

# FRANCHISING 101

Everything you always wanted to  
know about Franchising...  
But didn't know whom to ask!



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## Preface:

Franchising has emerged as a popular marketing tool that has been tried and tested over several years. From its humble beginnings as an ad-hoc method to license and sell goods, it has metamorphosed into a full fledged industry in its own right.

Franchising has proven to be a great marketing tool for those entrepreneurs who are ambitious enough to start their own business, but are not sure how to go about it, or do not have the requisite funds to get started. They may also be lacking a network of contacts and suppliers who can get the business going. All in all, these people are looking for some guidance and support.

At [Bizymoms](#), we are dedicated in helping the work at home community, especially moms, to start their own business. Our site provides in depth information on what it takes to start your own business, the latest trends in the market, interviews with the experts in the industry as well as a whole lot of information all enterprising moms can use. Our ultimate goal is to help moms have sufficient free time to spend quality time with their family, while also having a chance to pursue an alternate career. It's a win-win situation which helps both mom and family.

This e-book aims to provide a comprehensive insight into the Franchising industry, the opportunities franchising provides, how you as an entrepreneur can benefit from it, the finance needed to get started, mistakes to avoid and a lot of other information you will find useful.

## Chapter 1: Why Franchising can help you

Typically, most people assume that Franchising involves spending loads of money in order to be able to associate with a big brand name such as McDonalds, or it may be a business flooded with scams. Although this is the popular perception floating around, it is definitely not true. There are thousands and thousands of franchising opportunities available and there is a suitable franchise for each and everyone. Ranging from computer trouble shooting solutions right down to a home based business, the gamut of opportunities can make it difficult to choose!

While you may have a fantastic idea or concept in mind to start your business, we would like to help you understand how franchising can help you jump starting your business.

Here are some reasons why you should consider franchising:

1. **Tried and tested:** Franchising has been tried and tested for several years now. While franchising may not guarantee success, it does ensure complete assurance in being able to help you with the issues while starting up any enterprise, till the point when you're ready to spin off on your own.
2. **No business decisions:** All critical management decisions will be taken by the franchisor. Right from the marketing strategy to the business plan, everything is chalked out by your franchisor beforehand. This saves you a lot of the anxiety that stems from having to make strategic business decisions all by yourself, if you were to start off on your own.
3. **Networking issues:** With a franchise another advantage you get is having an already established network of contacts who have been in business for several years. Therefore, you do not need to make numerous phone calls to establish a network, which you would, if you were starting off alone, without a franchise support.
4. **Support and training:** It is often in the best interests of the franchisor to provide as much of training and support as the franchisee requires to remain competitive in the business. Therefore, to get any kind of help or support, all you usually need to do is give your franchisor a quick call.
5. **Getting finance is easier:** If you were to start off on your own, you would be having a tough time trying to get finance from institutions – that's because they do not know if your idea will sell. So that implies an additional effort of selling your idea to them, convincing them for a loan. However, if you're with a franchisor, it is that much simpler to get a loan. The financial lenders are more comfortable lending money to a business plan that has been tried and tested. The parent company of the franchise will also guide you on the typically overwhelming process that goes along with financing your business idea.

- 6. Greater chances of success:** Statistics reveal that franchising may actually guarantee you a greater probability of success. It has been seen that on an average, a franchise continues to function even 5 years after it has been established, as opposed to a self started business, which fails most of the time, or at least doesn't last that long a span.

## Chapter 2: How Franchising works

Franchising has become a proven business model and it has become a highly successful marketing tool for all aspiring entrepreneurs. If statistics are anything to go by, franchising contributes approximately 3 trillion USD every year in retail sales and approximately 1 out of every 16 people are employed in the franchising industry.

During times of the economic downslide most people fear losing their jobs and getting laid off. So they start looking for other means to ensure their independence and stability. Franchising is a great way for such people to ensure their independence and financial growth even in such an economic scenario.

