

Franchise Insider

YOUR THREE STEP GUIDE TO CONDUCTING A FRANCHISE INVESTIGATION

YOUR JOURNEY BEGINS HERE

As you begin your investigation, print this handy guide and use as a resource.

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Your Three Step Guide To Conducting A Franchise Investigation

Okay. Your consultant has discussed possible franchise opportunities with you that he or she feels are most appropriate for you. You're about to have your first phone call with each of the franchise representatives – AND YOU'RE NOT SURE WHERE TO EVEN START.

Your consultant has probably explained to you that these conversations are akin to having a job interview. And, like a job interview, you want to develop a strong relationship with your “interviewer” – while also learning everything you need to learn about the company. We call this “establishing your personal success strategy.”

So, just how do you do this? We're going to introduce you to a proven interviewing approach. We're going to break down all of your potential meetings with your franchisor representatives into 3 phases, making it easier for you to focus on distinct objectives for each meeting – and thereby have better results. This document – The FIRST STEP – will get you started, and your consultant will follow up with suggestions for the second and third phases when you are ready.

YOUR FIRST STEP

Personal Success Starts With Making Great First Impressions

Most franchisor representatives will call you within 24-48 hours of your consultant's introduction of you to them. Some will attempt to speak with you right away, while others will simply schedule a more formal appointment with you for a slightly later time (1-2 days later) after you have received their marketing materials, (which they tend to overnight to you the minute they receive your introduction.) (You need to be aware that these first calls can run up to an hour in length, so if you do not have the time when they first reach you, be sure to let the representative know, and try to reschedule for something within the next 24-48 hours. You DO want to appear enthusiastic...don't be "unavailable" for an extended time or they will think, rightly or wrongly, that you have no interest.)

All of these representatives are professionals. When you begin your phone call, they are going to "warm you up" by asking some simple questions about your background, your family, and why you are interested in their franchise. You, in turn, want to be ready to answer these questions and to also have some questions prepared that underscore your interest (see page 3 for some suggestions.)

Keep your exchange of information light and simple. Don't overwhelm them with questions on this first call. Your primary goal in this session is to help the representative feel as if you're a strong and viable potential candidate that they want to learn more about. In other words, you are going to make a fabulous first impression with that representative. And you're going to accomplish this by showing you are 1) interested and enthusiastic 2) smart and capable, and 3) attentive and a good listener.

WHY? Our goal, when we begin this process with you, is for you to have been so well-perceived by your franchise companies, that they all acknowledge you to be a strong candidate – and will want you to come to Discovery Day at their headquarters to meet you. When this occurs, YOU are in the driver's seat – and are able to simply choose the ONE company you want to visit.

Typical Opening Conversation Flow – and Questions You Might Consider

Franchisor Representative: Good afternoon! I received your name from Patrick Elsner and wanted to call and introduce myself. How are you today?

YOU: I'm just great – how are you? I'm glad you called – I've been looking forward to hearing from you.

Franchisor Representative: I'm happy I was able to reach you. By the way, is now a good time to chat? I was hoping we could spend about an hour and I could give you a little background on our company. Great!

Here's what I'd like to do. I'd like to spend some time getting to know a little bit about you – and then I'd like to give you a brief overview of our company – then we can open it up to any questions you might have? Fair enough?

YOU: That works for me.

Franchisor Representative: By the way, before I get started, just what is it that interested you in our company, anyway?

YOU: Several things, actually. It appears to be a solid business with a strong customer following. It's not a category I have prior direct experience in, but I have indirect experience I believe will be applicable. It also seems to be an area where I can comfortably start – and still grow. That's important to me, as I don't want to get bored in my work.

Franchisor Representative: Interesting! I'll be anxious to hear more about all of that. It's funny you say that you don't want to be bored, because that's something our most successful owners tell me all of the time – there is never a chance to be bored because the business is always changing and growing!

YOU: Sounds perfect. Fire away! I'm taking notes and am anxious to learn.

OK. What just happened in that exchange? A simple exchange of information – yet in the first 2 minutes, you were able to show your enthusiasm, demonstrate your “smarts” and interests, and prove to him you were ready to listen.

As the conversation proceeds, you might want to ask them more “general” questions like this:

Has this been a good year for the company? How has the company been faring amidst the current economic turmoil? How do you see the economy further changing your business in the next several years (if at all?)

