

Understanding THE UFOC

Read it and reap.

BY ANDREW A. CAFFEY

YOU LEAVE YOUR first meeting with the vice president of franchise sales, and your head spins with an exciting overload of information and impressions. The vision of a new business is taking shape in your mind, and you think this may be the one.

Among the site location guidelines, product samples and promotional materials stuffed in your briefcase is an imposing legal document titled "Uniform Franchise Offering Circular" (UFOC). You crack it open and scan a few pages. Reading the title page is enough for you to conclude that this is mostly legal mumbo jumbo, probably all fine print required by some government agency, and that reading it will mean plenty of tedious mental work on your part. You put it aside, promising yourself you will get to it . . . soon. Then you eagerly turn to the glossy promotional materials and vivid images of happy franchise owners enjoying their new-found independence.

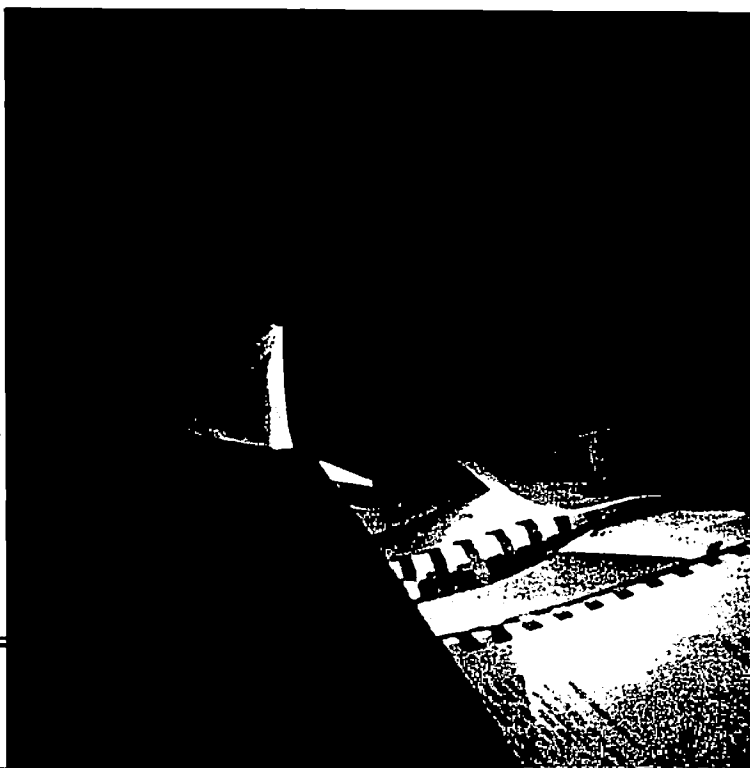
Thousands of franchise buyers make the mistake of never reading the UFOC. They stuff this invaluable document under a stack of paper and forget about it. In franchising, there is probably no oversight that leads to more misunderstandings, frustration and unhappiness.

The UFOC is a mother lode of information for the investor considering a franchise purchase. It contains a broad array of required disclosures about the franchisor and the franchise program that are indispensable to your decision-making. And the UFOC is getting easier than ever to read, thanks to a new format.

Franchise law requires franchisors to provide this document to prospective franchisees. The objective: to level the investment playing field by ensuring that you receive information essential to making an informed decision.

■ TRIPLE THREAT

The UFOC is something of a triple-decker sandwich. The first layer is a required narrative about the

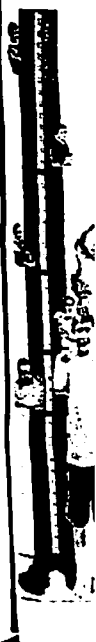


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franchise offering and the franchisor. The second layer is financial information about the franchisor—three years of audited financial statements, to be exact. Last is a sample copy of the franchise agreement and other legally binding documents you will be asked to sign.

Starting this year, the franchise community will be rewriting its documents to comply with a radical set of changes adopted by The North American Securities Administrators Association (NASAA), which is the governing body of the UFOC format. The new UFOCs will be shorter and written in decidedly plain English. Much of the repetitive, mindless recital of contract terms in the current UFOC format has been replaced by simple cross-referenced tables and useful, readable summaries. The changes promise to make the UFOC quite a bit more readable and not so intimidating to the nonlawyers among us.

Franchisors are required to use

the new format the first time they renew their UFOC this year. This means that although you may still receive old-format UFOCs over the next few months, by the end of the year all UFOCs will be in the new format.

Whatever the format, the UFOC is designed to convey basic information about the franchise offering and key information about the franchisor. By no means does the document contain everything you need to know, and your inquiry should not stop there. The cautious investor will investigate the franchise further.

■ KEY BUSINESS INFORMATION

The narrative section of the UFOC covers a lot of business information in very few words.

♦*Franchisor summary:* Item 1 includes the corporate name of the franchisor, its place and date of incorporation, and a basic description of the franchise(s) being offered. The busi-

ness experience of the company's officers and principal franchise executives is summarized in Item 2.

