STARTING UP A NEW BUSINESS, CONSIDERING FRANCHISEE AS AN OPTION

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FRANCHISE

The word "franchise" comes from an old dialect of French and means privilege or freedom.

It is one of the fastest growing areas of new business development during the last 15 years

WHAT IS FRANCHISING?

It is the transfer of the right to sell a trademarked product through a system prescribed by a "franchisor" who owns the trademark.

TYPES OF FRANCHISING

Product and Trademark Franchise

A relationship wherein the franchisor grants the right to use its trademark and buy its products to the franchisee.

This approach connects a single manufacturer with multiple franchisees

For example, Lehar Pepsi, General Motors.

TYPES OF FRANCHISING:

Business Format Franchise

An arrangement under which the franchisor provides a method/formula for doing business to the franchisee along with operating procedures such as:

- ► Facility design
- ► Accounting & book keeping procedures
- ► Employee relations
- ► Quality assurance standards
- ► Overall image & appearance of the business.

Fast-food restaurants, convenience stores, and motels are well-known examples of business format franchises.

Examples: Mac Donalds, Lakme Beauty Salon

FRANCHISEE *VS*. FRANCHISOR

FRANCHISING FOR

THE FRANCHISEE-
It is a way to reduce
the risks of a new business by buying
into an established product or
concept.

THE FRANCHISOR- It is a way to
expand your business more quickly by
sharing some of the cost, risks &
rewards with the franchisees.

TRADITIONAL LICENSING VS. FRANCHISING

Traditional Licensing	Franchising
Licensing is the permission granted by the proprietor of the mark to third persons to use the mark with or without conditions or restrictions.	As licensing becomes more sophiticated the subject matter in one licensing arrangement may cross over many different types of ip rights.

THE ROLE OF TRADEMARKS

- Trademarks are typically the foundation of a franchise system.
- Trademarks are the words, signs, design, décor and color scheme that signify to the public the identity of goods.
- Trademarks have become a universal language for franchising that allow the retailers to readily distinguish their offerings from others.
- Trademark protection is the key to any franchise system.

THE DISADVANTAGES AND ADVANTAGES OF FRANCHISING

DISADVANTAGES

- High costs of agreement
- Too high expectations of success
- Over dependence
- Fixed performance standards
- Competition with performance of other franchisees
- Restrictions on freedom of decision
- No choice of suppliers
- Fear of termination of agreement

THE DISADVANTAGES AND ADVANTAGES OF FRANCHISING

ADVANTAGES

- Established product or service
- Technical and managerial assistance
- Quality control standards
- Less operating capital
- Higher probability of survival
- Opportunities for growth
- Potential lower cost supplies because of quantity purchasing
- Use of franchisor's SECRET METHODS

The advantages of franchise system as regards to

FRANCHISOR

FRANCHISEE

CONSUMERS

FRANCHISOR

- Attracts new talents and ideas
- Faster growth and the creation of a truly global brand
- Identity
- Confirmed financial earnings
- Provides expansion capital
- Fast growth
- Quality on-site management
- Fewer day-to-day operating headaches

FRANCHISOR

- Less corporate overhead
- Faster market penetration
- Higher system-wide sales
- Captive market for your products
- Financial leverage
- Opens up regional/national account opportunities

FRANCHISEE

- Being their own boss
- Selling a well established, high quality product
- Intensive initial training
- Continuous support
- Benefit from national marketing carried out by franchisor
- Forecasting

Consumers

Franchising is a wise choice because consumers like to purchase goods & services from familiar names with reliable standards of service and quality. They like to deal with businesses where the owner is on-premise.

WHAT ARE FRANCHISORS REQUIRED TO PROVIDE

- Copy of the franchise agreement, other contracts, and the franchisor's financial statements.
- The business operational manual with one week of training in one of the parent stores, and on going support and assistance.
- Guidelines on audits and rights to sell the franchise (assignment rights).
- Information on franchisee's initial licensing fees and other ongoing costs (e.g. royalties, promotional fees, cooperative advertising fees).

WORD OF CAUTION FOR THE FRANCHISOR

- Be sure to register your marks.
- Police its trademark among its franchisees to ensure that the franchisees do not debauch, injure, dilute or blur the trademark.
- The franchise agreement must be written to state what is permitted under the trademark license and to explain the limits of the permitted use of the marks.

WORD OF CAUTION FOR THE FRANCHISOR

- Agreement must also be enforced to ensure that the franchisees do not change the public perception of the trademark in a way that may affect the franchisor.
- Ensure that its products or services are displayed and distributed in a way consistent with the trademark or a franchisor may lose certain rights to, or protections of, its trademark.

- As the franchisor matures, it introduces new products & services and often change its new image and new marks, signifying a new direction.

