A guide to franchising.

At first glance, the appeal of franchising is obvious: for those franchising their business, it may seem like a brilliant way of expanding the business, and for those investing in a franchise, it may appear to be a quick and easy route to success, as the business's brand and reputation is already established.

However, careful consideration must be given to the terms of the franchise agreement, and key steps must be taken by business owners before opting to franchise their business.

How does franchising work?

When franchising a business, the business owner (franchisor) sells franchise rights to one or more independent investors (franchisees), who pay an initial franchise fee for the right to open additional outlets of the business. The franchisee uses the business's trademarked model and brand, and must also pay royalties to the franchisor.

Preparing to franchise your business

Before seeking potential franchisees, franchisors are strongly advised to ensure that all of their business's intellectual property is fully trademarked and protected. Franchisors should also examine their business model or even run a franchise pilot to ascertain how well said model works and how easily it could be adopted by franchisees. This is especially important, as prospective franchisees may want business owners to demonstrate how well their model could be applied to a franchise.

Key terms of a franchise agreement

The franchise agreement is pivotal to the success of the franchise. A qualified, experienced solicitor should therefore always be engaged to draw up the agreement and conduct negotiations. That being said, below are some key points to consider when preparing a franchise agreement:

- **Duration**

The contract should state the initial duration of the franchise agreement. Any probationary period, option to renew, and renewal costs should also be clearly indicated.

- **Training and support**

The agreement should clarify whether any training or support will be offered by the franchisor, and full details of the training should also be provided.

- **Royalties**

The royalties stipulated in the agreement should match up to what was promised by the franchisor. Typically, royalty payments are between four and ten per cent, but what matters most is establishing whether the percentage will be calculated based on the franchise's profit or on its turnover. If it is the latter, the franchisee must continue to pay the same fee regardless of whether or not the business is operating at a loss.

- **Territory**

When a franchise is being sold with an exclusive territory, this means that the franchise agreement will contain details of an exclusive area in which the franchisor (or any other franchisees) will not set up another franchise to compete with the franchisee that holds that territory. Similarly, restrictions will apply to the franchisee whereby they will be prohibited from competing in any territories other than those stipulated in the franchise agreement.

• **Exit strategy**
The agreement should include provisions for the sale of the franchise business. The terms for selling the franchise should state whether the franchisee is required to pay the franchisor a percentage of the final sale, whether the franchisor has first rights to buy the franchise business, or if the franchise can be sold at market value before the expiration of the agreement.

• **Post-termination provisions**
The post-termination provisions or restrictive covenants in franchise agreements typically include non-compete, non-solicitation, and non-dealing clauses to protect the franchisor's business and intellectual property. Franchisees must therefore be extremely mindful of complying with these clauses to avoid the risk of lawsuits.

• **Area of operation**
The post-termination provisions also stipulate the period of time and area of operation within which franchisees have a right to open a similar business if the franchise closes. Franchisees should ensure that these stipulations will not unreasonably hinder their ability to do business.

Franchising can be a lucrative and exciting step for both franchisors and franchisees, but it's essential that the agreement is negotiated and completed by solicitors with an in-depth knowledge of franchising in order to get the best value for both parties.

For more information, or for expert advice on business or personal legal issues, call us on +44 (0)20 3475 6751 or via email at info@carterbond.co.uk

"I would highly recommend the services of Carter Bond for any type of corporate or commercial work."

Enis Rifat, MIYA Solicitors

HIGHLIGHTS

We were awarded the 'Commercial Lawyers - London', in the prestigious 2020 UK Enterprise Awards

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