Franchising is basically a concept used to describe a situation where the organization that is franchising (also known as franchisor) provides necessary support, training and a limited “license” to a businessperson (franchisee) to sell the products and services manufactured by the franchisor. Since the franchisee is a part of the parent company, he or she has to use the brand imagery, and other attributes pertaining to the parent company’s brand.

An initial investment is required to be provided by the franchisee in return for which, the franchisor provides all the requisite support and training needed for the franchisee to get started. This is a great marketing tool because all the necessary infrastructure, supplier network and business plan is already in place. All the franchisee needs to do is try and sell the products and services of the parent company.

## Chapter 3: Pros and Cons of Franchising

Most people find a standard 9 to 5 job very boring. More and more people are trying to free themselves from the routine of a scheduled job and instead try their hand at starting their own business. Usually these people believe in themselves and their own entrepreneurial skills. For such people, franchising can prove to be the perfect opportunity to jump start their business.

However, while there is a lot of hype surrounding franchising and while most people have heard all the ‘biggies’ say this is the way to go, it makes sense to take a reality check before getting carried away with all the hype. Franchising, for all its benefits, has its own set of disadvantages too. We try and list down some of the advantages and disadvantages of franchising to help aspiring entrepreneurs decide better.

First we talk about the advantages of franchising. There are several benefits of franchising:

1. **Established customer base:** A reputed franchise will have a strong customer base and brand value. That means you don't have to spend a fortune on marketing your product or service or even on advertising to develop your brand.
2. **Prior infrastructure for marketing campaigns:** Another advantage a franchise has is the backing of a nation wide campaign. If needed they have prior marketing collateral for even a local campaign.
3. **Reputed suppliers:** Franchises have a network of reliable suppliers who can be trusted because they have been in business for many years.
4. **You're not alone in business:** The very fact that you know you are here is to see your business grow yet have the backing of established franchises, brings with it an implicit assurance.

Apart from these, you also have access to all confidential and proprietary information because now you're part of the franchise. Besides this, you have the added joy of being in complete control of your own business.

Now we come to the other side – the disadvantages. Some of the disadvantages of franchising are:

1. **Large initial investments:** If you're going for a reputed large franchise, then the initial investment can turn out to be quite a lump sum. It might even work out more expensive than what you'd need to start your own business
2. **Royalty:** The fact that you're part of the franchise would mean that you would need to shell out a certain percentage of your profit to the franchise every month.
3. **Marketing charges:** In order that franchises can market and advertise you products they are going to charge a marketing fee.
4. **Restriction of creativity:** As the franchise has its own brand identity, it will have certain guidelines for you brand as well, since your brand is now part of the franchise. This limits the amount of creativity you can apply to your brand.
5. **Dependence on franchisor's success:** All the success of your business will ultimately depend on the success of the franchise.

At the end of the day, the choice of whether to franchise or not rests on you. However, in both cases there is a certain amount of risk involved, as is to start any business. As long as you remain a sharp business person, there is no need to worry.

## Chapter 4: Find out if you have what it takes

To be able to figure out if you can pull off a franchising opportunity with success, it is essential to first understand if your idea is franchiseable or not. To do that you need to ask yourself a few basic questions like...

- Whether you have an existing operation that is generating substantial profits, do you already have a few units under your operation.
- Whether your business units have been in existence for a short period of time or have they been around for quite a few years now.
- You may also need to understand and analyze how your product or service offerings are unique and different from other key players in the market.
- You may also need to get an estimate of the costs involved in starting a new location for your business. This would need to be exclusive of franchise fees and associated costs.
- Try to also figure out what the target segment or market of your product or services is – whether it is restricted to a niche local segment or whether it can be expanded to suit a national or even international audience.
- A little bit of research on your competition goes a long way in helping you position your product or service. It also helps to take a stock check and analyze to what extent are your current processes and systems organized. This would help in understanding the extent of work involved to replicate these operational processes in any new location.
- Understand how much training and knowledge transfer might be required when you're opening a new location for your business.

