Replication:
Franchising & Licensing

• Replication is when a business idea or system is copied & rolled out elsewhere in another location
What is franchising?

“A franchise operation is a contractual relationship between the franchisor and franchisee in which the franchisor offers or is obliged to maintain a continuing interest in the business of the franchisee in such areas as know-how and training; wherein the franchisee operates under a common trade name, format and/or procedure owned or controlled by the franchisor, and in which the franchisee has or will make a substantial capital investment in his business from his own resources.”

- Definition by International Franchise Association

• Franchising is a faster, cheaper form of expansion than adding company-owned stores, because it costs the parent company much less when new stores are owned and operated by a third party. On the flip side, potential for revenue growth is more limited because the parent company will only earn a percentage of the earnings from each new store.
History

- Singer Sewing Machine – first franchise (mid-19th century)
- Automobile (e.g. Ford), petroleum products (e.g. Shell), soft drinks (e.g. Coca Cola)
- Food and restaurants (e.g. McDonald’s, Starbucks)

Why Organization goes for franchise

- Home markets saturated – attractive opportunities overseas
- Lack of/relaxation of regulations in most countries
- Expansion of international trade
- Exposure to international media
What is Franchising

• Franchising:
  – Is NOT a business or an industry.
  – Is a method of distributing products and services to consumers.
  – Utilizes a network of local owners ("locally owned and operated") operating under a shared brand.

• Franchisees:
  – Pay the franchisor for the right to do business under the shared brand
  – Operate under a specified, controlled business method or format

• Franchisors:
  – Provide significant initial and on-going support

Role of Franchisor & Franchisee

<table>
<thead>
<tr>
<th></th>
<th>Franchisor</th>
<th>Franchisee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Site Selection</td>
<td>Oversees, may choose</td>
<td>Chooses with approval</td>
</tr>
<tr>
<td>Design</td>
<td>Provides Prototype</td>
<td>Implements design</td>
</tr>
<tr>
<td>Menu</td>
<td>Set by Franchisor</td>
<td>Changed only by approval</td>
</tr>
<tr>
<td>Prices Decides</td>
<td>Recommendations</td>
<td>Decide actual prices</td>
</tr>
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</table>
Common Franchising Terms

• Franchise Fee – one time fee paid at signing
• Total Investment – the amount you will spend to open business
• Royalties – % of gross or flat fee
• Ad Fund – % of gross or flat fee
• Term – # of years of agreement
• Renewal – terms outlined in agreement
• License Transfer – selling your franchise
• FDD – Franchise Disclosure Document

What Franchisor offer

– Training
– National & Regional Advertising
– Operating Procedures & Operational Assistance
– Supervision & Management Support
– Increased Spending Power, Access to Bulk Purchasing & Economies of Scale
Advantages

Franchisor

• Expansion
• Legal Consideration
• Operational Considerations
• Competition

Franchisee

• Expansion
• Quick Start
• Training
• Reduce Risk of Business Failure
• Ready Product Acceptance

Types of franchise

• There are three main types of franchise:

• Product distribution franchise;
• Business format franchise; and
• Management franchise
Product Distribution Franchises

- A product distribution franchise model is very much like a supplier-dealer relationship.

- Typically, the franchisee merely sells the franchisor’s products. However, this type of franchise will also include some form of integration of the business activities.

• The franchisor licenses its trademarks and logo to the franchisee but does not necessarily provide them with an ENTIRE system for running their business.
Examples of famous product distribution franchise:

Product distribution franchise

- **The Coca-Cola Company**: Produces the syrup concentrate.
- **FRANCHISEE**: Sells the syrup concentrate.
- **Restaurants & F&B Outlets**: Produces the final drink.
- **Retail Stores**: Produces the final drink.
- **Vending Machine Operators**: Produces the final drink.
Business format franchise

- In a business format franchise, the integration of the business is more complete.

- The franchisee not only distributes the franchisor’s products and services under the franchisor’s trade mark, but also implements the franchisor’s format and procedure of conducting the business.
Management Franchise

• A form of service agreement.

