

PROTECTING YOUR POSSIBILITIES PODCAST WITH LUKE FEDLAM

Episode 50: Franchises – What You Really Need to Know | July 21, 2021

The following is a transcription of the audio podcast recording. It is largely accurate but in some cases it is incomplete or inaccurate due to inaudible passages or transcription errors.

Luke: I'm sports attorney Luke Fedlam, and welcome to the Protecting Your Possibilities podcast. Each conversation we focus on sharing information and having conversations around how athletes can best educate and protect themselves or their life outside of their sport.

Thank you so much for tuning into the protecting your possibilities podcast. I'm your host, Luke Fedlam. And I am pumped for this episode. Today, we are going to talk about franchises. But before we get into it, I just want to share a little bit of the behind the scenes. So this is actually my second recording of this episode. The first one, you know, just so you understand how these podcasts work kind of behind the scenes. The first one I went through and recorded everything was really excited about it really excited about this topic, because so many people have reached out about it. And then I uploaded it to our system and our marketing team, shout out to the marketing team, they do such a great job of making this thing look and sound great. And so I was just like, let me just listen to a little bit of the playback. And I realized that I did not have my microphone plugged into my computer. So I will say I am very excited to do this episode a second time because usually it's just a one and done I've recorded and move on.

And you're hopefully going to get a little bit more of a special episode here. So anyway, let's just get right into it. And let me share with you why I wanted to talk about franchises. So two reasons - one, I really liked to listen to friends and clients and others who reached out about various topics and I've had people reach out about the topic of franchising and asking questions about franchising. And here recently, I've had some clients who have reached out and had a lot of questions about franchises. And one of the biggest misconceptions, I think, when people are considering buying into a franchise, is the idea that oftentimes people think that the business will just run itself, that the franchise will run itself, that when they buy it, they open the doors. And all of a sudden, you know, people come in and people are there working and it just runs itself and they're able to collect a check. And that is just not the case.

And so I want to share this episode, in the hopes of helping people understand a little bit more about the process that they should consider when thinking about buying into a franchise and what that could look like and some tips and some thoughts to help make that a little bit more smooth experience for folks. So, with franchising as it relates to athletes, we've seen a lot of different famous celebrities and famous athletes who have gotten into franchising. You know, Shaquille O'Neal, Peyton Manning, Junior Bridgeman has made a huge name for himself over the years with Wendy's franchises. So, I mean, there are a number of athletes who have done, this and have gotten very successful when it comes to franchising.

But what a lot of people don't realize is all that goes into it on the front end, especially when you're just starting off. And so I want to share some thoughts around what to think about what, what type of due diligence should someone do prior to going down the path of buying into a

franchise? And first and foremost, I think the first place to start is to think about what industry are you even interested in? What type of franchise would you want to purchase? I mean, there are franchises for everything, franchises for tax work that's being done, franchises for food and restaurants, that we're all very familiar with. Franchises for beauty supply and eyelashes. And so I mean, there's so many different kinds of industries that you could focus on when it comes to franchising. And so it's important to really understand kind of what industry interests you, right? What area do you even want to be involved in, because you will most definitely, especially if you're just starting off in franchising, you'll definitely be involved. Because you really want to get to that point that you understand the business, you understand the operations, you understand the financial commitment that you're making when getting involved in a franchise. And so thinking through that, thinking through the industry that you want to be involved in, the area that you want to get involved in, is a great place to just start. And oftentimes people will start thinking about franchises because someone has come to them about getting involved or buying into a franchise. And so then that becomes your first primary and maybe even singular experience.

