# Should You Franchise Your Small Business?

by Robert Lerose

According to the International Franchise Association, franchises are expected to create 247,000 new jobs in 2015—a 2.9 percent jump over last year—and outperform every segment of the overall economy for the fifth year in a row. Beyond the larger impact on employment, the rewards of franchising your own business include helping to expand your brand, giving you access to a handsome amount of capital, and recruiting passionate, knowledgeable talent in a relatively fast timeframe. But the downside for the franchisor is a certain loss of control over the management of a particular site and taking a smaller cut of the profits. Some small business owners rush into franchising without even adequately seeing whether their business is franchisable.

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## Returns on investment

Experts point to three major benefits of franchising your business: money, committed managers, and efficient expansion capabilities. "Money is certainly the biggest reason. The franchisee basically spends all the money on the investment, so you're freed from capital constraints and can grow using somebody else's money," says Mark Siebert, CEO of iFranchise Group, a Homewood, Illinois-based franchise consulting firm.

Second, franchisees are usually highly motivated, stay for the long-term, and show more commitment than store managers who don't have a huge stake in the operation. Siebert says that it is not uncommon for a franchisee to outperform company-owned managers by as much as 30 percent. Third, you don't need to tie up your resources to get the new location up and running. For example, a franchisee would be responsible for finding a site, signing the lease, hiring local workers, and training the staff.

"You can provide the franchisee with guidelines and maybe with outside resources, but they do all the work," Siebert explains. "You don't have to build a big infrastructure, so your corporate overhead is lower. The franchisee is the one signing all the leases. As the franchisor, you're minimizing your risk by letting the franchisee assume some portion of that."

And the drawbacks? The franchisee will get to keep the majority of any profits and you'll have to cede a certain amount of authority—not easy for some entrepreneurs to accept. "You'll still have absolute control when it comes to your brand's standards, but you're not going to be able to hire and fire a franchisee or their employees the way that you would with a corporate employee," Siebert says.

In evaluating whether a business is suitable to be franchised, Siebert says to consider three things. First, does your business have a unique business model or dominate its particular niche? Has the business shown that it can actually make sales consistently? Does the management team have credibility and experience in knowing how to run their business successfully? Second, can your small business be duplicated easily? Or will your business encounter regional or legal hurdles? Does it work because it occupies a preferred location or can it flourish in different markets?

"Third is what we call the acid test. We'd like to see a financial return on the investment and a financial return on the time," Siebert says. "Will the franchisee make a return on their time that is about the same kind of return they'd make if they got a job doing the same thing? If I'm going to be managing a sandwich shop, I would get a sandwich shop manager's salary. And then if I'm going to invest $200,000, I'd want to get a return on my total investment as well. Typically if you are looking at an individual franchisee—by that, I mean somebody who buys one location at a time—they're looking for a return in year two or year three of at least 15 percent. For someone who is going to do multiple locations, that individual would typically be looking for a return that's closer to 20 percent or more."

## Having a similar philosophy

Setting up your business to be ready for franchising comes with certain costs that some small business owners may find daunting. For example, franchisors need to prepare documents to cover legal, operational, and training concerns, which can be expensive.

"Getting your documents done—such as the legal documents, franchising agreements, operating documents, and the training material—varies in cost depending on where you go," says Lizette Pirtle, co-founder and CEO of Expansion Experts, an Ashville, North Carolina-based franchise consultancy specializing in working with small businesses. "If you go to a big firm, you're going to be paying $150,000 and over. If you go to a smaller boutique firm, you're spending between $65,000 and $95,000, depending on the complexity of your business and how much [work] you already have done."

Besides having enough cash to cover preparation of the documents, Pirtle says that small businesses must be able to give some kind of continuing support to the franchisee, such as a durable business model or a solid reputation in a particular niche, that makes it attractive and desirable to stay connected with the franchisor even without the legal binding.

Franchisors should be selective when choosing a potential franchisee, looking for people who easily complement the existing culture of your business. "The most important thing to look for would be a connection on an emotional level and a buy-in into the ethics and culture of the company," Pirtle explains. "If that exists, then any problem can be solved in my book. The basis of a relationship is understanding, communication, and similarities between what we believe is important in life. If that is there, then there is room for anything to take place. If that is missing, then conflict arises eventually."

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## Selling your vision

A passionate belief in the purpose and ethics of their business is a prerequisite for many entrepreneurs, but it can also be a driving force in the franchise process. Case in point:

Feeling dissatisfied with his corporate banking job in London, Australia-born Phillipe Christodoulou moved to Argentina and discovered his real purpose in life was to make a positive difference in the world through the power of business.

In 2010, he opened The Eco Laundry Company in Buenos Aires—the only laundry to be a Certified B Corporation, meeting “rigorous standards of social and environmental performance, accountability, and transparency.” Christodoulou says that every part of his business is as environmentally-friendly as possible. He uses reusable laundry bags made from recyclable unbleached cotton, a 100 percent organic dry cleaning process, high-efficiency machines that consume small amounts of water and energy, and biodegradable nontoxic soaps and softeners.

Christodoulou became co-owners with Jean Calleja, a former global head of communications at an investment bank, who opened a location in New York City in June 2012. After a long and thoughtful consideration of their goals, they decided that franchising should be the next step in their business strategy.

“We realized that franchising—and having owners operating each individual unit that had a vested interest in making sure that the quality of service was being delivered—would give us the best chance of creating an overall brand that was known for excellence as well as all of the other things that we stand for,” Christodoulou says.

In January 2015, they began looking for franchisees who would be committed to their ethos and vision. “We feel that the right candidate will be someone who is genuinely interested in sustainability,” Calleja says. “That would be the number one reason someone would be interested in our business model.”

Franchisees should expect to invest between $230,000 to $350,000 initially, and will receive a range of support, including extensive mentoring at the corporate training center and onsite, an in-depth operations manual, and marketing assistance. “People know the difference between when you’re reciting a spiel or when you’re talking from the heart about something,” Christodoulou says. “That’s what people connect to, so being genuinely connected to what you’re doing is a fundamental key to being able to get people to buy into your philosophy and to your brand.”