

# Franchising

## What do you need to know?





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# 1. The Franchise Journey

Franchising - The Good, the Bad and the Ugly.

As is often said, small business is the backbone of Australia. 96% of all businesses in Australia are small business and there are more than 2.1 million small businesses operating in Australia today. (ABS 2014)

Franchising is part of that number. According to the recently released Franchising Australia 2014 Report\* there are 1160 business format franchise systems operating in Australia with 79,000 units operating business format franchises.

Over time, statistics have shown that franchise businesses have a lesser failure rate than other small businesses where there is not the same support and training available.



Why is that? Some of the reasons are that franchising is regulated by the mandatory Franchising Code of Conduct and this requires franchisors to provide a Disclosure Document to prospective franchisees which gives them a very good start on their due diligence process. It is also that many franchisors require that franchisees obtain independent advice from an accountant and a lawyer and sometimes a business advisor.

Buying a franchise is all about buying a proven concept and that means many others have been there and done that and therefore the business systems that are set up in the franchise should alleviate many of the problems that start-up businesses have. Franchisors also provide initial and ongoing training and provide ongoing support with all aspects of the business.

\*Asia-Pacific Franchising Centre for Excellence.  
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That is not to say that all franchises are good or all franchisors do everything right - and yes there are some horror stories out there about franchising. Franchisors:

- whose concept wasn't proven, let alone going to last;
- whose brand wasn't great in the market place;
- whose business model didn't make sufficient profit for franchisees;
- who failed to provide meaningful support and really offered no value for the royalty paid by franchisees -

BUT with the right business suited to you, thorough due diligence and a good franchisor who provides great systems and support, as a first time business owner - you can be way ahead of the game when buying a franchise, rather than doing it all on your own.





## 2. Buying a Franchise Business that's right for you

You know the old saying “do what you love or are passionate about and you won't have to work a day in your life”. When thinking about buying a franchise business, it pays to keep that saying in mind. Have a think about what you love doing, what your strengths are, where your skills lie and what you can see yourself happily doing for the next 5-7 years.

Do you have an interest in food?

Do you love driving?

Do you love working with people?

Can you handle staff effectively?

Do you have the sales knack?

Sure, if you have the right attitude, things can be taught, but it's so much easier if you play to your strengths. So indulge in a bit of naval gazing and be honest with yourself – get the opinion of your family and friends.

Once you are clear on what sort of business might suit you – then start the search – keep your options wide open and make sure your business brain has as much input as your emotional brain. If it's all about the money and it's purely a business decision, then what franchise you choose is less important. If you want to love what you do, then making the right choice of franchise business is vitally important both for your wellbeing and for financial success.

Remember buying a franchise business means using the business format and system set by the franchisor – if you don't like the idea of following a business format /system and being accountable, then maybe franchising is not for you.



### 3. Franchise Education

It's free and it's worth its weight in gold.

Okay, so you have an idea of what sort of business you think may suit you – now BEFORE you take the next step – do yourself a favour and get up to speed with all the ins and outs of buying a franchise business.



The best thing is that franchise education is free and available online 24/7. You just need to invest the time and effort to upskill. Go to [www.franchise.edu.au](http://www.franchise.edu.au) and see the courses available through Griffiths University.

1. Pre-entry Franchise Education.
  - Covers off on things like:
    - assessing opportunities
    - questions to ask
    - skills you'll need
    - basic understanding of what's involved
2. Franchise Business Management Essentials.
3. Franchise and Small Business Survival e-class.
4. Franchise Forums on Demand.

Making the effort to educate yourself will pay dividends in the future. You will likely be making one of the biggest decisions of your life in dollar terms (after buying a home) so spend a few hours investing in yourself and gathering information and knowledge.

Remember knowledge is power and with the right knowledge your likelihood of making a poor business decision is reduced. There are also many great resources to broaden your franchising knowledge – check out:-

## Links:

1. [www.franchise.org.au](http://www.franchise.org.au) (Franchise Council of Australia)
2. [www.accc.gov.au/business/franchising](http://www.accc.gov.au/business/franchising)
3. [www.ipaustralia.gov.au](http://www.ipaustralia.gov.au) (trade marks)
4. [www.franchisebusiness.com.au](http://www.franchisebusiness.com.au) (franchise opportunities, advice, trends etc.)
5. [www.franchise.edu.au](http://www.franchise.edu.au) (franchise education – Asia Pacific Centre for Franchising Excellence)
6. [www.franchiseadvice.com.au](http://www.franchiseadvice.com.au) (Franchise Advisory Centre)
7. [www.spectrumanalysis.com.au](http://www.spectrumanalysis.com.au) (Spectrum Analysis Australia – site/territory selection decisions, free e-books available)





## 4. Make sure you do your Franchise due diligence

So now your search is over – you have found a franchise business that suits you – what next?

