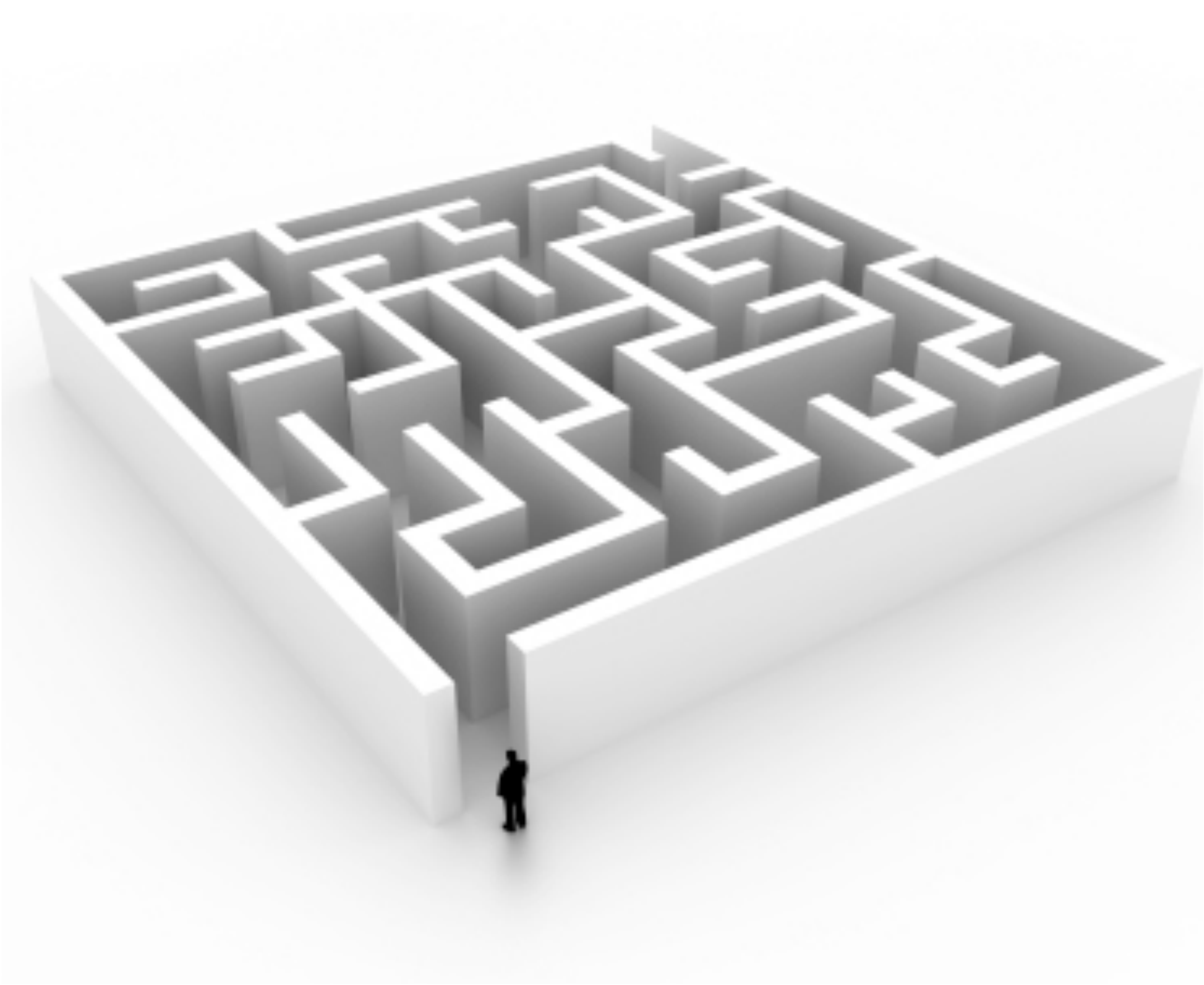
Legacy Franchise Group

How To Buy a Franchise



HOW TO BUY A FRANCHISE

Prepared by the consultants of

LEGACY FRANCHISE GROUP LLC

Scottsdale, Arizona

Foreword

This eBook is intended for prospective franchise buyers, although all of this information is important for existing companies just in the process of considering expanding through franchising. It will give most readers an adequate understanding to begin their search for a franchise opportunity appropriate for them. Most of the terms used in the franchise industry are defined in the glossary at the end.

Legacy Franchise Group prepared this eBook to help you understand some of the fundamentals of franchising. We can help you in your process and we have a unique service to help prepare you to navigate the franchise maze before you invest in a franchise. If you're ready we can start with a profile assessment that will help you decide if franchising is right for you and if you're right for franchising. Contact us today to take this free assessment, valued at $200.

Are you ready for business ownership?

Start at the beginning. Ask yourself: Why franchise? The very idea of going into business for yourself is at the same time exciting, maybe even thrilling….yet scary. For someone just getting started in serious self-employment, owning a franchise has proven to be one of the least risky approaches to starting a business. But even experienced business owners are attracted to the franchise model because it affords them an easy way to expand rapidly into diverse kinds of business operations without having to invest years in learning a particular business. If you're teachable, coachable, and hard-working, you can succeed in franchising.

Franchising isn't the only route to small business ownership. Although with a good franchise (there are bad ones!) many of the risks and uncertainties of a raw startup or of acquiring an existing non-franchised business are reduced. Good franchises are the proven "most likely to succeed" small business operations. But there are other options. For example, you could:

- **Start your own business concept from scratch**. You will be the leader, but you'll have to bear the cost of mistakes made while you learn. SBA statistics over decades of data collection show that the failure rate of start-ups is huge.

- **Become a distributor**. MLM or other independent sales arrangements fall under this business model. These are often home-based businesses or add-ons to other business operations. This can have a low cost to enter, but distributorships rarely can be sold later at high multiple of earnings.

- **Buy an existing non-franchise business**. An existing business can be dangerous and will typically have some amount of "blue sky" (inestimable value) in the price. You have little regulatory protection from misrepresentation of the seller.

Why franchise?

There are so many good reasons to buy a franchise. Here are a few:

- You can be in business for yourself but not by yourself, with the support of the franchisor and fellow franchisees.
- You will enjoy a level of independence with established guidelines and boundaries.
- You will offer established products and/or services already recognized by many consumers.
- You can ride on the success of a recognized brand. You won't have to build a brand/or market that brand alone.
- You will benefit from the knowledge learned from the mistakes of those who went before you. The operations are easy to duplicate, and systems easy to train.
- You have the comfort of some regulatory protection since franchisors must comply with federal and state reporting requirements.

What are the disadvantages of franchising?

You're boss of your franchise, but only up to a point. You're not completely independent or free to decide what products or services you offer, or even what prices to charge. Your territory is pre-determined and contractually outlined. You are not free to alter the business model to suit your personality. You sign a contract to operate according the franchisor's model.

Royalty fees are ongoing. Some people may not like the ongoing training and brand promotion that this fee supports. The franchisor sets rules that protect the brand and all of the franchisees as a group, but they may not suit you as an individual.

There is some systemic risk. A bad franchisee unrelated to you can affect your business with mismanagement. Customers who have a bad experience with another franchisee might think badly of all franchises in the network. If the franchisor makes a bad strategic decision, you can be impacted by it.

What do you need to consider when buying a franchise?

Cost. Can you afford to start? Do you have enough cash and/or credit? The franchise fee and royalty are only a few items to consider. These fees cover licensing the trademark, products, or services as well as ongoing training and support. Cost considerations should also include the build-out expenses, and the amount of money you will need to maintain operations before becoming profitable. It takes time to build customers and become a profitable business in each location.

Your abilities and work preferences. Are you able to follow directions and guidance? Are you able to be a good manager or want to buy a job? Are you an effective trainer of employees? Do you intend to work at the franchise yourself, or merely to be an absentee owner? A good profiling service can help by administering a personality profile that can reveal aspects of you that might affect your ability to be successful as a franchisee, and what type of franchisor would best fit your work style and preferences. This can help you evaluate choices and decide what kind of business would be right for you. Legacy Franchise Group can help you find out your strongest traits that will help you decide if franchising is for you, what capacity of investment (single unit, multiple units, or master territory/regional developer) and what franchise industry would best suit you.

Your interests and passions. What are your hobbies and personal interests? If you like food then running a restaurant or catering business might fit you well. If you have been in the healthcare industry you might like senior care franchises. If you like to work with your hands there are many service industries like automotive and home repair. Here is an opportunity to work in something that you naturally enjoy. Some franchises can satisfy highly sophisticated specialists, while others appeal to the general public. Others cater to specific groups, like hobbyists, or young women, or homeowners for instance.

Demand/or competition. You want to be in tune with evolving consumer taste trends. Consider what and who your competition might be. Is the franchise you're considering catering to a diminishing group or a growing one? Are substitute products or services that could threaten or disrupt your franchise concept on the rise? How crowded is the franchise sector you're considering in your area? In some cases it can be a good thing to be a newcomer in a crowded market. It's not unusual to see a McDonalds next to a Burger King. Studies show that both do better when they are closer, just like most car dealerships are clustered in the same area. Other times competition can be a challenge. Coffee franchises have experienced challenges in finding a location near a Starbucks because the first one to arrive often has negotiated exclusivity provisions in the real-estate agreements that allow no competition nearby.

Training and support. Training is vital. You need to be able to be trainable and open to learning new ways. Even if you have already been in the industry, the franchisor will be expecting franchisees to conform to their proven practices and procedures. If you catch yourself saying "I know how to do this," or "I don't need to know that," or "I can do it better," then you might not be a good fit for franchising. The franchisor should have a complete training system to help people who have never been in that industry to become proficient operators and managers to represent the brand well, and make a lot of money.

The franchisor's experience or rating. How long has the franchisor been in business? How many franchises have been awarded? What are the expansion plans? Does the company have the management depth and capital to make it happen? Are you able to be protected in your area? How many units have they opened that are profitable? What do the current franchisees say about owning a franchise? (You will have the opportunity to talk to some of them during "validation" stage of the franchise buying process.) These are questions that a good sales advisor can help you navigate.

What are the top 10 franchise industries?

It's hard to find a consumer or business-to-business industry that has not been franchised. There are those industries that are on the rise and some that are consistently stable, and unfortunately some that are declining. You need to be aware of the trends, and to consider an industry that has staying power. If it is recession-proof too, that's even better.