♦*Fees:* The details of the fees charged to franchisees are laid out in Items 5 and 6. Read Item 5 carefully; if the franchisor has negotiated a lower initial fee with any purchaser in the past year, it will be noted in all new-format UFOCs, although it may not be disclosed in the old format.

Are franchise fees negotiable? You bet they are, but that fact is not widely discussed among franchisor salespeople. Ask the company for information on the fee variations described in Items 5 and 6, and don't be afraid to negotiate with the franchisor.

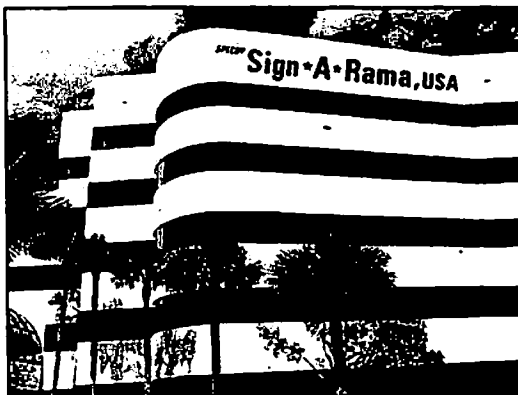
♦*Expenses:* The heart of the business information in the UFOC is found in Item 7, the estimate of your initial expenses. Expect to find ranges of expenses broken down into about a dozen different categories, such as real estate expenses, costs during training, leasehold improvements, opening inventory and working capi-

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SIGN*A*RAMA IS BOOMING

Speedy Sign*A*Rama, USA, is having its best year ever, and it can be directly attributed to its more than 200 Franchise Owners nationwide. The company, started in 1986, was founded by Roy Titus who also started Minuteman Press in the early 70's. It is really a family affair at Sign*A*Rama, where Roy's sons, Ray and Gary are Executive Vice President and Vice President, respectively. "The company was built around a tremendous commitment to local backup and support for our Franchise Owners, which we feel is unmatched by any franchise company", states Ray Titus. Keeping that commitment,



Sign*A*Rama has 14 regional offices, each with a corporate officer of the company, with marketing and technical support for the franchise owners. Sign*A*Rama is the largest full-service sign franchise in

America today. The store owners sell an incredible amount of different types of signs, from computer generated paper signs, to the largest outdoor box signs. "We do everything a quick-sign shop does, only better, because of our equipment, but we also get deeply into the commercial end of the business. We really don't look at the quick sign shops as competition, in fact, some of them are good customers of ours," adds Titus. Just think of the possibilities. Every business is a potential customer. Every trade show or event. Every truck or house for sale. It's incredible.

For a personal tour of local stores and to find out how you can own your own Sign*A*Rama call (800)776-8105 or write to 1601 Belvedere Rd., Ste. 402E, W.P.B., FL 33406 or fax to 407-640-5580.

tal. The value of this information will depend on the years of experience it is based on and whether it is current. When checking with other franchise owners, be sure to ask about their initial expenses. How do their figures compare with Item 7?

❖*Product supply:* Don't overlook the product and supplier information in Items 8 and 9 (Items 8 and 16 in the new format). Many franchisors require franchisees to purchase from approved suppliers; others have organized a purchasing cooperative; still others simply impose standards on products to be used in the franchise. All this information is addressed in these items.

❖*Franchisor services and obligations:* Organized in a single section in Item 11 is a listing of the services and commitments the franchisor is required by contract to deliver to franchisees before and after

the commencement of the business.

❖*Earnings claims:* What about earnings potential? In approximately 80 percent of all UFOCs, franchisors have chosen to provide no information regarding franchise earnings potential. So how do you decide whether there is sufficient earnings potential to make your new business

a success if no information is provided in Item 19? In most instances, the information you need is available only from current franchise owners, not from the UFOC.

■ LEGAL EASE

Don't be put off by the legal information in the UFOC; much of it is essential to your research.

❖*Contracts:* The UFOC contains a sample copy of the franchise agreement and other documents you will be required to sign for the franchise rights. This complicated legal contract is summarized in a few different places in the current UFOC format (see Item 17 and numerous other places); in the new format, the contract is described by short summaries and detailed cross-referencing.

Prospective franchisees should retain an attorney or other business advisor to help

Research Resources

❖The *Federal Trade Commission (FTC)* provides a package of information about the FTC Franchise and Business Opportunity Disclosure Rule free of charge. Write to the Division of Marketing Practices, Federal Trade Commission, Washington, DC 20580, or call (202) 326-3128.

❖The *American Business Opportunity Institute Inc.* is a national information clearinghouse and seminar company specializing in business opportunity and franchise investment and regulation. For information on the Institute's publications, programs and services, send a self-addressed, stamped, business-sized envelope to American Business Opportunity Institute, 3 Bethesda Metro Ctr., #700, Bethesda, MD 20814.

