

FRANCHISE



WHAT IS A FRANCHISE?

Definition: A license granted by the franchisor to operate a particular business using the franchisor's name, where the franchisor provides assistance to the franchisee, exercises continuing control and received periodic financial consideration from the franchisee for the services provided.

The first modern day franchise was developed by the Singer Sewing Machine Company in the United States in the 1860's but it was not until the 1970's that the system became better known in New Zealand with the growth of fast food chains such as KFC and McDonalds.

WHY FRANCHISE?

- Business surveys show a very strong success rate for franchised businesses.
- Comparisons of independently started businesses indicate that 80% of these fall through within five years of commencement. Franchised businesses tend to have the opposite success rate with more than 80% still operating five years after commencing operation.
- If you already operate a business, would you rather pay employees to sell your products or services or have them pay you for the right to sell them?
- If you want to go into business, would you rather do it all by yourself or with the support and goodwill of an established company behind you?
- Who would employ people in today's competitive economic climate when they can arrange their marketing systems so that people (franchisees) will pay for the rights (franchise) to sell their products or services on a committed and very controlled basis.



THE FRANCHISOR

In order to succeed as a franchisor or a franchisee it is necessary to consider the advantages and disadvantages of involvement in a franchise system.

ADVANTAGES FOR THE FRANCHISOR:

- Low capital expenditure. Franchising is an excellent method of expanding your business with a limited amount of ready capital.
- Personal commitment and motivation from franchisees is greater than from employees.
- Reduced daily involvement. It is a method of obtaining conscientious and dedicated personnel who work hard to safeguard their investment.

DISADVANTAGES FOR THE FRANCHISOR:

- Loss of ownership. The franchisee has a license to operate the business. Usually this prevents the franchisor from competing in the territory in which the franchisee operates.
- Lower profits. The nature of the relationship between the franchisor and franchisee means that profitability considerations need to have regard to both parties. As a rule of thumb, 90% of the profit should go back to the franchisee.
- Interdependence. A large amount of management input from the franchisor is required. You have responsibility for other people's future.
- Substantial management and personnel skills are necessary to persuade the franchisees to follow the franchisor's directions for the sake of uniformity within the system.

THE FRANCHISEE

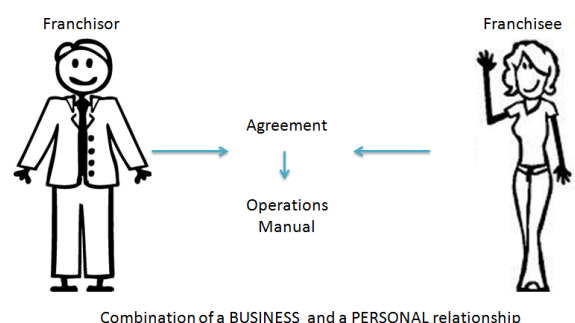
An advantage for the franchisee is the opportunity to share some of the benefits of a large business. Franchising also offers the independence of a sole proprietor.

ADVANTAGES FOR THE FRANCHISEE

- An established reputation
- A known brand name and image
- Skilled management
- Large scale advertising which is usually paid for by an advertising levy
- Economies of scale

DISADVANTAGES FOR THE FRANCHISEE

- Royalties/fees are payable to the franchisor
- Territorial restrictions may apply
- Contractual constraints and the degree of control exercised by the franchisor may be onerous
- Management assistance may not materialise
- A lack of ownership of the goodwill or intellectual property rights associated with the franchise system



FRANCHISOR – WHAT IS REQUIRED?

- Are you honest and ethical?
- Are you financially stable?
- Are you committed to franchising?
- Has your format been thoroughly tested and refined in the same market conditions into which your franchisees are to trade?
- Can you provide your franchisees with a “total package” to enable them to start and run the business?
- Are the costs of franchising manageable and the returns worthwhile to both franchisor and franchisee?
- The format should be simple, easy to replicate and teach. Most successful franchises do a limited number of things very well.
- A pilot scheme should be operated.
- An operations manual should be developed, the systems and business methods must be capable of being passed on.
- A franchise agreement written.

FRANCHISE AGREEMENT

The franchise agreement sets out the contractual position between the franchisor and the franchisee. Matters addressed in the agreement may include the following:

- What exactly is the franchisor allowing the franchisee to do.
- The length of the franchise and renewals of term.
- Obligations of the franchisor to the franchisee.
- Obligations of the franchisee to the franchisor.
- Where can the franchise operate geographically
- Is the franchise agreement exclusive or non exclusive.
- What payments are required and when are they to be paid to the franchisor.
- Does the franchisor require the franchisee to perform to a given budget.
- What training does the franchisor provide and at whose cost.
- The franchise agreement usually requires the franchisee to adhere to the Operations Manual.
- Transfer/assignment – how is this done and what restrictions are imposed.
- What provisions apply for non completion and restraint of trade and are they enforceable.



FRANCHISEE QUESTIONS TO ASK

- Do you see yourself being involved in the franchise business for the next five to ten years?
- Do you have the tenacity and persistence to succeed?
- Are you prepared for the long haul?
- Are you a team player who is able to adhere to a system?
- Do you have sufficient money available?
- Do you possess a knowledge of the territory involved?
- Do your personal/business goals suit franchising?

