



Submission to the Parliamentary Inquiry on Franchising 2018

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CEO and Founder



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Introduction

I first became involved with franchising in 1982 when I became a multiunit Bedshed franchisee, in WA. When I sold these in 1987, I founded a franchise consultancy, the Franchise Alliance. The Franchise Alliance started as a franchise broking service but soon became a full-service consultancy to the industry, offering franchising advice to business owners wanting to convert, franchise broking, and general advisory services to both new and well-established groups assisting a number of major Eastern States groups to set up in WA. We also established our own franchise groups to fill areas of the market not being catered for at the time. And we franchised The Franchise Alliance so it operated in all States and New Zealand. Needless to say, we learned much about operating a commercially successful franchise group through those years.

We found franchising was a powerful business format which allows business to grow provided care is taken to ethically look after people on all sides and address the full suite of business elements which need to be modified for success. We often had to simplify the original conventional business or concept whilst adding the critical layers essential for success as a franchise.

We learned Franchising is not just a legal agreement and good product. To be commercially successful, it involves modifications to every element of business from its financial structure, to branding and marketing, online structures, corporate structures, intellectual property protection, systems and documentation, support services and above all the relationship between the people who make it function, the franchisor and franchisee. This is why it takes a team to get it all working. In addition, so many seem to overlook the fact that this is a business partnership and needs to be treated respectfully as such if it is going to be successful. Both sides need to be profitable and the leader, holding it all together is the franchisor.

These concerns are why we made submissions to the first Bedall Inquiry in 1990 and the Franchise Taskforce Inquiry in 1991. At the time I was WA Chapter State Secretary of the Franchise Association of Australia (later succeeded by the FCA) and secretary to the then President Alannah McTiernan.

The Franchise Alliance, somewhat controversially, fully supported the Code of Conduct when it was first introduced in 1993 and later supported its introduction as a mandatory code in 1998. We believed carefully structured franchise groups with diligently supported franchisees make for commercially successful businesses which are valuable assets for franchisor and franchisee. We concluded that the uniform disclosure documentation would make fair and direct comparison between franchisors and good franchises more attractive to buyers. Overlook any one of the elements that make this relationship work and the business will struggle and commercial failure for all sides of the equation will often result. We avoided such groups.

Today my position has not changed. I am at the later stages of my career and seriously concerned about the future of franchising in Australia, my passion of 36 years. Franchised business is an important growing part of the economy today and, managed properly, will lead to

increased employment and export to overseas markets. I do not want to see it deteriorate.

So, after retiring in 2008, I returned to the industry in 2011 because I saw franchise consulting had not changed over the years and I was convinced that with the continuing sophistication of business across the board, the time had come to show a different way of doing things more suited to modern digital businesses operating within an ethical framework. It is no accident that I work with a team of franchise savvy business specialists in my new venture, Franchise Simply. And it is no accident that I have systemised the process to franchising so that my clients understand what is required upfront and go through each clear step with my input and, as necessary, the advice from my specialists. My Franchise Training Workshops and Franchise Programs are accredited by the FCA and IFA.

Some of the current shortcomings I see

Franchisors not understanding or covering their areas of responsibility

It has broken my heart to see new business owners trying to franchise without understanding what is involved and failing or at best falling well short of their true potential, and some of the long-standing household names doing the same as new management comes on board with a similar gap in knowledge. It is the recent suite of failures of these big groups which make the point so clearly.

To be commercially successful franchisees do need to bring in their part of the deal, providing the best service to customers and bringing in the money.

But franchisors also have to understand they are responsible for their interlinked part of the deal...

- Keeping the brand and marketing on trend and successful for the group
- Selecting the right franchise business partners (franchisees) to become their partners on the ground
- Structuring the group so the balance between the people and the money works in the long term and all necessary business elements are addressed
- Supporting their franchisee business partners so they have the best possible environment to be successful
- Maintaining this structure and support services through careful procedures for both the franchisor and franchisee so there can be consistency in service throughout

I expand on this in the Attachment describing my approach to franchising.

The element most overlooked is probably the balance between the people and the money and it hinges around the likely personality a particular franchise needs to deliver the service or product to their customer base and the likely ability of that personality to handle some of the business aspects.