And so it just sounds like everything sounds great. This is this is awesome. But don't forget people get compensated. People make money off of you making those decisions. So they're going to make it sound great. And we'll get into kind of some of those particulars and ways to protect yourself and think through that. But my, my encouragement to you is to think about research the industry that you want to get involved in. And if you want to get involved in, let's say, food, for instance, then you want to think about, okay, do I want a quick casual type of experience, like, Panera Bread or something like that, where, you know, you get food pretty quick, but it's more casual in dining experience, etc. Do you want just the traditional fast food, the pizza, the burgers, etc? Right? Do you want something that's more of a formal kind of, you know, sit down type of franchise restaurant, the old Charlie's or the Red Lobster is or those types of restaurants, right?

I mean, there are so many different segments, even within the food industry that you'll want to think about and consider. So these are all things to think about, even just when you're starting your process of evaluating, but it gives you the power, right, because now, it's you considering the types of organizations that you might want to affiliate with you reaching out and being able to compare and contrast, as you're considering what potential franchise you might buy into, which is much different than someone approaching you. And then you getting sold on that one particular opportunity in a in one specific industry. So again, just understanding what's out, there is a great place to start.

The next thing that I would I would share with you is to be very careful of people, and these people might be very close to you. You know, maybe it's an advisor, maybe it's a family member, a friend, a teammate, right, that is trying to get you to buy into a franchise, oftentimes, franchises or right the main office, the home office, if you will, of that particular franchise brand, they will pay someone a finder's fee to get someone else to buy into the franchise. And so when you pay that franchise fee at the very beginning, oftentimes that franchise fee will get split or somehow shared with someone who brought you to the table. And you want to know that right away, because you want to make sure that you're at least getting independent and objective advice when it comes to potentially buying into a franchise. So knowing from the very beginning what's the financial arrangement that's in place, for someone who's bringing you to the table of potentially buying a franchise that's so critical for your own protection and your own knowledge and understanding as you're going through the process.

The other thing that I'll share with you is understanding finances is so critical. I mean, this is probably the most important step, or the most important tip that I can give you, when thinking

about an analyzing whether or not you want to get involved with a franchise, you want to understand all of the money, where it comes from, where it goes, how it's spent, who's responsible for it all, you want to know it all right. And so oftentimes what you'll hear on the front end of considering buying into a franchise, you'll hear this idea of the franchise fee, right? So whatever it costs \$50,000 or \$100,000, or 250,000, whatever that franchise fee is that you that you pay in, and then you know you have to pay for equipment. And that's typically what you'll hear from the front end of people that are trying to get you involved and get you to buy into a franchise. But don't forget, you are you are creating an operating business, you're not creating it from scratch, right, that business that franchise already has a brand following it has a brand kind of strength in the industry, it has consumers who are following that business that that brand. And so yes, you may have clients and/or customers already for that particular franchise, but that is that is only, you know, kind of the beginning. So you want to understand kind of the financial piece in totality.

So you're obviously going to have to lease of a location and that location is going to be within the geographic area that you're authorized to open, whatever that franchise is. So you want to understand the lease aspect and it's a commercial lease, which is much different than if you've only experienced leasing from a residential perspective, when you think year by year at a time, you have to understand that these commercial leases are much much longer. And so what happens if your franchise does not succeed, and you're stuck in a 10 year lease or a five year lease and you in the franchise fails after year two, and you've made a personal guarantee on that particular location, real estate location.

So there are some significant financial implications for yourself, you know, personally as well as the business, but you also want to know the operating costs Think about this, you're going to have to hire people, you're going to have to market even though that particular, you know, brand has its own following, and they'll do some marketing for you, you're going to also have to market and promote the business to get customers to come into your store, you're gonna have to hire people, you're gonna have to probably hire, if you're not going to be involved with the business on a day to day basis, you're gonna have to hire some type of General Manager to actually run the business on a regular basis, someone who is responsible in handling the day to day of your business for you. So it's clearly got to be somebody that you either trust, or that you can build trust with someone who has experience in doing this, because they're going to be hiring people, potentially firing people on your behalf or on behalf of the business, they're going to be touching your money every single day, right the money of the business. And so you really want to make sure that you've selected the right person to be able to do that for you. But you're going to want to understand the financials for let's say, a year, a year's worth of financials to understand what are all the costs?