You would also need to analyze things such as your **success factor** – that is if you are a service-oriented and customer oriented person (remember in any business customer is king), if you are able to set definite goals and make strategic decisions for yourself, if you always feel the need to control and lead people, if you thrive on success and are a result oriented individual, if you have a high confidence level yet are able to follow others and be coached as well. If you have these traits, it means your success factor is very high.

There are certain experience levels that certainly add to your entrepreneurial abilities, the first of which is a **management degree**. A management degree teaches you the ins and outs of business, how to solve specific business problems and offers in depth exposure to simulated situations where you act like a business head yourself. This exposure goes a long way in providing the self confidence to carry off a new venture.

Your **net worth** also plays a crucial role in deciding if you will be able to afford the expenses of starting a franchise. The initial expenses are quite heavy on the pocket. Therefore if you have sufficient capital on hand, it definitely helps a great deal.

The amount of **time** you are able to devote to franchising is also very important. This is because franchising is a demanding profession in itself. It needs your full attention and care. Therefore, if you are already in a part time or full time job, it may not be feasible for you to devote the required amount of time and attention to make your business a success.

## Chapter 5: Is franchising for you?

Even before you take the plunge into franchising, consider this. Franchising is probably going to be a big part of your life for at least 5 or 6 years down the line or even more, if your business is able to sustain success. Therefore, it is essential to figure out if franchising is really what you want to do and more importantly if franchising is ideal for you.

Different people have different interpretations of an advantage or disadvantage. So, while in our earlier section we spoke about how franchising can be great for you, here we try and reveal the positive and negative manner in which these can be imbibed. Therefore, try assessing yourself honestly to see which of these feelings are closest to your interpretation of these ideas.

1. **Critical business decisions are made by business owners:** While this is great news for some, if looked at from an alternate perspective, it can spell the thwart of creativity and involvement. Some people who look at it positively may think this is great because now they do not have to bother with making crucial business decisions and therefore they have lesser anxiety and get to spend more quality time with family and friends. Others who are more independent and hands-on in their approach may not like the idea of not being involved with something as crucial as the groundwork of laying the business plan.
2. **Franchising provides an outlet to sell effectively:** While this means good news for those who believe it gets them a good marketing tool to sell effectively and earn more, for some it may mean also having to pay royalty which eats into a big chunk of the profits.
3. **All training and support is provided:** This is great for those who like to be guided on how to sell the franchisor's products and services. For those who do not like to be coached and goaded into scaling up, this can be as painful as the 9 to 5 job they ran away from!
4. **A ready network of established suppliers:** This can be great for an entrepreneur who doesn't have too many contacts and can utilize the franchisor's network of suppliers effectively. For someone who is more independent and does not like restriction, simply sticking to the franchisor's supplier and vendor network can signal a lot of limitation.

5. **Franchisor's success ensures mine too:** If the franchisor's business succeeds in the market, then it is a sure signal the franchisee will also thrive in it. However, if the business fails, it also means your business suffers a major loss.

We have merely tried to lay down both positive and negative interpretations of the same thought. It is best to honestly evaluate yourself and figure out which feelings resonate with your own. Once you are able to decide that, making the decision of whether franchising is right for you or not, will be much easier and will be more in sync with you as a person.

## Chapter 6: The financial remuneration in Franchising

The primary question every entrepreneur asks before considering franchising is: how much money will I be able to make out of it? This depends on the level of involvement you wish to put into the franchisor. If you invest in a kind of superficial way, where most of the decisions and work is done by the franchisor, then obviously the returns are also not going to be that great. Whereas if you're more involved in the business, chances are your profit margins will rise.

To get a perspective, you can try speaking to existing franchisees in the same vertical or industry. That way you would get an idea about the level of involvement expected, how much you can potentially earn out of a franchising opportunity, etc.