According to *Entrepreneur* magazine (June 2013) the most popular types of businesses that were invested in 2013 were:

1) Children's Enrichment
2) Children's Entertainment
3) Fitness
4) Frozen Yogurt
5) Hamburgers
6) Health Services
7) Retail Stores
8) Restoration Services
9) Senior Care
10) Spa Services

Do you (really) understand financial statements?

You're going to need to do your homework. Selecting a franchise is kind of like entering a marriage. It's a long-term contract with a partner, so you need to fully understand the arrangement and its pros and cons. You have to size up the potential franchise partner's culture, personality, finances, and the financial deal being offered. This means you must know how to read and analyze a balance sheet and income statement, as well as how to find and read the news about your prospective franchisor in the financial and trade press. (Start with Google.)

It's okay to be financially illiterate, and you don't need to become an accountant to be successful with a franchise. But you have to be honest with yourself. If you can't make heads or tails out of a financial report, get some professional help. It's well worth the expense. If you do your homework before you invest time visiting franchisors you'll make better use of your time when you're there. Most people will spend more time reading up on the next car or refrigerator they're about to buy than they do on the business they're considering. But you won't be like most. You'll know how to do your homework first, and you will actually do it.

What should you ask the franchisor?

- What are the likely upfront costs for the specific location you are buying?
- What are the projected ongoing expenses?
- Who are the primary competitors?
- From whom do I get my inventory and supplies?
- What marketing support to you offer, exactly?
- What advertising will I have to budget for on my own?
- What is the training like and who (specifically) will train me?
- Who who will support me once I've opened?
- What does that support look like, exactly?
- Who are your most successful franchisees? Why?
- Who are your least successful franchisees? Why?

What should you ask other franchisees?

Part of the process is called "validation," which in this context means interviewing other franchisees. You need to be clear on what you intend to discover as you "validate" the program. Here are good questions:

- How satisfied are you with your franchise? Why?
- Are you making as much profit as you expected?
- How much do you pay yourself in salary, apart from profits you take?
- Is the franchisor fair?
- Is the franchisor supportive? How?
- How effective and thorough was the training?
- Do you and the other franchisees support each other with ideas for best practices?
- How hard is it to find and train good employees?
- What is the employee turnover rate?
- How much do you spend on advertising?
- What is the best part of this business?
- What is the worst part of this business?
- What was your worst mistake when you learned how to operate this franchise?
- Would you want to own more franchise locations with this company?
- Would you recommend this franchise opportunity to a friend?
- Can you offer me any advice?

What questions should you ask yourself?

Quality franchise companies don't want franchisees that are not suited for success in their line of business. Past success in other endeavors does not necessarily mean you can succeed in this particular business, and a quality franchisor wants to award precious territories only to those who they feel have the personality and resources to make it work. So before you waste your time and theirs, you need to ask yourself some serious questions first, like:

- Am I ready to be in business for myself?
- Would my spouse support me in a franchise business?
- Do I have the patience to do the homework before I start?
- What kinds of work do I enjoy? What hobbies or passions?
- Do I know if I have the personality to be a boss?
- Do I know if I have the personality to be a successful franchisee *in this particular franchise*?
- Can I happily follow other people's rules and direction?'
- Am I teachable (to learn systems and info)?
- Am I coachable (to take advice and direction)?
- Can I set aside old habits to work with the franchisor's system, *his* way?
- Do I have enough capital and/or credit to afford the start-up?
- How long to I intend to be in a franchise business before I exit? Is this a practical plan? Will it work with this particular franchise?

What are the six steps to evaluate and win a franchise?

You're considering embarking on a major career move that will impact your life and your family's well-being for years to come. So isn't it worth doing these steps carefully and deliberately? If you haven't already taken a personality assessment, it's wise to do so before you start talking to franchisors. This simple advance step is inexpensive and it can save you a lot of work and time evaluating franchises that will prove to be inappropriate for you. Franchisors will respect you more for having done this.

Step 1: Pre-qualification call. This initial meeting is between the franchisor (or the franchisor sales advisor) and the franchisee candidate to get to know each other. It can be by phone or in person.

- Ask initial questions of each other
- Review key points of the franchise
- Discuss an overview of how the franchise license process works (Legacy six step process)
- Understand the industry
- Review rules in the qualification and award process
- Set the tone for a working relationship

***Step 1 homework for franchise candidate**:*

- *Complete the RFC (Request For Consideration) and return to sales advisor*
- *Formulate questions to ask franchisor*

Step 2: Program Review. The franchisor sales advisor reviews RFC application and introduces the Federal Disclosure Document (FDD) to the candidate.

- Review RFC questionnaire
- Explain what the FDD is
- Ask and answer more questions
- Sales advisor sends FDD, franchise agreement and candidate evaluation to candidate
- Discuss financing options

Step 2 homework for franchise candidate:

- *Return the receipt page from FDD*
- *Review FDD, Agreement and other materials alone or with spouse, and then with professional advisors (franchise attorney)*
- *Formulate more questions*

Step 3: Disclosure Review. The franchisor sales advisor reviews the FDD in detail with the franchisee candidate.

- Review key points of the Franchise Disclosure Document
- Answer questions about license agreement of the FDD
- Review candidate's application and point out strengths and weaknesses
- Evaluate the candidate

Step 3 homework for franchise candidate:

- *Formulate more questions*
- *Do validation calls with 3-10 franchisees. For a small fee this can be done with help of an interview expert.*

Step 4: System Verification. The franchisor sales advisor reviews and confirms understanding of the franchise system and agreement.

- Review validations
- Review additional questions
- Introduce support team and/or the franchisor (generally by conference call)
- Set time and date for discovery day

Step 4 homework for franchise candidate*:*
- *Formulate additional questions*
- *Complete short business plan*
- *Review documents with professional advisors (If necessary)*
- *Schedule location visits and attendance at a formal discovery day*

Step 5: Verification of Support/Discovery Day. The franchisee candidate goes to meet the franchisor (in most cases) and see the training facility or the operations of a franchise location to get an understanding of the franchise support system.
- Visit stores and/or office
- Meet approval committee
- Visit with support team
- Review terms of agreement

Step 5 homework for franchise candidate:
- *Formulate additional questions*
- *Schedule location visits and attendance at a formal discovery day*
- *Discuss potential start dates, training and opening schedules*
- *Final review documents with professional advisors (If necessary)*

Step 6: Contract Signing/Awarding the Franchise. This is the final step in becoming a franchisee.
- Review any outstanding questions
- Franchise is awarded by franchisor's franchise committee
- Sign franchisee disclosure questionnaire with sales advisor
- Upon approval of all parties, execute license agreement with payment of franchise fee

Step 6 homework for franchise candidate:
- *Begin working with market/location planner*
- *Work through financing arrangements*
- *Set date for training*

How to Read a Franchise Disclosure Document

The Franchise Disclosure Document (FDD) exists to provide prospective franchisees like you the information you will need to make informed decisions. It includes details about the franchisor, the franchise program, and the franchise contracts you will have to sign. The FDD has to meet federal regulatory reporting standards in order to protect you from fraud. Misrepresenting material information in the FDD is a crime, so franchisors are very careful to be complete and truthful. If you miss the opportunity to benefit from this in your evaluation, you would be making a big mistake.

This eBook chapter will help you identify some *red flags* in the FDD - warning signs that you should investigate further. Red flags don't necessarily mean that a program is bad, but only that there are some variances from what might be expected in good franchise opportunities. There are three reasons why you need to read the FDD before purchasing a particular franchise:

1. To know exactly what you are buying.
2. To help you determine if the franchise is stable or headed for trouble.
3. To help you estimate the financial possibilities for yourself in owning the franchise.

Fortunately FDDs are uniformly organized to be the same in every state for every franchise opportunity. This next section on how to read an FDD is outlined in the same order as an actual FDD to easily refer back to each section.

FDD – THE SUMMARY PAGE

This page tells you how much your total investment in the franchise should be and the services or products the franchise offers. A typical franchise fee for a unit franchise is between $35,000 and $50,000, but could be much more for some high-value franchises or for some prime territories. The summary also includes and estimated range for start-up fees, which might include build-out and operating capital needed to start the operation.

Some franchisors will indicate a large range to avoid possible liability for understating. Or they may not know the actual range*. But they should.* If the estimated expense range for the franchise you are investigating is wide, ask the franchisor why. There may be logical reasons for the wide range in start-up costs. For example, the franchisor may offer two different types of stores, one that is a central service or supply plant and another that is a satellite location, or they may have different format styles of restaurants under the same brand.

> *Red Flag: Look at the range of the estimated start-up expenses. If the range from lowest to highest estimated start-up costs is more than $100,000 this is a red flag, which might indicate that the franchisor does not know enough about the start-up costs or that they are excessively high and they do not want to reveal that.*

Item 1 – THE FRANCHISOR AND ANY PARENTS, PREDECESSORS, AND AFFILIATES

This section of the FDD should tell you if the franchisor owners or executives are qualified by personal experience to teach, train and advise you on the business. Do the executives of the company actually operate the same kind of business or location they are franchising? Do any of them own franchised locations in the same company? Or is the franchise a new concept with short track record? Look to understand who the franchisor operators really are, as individuals. You also want to know specifically what key individuals would be responsible and available to help you if something goes wrong.

Look to see if there has there been a recent reorganization, merger, or takeover of this franchisor. If so, what is the reason? Has the company had financial problems? Has there been a major management change? With the Internet, you can do quick background checks on the company *and the key managers* too. Do your homework.

Some franchisor companies are subsidiaries or affiliates of other companies, which should be disclosed in the FDD. Look to see how many different programs the parent affiliate is selling. Some multi-concept parent companies may have more concepts than they can handle successfully while still retaining the quality in each of them. Be sure to check them out. Do an Internet search that includes the affiliates' names. This will give you an idea if there are a large number of complaints against the entire group of companies or against other companies in the same group.

Look for industry-specific regulations. Make sure the laws of your state allow the franchisee to conduct the business activities the franchise offers. This is especially important for medical and healthcare franchises, or franchises involving sale of alcoholic beverages. Most states have official websites that explain licensing rules and license costs for every line of business.

