

Carl Khalil, Esq. and Sada Sheldon, Esq.

CHOOSING BETWEEN FRANCHISING AS A UNIT FRANCHISE OWNER VERSUS AN AREA DEVELOPER or MASTER FRANCHISE



Many franchisors offer prospects the option of purchasing a unit franchise, on one hand, or an Area Developer territory, on the other hand.

Often times, the terms “Master Franchise” or “Regional Developer” are used interchangeably with “Area Developer.” When presented with such a choice, the question becomes, which one is right for you? This article will consider some relevant issues to help you make the right pick.



Your Initial Investment

Perhaps the first question to ask yourself is what level of capital investment do you want to make? Typically, the initial franchise fee for a unit franchise territory is much lower than for an Area Developer territory. The unit owner is simply buying the right to operate a franchised outlet in one territory. But an Area Developer purchases the right to solicit, sell, and support franchisees in many unit territories in exchange for a portion of the initial franchise fee and royalties paid by the unit owners in those territories. The loss of this revenue to the franchisor generally requires the Area Developer to pay a higher initial franchise fee.

The initial franchise fee, however, is only part of the picture. Other start-up costs must also be considered. In this respect, the equation is reversed. An Area Developer tends to have very low remaining start-up costs because little is necessary to work internet or phone leads to try and obtain franchisees. And Area Developers can normally work from home without a staff, at least initially. On the other hand, unit owners often set up retail outlets, which customarily involves leasing, build out costs, equipment and furniture costs, as well as staffing and payroll.

Reviewing Items 5-7 of the Franchise Disclosure Document with a certain scrutiny will help you to analyze the costs associated with the initial franchisee fee, other fees, and start-up costs, to determine which investment level is right for you.

Would You Rather Sell and Support or Offer Ultimate Services

The next question to ask yourself is what job duties suit your personality? The roles of Area Developer versus unit franchisee

are significantly different. Area Developers focus on developing franchise leads, selling franchises, and supporting those franchisees once in the system. Good Area Developers generally have a sales mentality, enjoy networking, and the excitement of closing deals. Once a franchisee is brought into the system, however, Area Developers must invest time in supporting their franchisee's business development. This may require travel between locations and being on-call to address problems and concerns from multiple angles. Therefore, an Area Developer must be a sales person, mentor, and problem solver.

Additionally, an Area Developer's role tends to evolve over time. Initially, when an Area Developer does not have unit owners in place, most time will be spent selling franchises. But as unit owners are established, the selling function diminishes and the Area Developer focuses more on supporting unit franchise owners.

On the other hand, a unit franchise owner will be delivering the franchisor's services to the ultimate end customer. Someone who has an interest or background in the franchise concept may find this role more appealing. For example, a person with culinary skills or restaurant management experience may want to purchase a restaurant franchise because he has a desire to operate his own restaurant.

The role of a unit franchise owner does not necessarily change over time, but it can. A successful unit owner may gradually acquire additional unit territories and thereby become a multi-unit territory franchisee. In this role, the franchisee focuses on managing an operational structure and staff to carry out the various duties needed to run the franchised outlets. This would be a good route for someone who enjoys the logistics involved with the operations and management of a business over the ultimate services.

Another possibility, and one that may be required by the franchisor, is to do both.

You may feel that your personality would mesh in either a sales or product delivery environment. Or, you may find that you are passionate about the brand after spending time as a franchisee. Hence, you want to sell and bring others in the system. In some cases, a franchisor may require an Area Developer to own a franchise to gain an understanding of the system, provide quality support to unit franchisees based on that understanding, and serve as a model for those franchisees.

A single-unit franchisee's revenues are tied to the fortunes of a single location. A multi-unit franchisee will have a more diverse portfolio with risk spread among stronger and weaker outlets.

Long Term Goals and Return on Investment

Finally, you should consider your long-term goal and return on investment. A single-unit franchisee's revenues are tied to the fortunes of a single location. A multi-unit franchisee will have a more diverse portfolio with risk spread among stronger and weaker outlets. In either case, the return on investment will depend on various factors including location, choice of franchise, and business acumen.

With an Area Developer or Master Franchise territory, the long term goal is often more passive. Obviously, because the Area Developer's income rests largely on the success of its franchisees, you will still need to do some coaching of your unit franchisees. But as they become more seasoned, they will need less and less assistance. Your role will transition into a semi-passive form of an investment income stream. Further, like the multi-unit franchisee, income among the franchisees in your territory diversifies the investment.

Conclusion

The choice between entering the franchise world as a unit owner versus an Area Developer or master franchise is an individual choice entailing considerations of capital available to invest, what type of job functions you prefer, and whether you want more active or passive long term lifestyle goals. Hopefully, this article has provided some insights to help you make the right choice.

About the Authors:

Carl Khalil is a Partner in the law firm of Carl Khalil and Sada Sheldon, PLC. He has 17 years of franchise law experience and previously worked as Corporate Counsel for Jackson Hewitt and Liberty Tax Service. During his tenure at Liberty Tax Service, it grew from 35 offices to nearly 4000 offices and 100+ Area Developers.

He may be contacted at:

Phone: (757) 263-4596

Email: carl@khalilsheldon.com

Web: www.Carl-and-Sada-Law.com.

Sada Sheldon is a Partner in the law firm of Carl Khalil & Sada Sheldon, PLC in Virginia Beach, Virginia, a nationwide franchise and trademark practice. She is admitted to the State Bars of both California and Virginia. She is a member of the ABA Forum on Franchising.

She can be reached at:

Phone: (757) 263-4596

Email: sada@khalilsheldon.com

Web: www.Carl-and-Sada-Law.com.