What would you say are the most important characteristics you are looking for in an owner?

What would you say is the greatest advantage you offer the marketplace versus your competitors? Do you see this changing in the near future?

What might you say are the 1-2 things that have changed the most in your business of late? Have these had a positive or negative impact? Could you share the company's perspective on what a longer-term outlook might be?

When you are conversing, other questions will come to mind – and feel free to just “be yourself.” Just keep it light. (Have you ever met someone for the first time that “blew you away” with their intensity? You don’t want to be perceived this way.) There is no shame in saying that you’re goal is to “absorb first, and ask questions later.” But remember one thing: be prepared to answer any questions they may also ask of YOU – about your work experience, your family, your finances, and so on. Have your Confidential Personal Profile form in front of you so that you’re prepared to respond as you did on the form (as they will have a copy of your form.) Sometimes people are so anxious to learn about their franchise choices, they forget to prepare themselves for some of the most basic “interviewing” questions like:

- Why are you interested in franchising?
- What makes you believe you would be good at owning one of our franchises?
- How do you think your prior experience will help you be a good owner for us?
- Have you managed or hired people before? Fired anyone? What was your greatest challenge here?
- Have you ever managed a budget or a Profit and Loss statement? Do you have Quicken, or Quick Books, or any such software at home to help you with your personal finances?

Most of the time, a company will send you their FDD at the same time they send you their marketing materials. We strongly suggest that you hold your questions on the FDD for a later conversation. Keep this meeting focused on “setting your mark.” There will be plenty of other forums to ask your questions.

Okay. You have had your first phone conversation with several franchise opportunities. How are you feeling? It’s interesting, isn’t it? But we’ll bet you also feel like you have a ton of information flowing through your head – and you’re not sure what’s really relevant to you.

Don’t let this alarm you. You’re going to learn even more detail as we go forward, but we’ll help you sort out what’s most important to you. In the first phase of your evaluation meetings, you hopefully made an outstanding first impression, or, as we say, put you “on your mark.” Now we’re going to immerse you in all of the details about your possible franchise choices. It’s going to be a bit overwhelming for a while, but don’t worry – you’ll start to see that a lot of the information is fairly consistent from franchise to franchise – and that all you need to concentrate on is what’s different and what’s relevant to YOU.

NOTES

YOUR SECOND STEP

Personal Success Occurs When You Are Able To Make Informed Decisions

In this phase, you're going to get into the real "meat and potatoes" of learning about a franchise. There are two parts to this phase: learning about the franchisor's FDD from your franchise representative, and then conducting validation calls with franchise owners, where you can "fill in the blanks" of your knowledge bank about that franchise from those who work first-hand on the business. And while you're learning, you want to maintain the strong impression you made in the first meeting.

Let's start with the FDD meeting. Your consultant will have already explained to you the importance of the FDD – and how you need to go over it with a fine-tooth comb, learning every single aspect about it. We would suggest you go through your questions first with your consultant – then prepare for your meeting with your franchise company representatives.

Okay. Just what are your objectives for FDD review and validation meetings? You're going to LEARN what it means to become a franchise owner. Your goals for learning are to be a "sponge" – asking any and all questions that come to mind, so that you may learn what you need (and want) to learn about a franchise opportunity. AND in order to maintain that impression of yourself, you need to be a demonstrated "thorough listener/organizer," whose continued interest in the franchise is apparent. For example:

- You are on time for all meetings – and you reschedule in advance if for any reason you can't make a meeting.

(There is no quicker way to be disqualified from franchise consideration than being discourteous and missing scheduled meetings.)

- You have your questions prepared in advance – to the extent you are able – so that you maintain that great impression you made in the first phase.
- You are careful to "check any attitude at the door." In other words, be positive and remain enthusiastic! If a "doubt" has surfaced, don't let it show.

- You are courteous in how you ask your questions. If a question is somewhat “sensitive” be sure to qualify it as such in advance. For example, “This might be a difficult question to answer, but could you play the ‘what if’ game with me for a moment? ‘What if’ I purchase this franchise, and 5 years into it, I decide it’s not for me – what do I do then?”

Not all franchise representatives will review the FDD with you – unless you request it, and you WANT to request a thorough meeting. With this request from you, they will arrange a meeting whereby they simply ask you to have your questions prepared – and they will answer them one by one.