Red Flag: Sometimes franchisors are undercapitalized. If in the future you have a dispute with an undercapitalized franchisor, you could be going up against a shell company with little or no ability to indemnify you for losses. Even if your franchisor goes bankrupt you could still end being liable for ongoing royalties and fees to a receiver or bank with no experience supporting your kind of business.

Item 2 – BUSINESS EXPERIENCE

This section will also tell you if the franchisor owners have an active location to test products, services and developments. It's also an indicator of the commitment level those individuals, because if they own their own stores they probably believe strongly in value of the investment. How long have the executives been with the franchise? Are there corporate stores, or do the president and key members own stores as separate franchises? That could be a good sign.

Red Flag: Evaluate what franchises or businesses that the key executives have lead in the past to see if they have been successful. Having an unsuccessful business or franchise may be a red flag. Also, determine whether the franchisor has experienced franchise professionals on staff, as this could lead to a higher probability of success.

Item 3 - LITIGATION

This section is an indicator of how the franchisor might handle conflicts. How many lawsuits, if any, have they had? They should not have had many. Is there a pattern to the types of lawsuits? Are there any open lawsuits? If so, this section can give you some idea of future financial pressure on the franchisor if they lose the litigation. Also look for any cases of fraud or felonies. You may want to conduct Internet research on the franchisor as well as key principals to determine if there any legal issues that might interfere with your potential for success.

Red Flag: A pattern of litigation may indicate that the franchisor is not willing to work out disputes with franchisees.

Item 4 - BANKRUPTCY

A bankruptcy in the distant past is not necessarily a drawback if the company ended up coming out of it stronger with provisions for curing what caused the bankruptcy in the first place. If there was a bankruptcy in the past has the company reorganized and revitalized since? Has ownership and management changed since the bankruptcy? The financial reports will tell you the story.

Red Flag: Any past bankruptcies of the franchise or key executives could be an indication of financial mismanagement. It is up to you to determine if there is a possibility of future financial issues.

Item 5 – INITIAL FEES

The franchise fee is supposed to cover the cost to get a franchisee signed and then trained. Often times, the franchise fee is split with a franchise sales person who has helped to find you and work through the sales process for the franchisor so that the franchisor can stay focused on running the franchise. The part that is retained by the franchisor is used to help cover training, legal fees, and other costs to adding a franchisee. If the fee is too low it could be a sign that the franchisor is struggling to find qualified franchisees, or isn't getting enough cash from new franchisees to cover the actual cost of effective training and support. Very low franchise fees should make you suspicious.

When reading the initial fees section you should decide if the fees are reasonable *compared to similar franchises*. Your sales advisor can help you with this information. In the situation of an Area Development franchise, where you buy the rights to an entire region, does the franchisor require all of the money up front before a unit site is opened, or does it allow each unit fee to be paid at the time of the territory or store opening?

> *Red Flag: If the franchise fee is too low, it could be a sign of financial distress, or that the franchisor might not provide adequate training.*

Item 6 – OTHER FEES

The other fees section outlines any other franchise fees. You need to check if these other fees are reasonable compared to similar franchises. Do the fees make economic sense *for you*? Are they so high that it would make it difficult for you to make a profit? You need to consider these as you prepare your own business plan.

Look for unusual fees like liquidation damages for early termination. Better franchisors want happy, profitable franchisees that are in it for the long term.

> *Red Flag: Fees in this section should be minimal. An advertising fee is common; however, if the franchise group is still small, make sure that there is an active program to support your business. Some franchisors collect fees and wait until they are big enough to do national advertising, so make sure you have support in your market.*

Item 7 – YOUR ESTIMATED INITIAL INVESTMENT

This section should include three months of estimated operating expenses as it often takes this long to start building your business and start making enough revenue to cover monthly overhead. Look at this chart carefully. Do the numbers make sense? We advise that in your own business planning you should estimate for the entire first year. Later, when you're actually in operation, you can use your business plan projections as a budgeting tool.

Read the notes carefully. Look to see exactly what all of the fees cover, and determine whether you think anything is missing. Do the fees make sense and seem reasonable? Some franchisors' numbers do not include real estate, which can be a large portion of your expenses. You will need to check out real estate rents in your area, and landlord allowances for leased space improvements in your evaluation.

> *Red Flag: Create your own financial projections to make sure that you are considering all costs to run the business and the specific real estate costs for your area. It might benefit you to hire a professional to help you with this so that you are not overlooking anything, especially if you think you might not know what questions you should be asking.*

Item 8 – RESTRICTIONS ON SOURCES OF PRODUCTS AND SERVICES

Check to see if there are restrictions on sourcing. There may be a good reason for this if the franchisor has a proprietary formula or recipe, or special quality requirements, or if the franchisor has negotiated volume discounts that they pass on to the franchisees. Determine if what you must pay the franchisor for supplies or inventory is high for identical items you could buy for less somewhere else. Does the franchisor overcharge you for products you are required to purchase through them or their designated vendors? Are you allowed to purchase from outside vendors? You should consider if the franchisor getting rebates for making you use certain vendors. If so, are volume purchase savings being shared with franchisees?

> *Red Flag: If the franchisor is requiring you to purchase through certain sources and the costs are compared to buying the same items on the open market, this may be an issue for you. Also, verify that these suppliers are able to support your market area.*

Item 9 – FRANCHISEE'S OBLIGATIONS

This is a directory of where to find your various obligations throughout the FDD. You need to know these clearly before you accept a franchise award.

> *Red Flag: Make sure you are willing to meet all the obligations. Circumventing any of these can lead to termination.*

Item 10 - FINANCING

This section describes whether the franchisor offers financing and what kind. If you need financing you should take time to be sure you can qualify before you invest too much time.

> *Red Flag: Make sure you look at the cost of financing through the franchisor versus other financing options. Interest rates and fees may be more costly through the franchisor, and terms may vary greatly.*

Item 11 – FRANCHISOR'S ASSISTANCE, ADVERTISING, COMPUTER SYSTEMS, AND TRAINING

This is a very important part of the disclosure. These are the obligations the franchisor agrees to prior to your location opening. Look for a well-developed training program. There is a training chart that shows the training program and type of training you will receive. More support is always better.

Are the items listed generic, or specially developed for this franchise program? Are they given at your franchise site or somewhere else? When your location opens having on-site support may be very helpful for you, especially if you are new to the industry.

Next look at the franchisor's obligations to you after you are open. Can you expect much ongoing support? Are there online manuals and online training to train past the initial opening? Look to see what individuals will present and manage the training.

> *Red Flag: If you do not see a clear and detailed summary of the support and training in this section, it may not be available or may not be thorough enough to be successful. Consider this carefully against your own experience.*

Item 12 - TERRITORY

What is the protection for the territory you are buying? The territory should be clearly mapped, defined and agreed upon *before* you sign the franchise agreement. You want a protected territory for most retail and service franchises because it is common that as the brand gets larger, a franchisor may allow for more units in each territory. You want to make sure the territory is not over-saturated.

Check to see if the franchisor is using alternative channels to sell its products or services, or if it sells products under a different label. See if they can sell the same product you sell for a lower price in a grocery store, catalog, big box store, or on the Internet. It can negatively affect you if you end up competing with different labels from your own company offering the same products for less to your customers through different channels. On the other hand, with some programs it could help support your business if done well. Make sure you are protected here.

Red Flag: Make sure you are comfortable with the protections afforded to you for your territory, both in terms of franchise unit saturation and potential competitive products offered by the franchisor through different channels.

Item 13 - TRADEMARKS

Check to see if the company has any registered trademarks. A good resource for information and checking the trademark is www.uspto.gov. Who actually owns the trademark? If the franchisor has a license for the trademark owned by someone else, will you be able to use it if the franchisor's license is terminated? Look at this carefully. You must have federal protections of the trademark to ensure brand value.

Red Flag: If the franchisor does not own its trademarks, there is a potential of loss of use if licensed. Also, if the trade names are not protected at all, competitors may use similar names or logos to knock off the brand.

Item 14 – PATENTS, COPYRIGHTS, AND PROPRIETARY INFORMATION

Are there patents? If so, how important are they for the success of the franchise? Are they critical? A patent only lasts for 17 years. Check to see how many years are left on the important patents. Consider the impact to your franchise when the patent expires.

Red Flag: Having patents does not necessarily guarantee protection in the market. Small adjustments in design or formula can be made to circumvent the patent if not correctly worded by a patent attorney. Make sure the product or service is viable with or without a patent.

Item 15 – OBLIGATION TO PARTICIPATE IN THE ACTUAL OPERATION OF THE FRANCHISE BUSINESS

This section is important if you would like to run your franchise as an absentee owner using hired management. The obligations about your degree of involvement in the day-to-day activities should be listed in this section.

Red Flag: Some franchisors require that the franchisee be an active participant in the franchise, actually working at the operation. If you want to be an absentee owner, make sure that this is allowed by the franchisor.

Item 16 – RESTRICTIONS ON WHAT THE FRANCHISEE MAY SELL

Are there any restrictions on what you can sell at your franchise location? What restrictions will you have on advertising, soliciting and selling? Can you add products for retail sale or is it restricted to only what is offered by the franchisor? This is an important consideration which could impact your financial projections.

Red Flag: Make sure you understand and follow any restrictions. Violations may lead to penalties or termination.

Item 17 – RENEWAL, TERMINATION, TRANSFER AND DISPUTE RESOLUTION

Renewals should be available so the franchise can operate for 20 years or more. Renewals in perpetuity are ideal. Check for renewal fees. Are they predictable and reasonable? The franchisor does not incur much expense when you renew, so the fees should be minimal.

Check for low transfer fees. If a new operator takes over your franchise he will be paying a whole new set of fees so the transfer fee portion should also be minimal.

What franchise termination provisions are described in the FDD? It's not uncommon to make unintended violations when you are new. You should have a reasonable time to cure any minor violation of the agreement.

Red Flag: Make sure that your rights as a franchisee are protected as well as the rights of the franchisor. Make sure that there is adequate time allowed to repair any issues with the franchisor, and that the process and guidelines are clearly defined.

Item 18 – PUBLIC FIGURES

This section lists any public figures involved in the promotion of the franchise. Are they owners, spokesmen, or actual franchisees? You will want to consider the length of contract and whether they are critical in having a successful business. What will be the impact if they stop promoting the franchise? What happens if this high-profile person is involved in a scandal or lawsuit? What if their political or religious views are controversial? Make sure you consider the ramifications of this agreement.

