

## February 2012 Newsletter



If you are not on our Constant Contact mailing list for monthly news and event information, you missed this month's newsletter information about President Obama's SBA cabinet position and the IRS on-line tax tip for small businesses and independent owners. Email SCORECPA today to be on our Constant Contact list. Your name will never be sold or transferred.

### Owning your own business – Learn more about Franchises



**John Tubridy, Franchise Advisor**, (FranNet) Franchise Network of Pittsburgh will discuss franchising in depth at the February 21, 2012, SCORE Central PA, Beyond the Basics seminar, **"Owning Your Own Business"** at the Nittany Bank (near the Nittany Mall) in State College, PA, from 10am-Noon. Tubridy will discuss franchising from several important perspectives:

- What is a franchise business?
- Benefits to you as franchisee
- Four Step Franchise Research Plan
- Dos and Don'ts
- Franchise regulations

FranNet has been in the business of helping entrepreneurs since 1987. It is also a resource and strategic partner of SCORE/SBA/SBDC.

FranNet consultants work individually with clients who are interested in purchasing a franchised business or just want free expert assistance reviewing franchise opportunities and general business startup assistance. FranNet consultants can assist you with:

- Understand the pros and cons of owning a business.
- Receive your assessment with their exclusive matching profile process.
- Determine the best business for your unique goals and skills.
- Build a business and invest in yourself.
- Meet your high expectations and implement a plan.
- Use a process that makes sense and has helped thousands of people.
- Receive expert advice 100% free.

Research is the key to any sound decision. In a sense, franchising is a business opportunity with the primary purpose of risk minimization. Every study ever done on the success rate of new (non-franchise) business startups concludes the same thing. Starting up a new business is very risky. Most studies show that more than 90 percent fail within three years. The primary reason that the failure rate is so high is the learning curve of operating that specific type business. Unfortunately, the market place is not very tolerant of the inexperienced beginner trying to learn how to operate a new business. If you can't compete in the marketplace, you can lose your money, your credit, your home, your reputation and sometimes even your family. Failing in business can be a horrible experience. Unfortunately this happens to thousands of people every year in the United States, and it can be avoided. Unless you have considerable experience in the specific type of business that you are considering going into, it is very probable that you will fail.

Business format franchising is as close as you are going to come in today's marketplace to a guarantee of success. All of the studies done have found that franchised new business startups rarely fail and, when they do, it is typically because the franchisee did not stick to the franchisor's systems. There is a learning process involved in all human endeavors.

This learning process requires trial and error wherein knowledge is gained by trying and failing again and again until you eventually succeed. This process is generally called the learning curve. In the context of franchising, the franchisor has already gone through the learning curve and has learned the secrets of success for the specific business. In business format franchising, all that has been learned by going through the learning curve is transferred to the franchisee. This is fundamentally why you buy a franchise – to minimize risk and give yourself the best possible chance to succeed. **Avoid detours. Take a better route.**

It is also prudent to buy a franchise because the investment can be thoroughly researched before any significant expenditure is made. With a new business startup (non-franchise) you are always operating in the dark. No matter how much research you do, it is very difficult to get a handle on so many aspects of the new business. With a franchise, the franchisor can provide a wealth of information about the business opportunity – from how to prepare a pro forma to the best personality traits for the business. But the most important information comes from the existing franchisees. With a good systematic approach, you can get answers to nearly all the key questions such as:

- Do you feel that you were properly trained?
- How long did it take before you broke even?
- What is your annual return on investment?
- How do you feel about the day-to-day duties of the business?
- If you had it to do over, would you do it again?

Another very important reason to buy a franchise is due to its basic nature. Franchising inherently leads to rapid growth, because the franchisees provide the expansion capital. There are few restraints to growth in franchising. As a franchise system expands into hundreds of units, many positive things begin to happen. The name begins to become well known because people see it everywhere. Most people associate size with success.

The bigger the franchise, the better it must be. The large number of units enables the franchise to advertise heavily, which tends to increase sales. A synergy begins to be created in which success begets success. The franchise begins to squeeze out competition through its sheer size. The franchise can buy products in large quantity at significant discounts, which it passes on to the franchisees. The synergy just grows and grows.

A Gallup Poll of franchisees found that more than 94 percent considered themselves successful and that more than 75 percent would buy their franchise again if they had it to do over. The same poll also found that the average pre-tax gross income was \$124,290.

In summary, the primary reason you should buy a franchise as opposed to starting up a non-franchise new business is to **minimize risk and enhance your chances of success.**

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## Franchising: An old economic concept that benefits you today

**F**ranchising is not modern practice. Actually, the concept goes back to the middle ages when the term “franchise” was derived from an Anglo-French word meaning “privilege” or “freedom.” During the middle ages, the local sovereign or lord would grant the right to hold markets and fairs, operate the local ferry or hunt on his land.