Surprisingly, many people find it very difficult to get a straight answer from the franchisor, on the profit potential or the payment they can expect over a period. This is because while there is no regulation prohibiting an organization to tell you the potential earnings of its franchise, there is an organizational policy that does not allow organizations to disclose estimates on the potential earnings of its franchisees, to an investor. This is because most organizations would like to paint a rosy picture to boost their sales. So naturally they would not like to de-glamorize it by stating the real truth of the earning potential. It might even discourage an investor.

On the whole, franchisees' earnings are pretty good. As statistics say, franchising contributes 3 trillion USD per year in retail sales. This is not a small figure and there must be a good earning potential in it, or else so many people would not be investing their hard earned money in franchising.

The best way to extract inside information such as earning potential, the level of involvement etc, it is ideal to speak to other franchisees in the same business. That way you get genuine details and by a mere phone call you may get access to a wealth of information.

## Chapter 7: Business opportunity vs Franchising

For many people, it is often perplexing to understand if the opportunity they're considering is a business opportunity or a franchise. While both may seem to be the same, there are differences. Often the differences between the various states in the U.S. make it all the more difficult to figure out the exact difference. Here we try to elucidate on the differences.

A business opportunity is almost the same as a franchising opportunity – that is, both are a means for any larger sized organization to distribute its products and expand its business further with the help of smaller business units. For this, the parent company provides all the required support and training and the smaller company continues to sell the products and services, using limited 'license'. A business opportunity is a lighter version of a franchise opportunity – as in, it does not carry with it the same level of commitment with it.

Another significant difference between the two is that a business opportunity is more of establishing an initial, one-time business plan, as opposed to a franchisor franchisee relationship which is more ongoing and stronger.

A business opportunity is more a scenario where it is only at the initial stages that the business owner provides all necessary guidance, business plan as well as support and training. Then once the business is established, it is the individual's responsibility to spin it towards success. Therefore, the individual is not expected to pay any form of royalty to the owner and neither does the owner provide any support services to the individual.

A franchise on the other hand is more of an ongoing commitment. The franchisees continue to receive support, training and any help needed even after the business has been established and is running smoothly. That is the primary reason why most franchisees are able to succeed and at times sustain their business even 5 years after start of the business. The ready network of suppliers and contacts, coupled with the ability to ask for help from the franchisor any time, is a great advantage.

However, while deciding which one is more suitable for you, you need to get an objective assessment of both. There are plenty of regulations that go hand in hand with both a business opportunity as well as a franchise. Therefore it's best to seek the guidance of an attorney to get an idea from the legal perspective. However, in this section, we are merely providing a basic perception of what all this involves.

While a business opportunity may sound a little daunting because of its lack of support as compared to a franchise, it should be remembered that a franchise

requires large amounts of investments along with royalty fees to be paid for selling the products.

Business opportunities provide independence, no obligation to pay royalty and a creativity to provide your valuable insights to start your own business. However, a franchise offers continual support, an opportunity to utilize the brand image of the parent company, in exchange for regular royalty fees.

## Chapter 8: About Master Franchisees

Franchising has emerged as a highly successful and popular marketing tool to expand ones business and see it grow. As franchises grew, there was a need to delegate work and prioritize it to meet the ever increasing demand posed by the industry.

A large part of the success of franchises today can be attributed to the Master Franchisee. A master franchisee is a single individual or an organization that takes care of recruiting, training and supporting new franchisees in a particular area. Usually the franchisor provides a lengthy list of responsibilities to the master franchisee to take care of the entire area development. Therefore, all ongoing support and training, as well as sales of the new franchisees, are the sole responsibility of the master franchisee.

The designated area of a master franchisee varies to a large extent based upon the organizations growth plans, the population density and other factors. However, most of the time, the areas cover large geographic locations and at many times may include more than one state as well. Some organizations prefer the direct franchising method more than the master franchisee arrangement. However, all the organizations that use master franchisees have made them an integral part of their organization. It also provides a new franchisee a single point of contact for any help or support issues that it may encounter.