You can ask detailed questions about any and all aspects of the document – the background of the company, the principal players, the investment, royalties, marketing fund contributions, additional operating expenses, legal history, financial status of the company, obligations of franchisees, obligations of the company, “turnover” rate of franchisees, and so on. Use those Post-It notes we mentioned earlier – and paste them to any page of the FDD on which you have a question.

You probably want to review your questions first with your consultant. They can help you “weed out” any superfluous questions so that your time can be well spent with your franchisor representative. AND you always have the choice of going to a franchise attorney to have them explain this document and its importance to you. (We say “franchise attorney” because there is little value in using your family attorney for this task – they will simply learn about franchising “on your dime.”)

IF you choose to use an attorney, you need to be aware of one thing: this document is, by federal law, largely universal and unalterable. In other words, all your attorney can do is to help you better understand the document – they cannot alter it or change it for you. In rare circumstances, a company will write a “letter of understanding” that merely clarifies a point or two about the Agreement or the company’s policies related to it – that’s it.

NOTE: Some of the franchise companies will include an indicator of average financial performance – be it gross income, or profit, or average transaction income -- in their FDD. This is what is called an “earnings claim.” And please understand also that a franchise representative can only discuss financial

performance to the extent they have included an earnings claim in their FDD. EVEN if a company offers an earnings claim, you should not make final judgments about potential performance of a system until you have completed your validation calls with other owners of the system (the second part of this phase, covered below.)

Some of the questions you want to make sure you cover when reviewing the FDD – which may not be as obvious to you as others, include the following:

- I want to be absolutely certain I understand all of the costs. May I be certain that this breakdown is comprehensive – and that there will be no other costs necessary to open the business? Are these averages? How might I equate them to my area?
- If I pay a franchise fee – and something happens that prohibits my getting funding – do I get a refund on my franchise fee?
- What help can you provide me in preparing my business projections? Are there any franchise owners to whom you can direct me that could help me in this exercise? Do you have a template I might use?
- What are your longer-term plans for marketing and advertising? Do you anticipate that I will need to contribute to a supplemental fund for advertising? I see that the marketing plan is heavily (sales and promotion-driven) right now.

What help, if any, will I receive if I would like to do some advertising and promotion on my own?

- What specific help do you offer in site selection? (If relevant)
- Territory rules...please walk me through this.
- I know I can contact any of the franchisees in the network – but are there any in particular you might suggest I speak with? (To focus on special questions you might have)
- Do you provide operational manuals and training manuals that I can see prior to signing?
- Help me understand what process I would go through if I chose to sell my franchise before the end of my contract?

By all means, don't forget to ask "the tough questions" that demonstrate you've done your homework – and that you are serious about their business. This is your chance to get them answered.

When you have completed reviewing the FDD with your franchise representative (s), you want to feel fairly confident that you:

- 1) understand how the business works
- 2) understand what role and obligations YOU, as an owner, specifically have in making your franchise successful
- 3) understand what the franchisor's obligations are in helping you – both in the day-to-day and in the long term
- 4) understand in general what kind of performance you might expect from your franchise (if an earnings claim is made in the FDD.)

YOU WILL NOT YET HAVE ALL THE ANSWERS YOU NEED TO MAKE A DECISION AT THIS POINT. Again, be patient. Every step will continue to provide more and more information for you.

Assuming both you and your franchisor representative are still feeling good about each other – and you want to go forward, they will likely give you permission to begin what we call "validation calls" to existing franchise owners. In this part of the SECOND PHASE, you will have all of the same personal objectives as the FDD review – but with one more, very important, objective added:

- You want to get all your questions answered that CANNOT be answered by your franchisor representative.

This is extremely important. The ONLY way you can get more extensive performance estimates or ranges is to speak with owners. The BEST way you can get some of your more personal questions answered is by posing them to owners. These are the people "in the trenches" so to say – and they have nothing to gain, nor lose, by being honest and forthright with you. So make good use of these conversations – they are critical to your learning process.

Okay. You want to sit down and prepare for how you're going to conduct your validation calls.