You will likely have received a Disclosure Document from the franchisor and a draft franchise agreement together with a copy of the Franchising Code of Conduct – no doubt it is an impressive stack of paper and yes, sometimes the devil is in the detail – we will cover off on that in Part 5 about “Getting the right advice before you commit”. This is about doing your due diligence on the franchise opportunity that you are considering.



Due diligence really means doing your homework and that includes:

- **reading the paperwork** that has been provided to you first and understanding your rights and obligations;
- **talk to other franchisees in the system** - there will be a list of names and telephone numbers in the Disclosure Document, including those that have recently commenced and also those who have been in the system for some time and some in between. Also included are those who have left the franchise system recently or have not renewed their franchise agreement. Ring them all and ask a lot of questions – are they happy in the business, what is really involved on a day to day basis, what was the initial training like, was it comprehensive enough, what support does the franchisor provide, has the franchise business met their expectations, why did they leave or not renew, how profitable are they and how does that compare to any financial information that the franchisor may have given you? Have there been any disputes with the franchisor and if so how were they resolved? Would you renew your agreement, would you acquire another territory or site etc?

• **undertaking research about the franchise business opportunity and its potential**  
and then undertaking more work as follows:

- Prepare a detailed Business Plan including a cash flow and forecasts - get help from your accountant if need be;
- Do a SWOT analysis to assess the strengths, weaknesses, opportunities and threats relating to the proposed franchise business acquisition that you are considering and then assess the risks involved;
- Get legal advice from a lawyer who specialises in franchising. While a franchise agreement is a contract – it really takes a lawyer with franchise experience and knowledge of the Code to ascertain what is standard in that industry, what is unusual, what is plain wrong and what needs to be clarified and negotiated and what changes can be made in your favour.
- If you are buying an existing franchise business, i.e. one that has already been operated by an existing franchisee, then get your accountant, if they are experienced in small business or franchising, to review the last 3 years' financials and give you their opinion about the business and its viability, profitability, room for improvement etc.
- Look at the demographics of the area and capacity for growth - this can be very important;
- Do your own observations of the business, speak to customers (if possible), assess foot traffic etc.
- Talk to trusted advisors – which may include family and friends;
- If the business is in a retail centre, find out what is planned for the centre e.g. refurbishments or redevelopments – these can have a significant impact;
- Do some research on the franchisor (have no doubt they will be doing their due diligence on you) – Google is a powerful tool to turn up all sorts of things – however beware – not everything you read on the internet is accurate; and
- Do a credit check on the franchisor.

## **The Do's and Don'ts**

Do not fall into the trap of thinking that because the business is a franchise that you can trust the franchisor and the franchise system and that there is no need for thorough due diligence and research.

Do not fall into the trap of not doing due diligence or doing it in a cursory manner.

Do not end up regretting your lack of thorough due diligence.

Do not let your heart rule your head – try and be dispassionate when assessing the opportunity and have your business hat on.

Do yourself a favour and expect to spend some money on your professional advisors – get the right advice before you sign up. As mentioned before, it is better to pay and get the advice and walk away if it does not stack up, rather than proceed and end up with a lemon - that will only cost you more – much more.

## 5. Getting the right advice before you commit

So you have made a start on your due diligence and now is the time to seek some advice.

The Franchising Code encourages franchisees to get advice from an independent legal advisor, business advisor and accountant.

Most commonly prospective franchisees source advice from an accountant and a lawyer.



### Legal Advice

Legal advice can help in ensuring that you understand your rights and obligations that are set out in the franchise agreement.

It is important to have a really good grasp of the fundamentals of your franchise agreement e.g. fees payable, what are the terms relating to renewal, how does advertising and marketing work, what are the terms relating to you on selling the business, terms relating to the supply of products and services etc.

Your lawyer should read all the documentation and preferably sit down face to face and go through it with you in detail - you can ask questions as you go. This meeting is invaluable for teasing out the detail and trying to make sure you have a realistic understanding of what you are getting into in a legal sense.

If there is a related lease or sublease of premises, then you will need your lawyer to advise on those terms as well – both the franchise agreement and the lease agreement need to work together.

If things go well with the franchise business, it is likely that you may not refer to your franchise agreement much at all, but, if things don't go well, then this is one of the first documents that will be dug out of the drawer for review to see what your rights and obligations are and that of the franchisor.

## Accounting Advice

Accounting advice can help you understand the figures of any existing franchise business that you may be purchasing. Your accountant can also help to prepare cash flows and forecasts for the new business – and be realistic about the top line. Generally it is the top line or income/sales etc. where the problems can lie or sometimes, it's in the expenses – when costs blow out for some reason.

Your accountant can also advise on your business structure and options to ensure tax effectiveness. If finance is required, your accountant can also assist with preparation of the necessary paperwork for submission to the bank and also on financing options.

## Business Advice

Business advice can help put all the pieces of the puzzle together and provide a good overview of the existing proposition and how that can be improved.