Red Flag: If the public figure is controversial, it may affect your business potential.

Item 19 – FINANCIAL PERFORMANCE REPRESENTATIONS

This section contains the past earnings of individual franchise locations. You and your accountant should study these carefully so you can judge:

1) What can you reasonably expect to earn from operating the franchise, both in salary and in profit?
2) Is it in line with your goals?
3) Is it worth the investment?

Be sure to look at the footnotes. Some of the most enlightening information is there. Also look at the individual location information to see if any of the units are struggling or showing losses. A failing franchise location might be the caused by the franchisee, the franchisor, by some extraneous factor that has nothing to do with the actual business, or a combination of things. It's not always easy to tell in an FDD, however, you can ask questions about this in validation interviews.

Red Flag: Look at the details to see if there are any franchise units with losses or poor earnings. You will want to understand what is happening with that location and determine if it is an exception and how it is being addressed by the franchisor.

Item 20 – OUTLETS AND FRANCHISEE INFORMATION

This is the list with all of the franchise units. Look to see if the location you are seeking is still available and to assess the health of the franchise. How many new franchisees are they selling? How many franchisees have left the program? How or why did they leave? Are there terminations initiated by the franchisor?

Red Flag: Franchise terminations indicate problems somewhere. You need to investigate the background to satisfy yourself that it's not a problem with the franchisor causing the terminations.

Item 21 – FINANCIAL STATEMENTS

These are the franchisor's financial statements. This section helps you estimate the solvency of this franchisor's system. If you like the other aspects then have an accountant review these statements with you, especially if you're not expert at financial statements. Look for the following items to see how they have changed from year to year.

- How much cash do they have on hand? Is cash tight? Does it seem adequate to support the franchisees?
- Is the franchisor's revenue increasing from year to year?
- Are cash reserves increasing?
- How much debt does the franchisor carry?
- Does it appear that they can service the debt?
- What money is owed to them? From whom?
- Are officers paying in capital to the company or is other money coming in to the company by other means?
- What were their expenses over the last year? How are they changing year to year? Have the expenses been changing proportionately with sales? In successful franchise programs the proportion of expenses to sales should be getting smaller each year, unless the company is plowing money into advertising and franchise support programs.
- Do the net earnings improve year to year?

Red Flag: Are royalty receivables going up or down? This factor alone can tell you if the existing franchises are growing their sales or if the system is starting to wane.

Item 22 - CONTRACTS

This shows all of the contracts you will need to sign to acquire this franchise. If you are serious about pursuing the franchise, you will need to read these contracts yourself, and also have your franchise attorney advise you. If you intend to operate this business with your spouse or a partner, both of you need to do this.

Red Flag: Using your family or business attorney is not advisable. Franchise attorneys specialize in knowing the regulatory requirements that are specific to franchising. Even if only to review these documents, it would be wise to hire a franchise expert.

Item 23 - RECEIPTS

The government requires a cooling off period of 14 calendar days after receiving the FDD before any transaction is allowed to take place. You must sign, date and return a receipt acknowledge for the FDD to the franchisor. Franchisors need this document from all candidates in order to stay compliant with Federal Trade Commission regulations. You should return the FDD receipt to the franchisor at least two weeks before the discovery day.

Red Flag: If the franchisor does not insist on the acknowledgment receipt, or asks you to post-date the paperwork, it means they are not concerned with following the letter of the law. This is a big red flag, as they may be willing to do other things that put your investment at risk in the future.

Major Advice

As in every business transaction you should have an attorney assist you in the understanding of every legal agreement. Buying a franchise will affect your life and happiness for many years. We recommend you use franchise law specialists, *not general business attorneys*. You want someone dedicated to this kind of law practice. It's worth the extra expense. Multi-practice attorneys may claim to understand an FDD but might not understand all the implications of its provisions. In addition, you may want to have a financial professional help you evaluate the opportunity to give you additional insight into forecasting and the profit potential of the investment.

How to Read a Franchise Agreement

The purpose of the franchise agreement is to provide franchisees and franchisor with all the necessary details about entering and operating this business. It will state the obligations of both parties. *If you have any expectations, you must be sure they are provided for in the agreement, even if you have to add an addendum to it.*

ENTERING A FRANCHISE AGREEMENT

Carefully scrutinize the franchise agreement. Depending upon the franchisor, you should be able to successfully negotiate some terms of the agreement. Franchisors generally will not agree to major variations; however, the widely-held notion that franchise agreements are non-negotiable is not true. Just because an agreement looks like it's permanently and indelibly printed does not mean it can't be modified by simply adding an addendum.

There are three reasons why you need to read and understand the franchise agreement before purchasing a particular franchise:

1) To know exactly what you are buying as it is a long-term contract.
2) To discover the fees and expenses you will be paying.
3) To establish the length and terms of the franchise and each other's obligations.

For ease of comprehension in context with most franchise agreements the following sections are arranged in approximately the same order as a typical franchise agreement.

Recitals

The recitals establish certain key facts and identify the parties that are referred to throughout the contract, such as Parties, Ownership of System, and Objectives of Parties.

Definitions

Industry and legal terms are usually explained in this section, such as Agreement, Territory Area, Area Licensee, Authorized deductions, Gross Receipts, License Network, the System Manual, Trademarks, Start Date, Trade name, Termination, Transfer of license.

Fees and payments

Franchise fees and other payments are listed here, such as Initial License Fee, Training Fees, Marketing Fund, Royalties, Renewal fee, and Transfer fee. In addition to the up-front franchise fee and royalties that you may be required to pay, additional hidden costs and expenses may be associated with the franchise operation. These can come in many forms, such as accounting fees, lease location expenses and supervision fees.

Trademarks

The franchise agreement should contain specific representations regarding ownership and genuiness of the trademark. Make sure the franchisor actually owns the trademark for the franchise and that it is registered and protected. International protection is preferred.

Obligations and duties of the franchisor

Here you will find the sections regarding Administration, Collections and Billing, Consultation, Marketing, Manual, and Training spelling out what the franchisor will actually do and how they will support you.

Obligations and duties of the franchisee

This is what the franchisor expects of a franchisee, such as use of trademarks, financial information, insurance, financial and legal responsibility, conformation to the FDD, and maintaining brand integrity.

Restrictions

Restrictions may be placed on goods or services provided so that you cannot add or subtract offerings. It is also good to make sure the franchiser is not selling competitive products (through other channels) that you will become your competition.

Length of term, renewal, termination, transfer of the agreement

This is usually a substantial part of the agreement with sections on Licensed Rights such as Territory, Rights Reserved, Term and Renewal, Minimum Performance Standards.

You should carefully consider the geographic scope of your proposed franchise territory while keeping in mind its location and your ultimate business plan. If you have negotiated first rights of refusal on expansion territories or on more franchise density in your territory, you need to be sure they are clearly noted in an addendum.

The franchise term is an issue that is sometimes disputed after the franchise has been awarded. By then it will be too late. Franchisors typically grant terms of 8 to 15 years. You, as the franchisee, should ask for a term that at least allows you time to establish the business and recover your capital costs.

Some franchisors, insisting on flexibility, can terminate franchise agreements *at will* simply by giving written notice to the franchisee. This is not in your best interest. You and the franchisor must also agree upon the ability to renew the agreement; what will happen to the franchise if the franchisee dies; whether the franchisor can sell competitive products; and the amount of ongoing services that the franchisor will provide during the term of the agreement. While these issues are too complicated to consider here, be aware that important business and legal issues arise when you enter a franchise arrangement. You should consult a franchise attorney and an accountant before signing.

Major Advice

As in every business transaction you should have an attorney assist you in the understanding of every legal agreement. Buying a franchise will affect your life and happiness for many years. We recommend you use franchise specialists, not general business attorneys. It is well worth the expense. You want someone dedicated to this kind of law practice. Multi-practice attorneys may claim to understand an FDD but might not understand all the implications of its provisions.

Additional Resources

For deeper understanding we recommend the detailed book written by Steve Olson: ***"Grow to Greatness: How to Build A World-Class Franchise System Faster,"*** lauded as the *"Driver's Ed Manual for franchise development"* by the President of the International Franchise Association's Education Foundation. It is available through Amazon.com, and consistently one of the top selling resources on franchise development. It is written targeted at the franchisor's point of view and needs, but anyone buying a franchise can benefit from a good understanding of this perspective.

Steve Olson, CFE (Certified Franchise Executive), is Legacy's chief development advisor. He is former President of Franchise Update Media Group. He helped accelerate system expansion for more than 50 established and emerging franchise brands. He entered franchising as co-owner of a multi-unit franchise in Houston, awarded Franchisee of the Year for overall sales performance and excellence. He has served on boards of franchise industry companies. He is former committee chairman for the International Franchise Association, and past board Member of the California Franchise Association, and Arizona Licensor and Franchisor Association. Steve has been quoted by national and local media as a resource for franchising, including *The Wall Street Journal, Smart Money Magazine, Financial Times, The Street, NPR, Orange County Register,* and other media.

Glossary of Franchise Terms

The following glossary of commonly used franchise terms is based on generally accepted definitions. Franchising is an ever-growing and changing business format and the terminology used is also evolving. The meaning of terms can change slightly over time.

A

Absentee Ownership
This is a franchise system with a franchise agreement that allows the franchisee to be away from the daily operations of the business on a full-time basis. Another option is semi-absentee ownership, which allows owners to be away from the day-to-day operations to some extent. See ""Semi-Absentee Ownership" and "Full-Time Work Requirement." Not all franchises permit this kind of ownership.

Acknowledgement of Receipt
The final page of a Franchise Disclosure Document (FDD), which, once signed and returned, confirms to the franchisor the date you received the document.

Advertising Co-op
A participatory body of franchisees which may occasionally include the franchisor. Members contribute money to a common fund to pay for regional or national advertising programs. Administration of advertising co-op funds varies from company to company. In most cases a committee of franchisees administers the fund. Alternatively, a special advertising committee made up of both franchisees and the franchisor may oversee the use of the funds.

Advertising Commitment
This is an amount that a franchisee commits to spend on advertising and promotion in his local market. These monies are controlled by the individual franchisee and used to promote the franchisee's individual business.

Advertising Contribution
The monies that a franchisee is required to contribute to the advertising fund or the advertising co-op. These funds are used to pay for system-wide advertising and promotional expenses. The manner in which advertising contributions are made varies from company to company. Many franchise agreements specify a percentage of gross sales to be spent on advertising; the breakdown of expenditures for local, regional, and/or national advertising may also be specified.