- The franchise agreement must be flexible to encompass the change and the franchisees need to accept that the new changes in their business with associated costs are necessary to stay ahead of the competition.

- Always be developing and protecting its marks from infringement by others so that it can expand into new products lines.

MCDONALD'S CASE STUDY

- Under a McDonald's franchise, McDonald's owns or leases the site and the restaurant building.
- The franchisee buys the fittings, the equipment and the right to operate the franchise for twenty years.
- To ensure uniformity throughout the world, all franchisees must use standardized McDonald's branding, menus, design layouts and administration systems.

MCDONALD'S CASE STUDY

- When the McDonald brothers, Dick and Mac opened their first restaurant in 1940 in California, they could never have imagined the phenomenal growth that their company would enjoy.
- From extremely modest beginnings, they hit on a winning formula selling a high quality product cheaply and quickly. However, it was not until Ray Kroc, a Chicago based salesman with a flair for marketing, became involved that the business really started to grow. He realized that the same successful McDonald's formula could be exploited throughout the United States and beyond.

MCDONALD'S CASE STUDY

- There are now more than 28,000 McDonald's Restaurants in over 120 countries. In 2000, they served over 16 billion customers, equivalent to a lunch and dinner for every man, woman and child in the world!
- McDonald's global sales were over $40bn, making it by far the largest food service company in the world.

MCDONALD'S CASE STUDY

- In 1955, Ray Kroc realized that the key to success was rapid expansion. The best way to achieve this was through offering franchises. Today, over 70 per cent of McDonald's restaurants are run on this basis. In the UK, the first franchised restaurant opened in 1986 - there are now over 1,150 restaurants, employing more than 49,000 people, of which 34 per cent are operated by franchisees.

MCDONALD'S CASE STUDY

- McDonald's views the relationship between franchisor, franchisee and supplier to be of paramount importance to the success of the business. Ray Kroc recognized the need very early on for franchisees that would dedicate themselves to their restaurants. He wanted people who had to give up another job to take on the franchise venture, relying on their franchise as their sole source of income and would therefore be highly motivated and dedicated.

MCDONALD'S CASE STUDY

Mcdonald's will not offer franchises to partnerships, consortia or absentee investors. The initial capital has to come from the franchisee as A guarantee of their commitment. The selection process is rigorous to ensure that mcdonald's only recruits the right people.

THE FRANCHISE AGREEMENT

- A written document outlining the rights and obligations of both the franchisor and the franchisee.
- A legal contract and binds both the parties.
- The content of which will regulate, to a certain extent, the way you operate the franchise.

Contract can be divided into the following two agreements

- **Purchase Agreement**

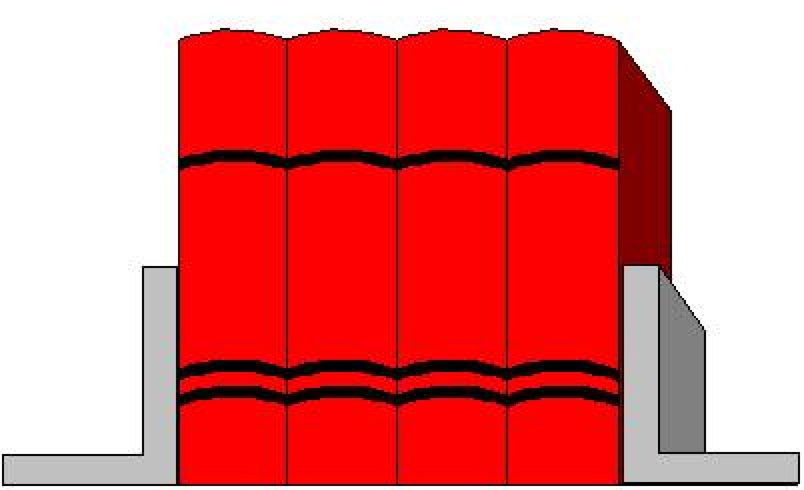
  Of the contract covers the Franchise package consisting of material and/or equipment list to be provided to the franchisee. The price, the specifics of price and method of payment related to stages of delivery of material/machinery etc. The services,a list of the franchisor's responsibilities to the Franchisee. Those to be provided before the business opens are called the initial services. Those services to be provided periodically thereafter are called continuous services.

Contract can be divided into the following two agreements

- **Franchise Agreement**

  Of the Contract covers the rights granted to the franchisee. It will confirm all the details you have been told and should be specified in the detail expected by you. The obligations undertaken by the Franchisor both before and after the setup. Obligation of the franchisee. Trade restrictions imposed on the franchisee by the franchisor. Agreements regarding assignment of ownership to others or termination of contract.

