

Cloning Around

You've read about the companies in our Franchise 500. Now find out how to join them by franchising your own business.

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You've started a successful business, and people want to pay you to clone your success. Now what?

One piece of common-sense advice I review with clients considering franchising is: Franchising is a unique business method that requires its own knowledge base and its own set of skills. If you are in, say, the hotel or auto-repair business now, when you launch into franchising, you'll be in that business and in the franchising business, too. A successful franchise needs:

- **Strength in numbers:** Do you own a retail business whose independent unit owners will benefit from a common identity in your customers' eyes? This is the essence of success: increasing franchisees' dollar leverage by being part of a larger group of merchants. In a healthy franchise program, the benefits outweigh the monthly royalty fee.
- **Transfer of know-how:** Can you teach others how to succeed in your business? The procedures and techniques that spelled success for your business must be written down in a training and operations manual to teach new franchisees how to run one of your units. Creating a manual is the largest task most companies face when creating a new franchise offering.
- **Trademark strength:** Is your trademark well-designed and federally registered? Not yet having your federal registration is not a bar to franchising, but you'll be licensing others to use your mark, and you don't want surprises from someone using the same mark who has superior rights. Registration doesn't guarantee you won't encounter surprises, but in the hands of competent legal advisors, it's an application process that identifies most problems in advance.
- **Franchisee investment:** Most successful franchise systems are

relatively simple businesses that require a modest investment: limited menus, uniformity, small-scale units, few moving parts and limited labor needs. That's why growth in the fast-food franchise arena has been so explosive. There aren't many restaurant franchises, for instance, that require \$2 million or \$3 million to build a single unit. Gold-plated investors at those levels are difficult to find, and the few numbers of prospective franchisees could cripple the growth of a fledgling franchise program.

- **The right temperament:** Just as not everyone is cut out to be a franchisee, not every management team is suited to run a franchise program. A successful franchisor must realize and believe franchisees are valuable business partners; they aren't employees and can't be treated as such. Control freaks will find the soft edges of franchising and the challenge of herding entrepreneurial cats frustrating.
- **Capital:** A franchise program requires the franchisor to provide audited financial statements, and regulators in the registration states put up roadblocks if you have a weak set of financials. I've consulted with companies in a great hurry to franchise because they've been offered a lot of money for a franchise, and the offer looks like an unearned windfall. Believe me, it's not. You need sufficient capital to carry the loaded up-front costs of franchising.
- **Disclosure:** Is your company ready for the bright lights of disclosure? The Uniform Franchise Offering Circular reveals litigation and bankruptcy backgrounds of your key people. What will tumble out of their closets?
- **Good legal advice:** Do you have the right advisors? Like most areas of the law, franchise regulation is a specialty where experience counts for a lot, and a great franchise attorney is an essential member of your franchise team. A good place to start finding one is online attorney directories. You can also ask lawyers you know for a referral to a franchise specialist.

Step by Step A few documents and legal steps are absolutely necessary if you lead your business down the path of offering franchises.

1. Create an operations manual. This will be your system's bible. It's used to train your franchisees and give them operational guidance as they establish their units.

2. Secure your trademark. No law requires it, but if you have not done so already, you may want to apply for federal registration of your trademark.

3. Prepare audited financial statements. You need an audit of your most recent three years, or your most recent year if you have not been audited before. You might also need recent unaudited statements since the end of your fiscal year.

4. Write a Uniform Franchise Offering Circular (UFOC). Federal law and several states require you to give a complete and current UFOC to a prospective franchisee at the initial meeting to discuss the sale or potential sale of a franchise, or 10 business days before the prospect pays or signs a binding franchise agreement.

5. Develop a franchise agreement. This governs the franchise relationship, and it had better be tight. It must be included in the UFOC and signed by the franchisee and franchisor when a franchise is granted.

6. Comply with state franchise law. Some states require you to register before making offers, while others require you to file an exemption under a state business opportunity law. Under many state franchise laws, you are restricted from advertising the franchise offer prior to registration.

7. Get a legal review. Once you've found an experienced franchise attorney, have him or her provide a detailed review of the franchise agreement and the UFOC. Your attorney will help you evaluate whether this is a document you can commit to and whether you should include specific provisions.

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