For all the hard work and responsibility taken on by a master franchisee, they also get rewards for it. The master franchisees get to collect a majority of the royalty payments in the designated area, from the individual franchisees. Some of them have even been known to collect the entire royalty fees as well. This would depend to a large extent on the arrangement between the organization and the master franchisee.

Master franchisees also take the crucial decision of analyzing if the franchisees in its area will perform well or not. Also, if it is the hard work of the master franchisee that is going to ensure the success or failure of the numerous franchisees that depend on the master for support and training, rather than the organization itself.

Before going for franchising, try finding out from other franchisees who report to a master franchisee, what level of success they're enjoying. This helps in analyzing the master franchisee's level of success and leadership qualities.

## Chapter 9: Choosing the perfect Franchise

### Chapter 9.a. Tips to help you find the right Franchise

If you have a unique concept or idea and would like to jump start your business, then franchising is the way to go. But how do you go about selecting the franchise that's perfect for you?

The first step in selecting the right franchise option is to understand if your idea is franchiseable or not. To do that you need to ask yourself a few basic questions like whether you have an existing operation that is generating substantial profits, do you already have a few units under your operation, whether your business units have been in existence for a short period of time or have they been around for quite a few years now. You may also need to understand and analyze how your product or service offerings are unique and different from other key players in the market. You may also need to get an estimate of the costs involved in starting a new location for your business. This would need to be exclusive of franchise fees and associated costs. Try to also figure out what the target segment or market of your product or services is – whether it is restricted to a niche local segment or whether it can be expanded to suit a national or even international audience. A little bit of research on your competition goes a long way in helping you position your product or service. It also helps to take a stock check and analyze to what extent are your current processes and systems organized. This would help in understanding the extent of work involved to replicate these operational processes in any new location. Understand how much training and knowledge transfer might be required when you're opening a new location for your business.

Once you have figured out answers to these questions, it becomes that much easier to fine-tune your search for the perfect franchise for you. Nowadays there are several organizations that are more than willing to get your business franchised. They can help define your business model, accelerate its distribution to help you attain high financial performance and even plan strategic methods to find the right franchises.

While choosing the right franchise, it is essential to ensure that the right people are in the right kind of job or else it can wreak havoc on your business and efficiency levels. The key is to strike a balance between a person who is entrepreneurial enough yet is flexible enough to be able to work with processes and operational systems.

## Chapter 9.b. Protect yourself from Franchise scams

As with any successful industry, there will be the scams and the genuine ones. You must have seen and heard of scores of work at home based franchises that seem to offer the world. Most of them are hoaxes and are not to be trusted.

So, how do you ensure you stay away from the franchise scams? The best way to do it is interviewing existing or earlier franchisees of the organization to know their experiences and the level of success they enjoyed. Try and also get an idea about the history of the organization. If they have not been in existence for a couple of years, then may be you should look at them with skepticism.

Also if these organizations are not associated with an international franchising authority like the IFA, then chances are they may not be genuine. A genuine franchising organization must have a well established executive team, must be active in its relevant industry and be affiliated to an international franchising authority.

Also make sure to review the Franchisor's disclosure agreement or the offering circular. As per law, this document needs to be provided to a franchisee at least 10 days in advance of signing any contract. This will give you ample time to scrutinize the document as well as check with your attorney to get legal advice.

## Chapter 9.c. Asking the right questions

While a franchise can be a great opportunity to earn good money and get all the brand recognition and support you need, it can also mean relinquishing a lot of the independence and control that you'd like while starting your business. While you do need to go for a franchise that has a well established brand presence and is successful, it should also be in sync with your personal goals and traits. Therefore, there are a few things you need to do to figure out which franchise is perfect for you.

One of the first things you can do is to get the copy of the franchise document. This will typically contain a list of all franchisees in business as well as those who have been terminated. Try and give them a call or visit them and find out how it was working with the franchisor. It is surprising how many people will either brag or complain about their job.