Advertising Fee
See "Advertising Contribution."

Advertising Fund
Similar to an advertising co-op, this fund is administered and controlled by the franchisor.

Agent
A person authorized by another ("principal") to act on his behalf as the principal's agent.

Angel Investor
An individual or group of individuals who provide capital for a business start-up, usually in exchange for convertible debt or ownership equity. Angel investors invest their own personal funds, unlike venture capital firms that manage the pooled money of others in a managed fund. In some cases, if a family member or a friend were to lend you money to start a business, they also would be referred to as an angel investor. (Legacy Franchise Group can introduce Angel Investors for qualified projects.)

Antitrust Law
Laws intended to outlaw or restrict business practices considered monopolistic or that restrain trade. In the U.S. the principal antitrust laws are the Sherman Antitrust Act (enacted in 1890 and frequently amended), the Clayton Act (originally adopted in 1914), the Robinson-Patman Act (passed in 1936 to add price-discrimination prohibitions to the Clayton Act), and the Federal Trade Commission Act (also adopted in 1914). Some states have also adopted antitrust laws, such as the Donnelly Act in New York. Outside the U.S., antitrust laws are often referred to as "competition" laws.

Approval / Consent
This is a provision within the franchise agreement requiring that a party who wishes to act must obtain the consent or approval of the other party. For example, the franchise agreement may require that before the franchisee can transfer interest or control in the franchise, he/she must obtain "approval/consent" of the franchisor.

Approved Supplier/Vendor
An approved supplier or vendor is an entity that has been approved by the franchisor to sell products and/or services to franchisees of its system. Items sold by approved suppliers may include equipment, ingredients, and other materials or items for use in operating the franchise business. The franchisor will generally approve several suppliers for each item and the franchisee may purchase the items from any of the approved suppliers. In some instances, a franchisor approves only one approved supplier of a specific product (i.e., a soft drink supplier) for purposes of system-wide uniformity. Also see "Designated Supplier/Vendor."

Arbitration
In disputes between a franchisee and a franchisor, submitting the dispute for determination to private, unofficial persons or "arbitrators." Agreement to arbitrate must be stated, for example, in the franchise agreement, and arbitration findings are binding on both parties. A court's only basis for review of an arbitrator's decision is whether it was arbitrary, capricious, and an abuse of the arbitrator's discretion or beyond the arbitrator's authority.

Area Developer
The franchisor awards a single franchisee the right to operate more than one unit within a defined area, under a development agreement and based on a mutually agreed upon development schedule.

Area Representative
A type of franchisee that can own and operate franchise outlets, represent the franchisor in selling new franchises, and provide ongoing local support to existing franchisees in a defined market. The area representative normally receives a portion of the royalty fees and possibly the upfront franchise fee payable by the franchisees to the franchisor. Area representatives may operate in a variety of geographical configurations, including metropolitan areas, a single state, or a combination of states. The area representative is not a party to the franchise agreement, which is between the franchisor and the franchisee. See for comparison, "Master Franchisee."

Assignment
Contractual authority of a franchisee to give away, sell, or otherwise transfer or dispose of all or certain ownership rights in the franchise agreement, the franchised outlet, and/or interest in the legal entity that owns the franchise. Assignment rights vary from franchisor to franchisor and may include the right to sell the business and transfer the franchise agreement to the buyer or to transfer ownership and rights to the family and/or for the estate to sell the franchise upon the owner's death or disability. Virtually all franchise agreements limit assignment in one way or another.

B

Bona Fide Wholesale Price
Defined in the Federal Trade Commission's Franchise Rule and one of three terms employed in defining a "business format franchise." Refers to the price of goods or services for use by or to be made available for resale by the franchisee, the price of which is established in good faith without fraud or deceit. The FTC Rule provides that payments for the purchase of reasonable amounts of inventory at bona fide wholesale prices for resale or lease are not "required payments" and therefore are not considered the payment of a "franchise fee." Also see "Franchise."

Breakaway Franchisee
A franchisee that has unilaterally terminated its franchise agreement. Obligations of a breakaway franchisee may include some or all of the following: payment of substantial damages to the franchisor, resale of the business to the franchisor, or an obligation to abide by a post-term, non-compete covenant.

Bundle of Rights
All those rights and obligations that pass to the franchisee under the terms of a franchise agreement. These may include such items as right to use the trade name, right to knowledge of trade secrets, right to use the format of the business, right to build equity, and right to manage day-to-day operations in the prescribed manner.

Business Broker
An intermediary who manages the sale and/or purchase of an existing franchised business. Brokers can represent either sellers, buyers, or both. They can be helpful in getting franchises awarded, but are not essential. A business broker commonly, but not always, has a "Fiduciary Duty" within the relationship.

Business Format Franchising
The franchising system wherein the franchisee buys from the franchisor a total blueprint for doing business. Usually included is the license of a trade name, the trademark, access to trade secrets, and a clearly defined method and set of guidelines for conducting the business. Occasionally referred to as "pure" or "comprehensive" franchising.

Business Opportunity Laws
Laws regulating the sale of non-franchised "business opportunities." States that have such business opportunity laws typically exempt franchise programs that have federally registered trade or service marks, but some nonetheless require franchisors to file some form of application to claim that exemption. Some common business opportunities include vending machines, worm farming, envelope stuffing, and in-home mail order enterprises. In 2007, when it issued amendments to the Franchise Rule, the FTC also proposed a separate Business Opportunity Sales Regulation.

Business Plan
A business plan is a formal statement of a set of business goals, the reasons why they are believed attainable, and the plan for reaching those goals. It may also contain background information about the organization or team attempting to reach those goals. They are important tools for obtaining financing, and for budgeting and post launch operation evaluation.

Business Valuation
The practice of valuing an existing business. There are a large number of approaches to Business Valuation, including but not limited to Multiple of Earnings, Fair Market Value, Book Value, Replacement Value, Present Value, Future Value, Going Concern Value, Asset Value, Liquidation Value, etc. Sales of existing franchise locations often involve a Business Valuation to determine price.

Buy-back Option

A term of the franchise agreement wherein if the franchisee goes out of business the franchisor retains the right to buy back all assets at a pre-agreed price. The buyback is an option that the franchisor retains and it is not a promise.

C

Camera-ready Advertising

Artwork and typeset materials that are ready for printing. Camera ready advertising is for use in print media (newspapers, magazines, store signs, handbills, flyers, brochures, etc.). Since the cost of producing professional, camera-ready advertising is generally shared by all franchisees, the cost per franchisee is usually quite reasonable.

Cash / Initial Cash Required

One of a number of terms the meanings of which vary from franchisor to franchisor that are used to describe cash monies that the franchisee must spend prior to opening for business. Any of the following terms may be used in this context: cash required, initial cash required, investment, down payment, equity investment. Information concerning the initial investment that a prospective franchisee can expect to incur can be found in Item 7 of the FDD.

Cash flow Projections

A spreadsheet that shows a month-by-month forecast of cash flow coming into the business and expected disbursements, including payroll, rent, insurance, debt, etc. A person considering entering into a business, including a franchise, should carefully examine their cash flow projections to determine whether there will be adequate working capital for the new business.

Commitment Agreement

See "Letter of Intent."

Company-owned Outlet

In a franchised system, the outlets that are owned by the franchisor (or sometimes by its affiliates).

Competing Operation

When a franchisee establishes, operates, owns, or has financial interest in any business that offers products or services the same or similar to those of the franchise, the franchisee may be said to have a "competing operation." Many franchise agreements restrict all competing operations during the term of the franchise. They may also restrict any competing activity or business after the term within a specific area and for a limited period. (Those parts of the franchise agreement are referred to as the "non-compete clauses.")

Comprehensive Franchising

See "Business Format Franchising."

Conversion Franchising

The process by which existing independent businesses or dealers within an industry become franchisees when they assume the trade name and trade dress of the franchisor. Conversion franchising has been particularly widespread in the real estate industry.

Copyright

Generally, the exclusive right of the author or creator to protect his or her creation, such as a movie, book, music, or other expression. As it relates to franchising, copyrights most often apply to confidential written material (such as the operating manual, proprietary recipes, and the like). Under a franchise agreement, the franchisor usually licenses the franchisee to use those copyrighted materials in the operation of the franchised business for the term of the agreement.

Covenant of Good Faith / Fair Dealing
At the heart of a franchise is an agreement that sets out the essential contractual obligations governing the relationship between franchisor and the franchisee. The franchise agreement, however, cannot spell out all the obligations that a franchisor may owe the franchisee, and it has been argued that the franchisor also has an implied duty of "fair dealing" not contained explicitly in the franchise agreement. Courts usually find that the implied covenant of good faith and fair dealing cannot be used to contradict clear provisions in an agreement.

Covenants against Competition
The clause or term of a franchise agreement in which the franchisee agrees not to engage in or maintain any interest in a business activity that competes with the franchise business. Also see "Competing Operation."

D

Default
The neglect or failure of either party franchisee or franchisor to fulfill obligations and/or take the steps required under the contract.

Deferred Balance
A sum of money that the franchisee owes to the franchisor. A deferred balance is generally some remainder of the total amount initially paid for items such as equipment, fixtures, inventory, construction, or rent.

Demographics
A range of factors that may influence consumer behavior in a specific trade territory such as age, income, home prices, and socio-economic conditions.

Designated Supplier/Vendor
A designated entity from which franchisees are required to purchase certain products and/or services necessary to operate a franchise business. This usually applies to proprietary products and/or private label products manufactured to the franchisor's standards and specifications, but might also apply to other products that the franchisor believes are critical to the success of the franchise system. Also see "Approved Supplier/Vendor."

Development Agent
See "Area Representative."

Development Agreement
A term used to describe the agreement traditionally used to grant multi-unit development rights to franchise developers or multi unit franchisees. In the development agreement, the franchisor grants semi-exclusive "development rights" to a developer, which in turn agrees to establish a specific number of franchised units within a certain geographic area (called a "development area") in accordance with a predetermined "development schedule." Before the developer opens each franchised business, it typically is required to sign a franchise agreement for that franchise. The developer typically pays a "development fee" to the franchisor, a portion of which may be credited toward the initial franchise fee due under the unit franchise agreements.