TERMS OF FRANCHISE AGREEMENT



- RESPECTIVE PARTIES
- RECITALS
- PROTECTIONS UNDER VARIOUS HEADS

TERMS OF FRANCHISE AGREEMENT

FRANCHISE GRANT AND TERM-

The franchisor would grant to a franchisee to adopt and use the company's system and the term of the license.

GENERAL SERVICES OF FRANCHISOR-

The franchisor shall advise and consult with the franchisee from time to time in terms of new developments, improvements etc.

TERMS OF FRANCHISE AGREEMENT

MANUALS-

The franchisor shall provide the franchisee with the business manuals which would contain book keeping, accounting, business procedures and policies, advertising policies etc.

ADVERTISING-

Franchisee must use only the advertising and programs provided by the franchisor.

TERMS OF FRANCHISE AGREEMENT

GROSS SALES-

All revenues from the sales of the franchisee based upon all the business conducted upon from or the company.

FRANCHISE FEE-

Franchisee pays an initial fee to the franchisor for the grant of this franchise and shall pay a monthly fee to the franchisor upon the execution of the franchise.

TERMS OF FRANCHISE AGREEMENT

REPORTS-

On or before a particular date of the month, the franchisee shall provide to the franchisor a statement as required by the franchisor.

RESTRICTIONS-

The restrictions could be as under (based upon every company's needs):

TERMS OF FRANCHISE AGREEMENT- Restrictions

1. During the term of this franchise the franchisee shall not without the prior consent of the franchisor acquire any financial interest for any company which is similar to that of the franchise business/company.

2. To make prompt payment on any purchase in connection with the business.

3. At own expense, comply with all the federal, state and local laws etc.

TERMS OF FRANCHISE AGREEMENT

ASSIGNMENT-

Without the prior consent of the franchisor the franchisee shall not assign any interest in the franchise to any third party.

FRANCHISEE NOT AN AGENT OF FRANCHISOR-

The franchisee shall have no authority to act as an agent of the franchisor.

EFFECT OF TERMINATION-

Upon termination and/or expiration of the franchise the franchisee shall stop any use of the trademark,and/or trade secret or any authority given to use the business' practices/policies.

1996 (16) PTC 181 (Del)
Interim Application Nos. 3959 and 8182 of 1992 and Suit No. 1570 of 1992

Pepsi Foods
Vs.
Jai Drinks (P) Ltd.

AND

Jai Drinks (P) Ltd.
Vs.
Pepsi Foods Ltd.

•PEPSI manufactures soft drink concentrate for beverages being bottled under the trade marks Lehar Pepsi, Seven Up and Lehar Mirinda,
Pepsi entered into a bottling agreement with "JAI" on or about 8th May, 1990 granting license to use the trade mark Lehar in conjunction with trade marks Pepsi Cola, Pepsi 7UP and Lehar Mirinda.
This bottling agreement was in respect of a territory known as Jaipur territory which included many districts of Rajasthan.
The agreement was initially for a term of 10 years from the date of the agreement with a right to "PEPSI" to terminate by giving 12 months notice , upon the failure of "JAI".

On receiveing complaints about the quality of products manufactured by JAI, PEPSI warned JAI to improve the quality, but JAI were not able to improve the same.

By a notice dated December 31, 1991 PEPSI terminated the agreement.
JAI did not challenge the said termination and subsequent to the date of termination PEPSI stopped selling any concentrate to it.

JAI despite termination continued to manufacture sub-standard quality beverages and market them under the trade marks of PEPSI, which acts of "JAI" were stated to be illegal without authority and malafide.
Hence, a suit was filed by PEPSI for a declaration that the agreement stood terminated and also for an injunction restraining JAI from manufacturing the beverages.

Damages for infringement and passing off were also claimed in the suit.

JAI filed an counter application under Order 39 Rule 4 Civil Procedure Code for vacation of the ex parte stay granted by Court and also filed a suit against PEPSI for a declaration that the termination notice was illegal, invalid and non-operative.

The contentions placed by JAI's counsel were

- that the agreement was for a period of ten years, "PEPSI" could not terminate the same; and
- that there were no complaints against "JAI" hence there was no reason for terminating the agreement

Held:

PEPSI had a right under the contract to terminate the license agreement and the only right available to JAI was to file a suit for damages, JAI cannot continue to manufacture or market the products for which the license had been given by PEPSI. Therefore, PEPSI is entitled to an injunction restraining JAI from manufacturing or marketing the products under the brand name of Lehar Pepsi, Lehar 7 Up and Lehar Mirinda.

Thus, PEPSI'S application was allowed while JAI's application was disposed.