Some of the questions you need to ask the franchisee are:

- Is the franchisee happy with the franchise? If the franchisee is not happy or is not keen on doing it again, take it as a warning sign.
- Has the training provided been comprehensive enough? If not, chances of failure increase.
- Do the franchise fees being paid currently match up to their interpretations or are they more?

- Before purchasing the franchise, what business experience did they have? If they are experienced and failing in the franchise, it may not be very different for you either. Whereas if they're new to business and are successful with the franchise, it is a positive sign.
- If the designated territory enough to earn sufficient? If not then it means lower returns.
- Does the franchisor advertise the same extent as promised? If not, it could hurt your long term business growth
- When talking to franchisees who have left the franchise, you can ask the following questions:
  - Why did they leave the franchise?
  - If in business, are you doing better in your current business than the franchise?
  - Within the same industry, if they had to pick another franchise, which would they pick?
  - Which are the other industries they like for franchising?

Asking the right questions can provide useful insight and help you make a decision much better.

### **Chapter 9.d. Choosing a Franchise attorney**

While starting out with franchising, the first smart decision you can make is to get yourself a well qualified attorney. This is critical as your lawyer will help you with the legal technicalities of the franchise agreement, help you negotiate suitably with the franchisor on the terms of the agreement, guide you when you're setting up a corporation to start the business, as well as review the proposed lease for the franchise location among many other things. The bottom-line? Your attorney will look out for your interests in an industry where it is very easy to get swindled.

Especially when it comes to negotiating contracts, disclosure agreements, software licensing agreements, power of attorney, as well as non competition agreements etc, you will realize having a lawyer to help you with the legal issues will help a great deal.

Typically an attorney will charge a flat fee for his or her services. The fee ranges between 200 to 300 USD hourly or 1000 to 1300 USD for review and a written analysis of an agreement. This may be expensive but you can be assured that the dividends you get are well worth it.

You can search for a suitable qualified attorney on the Internet. However, the best way to get a dependable and reputed lawyer is by talking to other franchises or franchisees in your area. This is by far the best way to get trustworthy lawyers.

## Chapter 9.e. Checking for legitimacy

You have narrowed your choice of a franchise. But now you're scared what if the amount of money invested is stolen by the franchisor, or what if the effort and time you put into the organization, is totally a failure? These questions can never be completely and satisfiably answered. However, there are certain signs that help you decide if a franchise is legitimate or not.

One of the first signs that a franchise is fake or illegal is if they are being targeted with numerous litigations and the organization's lack of possessing government specific mandatory documentation. Also, if the franchisor is in a lot of hurry to close the deal, consider it as a warning sign. Also for any genuine franchisor it is mandatory for them to provide the UFOC (Uniform Franchise Offering Circular) packet for government filing, as well as provide a copy to the franchisee. This document is required as per law, to be provided to a franchisee at least 10 days before signing any contract or paying any money. However, it's best not to wait that long to get the UFOC document. Instead ask for it right away. It will provide useful information on the company's whereabouts and history. Look out for item number 20 in the document as it lists the franchisees who have left the organization. If the number is unacceptably high, there is something fishy. Item 3 in the document is also crucial as it provides a complete 10 year record of every piece of litigation made in opposition to the company. Also check item 19 to understand if the company is reporting the projected earnings of its franchisees. As per work ethics, the company is not allowed to project its franchisees' earnings. Therefore, scrutinize these sections carefully.

## Chapter 10: The costs to keep in mind

### Chapter 10.a. How much is needed to get started?

As per the IFA (International Franchise Association), a franchise owner can enter into business with an investment under 250000 USD. This is inclusive of fees and other associated expenses. The range may differ from 100000 to 200000 USD. Some franchisees even manage with an investment of 10000 USD initially.