• The franchisee provides the management expertise, format and/or procedure for conducting the business.

Examples

American Idol

Hilton

The UPS Store®
Why is franchising important to SMEs?

• Leveraging on a recognised brand name
• Enhancing business image
• Ensuring consistent quality
• Attaining higher productivity/better motivated staff
• Access to good locations
• Economies of scale
• Reducing risks of failure

Common Mistakes of Prospective Franchisees

• Not analyzing the local market in advance
• Not analyzing the competition
• Not making thorough due diligence of the franchisor
• Not choosing the right location
Franchise Documentation

- Operations manual(s)
- Training program
- Legal documentation
  franchise contract, franchise offering circular
- Franchise marketing materials
  brochure, application, press releases, web page
- Franchisor operations manual
- Franchise registration application(s)
• A company sells licenses to other (typically smaller) companies to use intellectual property (IP), brand, design or business programs.

• These licenses are usually non-exclusive, which means they can be sold to multiple competing companies serving the same market. In this arrangement, the licensing company may exercise control over how its IP is used but does not control the business operations of the licensee.

Form of License

• License is a form of foreign market entry based on a contractual relationship, where a company (the licensor) grants rights to intangible property to another company (the licensee) to use in a specified geographic area for a specific period time and the licensee ordinarily pays a royalty to the licensor.
Elements

• Contractual relationship
• Licensor
• Licensee Rights
• Intangible property
• Payment (Royalties)
• Specified geographic area and specific period time

Contractual relationship

• Is the relationship that exists between parts to sign a contract, establishing rights and obligations
Licensor & Licensee

- Licensor: Is obliged to furnish technical information and assistance, agrees to make available to another company abroad, use of its patents and trademarks, its manufacturing processes, its trade secrets, and its managerial and technical services.

- Licensee: Is obliged to exploit the rights effectively and to pay compensation to the licensor, agrees to pay the licensor a royalty or other form of payment according to a schedule agreed upon by the two parties.

Intangible Property

- Include any item of worth that is not physical in nature. Patents, inventions, formulas, processes, designs, patterns
- Copyrights for literary, musical, or artistic compositions. Trademarks, trade names, brand names
- Methods, programs, procedures, systems. Manufacturing techniques
Drawback

• The major drawback of licensing is the problem of controlling the licensee due to the absence of direct commitment from the international firm granting the licence. After few years, once the know-how is transferred, there is a risk that the foreign firm may begin to act on its own and the international firm may therefore lose that market.

Advantages of Licensing

• A license allows the licensee to use, make and sell an idea, design, name or logo for a fee. They are advantageous for licensors because they allow them to expand their business’ reach without having to invest in new locations and distribution networks.
# Franchising Vs Licensing

<table>
<thead>
<tr>
<th></th>
<th>Franchising</th>
<th>Licensing</th>
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</thead>
<tbody>
<tr>
<td><strong>Governed by</strong></td>
<td>Securities law</td>
<td>Contract law</td>
</tr>
<tr>
<td><strong>Registration</strong></td>
<td>Required</td>
<td>Not required</td>
</tr>
<tr>
<td><strong>Territorial rights</strong></td>
<td>Offered to franchisee</td>
<td>Not offered; licensee can sell similar licenses and products in same area</td>
</tr>
<tr>
<td><strong>Support and training</strong></td>
<td>Provided by franchiser</td>
<td>Not provided</td>
</tr>
<tr>
<td><strong>Royalty payments</strong></td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td><strong>Use of trademark/logo</strong></td>
<td>Logo and trademark retained by franchisor and used by franchisee</td>
<td>Can be licensed</td>
</tr>
<tr>
<td><strong>Examples</strong></td>
<td>McDonald's, Subway, 7-11, Dunkin Donuts</td>
<td>Microsoft Office</td>
</tr>
<tr>
<td><strong>control</strong></td>
<td>Franchiser exercise control over franchisee.</td>
<td>licensor does not have control over licensee.</td>
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