

NEIL
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SOLICITORS

Guide to becoming a Franchisee

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1 Initial Stages

- 1.1 So you've decided that you want to become a franchisee. Taking on a franchise is a long term, time consuming and potentially expensive project. Before you sign up to a franchise it is vital that you fully evaluate the opportunity to give yourself the best chance of success.
- 1.2 The British Franchise Association (the BFA) holds and attends regular exhibitions throughout the year and across the country. These exhibitions provide franchisors and other agencies that may be of assistance to both franchisors and franchisees with the opportunity to showcase their business. If you haven't already done so, go along and see what's on offer. Not only will you get the chance to speak to a variety of franchisors in an informal environment but you may come across a franchising opportunity that you may never have thought of otherwise. You can find BFA events at www.thebfa.org.
- 1.3 When considering a franchise opportunity you should consider:
 - 1.3.1 Why you wish to purchase a franchise business and specifically why have you chosen a particular franchise?
 - 1.3.2 Whether there is a genuine franchise opportunity being offered to you. For example, is the franchisor in a position to offer the support and assistance you require for the duration of the franchise agreement or would you simply be better off setting up a similar business on your own?
 - 1.3.3 Whether the franchisor has a proven track record of franchising. Is the franchise well established? Will you be part of a pilot scheme or are you the first potential franchisee? (The BFA require all of its members to have run a pilot scheme for a year). If you are the first franchisee then you may be in a stronger bargaining position with the franchisor to either negotiate certain terms of the agreement and/or agree discounts on any fees payable under the terms of the agreement.
 - 1.3.4 Whether the franchisor is a member of the BFA. The BFA promotes ethical franchising and sets out a number of requirements (it's ethical code) that franchisor's must comply with in relation to the terms of the franchise agreement, the information to be supplied to franchisees before they enter into a franchise agreement and how the franchisor operates its franchising business.
- 1.4 During the initial stages of purchasing a franchise the franchisor will use this time to assess your suitability to act as a franchisee of its business. However you should take this time to assess whether the franchisor is a suitable franchisor.
- 1.5 It is very common for franchisors to require any prospective franchisees to enter into a confidentiality agreement at the outset of negotiations. This agreement basically protects the information the franchisor will provide to you during discussions and negotiations before you sign a franchise agreement. We are happy to review any confidentiality agreement on your behalf before you sign it.
- 1.6 You may also be required to pay a deposit. This is often used to secure the territory you are looking at and is usually paid on the basis that the franchisor gives you a period of exclusivity during which you can buy the franchise for your chosen territory. You should be very wary about paying a substantial deposit to any franchisor and you should take advice on the terms that apply to the deposit.
- 1.7 Once the confidentiality agreement has been signed and any deposits have been paid, you should receive a copy of the proposed franchise agreement. You should read this very carefully and take legal advice on it. It is important that you obtain legal advice (irrespective of whether the franchisor is prepared to negotiate the terms of the franchise agreement), in order that you fully understand the rights granted to you and your obligations arising under the franchise agreement.

2 Review of the Agreement and our Reporting Service

- 2.1 We can review a franchise agreement that has been submitted to you by a franchisor and provide a report on it for an agreed fixed fee.
- 2.2 We are one of a very few number of North West firms that are affiliate members of the BFA. We have a wealth of experience acting for both franchisors and franchisees and we draft and review many franchise agreements every year. We have also done presentations for the BFA to prospective franchisees on franchise agreements. Our years of experience in franchising means that we have seen our fair share of good, bad and ugly franchise agreements, for all types of businesses ranging from relatively unknown businesses to high profile national high street brands.
- 2.3 Our report not only highlights the main legal issues that we consider to be of particular relevance to you but also identifies those issues that cause us concern or that are non-standard. We also consider whether a franchising agreement complies with the BFA's ethical franchising code. It does not suggest whether you should or should not enter into the franchise agreement (this is a commercial decision for you to take). However, the report seeks to make sure you will be aware of all your legal obligations and what will be expected of you as a franchisee.
- 2.4 The main matters upon which our report concentrates are:
- ***The nature of the rights being granted*** – This is to ensure that you have a licence and the right to use all of the intellectual property rights and materials you require in order to establish and operate your business.
 - ***The area within which you are able to operate your franchise and any limitations in relation to whom you can provide goods or services under your franchise*** – This area should be the area that you believe you are purchasing. Our report will also consider whether you are granted exclusivity in relation to your area. An exclusive agreement would mean that only you can provide the services or goods concerned with your franchise in your allocated area to the exclusion of all others including the franchisor. Exclusivity plays an important part in franchising as without it, you may not be protected from others establishing a franchise in your territory or promoting/providing their goods/services to your potential client base.
 - ***The term of the agreement*** – You should be granted the right to operate the franchise for a sufficient period of time so that you have the opportunity to initially make a good income and then sell your business at a profit should you wish to exit from it. It is common for franchises to be granted for a term of 5 to 10 years. You would also expect there to be the option for you to renew the franchise agreement for a further term, so in effect you can operate the franchise for between 10-20 years.
 - ***The initial and ongoing fees for the franchise*** – You may be required to pay an initial fee when entering into the franchise agreement for the grant of the franchise. However, in addition to a one off fee, there are likely to be ongoing fees that you will have to pay either annually or monthly. Such fees may be for a set amount during the term of the franchise agreement or they may be a percentage of your gross turnover. You also need to be aware of the consequences of failing to pay any such fees on time. It is likely that the franchisor will be able to charge interest at a particular rate for the late payment of any fees. The franchise agreement should also set out in detail how you are to make each payment.
 - ***The franchisor's obligations under the agreement*** – These tend to be split into initial obligations and ongoing obligations. The initial obligations should cover all matters that the franchisor is required to undertake so that once they are completed, you are in a position to start trading, and generally include the initial training that you must attend and pass before you can operate the franchise and provision of assistance by the franchisor in launching your business. A franchisor's ongoing