All franchisors are required to detail all fees and expenses in the UFOC document. Most franchisors in their own interest would want to see their franchisee succeed. Therefore they usually like to see a liquid asset worth approximately 200000 USD in the franchisee's account.

Some of the fee details are given as below:

- Franchising fees may vary between 15000 to 30000 USD.

- Building rent may range between 1200 to 6000 USD in the first three months
- Building repair, improvement and construction expenses range up to 20000 USD
- Equipment to operate the business can cost between 5000 to 30000 USD
- Furnishings cost up to 40000 USD
- Signage costs between 2000 to 7000 USD

## Chapter 10.b. Figure out if you can afford a Franchise

To be able to determine if you can afford a franchise or not, you need to take an objective look at the costs involved. The startup costs for a franchise can range anywhere between 20000 USD to even over 1 million USD. This will depend on the kind of business, the kind of store you wish to set up, furnishings, equipment etc. The more you spend on each of these, the more the overall costs.

There are several kinds of franchising fees as listed below:

- Franchise fees – The costs for these could range between 4000 to 20000 USD
- Royalty fees – This works out around 3 to 8 percent.
- Working capital – This may involve payment of first and last month's payment on rental agreement, in addition to a security fee.
- Location expenses – This can be around 50 to 100 USD per month.
- Equipment expenses – This depends on the kind of business. You can get equipment loans from banks.
- Initial inventory – You might need a two-week supply of inventory.
- Signage – Most of the external signs although attractive can prove to be very expensive.
- Advertising fee – This varies on a regional or a national basis and also depends on the brand value of the organization.

## Chapter 10.c. Franchising fees: What they cover

The initial investment costs associated with a franchise include the franchise and royalty fees. However, these are ongoing and continue during the tenure of the relationship. To understand how much you will be gaining in terms of return from the invested amount, you need to check item 11 of the UFOC packet. This gives a clear idea of the services the franchisor will provide. Therefore you can do a comparison of the amount invested versus the services provided by the franchisor.

- **Franchise fee** – Is the initial down payment made and provides the franchisee the right to the store, the right to the brand name as well as a host of other benefits.

- **Royalty fee** – This is paid in installments and it provides an assurance of the ongoing relationship between franchisee and franchisor.
- **Miscellaneous fees** – These include other fees such as advertising fees for all advertising campaigns to promote products and services, supply costs for all the equipment and supplies to your store, payroll for all the people working under you in the store as well as many other costs.

## Chapter 10.d. The nuances of financial statements

While choosing a prospective franchisor, it is essential to do a thorough research to find out if the company is stable financially and will be able to provide the return on investment etc. There are many basic criteria to look out for such as the growth of the organization, the net earnings of individual franchisees as well as the quality of services offered etc.

However, apart from these basic criteria, you also need to understand the financial situation of the company in detail. For this purpose, the UFOC document again comes handy. The UFOC is required to submit all information such as the franchisor's financial status, history of earnings as well as a host of other information.

To understand better, there are certain sections in the UFOC form to look out for. Item 19 lists down the projected earnings of its franchisees. Unfortunately most franchisors do not take the time out to fill this section. However you can get information from many other sources. Item 21 lists the balance sheets over the last 2 years of the company. It also includes the cash flow and earnings statement of the last 3 years. The stockholders' equity is also listed under this item. Try scrutinizing the balance sheet to get an understanding of the company's current net worth. Also find out if the franchisees are doing well everywhere in all locations or only in certain areas. If the franchisor is making money from its royalty fees, then ideally the numbers should be rising every year.

## Chapter 11: Will your credit history impact Franchise loans?

Most often than not, franchisors are going to check credit histories of potential franchisees in the best interest of the organization. Therefore, if a franchisee has a bad credit score, it may hamper the process of buying a franchise, however it need not rule out the possibility altogether.

For example, if a person has filed for bankruptcy earlier, then depending on the number of years ago it was filed; it can significantly affect the purchase of a franchise. If for example the bankruptcy was filed 7 years ago and since then if there has been a clean financial history with a conscious effort to restore the financial situation, then there is a chance of being able to purchase the franchise.