Development Fee
See "Development Agreement."

Development Rights
See "Development Agreement."

Development Schedule
See "Development Agreement."

Disclosure Document
Currently required under the laws of fifteen states, a disclosure document is provided by the franchisor to a prospective franchisee. The document contains information about the franchisor, the franchise being offered, and the terms and conditions of the legal relationship into which the franchisee will enter. The state agency that administers the franchise laws typically reviews the document and other pertinent materials the franchisor will use in promoting the sale of the franchise. Also see "Franchise Disclosure Document."

Discovery Day
An event set up by the franchisor so that potential franchisees may learn more about becoming a franchisee. A discovery day typically takes place at the franchisors headquarters and is often the final step in the due diligence process. It provides the opportunity to meet the management team, support team, and trainers face-to-face. Occasionally called "Meet the Team Day" or "Open House."

Discrimination
Treating one franchisee differently from another. A number of statutes and legal cases restrict a franchisor's ability to discriminate among businesses that are similarly situated.

Distributor
An individual or company through whom a manufacturer sells his products to retailers and/or consumers. Conventional distributors may handle several lines of competing products, whereas franchised distributors typically only handle the products of one franchisor. Franchised distributors operate exactly as other independently owned, franchised businesses, receiving training, management, and advertising support from the franchisor.

Down payment
See "Cash/Initial Cash Required."

Dual Distribution
When a franchisor operates a company owned outlet on the same marketing level as its franchisees.

Due Diligence
Usually undertaken by investors, but also customers, due diligence refers to the process of making sure that someone is what they say they are and can do what they claim (e.g.; Does the product or system really work? Does the franchise really have customers?).

E

Earnings Claim
See "Financial Performance Representation."

Encroachment
Any franchisee—or the franchisor—attempting to sell products or services within an area of territory that has been assigned to or designated exclusively for another owner.

Entrepreneur
A person who is willing to assume the responsibility, risk, and rewards of starting and operating a business.

Equity Interest
Any legal ownership of the franchise business or the corporation that owns the franchise business.

Estimated Initial Investment
A detailed listing of all fees and expenses you should expect to incur in starting a franchised business. This listing represents the total amount that a franchisee would need to pay or get financed, including fees paid to the franchisor and goods/services purchased from third parties. This estimate can be found in Item 7 of the Franchise Disclosure Document.

Exclusive Territory
A territory assigned to a franchisee within which a franchisor agrees not to operate a facility (or grant a license to another party to operate a facility) that is the same as the franchised business, under the same marks, and under the same system. Most franchisors reserve rights with respect to other methods of distributing products or services (such as internet sales). Not all franchisors offer exclusive territories.

Expiration of Term
In a franchise agreement, the date upon which the contract expires if it is not renewed.

F

Facility
See "Site."

FDD
See "Franchise Disclosure Document."

Federal Trade Commission (FTC)
An independent agency of the United States government headed by five commissioners, each of whom is appointed to office by the president and confirmed by the U.S. Senate. The president has the authority to designate one of the commissioners as chairman of the agency. The FTC has an extensive staff and is charged with administering and enforcing the Franchise Rule as well as general prohibitions against unfair and deceptive practices for example, involving advertising.

Fiduciary Duty
A requirement that a person act toward others and the public with the watchfulness, attention, caution, and prudence that a reasonable person in the circumstances would use.

Field Representative
See "Franchise Representative."

Financial Forecast
See "Financial Performance Representation."

Financial Performance Representation
Any oral, visual, or written representation to a prospective franchisees or for general dissemination in the media which states or suggests a specific level or range of potential or actual sales, income, gross, or net profit. If the franchisor makes earnings claims this information must be provided in Item 19 of the Franchise Disclosure Document. Previously called "Earnings Claims."

First Personal Meeting
Historically the Federal Trade Commission required franchisors and their sales representatives to provide the Federal Trade Commission Disclosure Document to the prospective franchisees during the first personal meeting. This

requirement was eliminated in the 2007 amendments to the FTC Rule. Two states have retained this requirement. Please see “Reasonable Request.”

Forum Selection
A term in the franchise agreement that designates the state and court in which disputes are to be litigated.

Fractional Franchise
A relationship that is exempted from the FTC Rule because the franchisee or its principals have had more than two years of prior experience in the franchised or similar business; and wherein the franchisor or the franchisee anticipates that the franchisee’s sales arising from the franchise would represent no more than 20% of projected volume in the first year of the relationship. Some state franchise laws also have a fractional franchise exemption.

Franchise
The FTC Franchise Rule defines a “franchise” as an arrangement whereby a franchisor grants franchisees the right to operate a business that: 1) is identified with the franchisor's trademark; 2) is subject to the franchisor's significant control and/or assistance; and 3) in exchange for which, the franchisee pays a “franchise fee” to the franchisor or its affiliate. Most state franchise laws adopt a similar definition (except in New York, where any combination of elements 1 and 3, or elements 2 and 3, are enough to satisfy the state law definition of “franchise”). A franchise will include a royalty fee on sales and a franchise fee in exchange of the use of trademarks, brand name, service or products, training and the ongoing support, and the complete method to conduct the business itself, such as the marketing plan and operations manuals. Licensing and distributorships are other forms of business duplication that many companies use, but they are not franchises and not regulated under franchise laws.

Franchise Agreement/Contract
The legal document that sets forth the rights and obligations of the franchisee and the franchisor. Commonly included are specific descriptions of the franchisee’s territory, location, training, management, renewal, termination, dispute resolution, suppliers, quality control, product standards, advertising, etc.

Franchise Broker
See “Franchise Consultant.**”**

Franchise Company
See “Franchisor.”

Franchise Consultant
An independent agent or middleman who acts as an intermediary between the franchisor and a prospective franchisee. Franchise consultants are commonly paid on a success basis by the franchisor. As agents of the franchisor, franchise consultants are required to act in accordance with all laws and regulations governing the sale of franchises.

Franchise Disclosure Document
In the United States, the Franchise Disclosure Document (FDD) is the form for providing disclosure under the FTC Franchise Rule. Before the 2007 amendments to the FTC Franchise Rule, the principal format for providing disclosure in the U.S. was a document prepared under the “Uniform Franchise Offering Circular” (UFOC) format. The FDD provides extensive information about the franchisor and the franchise organization in a uniform format, which a prospective franchisee can use to compare different franchise offerings. The FDD is meant to give a potential franchisee certain specified information to help make educated decisions about their potential investments. Also see “Disclosure Document” and “FTC Franchise Rule.”

Franchise Disclosure Laws
Federal and State laws that require a franchisor to deliver a franchise disclosure document ("FDD") to a prospective franchisee prior to selling a franchise to the prospect. See "FTC Franchise Rule" and "State Franchise Disclosure Laws."

Franchise Fee
A sum of money the franchisee pays to the franchisor when the franchise agreement is signed. The fee may cover a variety of expenses, including but not limited to training costs, on-site startup costs, and promotional charges. Also called a "License Fee" or "Initial Fee."

Franchise Operations Manual
The document detailing the operation of a particular franchised business. Franchise operations manuals, also called franchise manuals, describe such items as: quality control requirements; recommended hours of operation and financial and management practices; the correct use of any trademarks or trade names; forms and written materials for use in business operations; payment of fees and royalties; approved suppliers; and so on. Increasingly, operations manuals also address other matters, such as system- wide policies concerning data, environmental and energy standards, health and safety matters, etc.

Franchise Owner
See "Franchisee."

Franchise Relationship Laws
State laws regulating certain aspects of the franchise relationship, such as how and when a franchisor can terminate the franchise agreement, where lawsuits concerning the franchise relationship must be brought, and the circumstances under which a franchisor can refuse to permit the franchisee to renew the franchise agreement.

Franchise Representative
An employee of the franchisor whose responsibility it is to regularly visit with and assist franchisees within an assigned geographic area. Franchise representatives, also called field representatives, may inspect locations for quality and cleanliness; help franchisees solve management or technical problems; troubleshoot; give moral support; act as liaison between franchise owner and franchise company; and offer advertising and marketing advice.

Franchise Rule
See "FTC Franchise Rule."

Franchise Sales Material
Promotional and/or instructional materials made available to individuals who inquire about purchasing a franchise. Such "kits" commonly contain disclosure documents, a description of the business and history of the company, financial information, testimonials from current franchise owners, preliminary information about fees and costs, etc.

Franchise Salesperson
An agent of the franchisor whose business it is to market and sell franchises. The franchise salesperson's role is to meet with prospective franchisees, present disclosure materials, gather the prospect's financial information, answer questions, assist with obtaining financing, and facilitate the signing of a franchise agreement.

Franchise Term
The length of time for which a franchisee is granted licensing and other rights under the franchise agreement.

Franchised Outlet/Unit
Within a franchise system, a business location or site that is independently owned by an individual(s) to whom the franchisor has granted certain rights. For comparison see "Company Owned Outlet."

Franchisee
The individual or individuals who own and operate a business under a licensing agreement granted by a parent company known as the franchisor. Franchisees are commonly entitled to: use the franchisor's trademark and/or trade name, sell and/or market the franchisor's products and/or services, have access to the franchisor's pertinent trade secrets, receive management and other training, enjoy marketing and advertising support, build equity interest in the business, and benefit from the goodwill of the franchisor. Franchisees can also be called "Franchise Owners."

Franchisee Advisory Board
A franchisor sponsored organization of franchisees, either appointed by the franchisor and/or elected from among the franchisees at large, who represent or speak for the franchisees in discussions with the franchisor. Practices vary but franchise advisory boards may, with the approval of all franchisees, levy assessments; run marketing, advertising, and training programs; and represent grievances to the franchisor. Also called "Franchisee Advisory Council."

Franchisee Association
An independent association of franchisees who work together to address the issues that affect all franchisees within a given franchise system. Franchisee Associations generally speak for all franchisees that have chosen to join the association and are independent of, and not directed by, the franchisor. Also see "Franchisee Advisory Board."

Franchisee/Franchisor Relations
Refers to the manner in which franchisee and franchisor representatives interact. Such relations may be generally positive and cooperative or they may encounter periods of stress and distrust. To ensure smooth franchisee/franchisor relations, many franchisors have established franchise advisory boards comprised of franchisees who meet regularly with company representatives. Also see "Franchisee Advisory Board."

