

Submission to the Senate Inquiry

The operation and effectiveness of the Franchising Code of Conduct

from



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Introduction

We thank you for the opportunity to put forward a submission to the Senate Inquiry and anticipate it will further assist in the transparency of Franchising.

Background

Spectrum Analysis Australia Pty Ltd is a company of 5 full time staff, with expertise in statistical analysis as relates to many types of businesses including retailers and Franchisors. We hold many of the ABS datasets relating to demographics (2016 Census, population forecasts and business statistics and others), and use a Pitney Bowes MapInfo Geographic Information System (GIS) to undertake data analysis and mapping.

We also provide education into the franchise sector as I run the courses as sponsored by the Franchise Council of Australia (FCA) on Site Selection and Territory Planning, in conjunction with the Franchise Advisory Centre. (please refer to the links below).

[Franchise Site Selection](#)

[Franchise Territory Planning](#)

We are also on the Griffith University website, as part of the ACCC sponsored pre entry program for Franchising, as the expert in the field of what to look for in site selection and territory planning. Please refer Appendix 1.

Spectrum has been operating for over 20 years, and much of our work can be classified as:

- Sales analysis and sales prediction modelling – to place some forms of statistical analysis around the sales estimates for a location. This is normally based on a chain of stores, and learning off the existing network what are the Drivers of the business, and using that in predicting new store sales.
- Territory Planning - to use a logic in designing territories especially for Franchise systems, with the aim to give each Franchisee a similar amount of business opportunity.
- Strategic Network Planning – to assist businesses in where to seek new retail store opportunities, whether that may be in shopping centres, shopping strips, free standing stores, homemaker centres or other options. We are not acting in the site and lease negotiations with Leasing agents and landlords. We rather the recommend where to seek new stores, based on the success of the existing stores as defined more in terms of demographics, characteristics of their retail environment, physical attributes and competition.

Having worked in this area for many years, we are seen as specialists in this field, run a trade stand each year for the last 10 years at The National Franchise Convention, and I have been awarded both my Certified Franchise Executive (CFE) and Certified Management Consultant (CMC) by the Institute of Management Consultants. Hopefully that makes me reasonably qualified to speak on this topic.

More detailed information can be seen on our website, www.spectrumanalysis.com.au or in our Spectrum Catalogue:

https://www.spectrumanalysis.com.au/uploads/3/1/8/6/31864321/spectrum_catalogue_2018.pdf

Areas I wish to address

I wish to put forward some views on the specific topics / areas within the following terms of reference of the Inquiry:

“The operation and effectiveness of the Franchising Code (including the disclosure document and information statement) and the Oilcode in ensuring full disclosure to potential franchisees of all information necessary to make a fully informed decision when assessing whether to enter a franchise agreement, including information on:

- i. likely financial performance of a franchise and worse-case scenarios;
- ii. contractual rights and obligations of all parties (including termination rights and geographical exclusivity;
- iii. leasing arrangements and any limitations of the franchisee’s ability to enforce tenant’s rights; and
- iv. expected running costs including costs of goods required to be purchased through prescribed suppliers”.

Specifically I would like to address:

1. Financial Performance, especially addressing Sales Forecasting for new locations.
2. Geographical Exclusivity – as it relates to Territory Planning.
3. Site selection as described by Point 13.1.a of the Code

1. Financial Performance including Sales Forecasting for new locations.

I specifically feel this is covered in Point I, and to a certain extent in Points iii & iv of the terms of reference of this Inquiry.

To understand future profits, returns and financial performance of a business, you need to specifically address the Gross Revenue, or the sales of the business. Franchising has historically shied away from this, as to pass on a view or commitment to a Franchisee of what they should sell, or make as a profit, is a legal nightmare in the making. If they fail to reach that target, there can be all sorts of legal cases of misrepresentation against the Franchisor.

Many Franchisors still undertake work in this area, either internally or through a 3rd party (such as ourselves), but very rarely convey the results to the potential franchisee due to the legal risk, and this is the strong advice of their lawyers (both internal and external).