Franchisors and successful business people generally tend to have an entrepreneurial personality, happy to pick up the phone to make a marketing call and keep an eye on cashflow and budgets. The trouble is, so many sectors of the franchise industry today are asking franchisees to deliver a domestic, caring and supportive service – the health industry is a case in point – and people who will deliver that service with the care required are so often really not able to look after marketing or finance. So, if the network is to be successful, a franchisor has to take on these tasks and adjust budgets and the support services accordingly. Support given to a bookkeeping franchise or a retail franchise or real estate franchise requiring people with very different personality and skill sets will look very different.

So, it's not that simple. Getting a franchise structure commercially right requires an understanding of target markets and marketing, personality, finances as well as the commercial and legal environment and the way these elements work together in different industry types.

Yes, franchisee businesses need to look the same, feel the same and operate the same for the network to be successful and so franchisors will have rules in place which will need to be enforced from time to time. And yes, the relationship between franchisor and franchisee is probably the trickiest in business. And yes again, any franchisee has the responsibility for making sure they know what they are buying into and for running their own franchised outlet so it is profitable.

But the bottom line is, franchisors are responsible not only for the franchisor business operating successfully but the whole group and for giving their franchisees the best opportunity to be successful too. It is the franchisor who needs to know what makes a franchised group work and how to best help franchisees undertake their part of the deal, bringing in the money.

Overseas franchise groups entering Australia with the wrong idea about franchising here

Many of the same issues are seen with foreign groups establishing in Australia. Whilst their models may work effectively in their country of origin, many do not to understand the difference in the Australian market. Classic examples of these failures include giants like Subway, Domino's, and Krispy Kreme in their early days. Many others have tried and withdrawn quietly. I meet frustrated prospective franchisors frequently at Expos and other venues, trying to bring in master franchises from overseas and asking for advice on recruitment, not understanding that I am unable to help with this in the absence of a properly structured franchise suitable for the Australian commercial market and our legal requirements. I know there are lawyers and brokers who will provide the assistance requested without advice about business aspects outside their immediate area of expertise, even though the result will almost certainly not be successful.

The balance of power in Public Companies and large corporates with focus on shareholder returns is giving some a short-term view of managing franchised businesses

Many franchisors and franchisees are corporations. Much has been written about this relationship in this environment, especially when a franchisor fails and I will not go into the specifics.

However, I am concerned that, legally, corporate law takes precedence over the Code. This means corporate franchisors have to give their shareholders wishes precedence. What this leads to, especially when new management and advisors come on board, is a short-term view and a tendency to extract as much money from franchisees as possible, without understanding the essential responsibilities of a franchise group to keep their franchisees profitable in the long term within reason.

Examples I have seen include Pie Face, Eagle Boys and many others. In each case these businesses were launched or acquired by people with little franchise experience but big plans to draw significant profits for their shareholders, often at the expense of the franchisees whose needs were ignored. This issue is not restricted to the franchise sector. Dick Smith's recent episode is an example of the same principle in the conventional business sector

Retail Food Group, most recently fell into this narrow minded short- term trap, putting the whole group into jeopardy and giving the franchise industry a bad name. The thing is this approach does not serve anyone well in the long-term. Retail Food Group has experienced significant losses as a result and their shareholders have definitely not benefited.

Somehow, the message needs to come across that the long-term profitability of the whole group

is necessary if shareholders, investments and returns are to be protected and that means making sure each franchise group is correctly structured, correctly systemised with caring relevant franchisee support.

Franchisee due diligence is still off the mark

Understanding people is at the heart of selecting good franchisees. Every franchise needs to have the right people delivering its product and service.

Whilst franchisees are encouraged to seek professional advice, my experience is that many don't and many advisors across the board, from large and small commercial practices, often have a limited understanding of the operational aspects of franchising and so are unable to truly give appropriate advice. It's important to remember all forms of business are hard work requiring trust, commitment and a determination to succeed above all and franchisee business people are not exempt from that.

Unfortunately, many franchisors fail to understand the nuances around selecting people with the right approach to business and their product and, also unfortunately, all too often sales driven franchisors will recruit them anyway to get that sale.