So – some final advice before making the leap and committing:-

- Make sure you have done all the necessary groundwork to make an informed decision.
- If you buy a new franchise then there is a seven (7) day cooling off period (check the Code for details). If you buy an existing franchise business, there is no cooling off period.
- Don't be pressured into making rushed decisions – make haste – but slowly and be patient. If it is meant to be...
- Keep records of documents provided, emails and all meetings and conversations with the Franchisor before entering into your franchise agreement in case things go wrong.

Make sure as far as you can, that the franchise business proposition meets your expectations in terms of financial performance and lifestyle.





## 6. So now you are a Franchisee

There is a saying in franchising “you are in business for yourself but not by yourself”. You independently own and operate your own business within the franchisor’s framework, but you have the support of a franchisor which should include:

- 1) The benefit of a brand, a reputation and goodwill, which are already established.
- 2) Initial and ongoing support of the franchisor.
- 3) Assistance with finding a suitable site or territory and then shop fits, product mix, equipment etc.
- 4) The benefit of initial and ongoing training for your staff.
- 5) Assistance with setting up your systems and getting ready to start trading.
- 6) The benefit of some form of advertising and marketing which is tried and tested.
- 7) The benefit of the franchisor’s operational/field staff to assist with problems that arise.
- 8) The benefits of developments and improvements in the system (which you can contribute to as well).

On the flip side, as a franchisee:

- 1) You will be subject to operating within the system i.e. using the franchisor’s business format.
- 2) You will be paying ongoing fees to the franchisor for the support and services provided.
- 3) You will need to be doing everything right to have the right to renew the term of your franchise agreement.
- 4) You will need to obtain the franchisor’s consent to a sale of your business and the new incoming franchisee must fit the franchisor’s selection criteria.

So to make the most of acquiring your franchise business you need to focus on the following:

- 1) Accept the disciplines of the franchise system.
- 2) Don’t be complacent even though you are your own boss in your franchise business, there is still risk in the business undertaking – work hard and give it your all.
- 3) Be patient and understand that it takes some time to become established, build your business and make the profits you want. There may be losses for some time – make sure you have enough working capital to get through this period.
- 4) Do not think that you know more than the franchisor or know best and stop following the system.
- 5) Ask for help from the franchisor if you need it - ensure you have the ongoing support of family.
- 6) Be a positive, active franchisee, participate and attend franchise meetings and conferences and have your say.

## 7. Exiting your Franchise

For various reasons you may need to exit your franchise business. These reasons can be many and varied and include:

- ill-health
- separation and divorce
- family reasons
- time to sell and do something different
- disputes with your franchisor
- dissatisfaction with the system, the franchisor, certain aspects of the franchise business and perhaps a combination of some or all of the above.



The main ways of exiting are:

- to sell your franchise business as a going concern;
- negotiating your terms of exit with the franchisor;
- to simply let your franchise agreement expire at the end of the term;
- to agree on a mutual termination of your franchise agreement with the franchisor upon agreed terms.

Remember, when you sign your franchise agreement, you are signing a binding contract for a specified term and you cannot just decide on your own to exit or terminate that contract.

If you intend selling your franchise business, then you will need to carefully check the transfer provisions contained in your franchise agreement and understand your obligations. This will likely include payment of a transfer or assignment fee which will be a set fee or a percentage of your sale price. Note that the franchisor may also have right of first refusal to acquire your business.

The Buyer/prospective new franchisee will also have to be approved by the franchisor – note the franchisor cannot unreasonably withhold its consent.

There will need to be a business sale contract, which will need to be checked by your lawyers to ensure your rights are properly protected.

If you intend exiting before the end of the term of your franchise agreement and are negotiating your terms of the exit with the franchisor, those terms can be many and varied. Note however that the franchisor will likely require that you sign a Deed of Termination/ Surrender which will include details of your obligations post termination and often include an obligation not to compete in a similar business, in a geographic location, for a specified time.

If you let your franchise agreement expire then most franchisors will require an agreement to be signed to document your obligations post expiry, which again will likely include non-competition restraints.

Any agreement to mutually terminate the franchise agreement prior to the end of the term will also likely require the parties to enter into an agreement noting the terms of that mutual termination.

Franchise disputes that cannot otherwise be resolved result in some form of mediation. Often there is an agreed outcome at the mediation which is documented and signed off by the parties and may include the above options.

Part 4 of the Franchising Code of Conduct provides a process for dispute resolution – most well drafted franchise agreements will also have a dispute resolution clause.

Do not be afraid of availing yourself of this process – sometimes the assistance of an independent and knowledgeable mediator can be invaluable to facilitate a resolution.

## Now where to from here?

If you need help with your plans or need to get some clarity on your “next steps”, please contact Christine Matsinger at McColm Matsinger Lawyers for an appointment on (07) 5443 1800 or [info@mmlaw.com.au](mailto:info@mmlaw.com.au)

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