The point is this work can be done with some level of error expected, and it could be shared with potential franchisees if it could be shown to be statistically based, and not just a wet finger in the air approach. Many larger companies take this extremely seriously, and have post audit processes in place to hold Management accountable for their sales forecasting. I worked for Caltex Australia Ltd from 1978 to 1999 (in many different roles including property manager), and was directly involved in these processes both in Australia and internationally.

The Gross Revenue / Sales Revenue are the most important figure in the financial forecasts, as they hold the largest source of error if they are not achieved.

In most businesses you think in terms of Forecast Profit, and you are relying on this to live, pay back your debts and basically secure your future. The simplest way (in my view) of looking at a forecast P&L is as follows:

Sales Revenues – Very hard to predict

Less

Cost of Good Sold (factor of sales revenue)
Rent – fairly predictable cost
Wages – fairly predictable cost (with some variable component)
Other (power, phone, all fairly small)

= PROFIT / (LOSS)

Whilst most of the costs are fairly predictable, and the cost of goods sold is normally a factor of the total revenue, the Sales Revenue is the most unpredictable factor in a simple Forecast P&L.

If any of the other factors are out by a small percentage, there is a relatively small effect on the PROFIT (up or down).

If the Sales Revenue is out by a fair percentage, say + / - 50%, then the effect on the bottom line is either fantastic or catastrophic!

In our view, Franchisors should be held responsible to provide some logic on what a new site should sell, and therefore be able to generate a simple forecast P&L – at least to the

level to make the potential Franchisee be able to have a reality check as to whether the business is viable.

I would like to submit an article I wrote and had published back in 2010 on this topic (very little has changed).

"Using a Scientific Approach for better site selection" (please follow the Link below):

https://www.spectrumanalysis.com.au/uploads/3/1/8/6/31864321/2010.10.using_a_scientific_approach_franchisor_magazine_oct_.pdf

There are ways for Franchisors to be able to give some indication of sales expectations, normally by using their existing network as a starting point to understand the Drivers of the business, and therefore they should be able to indicate a broad range in which they feel the sales should fall (and why). If done to a reasonable standard (just like due diligence), then they should not be held responsible for failure, especially if it is seen to be the fault of the Franchisee.

Recommendation

That the Inquiry recommend that some logic be required within the Franchise Disclosure document to place some logic and rigidity to the sales expectations of the potential franchisee for all new stores. If the store has been run as a company operation for a period, then those sales shall suffice. If not, then some logic using analogue, regression or more advanced method of modelling should be required.

We have worked for many large Franchisors in many different areas over the years. We see Franchise Systems we respect who we feel invest well and do it correctly in relatively practical terms, and we see the opposite, where the Franchisor is not prepared to invest in the System, and either misrepresents certain things (like sales) to the potential Franchisee, or simply do not know, and do not wish to find out.

We have the view that using data in most business decisions will eventuate in a better set of outcomes than using your wet finger in the air.

2. Geographical Exclusivity – Point 13.1.b of the Code

Point ii of the Terms of Reference talks of Geographical Exclusivity, which I want to interpret to mean Territories or Marketing Areas, as a way of giving a Franchisee some control and exclusivity over a certain part of the market. In the case of a mobile franchise, this control could mean the passing on of leads generated by the Franchisor (eg for a lawn mowing franchise, or a mortgage broking franchise). In the case of a retail store, this may be to create an exclusion zone, to prohibit the Franchisor from opening another store in competition within a set area.

In the Draft Franchise Disclosure document as provided on the ACCC website, it mentions:

Model disclosure document for franchisee or prospective franchisee:

The following pages give a recommended format for a disclosure document for a franchisee or prospective franchisee in accordance with annexure 1 of the Franchise Code.

Within the Draft document, under point 13, we find the following:

13. Sites or territories

- 13.1 The policy of the franchisor, or an associate of the franchisor, for selection of as many of the following as are relevant:

(a) the site to be occupied by the franchised business;	Click here to enter text.
(b) the territory in which the franchised business is to operate.	Click here to enter text.

- 13.2 Details of whether the territory or site to be franchised has, in the previous 10 years, been subject to a franchised business operated by a previous franchise granted by the franchisor and, if so, details of the franchised business, including the circumstances in which the previous franchisee ceased to operate.
- 13.3 The details mentioned in item 13.2 must be provided:
- (a) in a separate document; and
 - (b) with the disclosure document.