Quality of commercial advice to the franchise sector is woefully lacking

So many of the issues addressed above exist because the commercial advice to the industry is lacking. The problem I see today is the consulting industry advising prospective and existing franchisors has, if anything, splintered and is now mostly focused on specific areas of expertise, not the whole.

So yes, the Code does advise prospective franchisees to seek legal, accounting and commercial advice before entering into a franchise agreement and franchisors are required to ask franchisees to get this advice too.

But the Code does not require new franchisors and franchise managers to seek such advice before they set up or take on the reins managing a franchise group, whether publicly or privately owned.

And unfortunately, many franchisees and franchisors choose not to seek guidance, except from the lawyer when they get legal documents checked (franchisees) or drawn up (franchisors).

And even if they do go to other consultants, my experience is that the quality of advice available to the sector is, for the most part, splintered and not the best.

There are a number of reasons.

1. Understandably, not knowing any better, prospective franchisees and new franchisors in particular will tend to go to their local accountant and legal advisor for professional advice. However, franchising is a specialist area of the law and accounting which local tax accountants and family law practitioners do not generally fully understand.
2. Pulling advice together from different disciplines to create franchise structures in different industries is tricky. Each specific discipline is not usually in the position to give generic advice on how to combine their area of specialty with other areas. This usually involves a discussion with the franchisor and a general franchise advisor as each aspect is dealt with and added to make up the whole. The Attachment giving the detail for the process I recommend describes the steps involving other disciplines which need to be covered before a legal agreement and associated documents are drawn up.
3. Although the legislation and advice around franchising suggests legal, accounting and commercial advice should be taken, not many understand what commercial franchise

advice actually means. I believe, this needs to be defined more clearly around the outline in the Attachment.

4. Unfortunately, I have experienced many very knowledgeable franchise savvy members of the legal profession who have worked in the industry for a long time, intimating to their clients that they have the expertise to give rounded commercial advice on structuring a franchised business. While they might know which business elements should be investigated, I do not believe they have the commercial expertise to advise on the whole, particularly on issues such as the complex interrelationship between, personality, support and franchise structure, operations systems and manuals, training and recruitment which are one of the cores of a successful franchise. My heart always sinks when I am all too frequently asked, *'I have my legal agreement already drawn up and now I want to set up my franchise, can you help me?'* Or, *'I want to franchise and have an agreement but it doesn't seem to be working, can you help me?'*
The answer is almost always yes, we can help, but you will need to discard the existing inappropriate legal documents (losing the money invested) and start again.
5. My experience is that these problems exist at every level of the franchise industry. I know some say advice received by the corporates is unbalanced because they can afford the best around. However, experience tells me corporate advisors from big name firms are probably the worst offenders, giving limited advice within their specialties of law and finance, with little understanding on how franchising actually works. They also suffer a little from hubris and, not knowing what they don't know, don't seek a more rounded and ethical input from elsewhere.

Is there a need for training and accreditation?

Do the questions raised in the previous section mean that there is a need for advisors to the industry to be accredited franchise specialists?

It is also easy to become outdated with the changes taking place in today's fast-paced business environment. Advisors and franchisors who have been successful for many years do not always understand the changes they need to make over time.

Because of all the issues outlined above and I do wonder if key people working in this amazing but tricky industry need to regularly receive training on their responsibilities:

- Before they start to work in the industry
- And regularly (annually) on the changes in the rapidly transforming climate of business and franchising today

I do believe it is also important that advice is not just theoretical. While there is a good case for training to come from our academic institutions, there must be some on the ground expertise in the mix.

Finally, there is no organisation clearly given the responsibility to examine and accredit franchisors, franchisees and their advisors. The FCA informally holds this role now, and only in a limited way. Of the 3000 or so franchise groups I believe operate in Australia today, the FCA only represents about 500.

An absence of clear systems and support

This is a two-pronged issue.

Franchisor operations are rarely adequately documented

I'm amazed even the biggest franchise brands initially take the greatest care in preparing the operations manuals for their franchisees, but far less to write their own. Many have none.

How then can their support staff know how to consistently deliver brilliant customer service to their franchisees, especially as the kind of support needed varies so much from franchise to franchise?

They can't. Because, as the network grows and new support staff are introduced, the doctrine of Chinese Whispers will rule...

