A Tale of Two Opportunities

If you're considering buying a franchise or business opportunity, here's what you need to know before making your decision.

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Homebased franchises and business opportunities offer investment opportunities built on a truly irresistible principle: Own a business, be your own boss, work out of your home and leave behind that hideous commute.

The basic appeal may be the same, but franchises and business opportunities are more different than they are alike. They share DNA--they both offer an opportunity to begin a new business--but each has distinct pros and cons. Understand those key differences, and your search for that perfect business investment can really pay off.

Comparing Investments

Lay the two investment concepts side by side, and their fundamental differences become evident. The similarities are simple enough: The investments both enable you to begin a business. That's about it for similarities. Every other aspect of the two investments falls in the differences column--the business opportunity is a one-time purchase, usually a part-time effort, and there is no continuing relationship with the seller. By and large, it is a smaller investment and does not feature ongoing royalties. The seller is a product provider, although some inexpensive guidance material is usually offered with the purchase. Trademark rights are usually not licensed to the buyer. The business opportunity seller is generally not available to provide business assistance when things go wrong. You're on your own.

Franchising is the more sophisticated investment-sophisticated in the sense of the greater number of moving parts. It is generally a full-time, absorbing business experience. The investment can be substantial; a freestanding franchised restaurant can easily cost you $500,000 in total investment. That said, the hottest growth sector in franchising today is the homebased business franchise. These programs are lower-level investments, often totaling no more than $30,000 to $40,000.

The franchisor is your operations partner, providing intense training and ongoing handholding. Of course, you buy that support for a price: You'll typically pay a $10,000 to $30,000 initial franchise fee and 3 to 7 percent of your business's weekly or monthly gross sales. You receive the right to identify your franchised business with the franchisor's (preferably well-established) trademark and to use its (preferably proven) operating techniques. When problems occur, the franchisor is there to walk you through them. You have the intrinsic benefits of purchasing power-as a member of a franchise system, you benefit from the strength of large numbers of buyers (think savings in volume discounts) when it comes to purchasing inventory and supplies. With a franchise, you have a valuable senior partner in your business.

With a business opportunity, you buy a package of goods and services, and there is little or no continuing relationship. If there is a continuing relationship, it's usually no more than that of a product supplier to your business.

Evaluating a Business Opportunity

The single most important aspect of a business opportunity investment is your fit with the program. Does it fit your plans, the skills you bring to the program and your financial resources? No amount of great product, substantive training or glossy brochures can overcome a poor fit. The best answer to this challenge is to assess your goals, how you think a business opportunity can help you reach those goals, and what you expect to enjoy most about being in business. Be sure to write down your notes on these thoughts and keep them nearby for reference.

What is the most common mistake people make when deciding to purchase business opportunities? As you look over the seller's materials, you may delude yourself into the purchase: "This product or service is so good (or cheap or valuable or innovative or clever) that it will sell itself. " Banish this thought immediately! There is nothing-nada-that is so good it will sell itself. You had better be prepared to do some selling. That means cold-calling people who won't give you the time of day. You'll have a lot of doors closed in your face and phone prospects hanging up on you-you have to be prepared for that bruising experience. How are your sales skills? Most business opportunities, when you boil down the hype and enthusiasm, are little more than independent sales jobs that you own, so your skills need to be sharp.

Gathering information about a particular business opportunity investment can be difficult. The person you most want to interview is someone who purchased the business opportunity and has had some success with it. Ask the seller for a list of owners in your part of the country. Assuming you receive a list, get on the phone with some of them. The key question to ask: "Knowing what you know now, would you make this purchase again?"

A body of federal and state laws purports to regulate business opportunity sales (see "The Regulators" on page 30), but unlike the franchise laws discussed below, the statutes are inconsistent in their definitions of what constitutes a business opportunity, and they do not cover much of the hyperactive business opportunity marketplace. Despite the designs of the legal authorities, odds are that you probably won't receive any sort of meaningful disclosure document. Make up for it by asking the seller the right questions (see "Question Everything" on page 31).

You could also visit the company headquarters to get a personal impression of the business. This won't be practical in many situations (why make a $1,000 trip for a $650 investment?), but it starts to make more sense at higher levels of investment. Check in with the Better Business Bureau and the FTC, and by all means contact your state consumer protection authorities for information on a particular seller or on business opportunity investments in general.

Evaluating a Franchise

Finding a comfortable fit is also important in making a franchise investment. There's a wide variety of businesses available; your job is to find one you'll enjoy building and operating. Yes, it should be a fresh, vital business concept that's going to be around for a while, and it should have the promise of profitability, but make sure you enjoy the operations. My wise youngest brother once told me that a prospective franchisee should not only understand the business, but also ask about the job; that is, find out what you will actually do every day to make the business a success. For example, a training business may appeal to your inner professor but may require you to make three hours of cold calls every day to generate clients. When evaluating a franchise investment, don't let the glamour of the business blind you to the hard, everyday work at hand.