The very worst thing you can do is simply “start dialing” and “see what you learn.” So read this list over before you begin:

1. You want to target certain owners, and also call some randomly. You want to call owners in other markets than your own first – and save the ones in your particular area or region for last, when you think that this franchise “might be the one.” We suggest you work with your franchise representative to get a customized list of really strong owners that you can learn from – and any other owners that might be able to best answer specific questions you have raised with them up to that point. All other owners you can choose randomly from the list in the FDD. The number of owners you call is up to you – most people call at least 10 owners.

2. You need to prepare a list of owners, in order, that you are planning to call – and have a questionnaire ready, or your questions ready – before you begin calling. Your consultant can help you prepare these tools.

3. As most owners are extremely busy, they will doubtfully drop everything to speak with you when you call. Instead, it makes better sense to introduce yourself and state the purpose of your call, (“I am hoping to spend about 15-20 minutes with you to learn more about your business,”) and schedule a time to speak with them. If you are unable to reach them on the first try, leave a message that states when you will try them again – DO NOT expect them to return a call to you on their dime. Most owners are easiest to reach at the earliest part of the workday – or latest, when they are finishing things up and are at their desks.

4. When you speak with them, be sensitive to their needs. They are providing their time to help YOU – so keep your calls to the length you promised (unless you have a jovial “talker” that is willing to talk much, much more. Just use your judgment.) Have your questions ready. In fact, some people get “warmed up” to the process by using a static questionnaire for the first 3-5 calls, and then tailor their questions for the remainder. Do what’s comfortable for you – but also be sure to get all of your questions answered.

5. Hone your list to the most relevant questions currently on your mind. Don’t ask the obvious things – the things you could learn from the FDD or from speaking with your representative. Learn about the company culture, what it’s like to work

with the home office, how they would rate the support they receive, and, most importantly, how their business is performing – and why.

6. Be sure to ask a couple of warm-up questions of each owner that help you later “categorize” their responses and interpret what you’ve learned. For example, ask each how long they have been building their business, and whether they are single or multiple unit owners – because their responses will vary based on their answers to these questions. Is there a good way (or bad way) to discuss an owner’s earnings with them? Absolutely. Don’t be too blunt, if you can help it. We even suggest that you plan to ask earnings questions at the END of your conversation -- so that the first thing they DON’T hear from you is “what did you make last year?” Put yourself in their shoes!

Earnings are considered a private matter – and some owners are not as willing to share them as you may think. If they don’t want to share with you, so be it. Learn what you can and move on. But the best “rule of thumb” is to keep your earnings questioning simple. For example:

You said you have been building your business since _____. What was the greatest challenge during your first year of operation? Your second year?

How is your business structured? LLC? C Corp? S Corp? Are there any tax (or other) advantages to one versus the other that you might share with me?

“What were your gross sales last year?” Did that meet your expectations? (If not, what do you think happened?)

Might I ask you what your net profit percentage was last year? Is this average for the business? (If higher/lower, what happened?) What factors tend to influence your net profits the most?

Are you making what you thought you would make from this business? If not, why not?

Do we have suggestions for getting at the “soft” information – like home office support and ease of doing business? Yes, we do. Understand that when you are probing for “human-related” pieces of information, people don’t always respond with 100% accuracy. For example, if you ask an owner how much time they put into their business, they will smile and say “all of the time.” The reason for this is

that they are including “thinking” time. It’s human nature when you own your own business to feel as if you are “on” all of the time. So you have to temper your questions a bit:

“How many hours is your average workday? -or- “How many hours per day are you physically working your business? Is this more or less than when you started the business? Why?”

Below are some other questions you may want to consider when you’re doing validation calls.

Ease of System

“How would you rate the initial training you received? Was it sufficient, in your opinion?” If not, why not?

“Did you find it easy or difficult to follow the company’s system for building this franchise? What, if any, would you like to have changed?”

“Several have told me that ‘once they got the business going’ it became easier to manage – and took less of their time. Do you agree with that statement? Why or why not?”

“Do you see yourself hiring others to fill part of your role in the future? Why or why not?”

“Are you having fun in your business? Why do you say that?”

Support

“How would you rate the support you received from the home office...when you were ramping up? After the first year? Now that you’ve turned a profit?”

“Is there anything about the support you receive that has surprised you? Is it more, or less, than you had anticipated?”

Do you feel as if your CSR (Customer Service Representative) really cares about your success? Why or why not?