SUCCESSFUL RELATIONSHIP BETWEEN FRANCHISOR AND FRANCHISEE

Franchise arrangements can work extremely well for the mutual benefit of the franchisor and franchisee. Problems tend to arise when the aims of the parties are opposed. The following can help to build a successful relationship:

- Well matched personalities
- Common goals and desires
- Respect for each other’s business ideas and improvements to the franchise system
- The feeling of belonging to a winning team
- Realistic profit motives



WARNING SIGNS

- No franchise package
- Inexperienced franchisor
- Franchisor relying on sub-franchising to finance “master” franchise
- Franchisor not allowing a reasonable profit to the franchisee
- Brochures claiming estimated profits and success stories that cannot be substantiated
- Advertisements giving only post office boxes for reply
- Promises of being able to get rich quick with little work
- Franchisor not providing a copy of the agreement unless a non refundable deposit is paid
- Franchisor refusing to disclose financial details
- Large up front payments
- Payments required to the franchisor for advertising with no provision in the Franchise Agreement which assures the money will be spent on such advertising
- Non disclosure of details of other franchises
- Unsuitability of franchisee by virtue of temperament or training
- Inability of franchisee to accept the regimentation of the franchise system

TRADEMARKS

A trademark is used to indicate the origin of a trade source of the goods/services to which it is applied or in relation to which it is used. Registration of a trademark is not compulsory in New Zealand but it is strongly advised.

A trademark is a valuable business asset, arguably a business’s most important asset. Many New Zealand companies are not putting the value of their trademarks in their balance sheets to better reflect shareholder value in a company.

Registration of a trademark is obtained under the Trademarks Act 1953. Registration provides the proprietor of a trademark with the exclusive right to use and control of the trademark throughout New Zealand for the goods/services for which the trademark is registered.

The Trademarks Act 1953 gives a registered proprietor a statutory right to sue for trademark infringement. This means that a registered proprietor may take a case to the High Court to prevent any infringement or use of the mark by any other person or company.

The right to use a trademark may also be franchised or licensed to other users.

WHAT ARE THE CATEGORIES AVAILABLE?

There are 42 classes of goods and services. Registration is effected on a class basis, eg. clothing, headgear and footwear is classified as Class 25. The goods classes are Classes 1 – 34 and service classes are 35 – 42.

WHAT CAN I REGISTER?

In order for a mark to be registerable it must meet the requirements of sections 14 or 15 of the Trademarks Act which in essence, is the requirement that the mark is distinctive.

The primary function of a trademark is to identify, in other words, to distinguish goods or services from one seller or group of sellers from those of their competitors. Distinctiveness is the most important attribute of a trademark from which the trademark derives its marketing value, effectiveness and legal strength.



WHAT TO AVOID

In developing a trademark it is advisable to avoid the following:

- Family surnames
- Initials
- Geographical names
- Descriptive or laudatory terms
- Any name which could be confused with any existing name
- Those names which carry any negative connotations in English or in any other language in which the name is to be used



HOW MUCH DOES IT COST TO SECURE TRADEMARK REGISTRATION IN NEW ZEALAND?

In the vicinity of \$1,000 per trademark class including search costs but excluding the application fee of \$112.50. This is based on the assumption that the application is relatively straight forward.

HOW LONG DOES IT TAKE?

Once an application has been filed, The Intellectual Property Office issues a report giving the applicant six months to place the application for acceptance. Once the application is in order for acceptance, it is advertised in the Intellectual Property Office Journal where third parties have three months from the date of the advertisement to oppose the grant of the registration. Accordingly, the entire process takes approximately one year from filing the application to receiving a registration certificate. The rights provided by a registration are back dated to the date of the application.

HOW LONG DOES THE REGISTRATION LAST?

The rights granted under a registration are granted for a period of seven years from the date of application and are renewable at fourteen year intervals thereafter.

KEY THINGS TO NOTE

In attempting to develop a legally protectable trademark the following should be noted:

- The more descriptive the name, the more difficult it will be to prevent its use by others. The reasons for this: they are indistinguishable from similar terms that are already used or soon to be used by the competition and they expose the goodwill accumulated by the company to easily capture the competition.
- A stubborn preference for descriptive names indicates the promoters select trademarks on the basis of their informative value, without consideration to the marketing and legal consequences.
- Choosing an appropriate logo and/or graphic support can reinforce the trademark. Like trademarks, logos can be an enduring asset. They should therefore be distinctive. If the legal status of a trademark is weak, a business can enhance the protectability of a trademark by the addition of a distinctive logo or graphic which may be registerable as a trademark.
- A trademark registration gives the registered proprietor of the trademark the exclusive right to use and control the trademark throughout New Zealand for goods/services for which the trademark is registered.
- Registration of the company name does not confer any proprietary rights to a name.

THE PROCESS

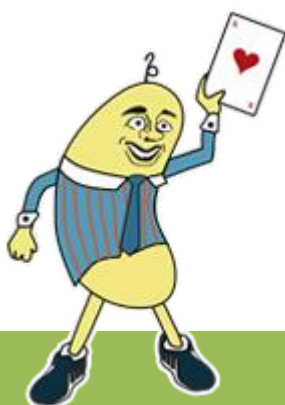
- Effect a search of the trademark and Companies Office registers to ascertain the availability for use of the trademark.
- Assuming the search is clear, file a trademark application with the Intellectual Property Office.
- Official action from the Intellectual Property Office issues.
- Submissions filed to overcome Intellectual Property Office's objections.
- Notice of acceptance issues from the Intellectual Property Office.
- Payment of registration fee.
- Receipt of registration certificate.
- Payment of renewal fees

COMPANY NAMES

The Companies Act 1993 requires a company to have a name. A New Zealand company cannot be registered using a name unless the name has been approved and reserved by the Registrar of Companies. Registration of a company name does not confer any proprietary rights in that name.

Prior to applying for a company name approval, it is recommended that a check of the Companies Office register be carried out. The purpose of this is to ascertain if in fact a name can be used. If name protection is sought, consideration should also be given to seeking trademark registration or incorporation of a limited liability company.

Due to increasing awareness and importance of intellectual property matters in trade, it is apparent that consideration to such matters at an initial stage is becoming increasingly important.



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