

The Basics of Franchising

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- **Introduction**
- **Why Franchise?**
- **Franchise Disclosure**
- **Franchisee Rights and Responsibilities**
- **The Franchise Agreement**
- **Sources of Disputes**
- **Other Legal Concerns**

- **ELEMENTS OF A FRANCHISE**

- Grant
- Payment
- Control

- **TYPES OF FRANCHISES**

- Unit
- Area Development
- Master Franchising

Why Franchise?

- Expansion alternative which requires less capital because the franchisees finance their businesses
- More complex network with fewer employees
- Better return on capital even if corporate stores were more profitable

Why Franchise?

- Easier to expand within larger geographic area
- Foreign expansion easier because compliance is franchisee's responsibility
- Less supervision means distance is less of a problem
- Ideal method for expansion when corporate network has reached its limit

Why Franchise?

- Franchisee as business owner will be personally invested in the success of the business
- Strength in numbers means
 - Larger network
 - Better purchasing power
 - Access to better locations
 - Advertising contributions

Why Become a Franchisee?

- Safe, fast way to become a business owner
- Benefit of franchisor's experience / mistakes
- Established goodwill
- Better access to better locations
- Group buying power

Downside?

- Loss of control
- Putting the value of your brand in someone else's hands

Is Your Restaurant Franchiseable?

- Is your product or service unique enough to stand out in a crowded field?
- Will it be manageable for someone else to copy that model under your supervision, or does it only work under your direct implementation?

Is Your Restaurant Franchiseable?

- How many corporate-owned units do you have, and how are they doing financially?
- What are your financial resources?
- Trade-marks?
- Where will you find franchisees?
- How's your team?
- **CAN THE CONCEPT BE STANDARDIZED AND REPLICATED?**

- **A disclosure document must be provided to prospective franchisees at least 14 days before the earlier of:**
 - any payment
 - the signing of any franchise-related agreement
- **The *Arthur Wishart Act* details what must be included**
 - Material facts
 - Relevant Documents

- **Business background**
- **Director and officer names and backgrounds**
- **Convictions or pending charges**
- **Advertising Fund**
- **Personal participation**
- **Intellectual property-trademarks**

- **List of Franchisees**
- **Earnings Projections**
- **Operating Costs**
- **Financial Statements / Opening Balance Sheet**
- **Certificate**

- **Material Change Statements-**
 - Prompt and accurate
- **Permits and licenses required (Ontario)**
- **Varies in each province**

- **Franchise Agreement**
- **Lease/Sublease Agreements**
- **Operating manual (index)**
- **General Security Agreement**
- **Confidentiality Agreement??**

- **Franchisor's future plans**
- **Information about other franchisees (apart from anything disclosed in litigation, or a list of present and former franchisees)**

- **3.(1) Every franchise agreement imposes on each party a duty of fair dealing in its performance and enforcement**
- **“fair dealing” includes acting in good faith and in accordance with reasonable commercial standards**
- **Can be “self interested” but consider other parties interests**

- **The *Arthur Wishart Act* also provides some other basic rights of franchisees**
- **Damages in case of breach**
- **Right to rescind within 2 years if no disclosure**
- **Right to associate**
- **Franchisee rights can't be “contracted out of”**

- **The *Arthur Wishart Act* provides franchisees with the right to associate and prohibits franchisees from interfering with that right**
- **Better to associate *before* a dispute arises...**
- **Useful for:**
 - Gathering and disseminating information
 - Facilitating or reacting to changes
 - Reducing misunderstandings

- What franchisees must do/must not do
- **it includes:**
 - Term
 - Renewal rights
 - Territory
 - Exclusivity

- **Initial Fees**
 - Cost of the opportunity
- **Continuing Royalty**
 - In return for ongoing rights
 - % of Gross sales
 - Paid weekly / monthly

- **Training**
 - Key employees before opening
- **Operational Assistance**
 - Franchisor may provide experienced person at first
- **Advertising - local and general obligations**
 - Local
 - General fund

- **Accounting – records, disclosures, and 3rd parties**
- **Insurance – franchisor picks, franchisee pays**
 - **Subject:** limiting liability for property, employee or product related claims
 - **Amount:** franchisor can dictate extent of insurance
 - **Insurer:** franchisor can dictate list of acceptable insurers

- **Restrictive Covenants**
 - Prevents competition
 - During and after term of agreement
- **Sale of the Franchise**
 - Assignment
 - Transfers
- **Termination**
 - Before opening
 - After opening

- **Review with a franchise lawyer**
- **Things to watch for:**
 - Severe/unfair default provisions
 - Excessive payments to franchisor for support, renewal, transfer fees, training...
 - Resale provisions
 - Consistency

- **Concept deficiencies**
- **Inappropriate franchisee-business match**
- **Poor location**
- **Communication breakdown**

- **Tax consequences**
 - Can't deduct many start-up costs
 - But can deduct many costs of running the business
- **May be eligible for the “Small Business Deduction”**
 - Reduced tax rate on the first \$300,000 income

- **Withholdings and Taxes**
 - Workers Compensation Insurance
 - Workplace Safety Insurance Board Registration and Premiums
 - Employment Insurance
- **Regulation**
 - Occupational Health and Safety Act
 - Employment Standards Act 2000

- **Human Resources**
 - Hiring and firing process
 - Compensation and benefits
- **Liability**
 - Franchisor-franchisee relationship is one of the independent contractors
 - Franchisor must supervise franchisees or clearly distance himself as separate operator to avoid vicarious liability

- **Location is very important**
- **Premises can be owned by**
 - Franchisor
 - Franchisee
 - 3rd Party – most common
- **Important especially if franchisee defaults**
- **Assignments of leases may affect right/responsibilities**

- **Lease must contain certain terms regardless of who negotiates it:**
 - Use Clause
 - % Rent
 - Records
 - Radius Clause
 - Leasehold improvements
 - Insurance
 - Assignment

- **Liquor**
- **Smoking**
- **Food Service Licensing**
- **Food Safety**
- **Allergies**



Any questions?

Thank You

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