I mean, think about what vendors do I have to have. So if you're someone that opens, let's say if a gym, right, like a physical fitness studio, or a gym franchise, you're going to have people who have to come in to clean, right to clean the equipment and clean the location. Right. So that's a vendor, how much do they cost on a monthly basis, a weekly basis, a daily basis? What about the person, or the company that provides towels, right? So your guests can wipe their sweat off when they're working out? Right? That's a vendor, that's a cost. So there, I mean, there's so many more that I could go into. But these are the kinds of things that you want to really understand.

As you think about potentially buying into a franchise, and so thinking about this is going to be really critical. One of the ways to get some of that information is by looking at what they call the FTD. Right, or the Franchise Disclosure Document. The Franchise Disclosure doc is a legal

document that all franchisors are required to provide to potential franchisees when they're considering buying into a franchise. And when you do that, this document is usually a big document, if you see a really smaller, really thin Franchise Disclosure Doc, there's probably something that's just not right going on. Right. So typically, you're gonna be looking at these that are, you know, 40, 50, 60 pages or more, and you're going to want to read every single page.

And I know that sounds like a lot, but the reason why is because you want to become a student, and ultimately an expert in this particular franchise or this particular business. So understanding how everything works, how the marketing works, how the finances work, the royalty payments, how they work, what the franchisor is going to be responsible for, what you're responsible for, the operations, what your requirements are, what your restrictions and limitations are all of that information, you're going to find in that Franchise Disclosure Document. Now, the FTD is not something that you sign, it's something that will help give you that information.

You'll ultimately end up negotiating, should you decide to go forward, you'll negotiate a franchise agreement, right. And that'll talk all about geography, what you're paying, I mean, all of that information, like your payments on a regular basis, and when they're due, and all that kind of all that, you know, rights of first refusal within either your geographic area, or the geographic areas that are adjacent to where you have locations, right, all that information is going to be in your franchise agreement. But you really want to understand that FTD while you're doing your due diligence on the front end to just see how is this even an opportunity that I want to explore?

The next thing if I could give you a tip here, maybe I'll give you a series of tips that you want to do is you really want to go out and talk to franchisees, right, other franchisees who are doing that particular franchise that you're interested in, right, because here's what's gonna happen, you'll go to the home office, you'll go to wherever the headquarters are for that particular franchise, and they will show you a great time, right? I mean, if you like golf, they'll take you out golfing, if you like a particular sport, they'll take you to a game or whatever it is, they'll wine and dine you because ultimately they are selling you on purchasing they want you to purchase into the franchise. And so in doing that they'll share with you the marketing and the success stories and they'll take you around even to some of the local franchises, and they're usually the franchises that are doing very, very well.

Right, they're oftentimes not going to take you to a franchisee that's struggling, right? So you want to go try to find those franchisees? So yes, go on the site visits, go to the visits, you know, with the successful franchises, ask as many questions as you can of the franchisees, right you want to know things like how long before they became profitable? What were some unexpected expenses that they didn't think about or know about? How did they plan for this, how are they financing their operations on a regular basis? What were some of their challenges? Give me the good, the bad, the ugly. Let me understand. How do you engage with headquarters or the franchisor. Is it successful or not successful in building that relationship? How are you finding, identifying and hiring staff? How hard is it to get capable, trustworthy staff to man your operations on a regular basis?

All of this information is information that you're going to want to get. But you're going to want to get that from every single franchisee that you talk to. And you should absolutely go identify other franchisees to talk to, especially if you were let's say, opening a franchise, in let's say, Arizona, but the franchise or the headquarters is in New York. Maybe you're the first one in the state of Arizona, let's say, you want to understand what are they going to do to help you even establish that brand within Arizona. How are you going to get people familiar with the brand. And so again, you are starting a business, even though you're not starting from scratch, you are going

to be starting an operating a business and you want to make sure that you have as much information as possible, but you're going want to talk to other franchisees as well, to find out who they are, pick their brain ask all of the same questions, and understand that you also want to do your due diligence on the franchise itself. Has it been in any lawsuits, any significant consumer or customer complaints, any filings with the FTC, the Federal Trade Commission, complaints by consumers, lawsuits by consumers, lawsuits between the franchise any franchisees or past franchisees and the franchisor.