On the other hand, if the bankruptcy has been filed more recently, it may mean it becomes more difficult to purchase the franchise.

If an entrepreneur does not have the required amount of finances needed to invest in a franchise, it may mean he or she needs to take a loan or even try multiple financing options, something that necessitates maintaining multiple credit lines with various vendors. This too requires a good credit score.

Also many times, franchisees will need to invest money in the location of the store and while going through the rent or lease agreement credit history plays an important role in being able to get the land or property.

While generally a good credit score does go a long way in enhancing one's chances of success at a franchise opportunity, it need not mean closed doors for someone with a poor credit rating. Some franchisors prefer to give their investors a benefit of doubt and if the financial blip has happened many years back it is often overlooked.

## **Chapter 12: SBA Loans – one of the best options**

In the US, the government has always encouraged the creation of a healthy and competitive entrepreneurial economy. That is the primary reason many financial institutions have been set up to finance small businesses. The most prominent among these is the SBA or the Small Business Administration. It provides consultation as well as financial assistance but its most popular feature is the guarantee it provides in its loans.

The loans funded by SBA cater to both those who are expanding their operations, as well as those who are starting out for the first time. There are two types of SBA loans – the 7(a) and the 504. The 504 is good for the goal of acquiring property. It can also be used for making building or street improvements in the locations of the franchise stores. It can also be used to construct new facilities, procure more equipment, modernizing existing facilities as well as conversion of existing facilities. Unfortunately the 504 in spite of all its advantages and uses, does not cover working capital or inventory neither does it cover refinancing options and debt repayments.

The 7(a) loan covers all aspects that are not included under 504. The proceeds from this loan can be used for construction of new sites, as well as used to procure new machinery and equipment, furniture and other ongoing supplies needed to keep the business going.

The best feature of the 7(a) loan is the fact that its proceeds can be used to cover expenses associated with starting out, that otherwise franchisees cannot afford. This loan provides for long term as well as short term capital requirements.

While borrowing from the SBA, make sure to approach a bank which is included under the SBA's "preferred list". Preferred banks are able to carry out the transaction faster because they possess the authority to make the decisions credit etc. The other banks which are not preferred will need to submit all documents to the SBA for approval. This can take an undue amount of time.

## Chapter 13: Franchising Myths uncovered

While franchising may seem like a highly viable option as far as startups go, this high-impact low-risk opportunity has been shrouded with many myths. Myths that have held back even the most daring of entrepreneurs. In this article, we try and break some of the myths that surround franchising.

The first predominant myth that is doing the rounds is – 'The more money you spend the more you're going to get'. Unfortunately, while this may hold good for most of the commercial products we purchase, it need not hold true for franchising. In franchising, what counts is to spend you money smartly. By that we mean, spending minimal amounts intelligently enough with a calculated approach. That will ensure you not only get you returns but probably much more than what you'd hoped for! A classic example is the consulting business where the amount of investment required would be substantially lesser as compared to a standard shop offering a particular product. While the associated costs are far lesser, the returns could turn out to be far more and much more profitable in the long term. Another example could be of a pizza chain. While each of the individual outlets would have cost the same to set them up, some of them perform better than the others. Therefore, the conclusion is that in the world of franchising, there is no direct correlation between the money invested and the profit gained.

Another myth is that only food chains turn out to be successful franchises. That's not true. There are millions of business opportunities that could be franchised. Take the example of consulting services. There are probably more guaranteed returns in a consulting opportunity than a restaurant chain.

The third myth is that there are limited finance options like SBA. Once again that's not true. There are many other finance options doing the rounds such as home equity loans, a government approved IRA rollover program or even an ERSOP.

The best way to go about setting up a franchise is to separate the myths from the facts. That's the only way to get clarity on the market landscape and stay clear of misconceptions.