Franchisee Training
Education and instruction on how to properly run the business, which the franchisor provides to the franchisee after the franchise agreement is signed. The training may be provided as part of the initial fee or may be an added expense for the franchisee. The training may take place at the franchisor's training facility, at the franchisee's actual business location, or both.

Franchisee Validation
During the process of investigating a franchise opportunity a prospective franchisee will interview current and past franchisees, obtaining unfiltered opinions about the quality of the franchise system.

Franchising
A method of marketing products and/or services under which a franchisor licenses its trademark and operating system and/or know-how to a franchisee in exchange for both ongoing fees paid by the franchisee to the franchisor during the term of the franchise and the franchisee's agreement to follow the franchisor's standards and specifications for the franchise system. Franchise arrangements have been subdivided into two broad classes: 1) product distribution arrangements in which the dealer is to some degree, but not entirely, identified with the manufacturer/ supplier; and 2) entire business format franchising, in which there is complete identification of the dealer with the buyer.

Franchisor (Franchise Company)
The franchisor owns the business system and associated trademarks or trade names. Franchisors allow franchisees to use these under license in a designated area and for a fee and royalty on the franchisees' sales. They then support their franchisees in startup and in continued support.

FTC Advisory Opinion
A finding of the Federal Trade Commission that addresses the propriety of certain franchise business practices and delivers an opinion on whether or not the practices conform to the FTC's "Franchise Trade Rule." The FTC's staff also

issues informal staff advisory opinions that are not binding, but that give guidance about how the FTC's enforcement staff thinks about a particular fact pattern.

FTC Disclosure Document

See "Franchise Disclosure Document."

FTC Franchise Rule

A nationwide regulation issued by the Federal Trade Commission that principally requires franchisors to provide disclosure to prospective franchisees. The FTC Franchise Rule requires disclosure in the form of a "Franchise Disclosure Document" (or "FDD"). The FTC Franchise Rule was issued in 1978 and took effect in 1979; the regulation was extensively amended in 2007. There is no requirement to file the FDD with the FTC.

Full-Time Work Requirement

This is a franchise system with a franchise agreement that requires the franchisee to be involved in the daily operations of the business on a full-time basis. Other options are absentee and semi-absentee ownership that allow owners to be away from the day-to-day operations. See "Absentee Ownership" and "Semi-Absentee Ownership."

G

Good Cause

In franchising, "good cause" is commonly invoked as legally sufficient grounds or reason to support the actions of one or the other party, particularly in the case of non-renewal or termination of the franchise agreement.

Goodwill

The positive reputation or image that a franchisor has earned from the public. Although goodwill cannot be measured in precise monetary terms, image, reputation, public awareness, and acceptance all contribute to a company's value or worth. Typically, the goodwill associated with a trademark does not legally transfer to the franchisee.

Gross Sales

Total value of all sales prior to adjusting for costs or discounting.

Group Purchasing Power

In franchising, the ability of a group of store operators, including franchisees and company owned units, to obtain a lower price for goods and materials when such goods and materials are purchased in large quantity. Also implied is the groups' greater influence with the supplier in terms of timely delivery, service, and so on.

Guarantee

A promise or assurance, especially one in writing, that something is of specified quality, content, or benefit; or that it will perform satisfactorily for a given length of time.

H

Household Cash Flow

Total household income minus total household expenses over a predetermined period of time.

I

Independent Contractor

For tax and legal purposes, an individual who is not classified as an employee but who is deemed to be in business for themselves.

Infringement
A trespass or encroachment upon one's rights; used especially in relation to invasions of the rights secured by patents, copyrights, and trademarks.

Initial Fee
See "Franchise Fee."

Initial Investment
The amount of money required for a new franchisee to open and operate a location for at least three months. This must include all startup expenses, but may not be reflective of total investment. Information about a prospective franchisee's initial Investment can be found in Item 7 of the Franchise Disclosure Document.

Injunction
A judicial process or order requiring the person(s) to whom it is directed to do a particular act or to refrain from doing a particular act.

International Franchising
Refers to the expansion of franchising beyond national borders. A growing number of franchisors are currently operating franchised and/or company-owned outlets outside their home country.

Investment/Equity Investment
See "Cash/Initial Cash Required."

J

Joint and Several Liability
Where multiple parties, such as shareholders or parties owning a franchised unit, share equal financial and legal responsibilities and therefore are together subject to any and all lawsuits or legal actions filed by creditors or other plaintiffs.

L

Lanham Act
A shortened name for the United States Trademark Act of 1946.

Lease Security Payment
A payment made to the individual(s) who grants a lease on the property where a franchise is located. The lease security payment is most often paid by the franchisee to protect the leaseholder against losses in case of business failure or default.

Letter of Intent
A written statement of intention to perform an act. In franchising, the franchisor sometimes provides to the prospective franchisee a letter of intent stating the company's intention to offer a franchise agreement. In commercial banking practices, a letter of intent, or commitment agreement, may state the bank's intention to make a loan to the prospective franchisee. Letters of intent are usually not binding legal commitments.

License Fee
See "Franchise Fee."

Licensee
See "Licensor."

Licensor
In franchising, another term for "franchisor." The term is also used to describe the party who grants another the right to use its trademark in connection with the sale of the licensor's products without the use of the licensor's operating system.

Liquid Assets
See "Liquid Capital."

Liquid Capital
Assets held in cash or in something that can be readily turned into cash. Also known as "Liquid Assets."

Location
See "Site."

Logotype (Logo)
A franchisor's trademark or name, as it is distinctively designed or written.

M

Management Fee
A sum of money the franchisee pays for continuing management aid and assistance. Such fees may be included in the royalty or service fee or may be an additional charge.

Manager Operated/Run
A franchise system that does not require the franchisee to be personally involved in the daily operations of the franchised unit on a full time basis. An operation that is well-suited for investors and part-time involvement. See "Semi-Absentee Owner" and "Absentee Owner."

Marketing Plan
Generally, a marketing plan is a written document that details the necessary actions to achieve one or more marketing objectives. In regard to franchising, the marketing plan is a term that is often used as a shorthand way of describing the second element of the term "franchise" under the FTC's Franchise Rule. See "Franchise."

Master Franchisee
A system whereby a franchisor grants to a party (usually referred to as the Master Franchisee) the right to operate franchised businesses and to grant sub-franchises to third parties, within an agreed upon geographic area. The Master Franchisee serves as if it were the "franchisor" within the sub-franchise territory, providing localized support services within the territory. The Master Franchisee typically retains a portion of the royalty as compensation for its services.

Maximum Investment Level
Maximum dollar amount an investor is both comfortable and qualified investing (cash and borrowed) into a business. This amount generally includes both cash and debt.

Minority Business Enterprise (MBE)
An MBE is a business that is typically majority-owned and controlled by U.S. citizens who are members of certain defined minority groups. Some MBEs may be granted preferences in terms of obtaining contracts, for example, when municipalities control a venue, such as an airport concession authority on toll roads, etc.

Multi-unit Franchisee
A franchisee that owns and operates more than one franchised location.

Mutual Evaluation Process
The understanding that both the franchisor and the prospective franchisee are evaluating each other during the due diligence process to determine if it would be mutually beneficial to move forward into a franchise relationship.

N

Net Worth
An individual's total assets minus his/her total liabilities.

Non-compete Clause
The provision in a franchise agreement which prohibits a franchisee from owning, operating, or having an interest in any competing business offering the same or similar products or services as those provided by the franchise. A non-competition clause may also prohibit the franchisee from involvement in any such competing business for a specified length of time following non-renewal or termination of the franchise agreement. Also called "Non-Compete Clause."

O

Offering Circular
See "Franchise Disclosure Document."

Offering Prospectus
See "Franchise Disclosure Document."

Opening Costs
Total franchisee costs to start the business and remain operating for a reasonable period (typically defined as three months). Opening costs may include franchise fees, costs of real estate and/or rent, zoning and business licenses, financing expenses, inventory expense, equipment, training fees, working capital, payroll, insurance, and salaries for employees. Please see "Cash/Initial Cash Required."

Operating Controls
See "Quality Control."

Operations Manual
The document detailing the operation of a particular franchised business. Operations manuals, also called franchise manuals, describe such items as: quality control requirements; recommended hours of operation and financial and management practices; the correct use of any trademarks or trade names; forms and written materials for use in business operations; payment of fees and royalties; approved suppliers; and so on. Increasingly, operations manuals also address other matters, such as system- wide policies concerning data, environmental and energy standards, health and safety matters, etc.

Owner Benefit
This is a descriptive term that describes business income minus all "true" business expenses. Any benefit a franchisee receives from the business either through pass-through expenses, retirement contributions, dividends, distributions, or salary is considered part of Owner Benefit. Other terms include "Owners Discretionary Profit" or "Earnings Before Interest Taxes Depreciation and Amortization (EBITDA) Plus Add-Backs."

P

Per Se
When used in antitrust law, a “per se” violation is one that is inherently illegal once proven. (Not to be confused with “*pro se.*"

Personal Living Expenses
The amount of money required for you and your family to live. Also called “Family Expenses.”

Pre-opening Promotion
Special marketing, promotion, or advertising that precedes the opening of a new franchised or company owned outlet by some length of time. Pre-opening promotion heightens consumer awareness and puts the new business on sound footing.

Preferred lender
A lender that specializes in franchise financing and has a pre-existing relationship with a target franchisor.

Preferred Supplier of Legacy Franchise Group
A service that specializes in franchising services that has a pre-existing relationship with Legacy Franchise Group. Services that have been developed as an approved list are attorneys, retirement conversion specialists and manual writers.

Price Fixing
A criminal violation of federal antitrust statues in which several competing businesses reach a secret agreement (conspiracy) to set prices for their products or prevent real competition and keep the public from benefiting from the competition. “Horizontal price fixing” among competitors at the same level of commerce (for example, two or more franchisees) is typically “per se” illegal. Under a series of decisions reached by the U.S. Supreme Court, parties such as franchisors are permitted to specify a maximum and a minimum resale price, which may still be reviewed under federal antitrust law under the “rule of reason” standard.

Principal Register
The U.S. Patent and Trademark Office (USPTO) maintains a list of all registered trademarks. The USPTO list includes the “Principal Register.” When a trademark is listed on the Principal Register, it puts all parties in the country on constructive notice of the registration as well as the registrant’s use of the mark. When a mark has been included on the Principal Register, the owner of that mark is entitled to exercise all of the rights provided by the U.S. Trademark Act.

