisees consider the franchisor's forecasts are usually achieved by new franchisees?
- Are the franchisees satisfied that adequate research and development is carried out by the franchisor? (see the section headed "Support from the Franchisor");
- Are the franchisees happy with the level of communication by the franchisor?

## The Franchise Location

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- Does the franchise apply to a specific defined geographical area? If so, are the boundaries clearly defined? Is the territory an exclusive one, and is it permanent or subject to reduction or modification under certain conditions?
- Who has the right to select the site?
- Will other franchisees be permitted to compete in the same area, now or at some time in the future?
- Does the franchisee have a first refusal option as to any additional franchises in the original territory if it is not exclusive?
- Does the franchisee have a contractual right to the franchisor's latest products or innovations? If so, at what cost?
- Will the franchisee have the right to use his own property and/or buildings? If not, will the franchisor sell or lease his property to the franchisee?

## Operating Practices Terms

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- Must the franchisee personally run the business - or can it be placed under management? If so, to what extent and under what specific conditions?
- What degree of control does the franchisor have over the franchise operations - particularly in maintaining the franchise identity and product quality?
- What continuing management aid, training and assistance will be provided by the franchisor, and are these included in the ongoing franchise costs?
- Will advertising be local or national and what will be the cost-sharing arrangement, if any, in either case?
- If local advertising is left to the franchisee, does the franchisor exercise any control over such campaigns or share any costs?
- Does the franchisor provide various

promotional materials point-of-purchase, mail programs, etc. and at what cost?

- What are bookkeeping, accounting and reporting requirements, and who pays for what?
- Are sales or service quotas established? If so, what are the penalties for not meeting them?
- Are operating hours and days open set out in the franchise contract or operations manual?
- Are there any limits as to what can be sold via the franchise?
- Does the franchisor arrange for mass purchasing and is it mandatory for the franchisee to be a participant buyer?
- Who establishes staff recruitment procedures initially and through the franchise term?

## Buildings, Equipment and Supplies Terms

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- Are plans and specifications of the building, from which the business is to be operated, determined by the franchisor? If so, does this control extend to selection of contractor and supervision of construction?
- Are there any restrictions on re-design or redecorating?
- Must equipment or supplies be purchased from the franchisor or approved supplier, or is the franchisee free to make his own purchases?
- When the franchisee must buy from the franchisor, are sales considered on consignment? Or will they be financed and, if so, under what terms?
- Does the agreement or manual provide for continuing supply and payment of stock (by whom, under what terms, etc.)?
- Does the franchise agreement or manual bind the franchisee to a minimum purchase quota each trading period?
- What controls are imposed relating to the facility appearance, equipment, fixture and furnishings, and their maintenance or replacement? Is there any limitation on the cost involved in any of these items?
- Does the franchisor have a group insurance plan? If not, what coverage will be required, at what limits and costs? Does the franchisor require that it be named as an insured party in the franchisee liability coverage?

## Your Franchise

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- Assess the competition within your potential area in terms of price, quality, delivery and service;
- What is the trading pattern of your potential franchise - is it seasonal, for example?
- Is there a market for the product or service in the proposed area?
- How wide an area will you have exclusive rights over - (see the section headed: "The Franchise Location" on the previous page)?
- Does the franchisor impose a minimum sales level?

## Support from the Franchisor

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- Does the franchisor provide marketing support, accounting facilities, technical advice, research and new product development?
- Is training provided? Is it sufficient?
- Is the franchise package comprehensive? Does it meet your requirements?
- Does the franchisor provide up-to-date product information?
- How are new products developed and introduced to the network?
- Is there a comprehensive operations manual?
- Can you obtain help in an emergency?
- Is the franchisor responsible for national advertising and promotional activities?
- Who is responsible for local advertising and promotional activities?

## Franchise Termination and Renewal Terms

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- Does the franchisor have a right of termination of the franchise agreement if certain conditions have not been met?
- Does the franchisor have the right to purchase the business from the franchisee - if so does the franchise agreement spell out the terms under which the franchisor may repurchase the business?
- Is the franchisor obliged to buy any or all of the franchisee's equipment, furnishings, stock or other assets in the event either party terminates the franchise for good cause?
- Is there provision for independent appraisal? Is any weight given to good will or franchisee equity in the business?

- Under what conditions (illness, etc.) can the franchisee terminate the franchise? In such cases, do termination obligations differ?
- Is the franchisee restricted from engaging in a similar business after termination? If so, for how many years?
- If there is a lease, does it coincide with the franchise term?
- Does the contract provide sufficient time for amortisation of capital payments?

## Other Points to Consider

- Can the franchisee sell the business and assign the franchise agreement to a new buyer?
- Is the franchise assignable or saleable on the franchisee's estate on death or disability?
- Does the lease permit assignment to any permitted assignee of the franchisee?
- Are all trademarks, trade names, or other marks fully identifiable and distinct, and are they clear of any possible interference or cancellation owing to any pending litigation?
- What is the duration of any patent or copyright material to the franchise? If time is limited, does the franchisor intend to renew, and is this covered in the franchise agreement?

## Further Information

This guide is for general interest - it is always essential to take advice on specific issues. We believe that the facts are correct as at the date of publication, but there may be certain errors and omissions for which we cannot be responsible.

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