Our experience is many Franchisors pay little attention Point 13.1.b and often have carved up territories in a relatively random manner, making some businesses very good, and some franchises almost impossible to sustain.

My view is the wording is already in place, however whether it is done to a reasonable level, and whether it is being enforced by the ACCC is another question?

Recommendation

That the Inquiry looks at the meaning of this section of the Franchise Code, and looks to enforcing this part of the Code of Conduct with some more rigour.

My suggestions would be wording along the following lines:

“When a Franchisor is granting territories or marketing areas within the franchise system, then they must provide the logic upon how the territories were formed, with the aim of

offering a similar business opportunity to each Franchise, or an explanation if this is not the case”.

For example regional territories may have less potential than metropolitan territories due to the limitation of distances a Franchisee can travel. There may be one set of standards for metropolitan territories and a different set of rules for regional areas.

Some analysis and a methodology report should be undertaken, and held by the Franchisor as a way of reference for potential franchisees to be supplied and understand.

3. Policy regarding the site selection to be occupied by the franchised business - Point 13.1.a

Again, the Code (above) refers to Point 13.1.a, where a Franchisor should be stating the policy of the Franchisor in relation to the site to be occupied by the franchised business.

The Code is quite clear in that a policy should be involved on what is being sought in terms of site selection, and we would say in terms of suitable demographics, site characteristics, and many other areas that should go into the site selection process.

In many cases the lease, and the fit out cost for a retail store are funded by the franchisee as part of their ingoing costs, and this investment can be one of the largest of their lives.

In Appendix 2 and Appendix 3 we have put forward examples of a Check Chart (which can be used by a Franchisor and a Franchisee), and a Property Guideline that should be used by the Franchisor, and possibly the Franchisee in assisting in creating a transparent Site Selection process. Property Guidelines are also used to instruct Leasing Agents and property owners in what you are seeking.

Recommendation

That the Code be enforced by the ACCC to require a Franchisor to meet the requirements of Point 13.1.a, and have meaningful documents on what they are seeking in their site selection policy, to give confidence to the potential franchisee that there is logic and process being undertaken in this area.

Please also refer to our e-book on Site Selection

https://www.spectrumanalysis.com.au/uploads/3/1/8/6/31864321/nine_tips_to_great_site_selection_v2.2.pdf

Summary

Thank you for the opportunity to submit to this Inquiry and I look forward to the recommendations to come.

Yours Sincerely

Peter Buckingham CFE CMC

Managing Director

Spectrum Analysis Australia Pty Ltd.

Appendix 1

Extracted from the Griffith University website https://app.secure.griffith.edu.au/apc-franchising/?page_id=136

Asia-Pacific Centre for Franchising Excellence

Pre-Entry Franchise Education Program Module Three: Franchisee support, site selection and marketing funds

Site & Territory Selection

Site selection can make or break a business. An unsuitable site may lead to under-performance of the business.

Next, hear an interview with Site and Territory Selection professional, Peter Buckingham, who provides an insight into key site selection criteria, which need to be considered before signing lease or territory agreements.

Important elements to consider:

- Even if a franchisor suggests a location, it's up to you to do your own due diligence to ensure it's the right location.
- For retail franchises you need to consider aspects such as pedestrian traffic, access, visibility and what sort of rent is charged and whether that suits. Also whether you're an impulse business or a destination business.
- It's recommend you look at the [Australian Bureau of Statistics \(ABS\) website](#), at the section called '*Census Data*' and then '*Quick Stats*'.
- *Quick Stats* allows you to enter a postcode, suburb name or local government area and up will come a map of that area and the basic demographics comparing that to the Australian average.
- If you're in the business to business (B2B) market the ABS also provides a database that allows you to look at the 17 Australian New Zealand Standard Industrial Classification (ANZSIC) categories of businesses. The database provides how many and what types of businesses operate in a particular area, as well as the number of employees.

Peter warns:

- Beware of the 'beer and pizza map' approach to territory selection. This is where the franchisor (over a beer and a couple of pizzas) draws territories on a big map, based on gut feel rather than logic, other geographical areas or the business opportunity.