Product Liability
In franchising, the term implies the risk assumed by franchisor and franchisee in providing the franchised goods and/or services to the consuming public.

Product Specifications
Commonly spelled out in the operations manual, product specifications are precise and detailed descriptions and/or designations of ingredients, materials, goods, and other items used in the operation of the business.

Product Standardization
Related to quality control, product standardization is the franchisor’s effort to provide in every franchised and company owned outlet, goods and/or services which are uniform in quality, appearance, and character.

Profit Projections
See “Financial Performance Representation.”

Prospectus
See “Franchise Disclosure Document.”

Protected Area
See "Exclusive Territory."

Protected Territory
See "Exclusive Territory."

Public Offering Prospectus
See "Franchise Disclosure Document."

Purchasing Power
See "Group Purchasing Power."

Pure Franchising
See "Business Format Franchising."

Q

Quality Control
The practices of a franchisor in supervising, regulating, and directing how business will be conducted in a franchised or company owned outlet. Strict quality control is the franchisor's most important method of insuring a uniform high quality of product and services in all franchise locations. Trademark owners are required, under the U.S. Trademark Act, to police their marks and the products and services sold under those marks.

R

Reasonable Request
Under the Federal Trade Commission Rule, franchisors and their sales representatives are required to provide the Franchise Disclosure Document to a prospective franchisee upon reasonable request. When the FTC issued the amended FTC Rule in 2007, the agency declined to provide a specific definition for the term "reasonable request," noting instead that "determinations about 'reasonableness' can be made only on a case-by-case basis."

Registration
In those states that have a state franchise law, franchisors must file an application to register before offering and selling franchises in that state. In some of these states, the application consists of filing a copy of the franchisor's FDD as well as certain additional forms. State registration applications typically are part of the public record.

Registration State
A state where there is a "state franchise law." Currently CA, HA, IL, IN, MD, MI, MN, NY, ND, RI, SD, VA, WA, WI. See "State Franchise Laws."

Relevant Market
A way of identifying a market area according to its geography. In franchising, the term usually identifies the area in which a particular business entity has control.

Renewable Option
See "Renewal."

Renewal
Most franchise agreements are for a specified period of time; at the end of that period the franchisee generally has the option to renew at a specified fee and upon signing the then current franchise agreement. The franchise agreement

presented at renewal time may be substantially different from the one originally signed; for example, the royalties and advertising fees may be higher.

Right of First Refusal
A franchisee's contractual right to purchase if he so decides and if he can meet all conditions of sale established by the franchisor any additional franchised outlets that may be for sale in the future within a predefined territory. This can also apply to a franchisor's right to repurchase a franchised unit at the same price as offered by a third party.

Royalty Fee
A regular and continuing payment made by the franchisee to the franchisor, often paid on a monthly basis. The royalty may be a percentage of sales, a fixed recurring fee, or a combination. Royalties commonly cover use of a trademark and trade name and also constitute a fee for services performed by the franchisor such as training and assistance, marketing, advertising, accounting, and so on. Also called "Service Fees" and/or "License Fees."

Rule of Reason
Under federal antitrust law, a method for judging illegality. Under the laws, certain practices are presumed to be illegal "per se" without regard to the precise harm they have caused or the business justification for their use. Other practices are judged under the "Rule of Reason," under which the practices are generally deemed illegal only if, on balance, they harm competition. Also see "Antitrust Law."

S

SBA Certified Bank
Commercial banks which have applied for and been accepted to participate in the U.S. Small Business Administration's loan guarantee program. While any commercial lending institution may utilize the SBA Guaranteed Loan program, such SBA Certified Banks are more likely to be familiar with the program, thus facilitating approval of the application. Also see "SBA Guaranteed Loan."

SBA Guaranteed Loan
A program of financial assistance available to small business owners from the U.S. Small Business Administration (SBA). While the SBA seldom loans money directly to franchisees, an SBA guaranteed loan makes it easier for a qualified individual to borrow money from a commercial lending institution, such as a bank. Under the program, the loan is made directly by the bank to the franchisee. The SBA protects the bank against financial loss in the event of business failure.

Semi-Absentee Ownership
This is a franchise system with a franchise agreement that allows the franchisee to be away from the daily operations of the business on a part-time basis. See ""Absentee Ownership" and "Full-Time Work Requirement."

Service Fees
See "Royalty Fee."

Service Franchising
A type of franchising which primarily provides a service, assistance or advice to the consumer. Service franchises are typically business format franchises and include, but are not limited to, the following: tax preparation, accounting, haircutting, staffing, window washing, business coaching, real estate, maid services, dry cleaning, painting, etc.

Service Mark
Marks used to identify services, rather than goods, and used in the same fashion as trademarks. Also see "Trademarks."

Site
The specific premises from which the franchisee is to conduct business. Also called “Location” and “Facility.”

Site Selection
The process of choosing the location for a franchised business. Professional site selection involves knowledge of such considerations as demographics, traffic patterns, buying habits, market characteristics, wage and employment patterns, zoning and other land use regulations, building and health code ordinances, and real estate patterns.

Standardized Operating Procedures
See “Operating Controls.”

Start-up Costs
See “Initial Investment.”

State Addendum
Refers to a document that contains additional disclosures required by a registration state. State addenda are added into the FDD as exhibits.

State Franchise Laws
In some states, a law requires franchisors to comply with certain requirements in addition to the FTC Franchise Rule. Typically, state franchise laws require a franchisor to do two things: 1) register with the state each year before starting to offer franchises; and 2) give disclosure. While most of these states have agreed to allow franchisors to use the FDD for providing disclosure, some states require slight changes or modifications to the FDD, which are accomplished through the use of state addenda and state amendments.

Sub Franchisor
See “Master Franchisee.”

Supplemental Register
This is the secondary trademark register for the United States Patent and Trademark Office (USPTO). It allows for registration of certain marks that are not eligible for registration on the Principal Register, but are capable of distinguishing an applicant’s goods or services. Marks registered on the Supplemental Register receive protection from conflicting marks and other protections, but are excluded from receiving the advantages of certain sections of the Trademark Act of 1946.

T

Termination
A declaration by the franchisor that part or all of the rights and obligations—of both parties—under the franchise contract cease or have ceased as of a certain date. Certain responsibilities and/or claims and damages may survive this termination, however. The conditions under which a franchise may be terminated by the franchisor are commonly addressed in the franchise agreement.

Termination Legislation
A number of states have passed franchise relationship laws which govern the reasons for and manner by which a franchisor may terminate or fail to renew a franchise agreement. Such “termination/non-renewal legislation” also has been proposed in Congress from time-to-time but has never been passed into law. Regulations regarding termination and non-renewal therefore differ from state-to-state.

Territorial Restrictions
See "Exclusive Territory."

Total Investment Please
See "Initial Investment."

Trade Dress
A term that refers to the visual appearance of an item, such as the interior or exterior of a building or a product's packaging. Typically, trade dress denotes some distinctive quality or look that is not functional, and that signals to consumers that the products, services, or the establishment is associated with a particular brand. The overall visual manner in which a franchise business presents itself to the public, including the interior and exterior design of buildings, its choice of color, use of dress of its employees, and so on.

Trademark
Any word, name, symbol, or device or any combination thereof adopted and used by a franchisor to identify its goods and/or services and distinguish them from those manufactured or sold by others. A careful franchisor grants only clearly defined or restricted use of its trademark. Such restrictions are spelled out in the franchise agreement and are therefore commonly referred to as "contractually limited use" of the trademark.

Trade name
Individual names and surnames, firm names, and trade names used by franchise companies to identify their business.

Trade Secret
A process, method, plan, formula, or other information unique to a franchisor that gives it an advantage over competitors. Appropriate legal provisions written into the franchise agreement, such as a covenant not to compete, are important in protecting trade secrets.

Training Cost/Expense
The money a franchisee pays for education and instruction. Training expenses may or may not include such items as: travel to and from the training location; room and board during training; the cost of tuition, books and supplies; and on-site startup aid. Practices vary, but training costs may be covered by the franchise fee.

Transfer Rights
See "Assignment."

Turnkey Operation
A term used to describe a franchise that is so thoroughly organized, fully equipped, and professionally set up that the new franchisee need only "turn the key" in order to commence business.

Tying
Under antitrust law, tying is a requirement imposed upon a buyer to purchase one product on the condition that the buyer also buys another product from the same seller. Whether alleged "tying" is illegal under antitrust law is often based on the facts of a particular case, and claims of tying are typically judged under the "rule of reason" standard.

U

Uniform Franchise Offering Circular (UFOC)
This term is no longer used. See "Franchise Disclosure Document "

Unilateral Termination
Wherein one of the parties to the franchise agreement decides, without the other's agreement, to put an end to the business relationship. Unilateral termination may be allowable with "good cause" and/or for pre-agreed reasons spelled out in the franchise agreement. Either the franchisor or the franchisee may seek to unilaterally terminate a contract; whether or not it is legal to do so will depend on circumstances and on the terms of the contract.

V

Variable Cost
Any costs that change significantly with the level of output, such as material costs.

Venture Capital
A person or group of individuals who invest in a business venture, providing capital for start-up or expansion. Venture capitalists are looking for a higher rate of return than would be given by more traditional investments.

Vertical Restraints
Restrictions imposed by a franchisor on its "downstream" customer or franchisee. An example of such restraint may be a limitation on where a franchisee may offer and sell products or services. Also see "Price Fixing."

Vicarious Liability
In franchising, "vicarious liability" typically refers to claims brought against a franchisor alleging that it is responsible for the action (or inaction) of a franchisee or one of its franchisee's employees or agents.

Vision Statement
A well written vision statement will provide both direction and motivation to help move a person or organization toward a pre-defined future achievement. A well-developed vision statement includes measurement standards and target dates.

W

Waiver
In a typical franchise agreement, there is an "anti-waiver" clause, which states that one party's acceptance of late performance or nonperformance of an obligation by the other party does not waive the requirement that the same obligation be met in the future.

Working Capital
A financial metric that represents liquidity available to a business or organization. A company can have both assets and profit but be short of liquidity if its assets cannot readily be converted into cash. Positive working capital is required to ensure that a firm is able to continue its operations and that it has sufficient funds to satisfy both maturing short-term debt and upcoming operational expenses.