You want to dig in and really understand as much as you possibly can, maybe there are some hater blogs out there on the particular brand, you want to be able to go in eyes wide open, you don't want to find out that, wow, there's a whole subculture of people who actually actively dislike your brand that you're buying into the franchise that you're buying into, and they have websites up and they target stores, or whatever that might be. You want to know everything because you're putting your money into it, you're putting your name and your reputation into it.

And so you want to make sure that you have all of the information that's possible from the very beginning. The other thing to think about is - start do visits. Go into different stores, talk to employees almost like the show Undercover Boss. Go around to different stores, and ask people about their experience, you can even let them, Hey, I'm considering buying into a franchise. And as somebody that works, let's say the cash register, or somebody that that does the cooking, or whatever it may be, what's your experience been? As an employee of that particular franchise, all of these things you want to understand so that you again, can have a full clarity when you're making these decisions to buy into a franchise.

The last thing that I'll say is, it is critically important that you have a team around you, when considering a purchase of a franchise. That team can include a lawyer who has dealt with franchising before an accountant that can help you think about the money and understanding that money piece a financial advisor along the same lines. And maybe you have someone that is a business advisor or someone who if this is your first time getting involved in business, you might want someone who can help you understand even just operating a business and thinking about how do you hire a general manager? How do you start to hire people and manage kind of the day to day of that business. But having a team of people is so critically important.

And take your time, slow the process down. As you're thinking about this, there is no rush, people will try to rush you, people will try to get you to buy you know as soon as possible. But take your time because you're making a significant personal, professional, and financial commitment to that particular franchise and you want to make sure that you're doing it in a way that will benefit you. Because, ultimately, that's why you're doing it.

So again, hopefully this information has been helpful for you. If you're considering a franchise or even if you know you've just never thought about it are curious, hopefully you found some valuable information here today. The other thing I would share with you too is if you have teammates or others that you've talked to who have considered buying into a franchise, please do feel free to share this podcast episode with them. Hopefully they'll find some value if you have any questions. If you're considering buying into a franchise and you have any questions and want to talk about it more. Obviously feel free to hit me up happy to have these conversations and provide the best protection because sometimes it might sound like I'm against franchising, and I'm absolutely not. My job is my clients, my job is to focus on making sure that my clients are making informed and educated decisions. And that when they do make those decisions, that then I work to negotiate, the best protection possible for them. I had a call a couple weeks ago about this with someone that was thinking about it and they were like, man,

I didn't even think about all of that. And I'm like, right, I'm not here telling you not to do this. I'm here making sure that you understand all of the implications, should you so decide to do this. And so you want to make sure that you have kind of all the information and having someone who's dealt with it previously will definitely help you as you go through your decision making process.

So again, thank you so much for reaching out and asking about this topic. I'm glad I could share it with you. If you have any questions, feel free to reach out, please do share this episode. Like it, give it some stars, all that good stuff. That's all helpful to the to the podcast for me. And again, thank you for taking the time. I really appreciate you tuning in to the Protecting Your Possibilities podcast. I love doing it. But again, thank you for tuning in. And we'll talk again real soon. Take care.

Disclaimer: Porter Wright Morris & Arthur LLP offers this content for informational purposes only, as a service for our clients and friends. The content of this publication is not intended as legal advice for any purpose, and you should not consider it as such. It does not necessarily reflect the views of the firm as to any particular matter, or those of its clients, please consult an attorney for specific advice regarding your particular situation.