Ravissant Pvt. Ltd. Vs.
D.F. Export S.A. (formerly known as Franklin Export S.A.)
MANU/DE/0812/2008

Plaintiff is a private limited company involved in the business of running Lifestyle Brand Stores by the name of 'Ravissant' in India as well as abroad.

The Defendant is engaged in the business of hair styling salons.

June 1, 2000: Franchisee Agreement was entered between the Plaintiff and the Defendant for running an exclusive ladies' luxury hair dressing salon at New Delhi under the brand name of 'Jacques Dessange', the defendant's trade name.

December 31, 2004: Termination of Agreement, if not renewed.

July 1, 2002: Another Franchisee Agreement was entered for a similar establishment at Mumbai.

December 31, 2006: End date of agreement.

May, 2003: Plaintiff expressed the desire to the Defendant for the possibilities of opening Jacque Dessange Salons in the other cities and requested rights for sub-franchise.

Defendant accepted the said proposal and informed it of having a Master Franchisee Contract for the said purpose, which was also to include the existing Jacque Dessange Salons in Delhi and Mumbai.

May 28, 2003: Defendant forwarded the draft agreement of the Master Franchisee Contract.

June 24, 2003: plaintiff sought confirmation.

July 3, 2003: defendant approved afore-mentioned Master Franchisee contract.

The defendant reaffirmed the said agreement by several letters dated **November 19, 2003**, February 13, 2004, March 20, 2004 and April 8, 2004.

February 15, 2004: Plaintiff also hired a trainer, Ms. Martin Fuzeau from Jacques Dessange, Paris.

The defendant continued to show its interest to implement the Master Franchisee Contract even after the Plaintiff through the letter dated **6.7.2004** confirmed that it had ceased the operation of their salon at Taj Mahal Hotel from **30.06.2004.**

The plaintiff by a letter dated **July 5, 2004** proposed the opening of the new salon in the new Ravissant Store in Mumbai.

The Defendant, on being informed of the same, not only approved of the said decision, but in fact informed the Plaintiff that they should use Jacque Dessange interiors for the said new SalonFor carrying out these changes, it incurred a cost of Rs. 75 lakhs towards such renovation work and Rs. 20 lakhs towards architect's fees and a rental of over Rs. 4 lakhs per month for the premises and that it had already cost over Rs. 18 lakhs on account of salaries of staff, allowances, cost of hiring the trainer from Paris.

July 19, 2004: Defendant informed the Plaintiff of their decision to cancel the Franchisee Agreement with respect to the Delhi Salon on its expiry date, i.e. 31.12.2004. It however, also evinced the intention to continue the relationship with the Plaintiff in respect of the Delhi Salon on modified terms and conditions, which were agreed to by the Plaintiff by the letter dated August 10, 2004.

Mr. Ravi Chawla, on behalf of the Plaintiff, visited Paris at the defendant's request to meet the latter's representatives on 7/8.09.2004 and reaffirmed the Master contract.

September 21, 2004: The Defendant faxed a letter terminating the Franchisee Agreement, with respect to the Mumbai Salon retrospectively effective from 31.07.2004 apart from casting cloud/doubts about the future of the otherwise concluded Master Franchisee Agreement.

ISSUES:

- plaintiff sought a declaration that the term of the Franchise Agreement dated 1-6-2000 stood executed beyond December 31, 2004 and a further declaration that a 'Master Franchise agreement' is deemed to have been concluded between parties.

- Whether the termination letter dated September 9, 2004 is illegal and of no effect.

- plaintiff sought permanent injunction against the defendant restraining it from giving effect to or enforcing the termination letter dated 20 September, 2004 and a mandatory injunction restraining the defendant from withholding any of its obligations under the Franchise Agreements dated 1-6-2000 and 1-7-2002 under the Master Franchise Agreement.

HELD:

In this case, a careful reading of the defendant's letter dated 8th September, 2004 would show that it sought the plaintiff's views about the proposal to enter into a more enduring relationship, i.e the Master Franchise Agreement. The plaintiff, in its letter agreed to the proposal, and sought confirmation. This clearly showed that the defendant had merely issued an invitation to offer, to the plaintiff; the latter in turn agreed. This resulted in a binding offer by the plaintiff. However, to crystallize into a binding promise or contract, the offer had to be accepted by the defendant. The defendant's letter of 20th September 2004 unequivocally stated that it was unwilling to enter into a Master Franchise Agreement. There was as such no concluded contract.

The plaintiff has not sought the appropriate consequential relief, i.e decree for any amount of money allegedly spent by it, towards expenses. Instead, it seeks two declarations i.e that the master franchisee agreement stood executed, and that the termination of contract was illegal. The plaint averments show that such a claim was available. In view of these facts, the reliefs of declaration are clearly barred.