obligations are usually to provide advice, assistance, support, further training as required and also to undertake national advertising on behalf of its franchisees.

- **Termination** – Who can terminate the agreement and under what circumstances? The franchisor's rights to terminate must be carefully analysed and understood because once exercised, you would lose your business and livelihood. The BFA has laid down guidelines as to what termination events should and should not be included in franchise agreements. It may be useful to have a way of bringing the franchise agreement to an end early particularly if your relationship with the franchisor has deteriorated given that there could be 5 or more years left to run on your franchise agreement. You should also be aware of what matters need to be dealt with on termination for example whether you are required to return all or any materials supplied by the franchisor to you during the term of the agreement or if you are placed under any restrictions following termination that would, for example, prevent you from operating another competing or similar business from the premises, or whether you are prevented from supplying similar services or goods in the territory and if so, for how long after termination of the agreement. This is important particularly if the effect of such clause means that you are unable to generate an income for yourself.
- **Personal Guarantees** – If you have set up a limited company to act as the franchisee then the franchisor may require you to personally guarantee the obligations of the franchisee. This is common particularly if your company is new and has little or no credit. The franchisor may want to ensure that he has the right to recover any losses he may incur from you personally if your company is in breach of the franchise agreement.

3 Your own investigations

- 3.1 Our report will identify any matters on which you should require further clarification from the franchisor. Therefore once you have read our report, you should arrange a further meeting with the franchisor to discuss any issues that we have identified.
- 3.2 If you haven't already done so, you should meet with existing franchisees and speak to them about the franchise, the franchisor and their experiences.
- 3.3 If possible you should try and obtain a copy of the manual from the franchisor and read this carefully. The franchisor's manual is essentially its business bible and should contain all information that you need to know about how to operate a franchise of the business. It will supplement the terms of the franchise agreement and it is likely that you will be under an obligation to comply with the terms of the manual.

4 Other Legal Assistance

- 4.1 There are other legal matters that you need to consider when purchasing a franchise and not just whether you should get advice and a report on the franchise agreement. Here are some additional matters that you may require our help on when you decide to become a franchisee:
 - 4.1.1 **Property** – Depending on the nature of the franchise, you may be required to obtain commercial premises to operate the franchise from. We have specialist commercial property lawyers who are able to assist with the review and negotiation of the necessary documentation you require to purchase or lease such commercial premises. It is important that the length of renewal and termination terms of a lease match the terms in your franchise agreement.
 - 4.1.2 **Company Formation/Limited Liability Partnership ("LLP")** – You may be asked by the franchisor to set up a limited company or LLP that will act as the franchisee. We provide formation services, and can act as your company's/LLP's registered office, if required.

4.1.3 **Shareholders Agreement/Partnership Agreement** – If you are not entering into the franchise agreement on your own but are doing so with one or more business partners, you should think about having a partnership or shareholders agreement prepared. Such agreement will set out how matters are to be dealt with between the parties and how the business as between the parties is to be operated. Such agreement would also govern how individuals can leave the partnership/company and how their share of the partnership/company is to be calculated.

4.1.4 **Business purchases** – If you are purchasing an existing franchise, we can advise you upon and prepare the necessary purchase documentation. We can also help you structure the deal and undertake a legal due diligence exercise on the existing franchise.

5 Other help and contacts

A key feature of successful businesses is that they tend to have specialist advisers that have the expertise to understand their business and give objective advice when needed. We can recommend suitable bankers, accountants, surveyors and tax advisers who can provide other specialist advice when required.

If you have any queries please do not hesitate to contact a member of our dedicated team:

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