Is senior management readily available to you?

“What’s the absolute BEST thing the company does for you? What do you wish they would get better at?”

Growth and Competition

“Is your business growing as you thought it would? How do you see next year? Beyond that?”

“What is it your customers like best about what you provide them? How do you fare versus your competition?”

“When you entered your business, did you have a lot of competition? Has this changed? How do you handle it?”

“Are you comfortable with the marketing program provided by the company? If not, why not? What would you like to see differently?”

“What would you say is the most important thing you will have to do in order to succeed with your business in the future?” Why do you say that?”

Comfort Level with Business

“If you had to do it all over again, would you still purchase this franchise, given what you now know?”

“What do you like MOST about owning your franchise? LEAST?”

“What was your biggest surprise when you started your business – if any?”

“If you had just one thing to tell a new owner, to help him (or her) better succeed, what would it be?”

When you are done, thank them and ask if you might contact them again in the future. All of these owners were once in your shoes, asking the same questions. They understand that once you're off the phone, you think of those one or two additional questions that will plague you until you get them answered. So, if you've had a particularly good phone call with an owner, and you want to “keep the door open” with them, don't hesitate to ask them. Most of them will help you in any way they can. Just be sure to get their email address – now that you know them, it will probably be easier to correspond with them this way.

Now. JUST WHAT DO YOU DO WITH ALL OF THIS INFORMATION?

If you've been well-organized from the start, (and your consultant has provided you with many tools to help you be so) you should now have all of the financial

information you need to begin “modeling” your business. By “modeling” we mean completing simple financial projections that will help you estimate your working capital needs, your expenses, your “best case” and “worst case” projections for income and sales – and profits. (Again, your consultant can provide you with templates for this.)

You should also have a really strong idea as to the strength of “character” of your franchise choices and the strength of their support to you as an owner.

You should also feel comfortable (or not) with YOUR role as an owner – being confident that you can do what will be required – or at least, grow into it.

You should also be able to answer what it is about each business that you REALLY like. You know -- that ONE thing or feeling that gets you out of bed in the morning and makes you WANT to go to work.

It’s time to narrow your choices.

Your weekly meeting with your consultant should be focused upon discussing the pros and cons of each franchise – or helping you organize all of your learning in a way that your ability to narrow choices -- or eliminate options – becomes easier. And while your head is probably a bit full right now – resist the urge to take time off and let it clear. Right now is when all of the information is most fresh, and most clear – and you need to take advantage of this window in time.

NOTES

YOUR THIRD STEP

In this THIRD and final phase of the evaluation process, we want you to first take a deep breath and relax. Before you begin, you're going to have one final chance to meet the people at your franchise of choice – and then make your decision – “on your terms.” If you've followed our success strategy, you are “in the driver's seat” at this point – as the franchisor you're most interested in has been saying very positive things about you.

The THIRD PHASE: Personal Success – A Decision Made On Your Terms

Just like in the first two phases, you should have objectives for this important third phase. And they are:

- Obtain answers (or reinforce previously received answers) to any remaining questions
- “Seal the deal” in terms of demonstrating your enthusiasm, business acumen, and interest – with the franchise company decision makers...and SMILE! Franchising is very much “a relationship business,” and don't ever forget it.
- Get to know as many people at the home office as possible – they will become part of your “future network.”
- Make your decision

When you attend a Discovery Day, you may or may not be the only candidate attending. Most companies invite candidates from all over the country to come together for these sessions. And not all companies pay for your travel expenses – be sure to cover this detail with your franchise representative before you attend.

You are encouraged to take notes while you are there – but most ask that you do not record their sessions. The reason is that many companies do share certain confidential “nuggets” about their business that they would prefer remain confidential.

You will have some residual questions – and you might also want to have some other questions ready that demonstrate your continued interest in their business, such as:

What growth rate has the company experienced over the past five years? Is this a franchise growth rate or an owner growth rate? Have there been differences, and why? What will be the most important factors, going forward, to ensure the company's success?

What would you say is your greatest strength versus your competition? Why do you say that?

Does the company have any pending legal actions that were not disclosed in the most recent FDD? If yes, could you explain them and their possible implications to the business? Similarly, do you anticipate any changes to the business (pricing, royalties, business structure, etc.) in the upcoming FDD that I need to be aware of?

