

The "DO" DILIGENCE DOZEN: Twelve Questions Ask When Buying a Franchise

The reasons for purchasing a franchise are numerous but center around the advantages that a franchise offers a new business owner in terms of name recognition, advertising, training, location assistance and on-going support.

Having determined that you want to purchase a franchised business, the question becomes whether the franchise you are considering delivers the “franchise advantage” and will be financially successful. In order to intelligently answer that question YOU, and not your accountant, attorney or business advisor, has the most important responsibility of conducting your own investigation.

Your investigation should touch upon twelve critical areas which I call the "Do Diligence Dozen" because it highlights the strengths and/or weaknesses of the franchise opportunity being considered.

PROFITABILITY: The first, and most important, area is that of profitability. You should contact existing franchisees and asking them about their financial experience. Rather than asking “how much do you make,” ask instead whether they are satisfied with the franchise’s return on their investment.

FRANCHISOR INTEGRITY: Does the litigation history section in the franchise disclosure document indicate that the franchisor has been sued by past franchisees for material reasons such as fraud, misrepresentation or breach of contract? Have there been any actions brought by governmental agencies which would indicate that some of the individuals associated with the franchisor are not trustworthy or have a history of disreputable business practices? How about bankruptcies? Are they related to the franchisor's business or just an unfortunate experience on the part of one of the principals in the franchise.

TERRITORIAL PROTECTION: Does your franchisor represent it will not “encroach” by opening a company store or selling another franchise within your trading area? How would you feel if your franchisor permitted the sale of the same products that you sell in a supermarket such as well known donut franchise did with its coffee?

MONETARY REQUIREMENTS: You should also inquire as to the monetary requirements necessary to start the franchise. Existing franchisees should be quizzed as to whether the money they spent was more or less than the franchisor estimated it would cost to start the franchise. This question is important in order to avoid one of the greatest pitfalls of opening a new business - insufficient capitalization.

NAME RECOGNITION: Are you purchasing a readily recognizable name? Are you buying a Jiffy Lube or a Jerry Lube?

INITIAL AND ON-GOING TRAINING: You should ask about the extent of initial training and whether it was sufficient to properly open the new business. Another question is whether the franchisor offers or ongoing support.

LOCATION ASSISTANCE: Does your franchisor have a detailed set of criteria for locating the franchise or are you set "adrift" to find a location without guidance as to demographics, traffic counts or locations to be avoided.

FRANCHISOR WORKING RELATIONSHIP: Ask existing franchisees whether they had any disputes with the franchisor and, if they were satisfactorily resolved.

LONG TERM VIABILITY OF THE FRANCHISED CONCEPT: The future of the franchise concept should be investigated. Is it a new concept? Is the concept merely a fad or does it have a long term future? Are there competitors and, if so, what is the quality of their product or service? Answers to these questions will focus not only upon the short term future of the franchise but will indicate whether the business can be later resold at a profit.

PAST TRACK RECORD: Has the franchisor successfully operated its concept? For how long? Have any franchisees been terminated and, if so, why?

You must attempt to find any franchisees that have left the system and find out why they left or were terminated. The answers to these questions will strongly reflect upon the future "health" of the franchise.

FRANCHISOR'S FINANCIAL STRENGTH: Is the franchisor's financial statement sufficient to market and supervise franchise operations?

QUALITY OF THE ADVERTISING PROGRAM: Generally, a good franchisor will have a plan which the franchisee will be able to follow in order to avoid utilizing inefficient advertising.

The "do" diligence dozen is designed to serve as a check list to disclose strengths and weaknesses. It up to you, however, to use it to protect the major financial and life style changes you will make in buying a franchise.

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