



TOP 12 THINGS A PROSPECTIVE FRANCHISEE SHOULD LOOK FOR IN OR ABOUT A FRANCHISE AGREEMENT

This paper reviews 12 important features in or about a franchise agreement. There are other important features, but these 12 are no doubt of great importance.

1. Location/Lease/Territory

The location of a franchise business must be approved by the franchisor and noted in the franchise agreement or a side agreement. The franchisor will also have the right to approve a lease of the location, unless the franchisor is leasing itself and then sub-letting to the franchisee.

You will also want the franchise agreement to include a “protected territory” around your location within which the franchisor will agree not to allow a second location to be opened. Sometimes, the franchisor will reserve the right to open a second location in the territory, but giving the franchisee the first right of refusal to take it on.

2. Term/Renewal

The term and renewal term of the franchise agreement must coincide with the lease. For example, if the franchise agreement is for a term of 10 years plus a renewal term of 10 years, then the lease should also be for the same term and renewal term. The franchise agreement will contain conditions for renewal which must be fulfilled by you. One of these could be costly, namely a requirement to renovate, your franchise location to comply with the franchisor’s then-current specifications.

3. Operations Manual

You should try to review a copy of the manual before you sign the franchise agreement, which will say that the manual forms part of it. Note, the franchisor will reserve the right to revise the manual from time-to-time to keep up with market conditions and to improve administrative procedures.

4. Payments

The franchise agreement will contain several payments that you will be required to make; these include an initial fee (which may or may not include training), as well as monthly royalties and advertising fund contributions. All of these will be based on a percentage of gross revenue, where “gross revenue” is defined in the franchise agreement.

5. Training and Support

You will receive a franchise disclosure document at least 14 clear days before you are required to sign a franchise agreement. The FDD will contain details of training and the franchise agreement itself will contain these details too, as well as details of on-going support to be provided by the franchisor. Training will normally be required in the city of the head office of the franchisor. The related costs of travel, accommodation, meals and employee remuneration will all be borne by you.

6. Website/Subsite

The franchisor will operate the website and will have the right to revise it from time to time. You should review the franchisor's website before signing the franchise agreement to see whether it is likely to be effective in attracting business from the public. Also, you should check the franchise agreement to see whether it allows you to share in sales being made over the franchisor's website. Often, the franchisor will have an "intranet" site which is private (only open to franchisor, its franchisees and perhaps suppliers, but not the general public). An intranet can provide a very useful communications conduit for you and other franchisees.

7. Advertising Program

The franchisor will control the advertising program and it will be funded by advertising fees payable monthly by you and other franchisees. You should learn some details about the advertising program, including what media (print, internet, radio, TV, etc.) are being used by the franchisor. Also, the franchise agreement should provide that you will receive an annual accounting of monies paid into and expended by the advertising program.

8. System Changes

The franchise agreement will entitle the franchisor to make changes to its franchise system to keep up with the marketplace for similar businesses. There is a trust factor here, namely that you will count on the franchisor to keep up with market trends and hopefully lead them.

9. Trade Marks

In a mature franchise system, its trade marks will be well-known to the public and you will be entitled to share in the public goodwill by having a license to use them under the franchise agreement. If the franchise system is new, the trade marks will very likely only be pending for registration and will not have attracted a lot of goodwill so far.

10. Sale/Transfer by Franchisee

The franchise agreement will contain conditions upon which you may sell your franchise to a third party. The franchisor will typically be entitled to review the financial strength and experience of the proposed purchaser and will require that he/she take and successfully complete the franchisor's initial training program. The franchisor may have a right of first refusal to buy your franchise itself, on the same terms as an offer you receive from a third party which you are willing to accept.

11. Default/Termination

The franchise agreement will contain a list of “events of default” which, if you commit one or more of them, may entitle the franchisor to terminate your franchise. You should ensure that defaults that are minor, allow you time to cure them; for example, 5 days to cure a late payment. The franchise agreement will also contain “post-termination covenants” including an obligation not to compete with the franchise system for a period of time (often 2 years) and not to solicit any employees of the franchisor or any other franchisee. These covenants will strictly limit a franchisee’s ability to continue in the same business after you have been terminated.

12. Franchise Disclosure Document

A Franchisor must provide you with a Franchise Disclosure Document at least 14 days before you are asked to sign a Franchise Agreement, if your Franchise will be located in one of the franchise-regulated provinces (BC, AB, MB, ON, NB or PEI).

The Franchise Disclosure Document will have attached to it a copy of the franchisor’s form of franchise agreement, as referenced above. It will also have attached a copy of the franchisor’s latest annual financial statements which you should review with your accountant to determine the financial strength of the franchisor. Further, the FDD will contain a list of current and past franchisees, including their contact details and you should contact several of them in each category to inquire about the quality of the initial training and on-going support provided by the franchisor and other matters which may be of interest to you.

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[Mr. Rogers has practiced franchise law for over 30 years; 8 of those years were spent practicing in Toronto, Ontario, where he became familiar with the requirements of franchise legislation in Ontario and other franchise-regulated provinces. During those 8 years, he prepared numerous Franchise Disclosure Documents and Franchise Agreements covering Ontario and other Provinces. Since then, he has prepared forms of FDD and FA for all 6 franchise-regulated provinces.]