Support staff won't understand the values or the care expected. They won't know how to report about things going brilliantly right or not so well. A franchisor won't know if franchisees are making interesting changes or floundering.

Getting franchisees to use the operations manuals is difficult

I am also amazed even the biggest brands tell me they simply cannot get their franchisees to use their operations manuals. The reason – most manuals are still text-based documents, much too detailed, difficult to use, not kept up to date, not relevant to the job being done on the floor – the list goes on.

As a result, franchisors have considerable trouble keeping their brand relevant and their franchise business partners running their outlets in accordance with the brand and fair business requirements. Busy franchisees just get on with the job trying to make money any way they can – outside the rules.

It makes sense relevant, usable interlinked cloud-based systems for both franchisor and franchisee are needed to make sure everything works together. Documenting just the franchisee process so it fits a clumsy text-based manual is no longer adequate.

And franchisor and franchisee systems in today's digital environment need to be easy to use, secure and cloud-based across all media formats distilled to the simplest form. And Franchisors need help in understanding how to create and keep their systems usable and up with the times.

Over regulation of the industry

In spite of my concern over many franchisors not having an understanding about their responsibilities, I am also extremely concerned that the industry does not become over-regulated. If changes to legislation are to be made, they need to be carefully thought through so the impact has the needed outcome, does not dampen the franchise sector which is an important part of the economy and so it is fair across all business.

Franchising in Australia is already the most regulated in the world.

It is also the most successful and is a significant fast-growing part of the economy.

Beware the dampening effect of red tape

Red-tape is acknowledged by Governments world-wide to be stifling business growth and it is an especially heavy burden for smaller operations. Onerous legislation creates larger administration costs which could otherwise be allocated to R&D and growth.

I believe aspects of the recent Fair Work legislation places an inappropriate responsibility on franchisors when it's the franchisee's own responsibility to address employment issues within their own businesses. The unfair work practices addressed by this legislation probably rightly affect all areas of business. It is the additional unfair burden on the franchisor and 'franchising' which I believe is undeserved. Having to bear the burden of their franchisees wrong doing has certainly caused some of my prospective franchisors to pause.

I believe unfortunately, this legislation is a result of the most recent well publicized issues with a number of large franchise groups which have been seized upon and unjustly portrayed as

typical for the whole sector. We are acclimatized to seeing building companies fail but continue to respect and support the rest of the industry. This has not been the case with franchising where fear mongering has been taken as a generalization. The impact of this legislation on the Australian economy is not known, but appears significant, dramatically affecting asset values of good honest efficient and hardworking franchisees and franchisors, reducing the salability and value of their businesses.

So, if new requirements are to be introduced, and I do see some need around, I am asking that this be kept to a minimum.

In closing

Today, much is said about the impact of disruption, particularly from online competition. But the majority of businesses across the board, conventional models as well as franchised, are falling seriously behind the requirements of the 21st Century with their practices, the tech they use and the systems needed to implement them efficiently. Many of today's household names are struggling and many will drop from market prominence.

Franchised businesses are a significant part of the Australian economy and need to be encouraged

This is where franchising, a model which has disruption at its core, can lead the way in Australia and present more efficient, profitable businesses offering more people the safest way to run their own business so effectively increasing employment and adding to GDP growth.

The future of business in Australia has the opportunity to lead the world in efficiency, profitability and create a significant export model. See current diverse examples such as Boost Juice, Domino's (Australia owned), Poolwerx, GJ Gardner, Cartridge World and Harvey Norman.

The statistics of franchising are well known, with the steady growth of people in the sector beginning to overtake those previous employment dominating industries such as manufacturing. This is not the time to suppress the energy and creativity of the franchise sector. It needs encouragement and fair and reasonable climate in which to operate.

All business is affected by change

The franchise industry is not alone in being affected by change. the retail sector (both conventional and franchised) has been the one to suffer most in recent times, affected by no small means by the predatory attitude of shopping centers, especially the major owners. Local strips and small centers have diminished, and so once the majors secure a tenant and their business is seen to succeed, rents are ramped up unnecessarily. It is take it or leave it and surrender your business asset at the same time.

