Breakfast for Business Seminar

Franchising from the Franchisee Perspective

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Presenters:

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Introduction

Considerations for potential franchisees, looking to enter into franchise systems include:

- Owning a franchise – is a franchise for you?
- Arthur Wishart Act – basic overview.
- Key provisions in a franchise agreement.
- Intellectual property considerations.

What is a Franchise?

- What is a franchise?
- A franchise is a business model and a means by which to expand a business.
- Broad, fact-based definition in Ontario franchise legislation.
- Ontario legislation is called the *Arthur Wishart Act (Franchise Disclosure) 2000* (the “Wishart Act”)

Is a Franchise for You?

- A franchisee must work within the system designed and controlled by the franchisor.
- Are you entrepreneurial?
- Do you wish to operate a business that is operated under a successful business model?

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How does a Franchisor make money?

Franchisors control certain financial costs of franchisees, such as:

- Initial franchise fee;
- Initial and ongoing training;
- Ongoing royalties/fees;
- Advertising fund;
- Sublet rent upcharges;
- Supplies and equipment;
- Transfer and renewal fees;
- Build out / purchase costs

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How does a Franchisor make money?

Franchisors control certain financial costs of franchisees, such as:

- Events / opening day / conventions;
- Interest charges;
- Compliance systems; and
- Fines / rewards.

Each of these potential charges can add to a franchisee's costs of operating, that it would not have if it was not part of a franchise system.

Introduction to Canadian Franchise Law

- Franchising is not as heavily regulated in Canada as it is in the United States.
- In Canada, franchise regulation is a provincial matter.
- All provincial legislation is derived from the U.S. model of mandated disclosure by a franchisor to prospective franchisees.
- No registration of franchisors in Canada.
- No government agency charged with regulating or overseeing in Canada.
- Provincial legislation is enforced by private rights of action and the right of the franchisee to rescind.

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Ontario's Wishart Act

Application of Ontario's Wishart Act

- Broad definition of franchise;
- Applies to all franchised businesses operated partly or wholly in Ontario.

Two separate kinds of franchises:

- Business format franchise; and
- Product distribution franchise.

Implications of Wishart Act

The implications of Ontario's Wishart Act are threefold:

1. The franchisor has an obligation to deliver a disclosure document to the prospective franchisee.
2. There is the imposition of a duty of fair dealing on each party to the franchise agreement in respect of the agreement's performance and enforcement.
3. Franchisees have an express rights of association with one another.

The Wishart Act provides broad protection for franchisees, while creating considerable legal obligations for franchisors.

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Elements of a Franchise Agreement

and

How they are different from other agreements

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General Concepts

A. There is a duty of fair dealing under the Act, which includes the duty to “act in good faith and in accordance with reasonable commercial standards”

General Concepts

B. The franchisee gets no ownership in the intellectual property (trade names, copyright, patents)

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General Concepts

c. Methods of operation are strictly controlled (operations manual, specific suppliers, decoration, uniforms, marketing, etc.)

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General Concepts

D. Non-competition strictly enforced after termination.

Term

- The term can be longer than many other agreements (10 years is common, but some can be even longer)
- Frequently provides for 1 or 2 renewal terms

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Training

- There is normally a training requirement, which can be either at the franchisor’s headquarters, or might be at a more local franchisee’s location

Location, Operations and Decorating

- Must have approval for location.
- The franchisee is responsible for keeping the location updated to the franchisor's then-current decoration plan. In addition, there may be extra expenses associated with adding new products to the franchise offering.

Fees

- Initial franchise fees, ongoing royalties, advertising fund, local ad spend requirements, renewal fees, etc.

Transfer Requirements

- Franchisor is normally very concerned about assignees and making sure they are willing and able to support the franchise concept.
- Some agreements contain a franchisor right of first refusal if the franchisee wishes to sell the business, often at unreasonable values.

Territory

- Normally exclusive, but may include a right of first refusal on new premises.

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What is negotiable?

- A careful franchisor could take the position that the franchise agreement is not negotiable, or else it has to provide the same terms to all subsequent franchisees.
- However, many are willing to be a little flexible by way of side agreements.

What is negotiable?

- Start dates, or royalty payment start dates.

Franchise fees

- Your chance of getting a reduced fee is greater if more than one franchise is included, if you are expanding, or if you can show that the territory is substandard (such as lower census numbers, etc.)
- Sometimes you can get time to pay the initial franchise fee.

Renewal fee

- Perhaps a fraction of the then-current fee, or a cap or a specific amount.

Transfer terms

- There may be some flexibility given on amounts if it is for internal restructuring or succession planning, such as non-arm’s length transfers.

Not negotiable

- Royalty rates
- Advertising fund contributions

QUESTIONS?

Wilson Vukelich LLP can help ensure that your matters are handled effectively and efficiently, and in manner that is reflective of new legal developments and obligations. If you have any questions or require further information, please contact:

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