Franchise purchasers have a significant advantage over business opportunity purchasers: A bodacious slab of information about the investment is handed to you on a silver platter in the form of an offering prospectus, or Uniform Franchise Offering Circular. Federal law and many state laws require that all franchisors deliver a UFOC at least a couple of weeks before the buyer pays any money or signs a binding legal contract. If you are at all serious about a particular franchise, by all means, ask for a UFOC early in the process.

A UFOC is designed to deliver a wide range of information about the franchisor and its franchise offering. You'll learn about the franchisor's business experience, its litigation background, financial dimensions of the franchise investment, detailed contact information about existing franchisees in the system, and background information on numerous other topics. In an exhibit to the UFOC, you'll find a copy of the form of franchise contract and a set of the franchisor's audited financial statements. Given the investment's advantage of ready information, it's surprising how many people don't actually read the UFOC before jumping into the franchise. It's well-organized and written in plain English, so it's not that tough to crack. Take the time to read it-it'll put you well ahead of the game.

The UFOC answers most of your basic questions and gives you information to drill down for a more detailed understanding of the franchise. The UFOC won't tell you everything you need to know, but it does provide the basics. You take it to the next level by preparing an accounting projection and a break-even analysis with a good accountant, considering locations and visiting with current franchisees. You can also work with an attorney to review the form of franchise agreement. You want to know from your legal counsel what rights are granted and what obligations are imposed on the franchisee, and whether any parts of the contract are unacceptable or injurious to your interests.

With a full list of franchisee contact information, your job of contacting franchisees is simplified. Get on the phone, make appointments, then visit as many as you think are necessary to get a good cross section of views and experiences with the franchise program. Ask the franchisees for their views on the franchise program, the value of the training and support they have received from the franchisor, the everyday work involved in the business, and the profitability of their operations. Sure, you can ask them what their gross sales were last year and what kind of performance they expect this year. Most franchisees will be candid and open with you, and freely discuss their experience. Their views are immensely valuable; they're not trying to sell you on the program, and they have firsthand experience. Don't expect 100 percent smiles and sunshine about the franchise investment, but if a majority of franchisees endorse the program and tell you they're making a profit, that tells you a lot about the value of the investment.

State authorities in franchise registration states can confirm over the phone whether a particular franchisor is registered to offer and sell franchises in that state. They can also tell you if initial franchise fees must be deferred until you open for business or if other financial protection is in place for investors in the state. Any protective arrangement will be noted in Item 5 of the UFOC and in the state appendix.

Franchises and business opportunities: The DNA may be the same, but their differences run deep. Put in the time and effort to research the offerings, and you'll find a program that offers an exact fit for your needs.

For more information on buying a franchise or business opportunity, visit *Entrepreneur*'s FranchiseZone.

Regulation & Investigation

The Regulators

The FTC is the federal agency that regulates the sale of franchise and business opportunities by requiring disclosure to be delivered before the buyer makes a commitment. Check out its website at www.ftc.gov for some useful overview information. The states also have a plethora of laws in these two areas. If you have a question, contact the attorney general or consumer-protection offices in your state. Whether or not your state specifically regulates franchise and business opportunities, these offices can probably help you.

The FTC and 14 Franchise Investment Law states require that a disclosure document be delivered. Then those states go further and require the franchisor to file with state authorities annually to receive the right to offer franchises in each state. The Franchise Investment Law states are: California, Hawaii, Illinois, Indiana, Maryland, Michigan, Minnesota, New York, North Dakota, Rhode Island, South Dakota, Virginia, Washington and Wisconsin.

Most of the state business opportunity laws also require pre-sale disclosure and registration. The Business Opportunity Sales Law states are: Alabama, Alaska, California, Connecticut, Florida, Georgia, Illinois, Indiana, Iowa, Kentucky, Louisiana, Maine, Maryland, Michigan, Minnesota, Nebraska, New Hampshire, North Carolina, Ohio, Oklahoma, South Carolina, South Dakota, Texas, Utah, Virginia and Washington.

Question Everything

If you're a serious franchise investor, you'll receive a disclosure document at least a couple of weeks before you sign up-but maybe not until then (tip: Ask for one early). And if you're looking at a business opportunity investment, you probably won't receive a disclosure document at all. Without that valuable document in hand, you have to quiz the sellers for information they may not be serving up at their sales presentations. Here are some key questions you should get answers to:

- What is the total investment I should expect with your program?
- How many business opportunities/franchises in your program have been purchased in the past six months? Have any been purchased in this market? Can you give me the names and telephone numbers of those buyers? Can I also have the names and numbers of people who quit the program in the last year?
- How long have you been in business? Are you a member of the Better Business Bureau? What is the name of the corporation making this offer? How substantial is the seller corporation? Can I have a copy of its current audited financial statement?
- Has the company registered this offering with any state agency as a

franchise or business opportunity? If so, where? Does the company comply with the requirements of the FTC's Franchise Rule by delivering a disclosure document? If so, how can I arrange to receive one?
- Must your buyers sign any contracts to close the sale? How can I get a copy of the form of contract you use?

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