

An Introduction to Franchising

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History of Franchising in the U.S.

- 1851.
- Turn of 20th century – product franchises.
- Baby boom – business format franchising.
- Interstate highways.
- Regulation, oil embargo.
- Rapid expansion.
- BYOB



Franchise Regulation

- California.
- Federal Trade Commission.
- Little FTCs.
- 17 states.



What Is a Franchise?

- Payment.
- Trademark.
- Assistance or control.
- All or nothing.



Exclusions

- Employer-employee.
- Cooperative associations.
- Single-license relationships.
- Certification programs.



Certification Programs

- Owns registered certification mark.
- Licenses mark exclusively to third parties.
- Does not discriminate between providers.



Inadvertent Franchises

- Fines.
- Rescission and buyback.
- Punitive and treble damages.
- Felony.
- Joint and several liability.



Why Franchise?

- Rapid and inexpensive growth.
- Reduced exposure to liability.
- No dilution of management.



Why Not Franchise?

- Failure to follow rules can lead to FTC and state liability.
- Could lose benefit of trademark exclusivity.
- Damage to brand reputation with failure.
- Distraction to core business.



What Is Regulated?

- No substance.
 - Securities.
- Disclosure.



What Do You Have to Provide?

- Franchise disclosure document (UFOC).
 - Plain English.
 - 14 days prior to execution.
- Franchise agreement.
 - Ancillary documents.
- Operations manual.
- Financial statements.



Franchise Disclosure Document

- Item 1 – Franchisor and Affiliates.
- Item 2 – Business Experience.
- Item 3 – Litigation.
- Item 4 – Bankruptcy.
- Item 5 – Initial Fees.
- Item 6 – Other Fees.

Franchise Disclosure Document

- Item 7 – Estimated Initial Investment.
- Item 8 – Restrictions on Sources of Products and Services.
- Item 9 – Franchisee’s Obligations.
- Item 10 – Financing.
- Item 11 – Franchisor’s Assistance, Advertising, Computer Systems & Training.

Franchise Disclosure Document

- Item 12 – Territory.
- Item 13 – Trademarks.
- Item 14 – Patents & Copyrights.
- Item 15 – Obligation to Participate.
- Item 16 – Restrictions on what the Franchisee May Sell.

Franchise Disclosure Document

- Item 17 – Renewal, Termination, Transfer, and Dispute Resolution.
- Item 18 – Public Figures.
- Item 19 – Financial Performance Representation.
- Item 20 – Outlets and Franchisee Information.

Franchise Disclosure Document

- Item 21 – Financial Statements.
- Item 22 – Contracts.
- Item 23 – Receipt.
- Exhibits – State Administrators and Agents for Service of Process, Operations Manual TOC, Financial Statements, Multi-State Addendum, Franchise Agreement.

Franchise Agreement

- Grant of the license:
 - Trademarks.
 - Geographic scope.
 - Exclusivity.
 - Competition by franchisor.
 - Term.
 - Renewal.

Franchise Agreement

- Franchisee's obligations:
 - Full time and attention vs. absentee ownership.
 - What can you sell? What services can you offer?
 - Advertising rules.
 - Reporting obligations.

Franchise Agreement

- Franchisor's obligations.
 - Site selection.
 - Training.
 - Operational support.



Franchise Agreement

- Fees:
 - Initial franchise fee.
 - Royalties.
 - Marketing fund.
- Transfer and assignability.
- Default and termination.



Other Agreements

- Confidentiality agreement.
- Non-disclosure & non-competition agreement.
- Guaranty & assumption agreement.
- General release.
- Electronic funds transfer agreement.
- Multi-state addendum.

Operations Manual

- Outline.
- The system.
- Incorporated into FA.
- Franchisor updates.
- Trade secrets.



Financial Statements

- Audited financial statements.
- Phase-in period.
- Affiliate company.



Amendments

- Annual.
- Quarterly.
- State requirements.



Questions?

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