As you are asking ANY questions – keep “sensitivity” in mind. If for any reason your question could be perceived as sensitive, try to pull the appropriate franchise executive aside, and ask them on a one-on-one basis. Avoid creating controversy in front of the group – you’ll get the same answers when you ask privately, and won’t risk disrupting their meeting.

Most franchise companies use Discovery Day to share with you their future company vision; to let you see their operations and training manuals, (which you may have only if you purchase a franchise); to see all of their headquarters and key support people; to fine-tune any and all understanding about your specific territory (if applicable); and to answer ANY residual questions. These are “feel-good” meetings, designed to help make you as comfortable as possible in your eventual decision.

Generally, after you have left, the franchise executives meet and decide if you are to be awarded an opportunity to purchase their franchise. Your representative would then call you and inform you of their decision.

If you have followed this process – this should be a happy moment for you! If you express equal interest in purchasing upon hearing this news, your representative will prepare your paperwork and forward the franchise agreement to you for your signature.

By law, you have up to 15 days from the time you get the FDD, (this will vary a bit from state to state) in which to make your decision. If they formally offer you a

franchise, then legally, that franchise is “off the market” until you decide and/or execute a franchise agreement. Most franchisors will submit the Franchise Agreement to you with a memo, indicating that the offer of the franchise is “good until (date).” You should know that this is fairly normal procedure. If they did not put a “kill” date on the offer, the franchise location or territory would be off the market for as long as you were still considering the purchase. This doesn’t mean you can’t change your mind and postpone your decision to after the “kill” date – it simply means they can no longer guarantee you the particular location or territory you had been considering. It means this particular contract has been withdrawn, and your territory was “put back on the market” so to say. You can certainly understand that they cannot hold it indefinitely for you, particularly if another candidate had expressed interest.

Assuming you say “yes” after receipt of your Franchise Agreement – then NOW is your time to begin your new future.

There are several things required to help you “close” on your purchase. One, you need to name your business entity (your representative will guide you here) and determine the type of structure you want to create – an LLC (limited liability corporation); a “C” Corporation; or a “Sub S” Corporation. Your representative and/or consultant – or any other professional you may have a relationship with, such as your accountant or attorney, can help you understand the differences between these structures and which might be right for you.

You will sign your franchise agreement per your instructions from your representative. This “holds” your agreement, pending financing. If you haven’t already, you need to secure your financing. (Earlier, your consultant will have suggested to you that you should actually start the finance process as soon as you have decided that you are indeed going to purchase a franchise -- any franchise. Hopefully, you heeded this advice, and you already have a “jump” on it.)⁴

There are a number of companies that specialize in providing financing for franchises – and both your representative and/or consultant can also help you here. If you have a desire to start your business at a particular time (e.g., to take advantage of the Christmas retail season) you want to start the financing process as quickly as possible, as it can take anywhere from 4-12 weeks.

At this point in time, you will be spending your time with your franchise representative – and will have ceased your weekly calls with your consultant. You have made your choice, you're excited to get going, and you're ready to start your new future. Your representative will provide you EVERYTHING you need to know to get your business launched – and it usually all gets started with your attending training at their headquarters. If you need locations (retail or offices), they will guide you. If you need equipment, they will provide a list. If you need to hire employees, they will help you define the hiring characteristics you need. And so on. Again, you have purchased a proven “system” – and now you are going to benefit from their experience.

When you are ready to launch your business – you will start to feel those all-so-familiar butterflies in your tummy again. This is perfectly natural – you're testing yourself! It's a bit unnerving! Just take a deep breath and remind yourself: you have THE RIGHT STUFF to do this.

While your franchise has customer support people to help you – as well as a network of owners and executives that are still available to answer your questions – you might, on occasion, feel a need to have a “neutral” soundboard from which to bounce ideas, or ask an occasional question. EVERY ONE of our consultants has owned their own business, and they will know first-hand what you are feeling.

If this occurs, give us a call. We'll do the very best to remain a valuable resource to you. As a valuable client, you will have access to our library of management tools – which we hope you find helpful in building your business.

And, as your business grows, you may even consider our “for fee” counseling services. Call us when you're ready – and we'll be happy to discuss those with you.

Our very best wishes to you – and call us when you hit those milestones, as we'd like to share in your success.

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