This concept was part of the king’s granting of franchise for all manners of activity from building roads to breweries. In economic terms, the kings or the lords were granting the right to a monopoly for a certain type of commercial activity. As time passed, these protocols turned into regulations governing franchises which became part of European Common Law. History tells us that franchising spread to many European countries and elsewhere. One example took place in Germany during the 1840s. German brewers granted franchises to certain taverns, giving them exclusive rights to sell their brew.

America’s first franchise was I.M. Singer & Company in 1851. Isaac Merritt Singer with New York lawyer Edward Clark established the company, later known as the Singer Manufacturing Company. Singer wrote franchises (contracts) for their sewing machines. By the 1880s, cities in America began to grant monopoly franchise agreements to various companies. In time, these companies provided street car services and utilities for water, sewerage, gas and later electricity.

As the 20<sup>th</sup> century appeared, other commodities utilized franchising. Soft drink (soda) bottlers, oil refineries and automobile manufacturers began to grant the rights to sell their products. At this stage of franchising, the process granted not only the selling, but also distributing the products. Today this is called “product franchises.”

### Modern era of franchising begins

After World War II another form of franchising became the dominate market model. It was known as “business format franchising.” This type or model includes an arrangement whereby the franchisee not only gets the right to sell goods or services, but also gets the company’s quality control, accounting systems, operating procedures, advertising schemes and promotions, training and other tangible operational techniques. This type of franchising created a boom during the post-war period when millions of U.S. servicemen and women returned and the baby boom era began. So did the expansion of real estate brokerages, auto dealers and rentals, fast food industries and restaurants.

### Problems and abuses require controls

Problems and some abuses in franchising were beginning to surface during the boom decades of the 1960s and 70s. Poor management and lack of capital were two of the biggest problems, but fraud was

also evident when certain franchisers took people’s money and absconded

During this time period, the franchise industry recognized that unless there were organizational changes, the industry would not survive public and political scrutiny. The International Franchise Association (IFA) was created in 1960. It is the oldest and largest franchise organization based in Washington DC. Professionalism through a code of ethics, training and standards setting is the basis of the organization’s goals to improve the industry. The IFA works closely with governmental agencies and Congress to improve the industry.

### State action and the Federal Trade Commission (FTC) Franchise Rule (16 C.F. R. Part 436)

States began to regulate franchises. The State of California was the first to enact regulations in 1971. Other states also took up the cause. In 1978, the FTC enacted the Franchise Rule requiring that all franchisers submit to all potential franchisees a document called the Uniform Franchise Offering Circular (UFOC), before receiving money.

The UFOC provides very detailed information on the franchise company, such as its history, officers, litigation matters, audited financial information and the franchise agreement. The agreement is the contract between the franchiser and the franchisee and a current list of franchises with owner’s names and telephone numbers. Today this document is not known as the UFOC, but the Franchise Disclosure Document (FDD). The FDD was ordered by the FTC in July 2007.

The FDD is a legal document which is presented to prospective buyers of franchises in the pre-sale disclosure process. Under the Franchise Rule, disclosure compliance obligations as to who must be the one to prepare the disclosures, who must furnish them to prospective franchisees, how franchisees receive the disclosures and how long franchisees must have to review the disclosures and any revisions to the standard franchise agreement.

Today there are 14 states called “registration states.” Each has their own requirements before a franchiser is allowed to sell franchises in their state. Pennsylvania is not one of those states. Pennsylvania is a Franchising non-registration State. It is not necessary to register your franchise in Pennsylvania. You are required to issue the FDD (Franchise Disclosure Document) as required by the FTC, 14 days prior to accepting any money or commitment from a potential franchisee.

Franchising today offers a great opportunity to those individuals who truly want to realize their dream and go into business for themselves in a regulated environment.

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## Business Improvement Workshops Always FREE for SCORE Clients

**Business Basics** Tuesday, February 14, 2012, SCORE Central PA will offer both a morning and evening Business Basics workshop. One at the Nittany Bank, near the Nittany Mall in State College, PA, from 9:30am–Noon. The other at Coble Creek Manor Clubhouse (off Blue Course Drive in State College, PA) 7pm-9pm. Business Basics is an A to Z topical workshop on either starting a new business or getting a tune-up in your existing business. Workshop includes exercises in fine-tuning your goals and objectives, plus a free CD on business resources—please register. Non-SCORE clients workshop fee is \$20.00, if you pre-register, cost \$10.00. Check deadline. [Information and REGISTRATION](#)

**Beyond the Basics** Tuesday, February 21, 2012, “[Owning your own business](#)” A FREE WORKSHOP [Information and REGISTRATION](#)

- [Index](#) of all articles both in Constant Contact and Chapter Newsletters
- [SCORE CPA Business Directory](#) : Accounting, Banking, Bookkeeping, Business Consulting, Energy, Franchising, Health-Fitness, Insurance, Investment, Media, Photography, and Remodeling/Custom Builder.