And finally:

- Think before you jump, there are people that can help, and do not be convinced by a real estate agent that says a site is the best thing for you and jump automatically in.
- There are consultants and businesses in demographics that can find information for you.

Site Selection video <https://youtu.be/ZBQyHKTd6ek>

Territory Planning video <https://youtu.be/M-dLvCJeOgc>

[Download the transcript of the interview with Site and Territory Selection expert Peter Buckingham \(PDF 43KB\).](#)

Appendix 2

Copy of a Check Chart – derived from statistics on the Brand:

METRO MALL ALFRESCO CHECK CHART

LOCATION: _____ DATE OF REVIEW: _____
ADDRESS: _____ REVIEWED BY: _____

(CHECK EACH FEATURE WHICH BEST DESCRIBES THE LOCATION)

Alfresco Restaurants in complex	>11	<input type="checkbox"/>	6 - 11	<input type="checkbox"/>	<6	<input type="checkbox"/>
Number Cinema Screens in S/C	>7	<input type="checkbox"/>	1 - 6	<input type="checkbox"/>	0	<input type="checkbox"/>
% HHold Inc > \$2000 pw. w/in 2 km	>50%	<input type="checkbox"/>	45% - 50%	<input type="checkbox"/>	<45%	<input type="checkbox"/>
Total Population 3kms radius	>90,000	<input type="checkbox"/>	50,000 – 90,000	<input type="checkbox"/>	<50,000	<input type="checkbox"/>

SCORE SUB TOTAL			
MULTIPLIER	X12	X6	x0
SUB SCORE	_____	_____	_____

Gross Lettable Area of Retail	85,000+ sq.m	<input type="checkbox"/>	50,000–85,000 sq.m	<input type="checkbox"/>	<50,000 sq.m	<input type="checkbox"/>
Total Inside Outside Size (sq.m)	220+ sq.m	<input type="checkbox"/>	150 – 220 sq.m	<input type="checkbox"/>	<150 sq.m	<input type="checkbox"/>

SCORE SUB TOTAL			
MULTIPLIER	X8	X4	x0
SUB SCORE	_____	_____	_____

Location within Alfresco Centre	Busiest	<input type="checkbox"/>	Middle	<input type="checkbox"/>	Quietest	<input type="checkbox"/>
Employing Businesses within 1km	>400	<input type="checkbox"/>	200 – 400	<input type="checkbox"/>	<200	<input type="checkbox"/>
Total Seats inside plus outside	>80	<input type="checkbox"/>	70 – 80	<input type="checkbox"/>	<70	<input type="checkbox"/>
Combined visibility	Good	<input type="checkbox"/>	Medium	<input type="checkbox"/>	Poor	<input type="checkbox"/>

SCORE SUB TOTAL			
MULTIPLIER	X4	X2	x0
SUB SCORE	_____	_____	_____

GRAND TOTAL

(ADD ALL THE ABOVE SUB SCORES)

Rating:	< 45	Poor	55 - 65	Good
	45 – 54	Average	> 65	Excellent

Appendix 3

Example of a simple Property Guideline

Property Guideline - Enoteca

Wine shops and restaurants

A quality wine shop is most often called enoteca in Italy now. Since some enoteca serve snacks with the wine, enoteca has also been used as the name of some wine bars or restaurants, especially bistro-style restaurants with Italian food. Because of the popularity of the enoteca concept in some locations, "regular high-end" wine shops sometimes also call themselves Vinothek, without focusing on local wines or catering to visitor's information need.

Our plan is to open one enoteca to start, with the idea of a chain of enoteca stores in the future.

Locations and store type

We are seeking a store location in a strong shopping strip. We see the major generators for our customers to be people coming home on public transport (eg near a railway station) or part of an upper market night time strip. Our initial target areas are higher socio economic areas, so our Melbourne targets are the inner east to begin with, such as South Yarra, Brunswick, Carlton and East Melbourne.



Size of site required

We seek a store of around 100 - 140 sq metres of retail floor space and ideally about 15 sq m for back of house. We require a minimum of 5 m. width due to our floorplan of a counter down one side of the store.