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review the legal documents required for buying a franchise. The UFOC makes the contract seem set in stone and non-negotiable. But just because a contract is included and summarized doesn't mean it can't be improved for your purposes. A good legal advisor can assist you with recommendations on provisions that are one-sided or otherwise unacceptable and can help in any negotiations.

♦*Litigation and other unmentionables:* Other legal information you should review in the UFOC is in Item 3 ("Litigation") and Item 4 ("Bankruptcy"). How should you react if Item 3 contains a long list of cases? Don't panic. Litigation is not uncommon in the franchise relationship, so don't jump to conclusions.

Ask your lawyer to discuss the cases with you. Do they involve fran-

chisees? Do they tell you anything about the franchisor's enforcement style? Is the company prone to filing lawsuits, or do the disclosed cases suggest a fundamental problem in the system?

♦*Trademarks:* The trademark disclosure section (Item 13) reveals whether there are problems with any of the principal marks and whether the company has taken steps to register the marks with the U.S. Patent and Trademark Office. If the primary marks are not registered, the legal situation warrants further inquiry. You don't want to open your business only to find that your use of the franchise system trademarks draws a challenge from the owner of a similar trademark. Double-check the contract to see if the franchisor promises to defend any trademark action brought against a franchise owner. All too often, that task contractually falls to the franchisee, not to the trademark owner.

■ THE INNER WORKINGS

Some of the most useful information in the UFOC describes key aspects of the franchise system.

♦*Advertising:* Do franchisees join buying cooperatives, or do they merely contribute to a centrally managed fund? How is this valuable resource managed, and do franchise owners have a major role in advertising decisions? These subjects are addressed in Item 11. Here you will also find a review of any advertising restrictions, such as the franchisor's prior written approval or a minimum amount of your revenues that must be spent on local advertising.

♦*Franchisee lists:* Item 20 contains a list of franchisees in your state as well as a list of those who have left the program in the prior year. Using these lists, personally interview at least five or six owners. Select your interview targets yourself; do not allow the franchisor to guide you to one or two select high performers.

Also check with a few who have left the franchise system, if you can track them down from the information in Item 20. Questions to ask: Why did they leave? Do they have information that would be useful to your investment decision? In all likelihood they

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do; your task is to put their comments in perspective.

❖ *Business information not in the UFOC:* Several fundamental points are not addressed in the UFOC. Is there a market for the products or services offered through the franchise? The UFOC will tell you only whether the market is competitive. Will the prices of products available through the franchise system allow you to operate at a profit? The UFOC doesn't come close to answering this one. Will the royalty structure—usually a percentage of gross sales, as opposed to net profits—allow you to run a successful operation? The UFOC will not give you answers to these essential questions; you need to research them on your own.

■ GETTING A UFOC

Franchisors are not required to give a UFOC to everyone who requests one. Rather, it must by law be delivered at the earlier of: 1) the first personal meeting for the purpose of discussing the sale of the franchise (a meeting at a trade show booth will probably not be considered a first personal meeting), or 2) 10 business days before you either sign a binding contract or pay money for the franchise.

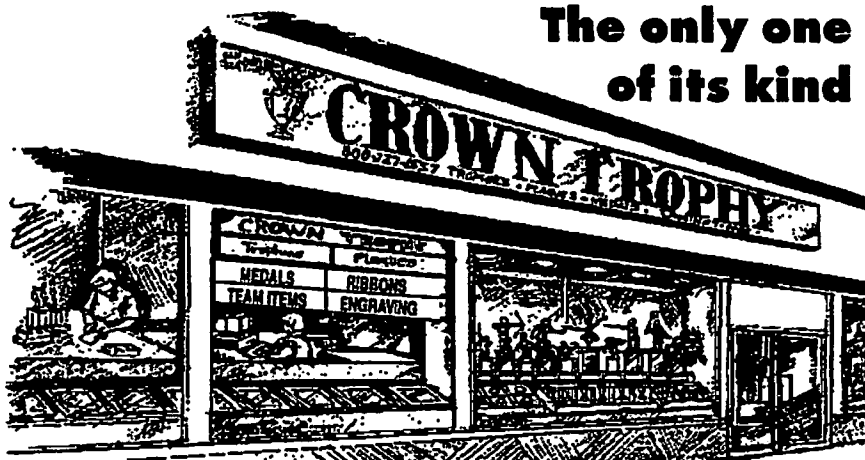
These rules mean no prospective franchisee can be required to put any money down on a franchise opportunity until the UFOC has been in hand for at least two weeks. This includes all deposits, "good faith" payments, training fees and "earnest money" payments.

As a franchise buyer, you enjoy a distinct advantage over other business package buyers: You receive essential investor information served on a silver platter well before you are asked to commit your funds. Unfortunately, too many investors squander this advantage by failing to review the UFOC themselves or at least take it to a trusted business advisor.

Buying a franchise has its risks, but you can lower those risks by simply reading the information presented to you in the UFOC, gathering other pertinent data, and seeking the counsel of knowledgeable advisors. E

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