Recently, Spectrum Analysis strategic network planning consultants have suggested that in the last five years Moving Annual Turnover of centres has increased by only 8 to 10%, yet rentals in those centers has increased by 25 to 30%. Little wonder all retailers are struggling under the pincer effect.

This issue is all the more concerning because the major shopping centers are dominated by a few very large players whose shareholders are attracted to and dependent on the high historic returns. Many of these are large established, super-fund owned centres.

And franchise outlets are a dominant element in every shopping centre precinct – just look at the food courts. The disappearance of these tenants would have a huge impact on the economy overall.

We need to take advantage of the growth opportunities offered by the franchise sector

Today with the rate of change, there are huge opportunities available. To take advantage of them we need brave entrepreneurs with vision who recognize the risks involved and can seize the chance without the severe constraints that governments seem inclined to implement, restricting free and open markets. Without free markets, there is likely to be a heavy long-term damage inflicted on the economy and social wellbeing of Australians.

To conclude

While I do believe there is a need to tighten up a couple aspects of the industry so:

- **New franchisors and franchise managers are aware of the full complexity of the commercial issues they need to take into account to be successful, and the legal structures are only a part of the mix**
- **Advisors to the industry need to have the right ethical, technical and contemporary skills in their specific area and understand how they fit into the whole picture**
- **Ethical, general commercial advice needs to be recognized as being an important, part of the mix**
- **So, I believe accredited training with annual reviews needs to be introduced for franchisees, franchisors, key franchise staff and the advisory industry**
- **Franchised businesses need to have good, relevant, easy to use systems and procedures for both sides of the franchise group**

I also believe any changes must not occur in a manner which will over-regulate and dampen this very important economic sector.

Attachment

Successful franchised business from concept or by converting a conventional business

The process

Whoever a prospective franchisor works with, I believe that the following four steps should be followed at least in general. This way, the commercial issues that need to be addressed can be carefully built, layer by layer, using the right advice at each step.

Step One

Develop the big-picture structure of your franchise group around the demographics of your brand and the likely personality of your future franchisees and the support they will need to give them the best chance of success.

This involves spending time working with franchisors to:

- a. Determine **exactly** the core business a franchisee will be delivering. This discussion, held with me, often involves simplification of the business itself. Entrepreneurial business people have a tendency to build businesses with many sectors, overlooking the fact that they will find it hard to find people similar to themselves to run their franchises. For example, I have dealt with a wedding business, which, as a conventional business, delivered both the wedding ceremony and the wedding breakfast. When building the franchise, the owner realised this was not possible for one person and that the two sides of the business needed people with different skillsets and personalities. She divided the business into two separate simpler franchise groups, interlinked so they could easily deal with the same clients. This scenario is very common but not understood by the industry.
- b. Check the brand to make sure it will meet the desires and fears of a clearly defined target market. Having a brand which is right is elementary business management but it is so much more in a franchise. It is the basis of the group, part of the IP being sold to a franchisee, and it is this which makes sure every outlet can look, feel and operate the same.
So, we work closely with branding specialists with experience in the franchise industry to make sure the target market is clearly defined and that the branding is attractive. We are very aware branding is not just logos and colours, it involves everything about the business, including quality of service, copywriting and much more.
- c. Develop the principles for online and offline marketing for the group and who will take on how much of the Local Area Marketing. This enables the franchisor to work out how much branding and advertising will cost, how it will be funded and what the contributions to the Marketing Fund will be.
- d. Through a. above, knowing the likely personality of future franchisees, we can work out the level and kind of support needed. For instance, some franchisees will require significant training in business as well as the technical and service aspects around the core product or service. Others not so much. From this, other royalty payments and Contribution Funds can be estimated.

The steps a. to d. above enable the franchisor to work out an organizational or department structure, the number of levels that will be needed to support such a group and many other fundamental structural issues.

Step Two

Define the detail of a number of business elements to support this structure including but not limited to:

Budgets and fee structures

Budgets are worked out for the existing business and then using the information from Step one, for the likely franchisee businesses and the likely franchisor business and for any other levels required

Once the budgets are confirmed, we work out the fee structures and royalties.

This work is done with a franchise savvy accountant and my, on the ground, input.