Retail Mix preferred around our sites

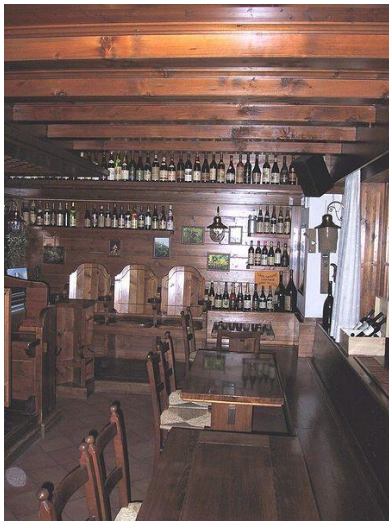
We are seeking busy areas with a dominance of trendy food and clothing type stores. Other restaurants in the area, picture theatres and other night time generators are seen as positives

Visibility from all directions

Visibility is very important to us as our signage needs to be seen in all directions. Our preference is for corner sites, and our current experience is showing mid-block sites are not standing out sufficiently.

Liquor Licence and Disability Access

We have to be able to have a liquor licence, so areas that will be too difficult to achieve this we are not interested in. We must have compliance with disability discrimination access rules, and the ability to realistically modify the building to comply.



External Characteristics

We like to have a courtyard if possible, for patrons to use and be able to smoke if that is their habit.

We do like external seating to support the internal seating, providing we can put up umbrellas or some form of awning.

Internal Requirements

We require 3 phase power of 80 Amps per phase, or 120 Amps per phase if we have to run air conditioning. We also need suitable drainage and a grease trap.

Food

We aim to serve light food, good for combining with very good wine.



Pedestrian Counts / Volume

High pedestrian traffic is a must for our brand. We see ourselves primarily as an impulse purchase at this stage of our development.

Demographics

Our brand / store type is well known to the European community as it originated from Italy and Spain. With our high quality wines, combined with our food and coffee offer, our research shows we are very popular with females. Our price point is also above the lower price bottle shops, so we are seeking higher socio demographic areas.

General comments

Our experience has pointed us towards powerful shopping strips in higher socio demographic areas. Target areas for us include South Yarra, Toorak, Malvern, St Kilda, Carlton, Bentleigh, Balaclava and Collingwood.

If you have a suitable store you feel we should consider, please contact **Peter Greenhill**, Business Development Director on **0411 604921**.

Potential Target Areas

Potential Areas - Tier 1 (Top 20%)				
ID	STREET NAME	Suburb	All Retail	TIER
M167	Chapel St	South Yarra	325	1
M042	Lygon St	Carlton	82	1
M055	Smith St	Collingwood	118	1
M172	Acland Court	St Kilda	73	1
M040	Camberwell Junction	Camberwell	142	1
M168	Toorak Road	South Yarra	93	1
M084	Geelong CBD	Geelong	164	1
M079	Brunswick St	Fitzroy	95	1
M091	Hampton Street	Hampton	123	1
M083	Frankston CBD	Frankston	142	1
M152	Bridge Road	Richmond	174	1
M096	Glenferrie Road	Hawthorn	80	1
M187	Watton St	Werribee	85	1
M067	Glen Huntly Rd	Elsternwick	79	1
M166	Clarendon St	South Melbourne	67	1
M012	Carlisle St	Balaclava	66	1
M013	Whitehorse Rd	Balwyn	63	1
M033	Sydney Road	Brunswick (South)	73	1
M144	Bay St	Port Melbourne	54	1
M029	Box Hill Junction	Box Hill	46	1
M020	Centre Road	Bentleigh	73	1
M081	Barkly St	Footscray	97	1
M031	Church St	Brighton	75	1
M088	Main Street	Greensborough	61	1
M135	Errol St	North Melbourne	27	1
M153	Swan St	Richmond	56	1
M138	Eaton Mall	Oakleigh	64	1
M127	Main St	Mornington	87	1
M112	Glenferrie Road	Malvern	107	1
M147	High St	Preston	80	1
M181	Toorak Village	Toorak	54	1
M180	High St	Thornbury	58	1
M030	Bay St	Brighton	46	1
M191	Anderson St & Ballarat St	Yarraville	32	1
M118	Balcombe Rd	Mentone	31	1
M124	Puckle St	Moonee Ponds	75	1
M188	High St	Westgarth	17	1
M087	Glenroy Road	Glenroy	44	1