Territories

Not all franchises have defined territories. But if they do, we work with territory specialists, experienced in franchise groups. This work is clearly based on the demographics from the brand and the budgets and fees above

Corporate structures

Franchised businesses require different corporate structures to both protect the IP owned by the franchisor and to deal with tax issues. This is dealt with by a specialized franchise accountant with experience in this area.

Trademarks and intellectual property protection

Needed to protect the franchisors brand and in so doing, giving franchisees security. Completed with a trademark lawyer

Communication and support plans

Although not often done, Communication and Support Plans give franchisors a clear picture of what they will have to do to support their franchisees to give them the best chance of success

Training for induction and ongoing support

Essential if this is going to work. Training plans are not often prepared at the beginning but the best franchises take care over planning training and its delivery. We have training specialists on call if needed

Step Three

Design the final structure of your franchise group through your legal and operational documentation

Legal documents

Only once the elements outlined above have been clarified, will a prospective franchisor have the information to give to a lawyer to draw up relevant and satisfactory legal documents.

Most franchise savvy lawyers have a questionnaire which helps them identify the issues to be addressed. I work through this questionnaire with my clients to make sure the information they are giving their lawyers is commercially appropriate for the kind of franchise they are about to create. I have had many a spirited discussion with lawyers

about what and how a specific issue is to be included.

For instance, these legal documents will be difficult to change in the future and there are issues which may be better placed in operations manuals where there will be more flexibility for adjustment if it is needed later.

Operation manuals

Franchisee manuals

We encourage franchisors to start to write the franchisee core business procedures at the beginning once the big picture of the group and the franchisee business has been clarified.

However, franchisee manuals need two other sections which cannot be added until the business elements have been detailed.

One of these sections will outline the responsibilities and tasks associated with running a franchised business, the relationship between the operations manuals and the legal agreement, how franchisees will be involved with franchisor support services, reporting, attendance at conventions and meetings, the Advisory Group, the list can be significant.

The other section is usually around how the franchised outlet will be administered – things around bookkeeping and finance, marketing, personnel management and so on. This is where things such as the Fair Work and OHS legislation will be covered.

These manuals must be simply constructed, simple to use, relevant, hyperlinked and tagged so things are easy to find and secure. Modern business really needs cloud-based procedures that form the foundation of any training so franchisees go to them first with a question.

Franchisor manuals

Not often in place in my experience. But where you have a franchise group which needs a specialized support service targeted around developing the skillset and business ability of your franchisees, it is essential.

Testing the system

Once the legal and operational documents are together, these systems will need to be tested with the first few franchisees or pilot outlets

Step four

Deploy your franchise group and lead your business partners into the future.

Finally, a franchisor will be in the position to recruit new franchisees.

Franchisee recruitment is detailed, bound by legislation and very different from either employing staff or selling a product.

Most business and franchise brokers do not appreciate this. And although brokers and other recruitment services are useful for attracting potential franchisees to the brand, final selection must be overseen by the franchisor, following a clear recruitment process. This way franchisors will bring on board willing business partners, understanding their responsibilities for running their own business and with the best skillset, personality and financial background to get the job done.

Because of these issues franchise recruitment training really needs to be mentored by someone with experience in the area.

The value of knowing what you are going to do before you start

Conventional consulting gives advice as required across the table verbally one issue at a time. And while this is a step by step process which is best approached sequentially from step one to the end, there is enormous value in understanding the big picture and how each element fits together.

This is why we require our clients to attend one of our Two Day Workshops before they begin the program and why we have documented the program so that people understand what is required at each step, making it more effective to go through the process.

Our workshops are presented by myself and some of my franchise savvy specialists.

They cover the following aspects.

Introduction	Brian Keen
Legal aspects of a franchise	Lawyer
Territories	Brian Keen
The flow of money in a franchise	Brian Keen
Corporate structures and budgets	Accountant
Organisation structure	Brian Keen
People, personality and support	Systems director
Training	Training specialist
Branding	Brand and marketing specialist
Franchisee recruitment	Brian Keen
Commercial applications of a franchise agreement	Brian Keen

The conclusion covering the commercial aspects of a franchise agreement, rounds up the sessions by explaining why elements from every topic covered are often added to a franchise agreement which is why the process builds the way it does with documentation happening at the end.