TRANSACTIONAL ANALYSIS OF THE SERVICE DELIVERY SYSTEM IN FRANCHISING

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Executive Summary

Franchising is growing in stature as one of the most powerful business methods. Fifty percent of retail sales in the USA are generated through franchised chains. Franchising happens when an entrepreneur seizes a viable business opportunity. A system is developed to extract the maximum value and the rights to use the business system are sold to a franchisee to operate a business along the same principles and systems as the original opportunity. The franchisee and franchisor work together as a team or alliance to build and maintain the brand.

In order to exploit the business opportunity in a meaningful manner, it is important for the franchisor and the franchisee to understand and to analyse the different relationships in the franchising model. The franchise relationship model developed by Spinelli et al is very useful and provides a sensible approach in analysing and identifying the different relationships in a franchised business. The most important aspect of the franchise relationship model is the relationship with the customer. The service delivery system is created by the franchisor and franchisee to provide the best service or to deliver the product in the most effective way to the customer. The service delivery system is the blue print of the franchise operation and outlines the flow of tasks and transactions in the franchise model.

In order for franchisors and franchisees to ensure that uniformity and standards are maintained across the franchised business, it is important for them to have a system through which franchisees can be monitored. The main focus of the monitoring system is to prevent shirking, free riding or to avoid that franchisees erode the brand of the business. An important tool in the monitoring process is the franchise agreement. The franchise agreement is a specialised agreement that outlines the relationship between the franchisor and the franchisee. Other important tools used in the monitoring function are field visits, external service...
audits, peer review, analytical tools, customer feedback and mystery shopping.

Transactional analysis is used to determine which tasks are to be carried out by whom in the franchise relationship. The service delivery system tasks are defined and different tasks awarded to either the franchisee or the franchisor. As an example of this method, the real estate function is analysed indicating what the essential tasks are when executing this function and who is responsible for it.
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To read and to write are two of my favourite activities. By enrolling for the MCom program, I had the pleasure of engaging in these two activities regularly, sometimes under huge pressure, but always rewarding. I received an enormous wealth of personal gratification and knowledge from the course and it opened my horizons to the world of business and commerce. It prompted me to read wider, understand commercial problems better and being able to provide a better service to clients in my practise as an attorney.

The research that I undertook for this study provided me with an in depth knowledge of franchising and opened interesting new opportunities for me in my professional career.

Rudyard Kipling wrote a beautiful poem about "The thousandth man". The poem is about how one in a thousand men (figuratively speaking) will stand by you, support you, laugh and cry with you and that one in a thousand men is truly an honestly a friend and one you can trust and rely upon with your life. I am fortunate to not only know, but be married to a "thousandth wife". This dissertation is dedicated with love to my wife, Irene, who inspired, encouraged, supported and assisted me with this dissertation every step of the way. You are such an inspiration to me and you are on second thought, not only one in thousand, but one in six billion!
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1. Chapter One: Introduction

1.1 Background

Franchising is a very powerful business method. A total of 50% of all the United States of America retail sales, are generated through franchised chains. At retail level, franchising in the United States has become a USD 1 trillion a year business shared amongst 600,000 franchisees who are engaged in more than 70 different industry sectors and employ approximately 8 million people. (Parker, 2003:167; Bradach, 1998: i).

Franchising as a business form occurs when an entrepreneur develops a business model that can be recreated somewhere else by utilising the same resources as the original model. The creator of the original franchise is referred to as the franchisor. He grants other individuals the license or gives him permission, to use the name of the business, brand names, insignia and other intellectual property that make up the "look and feel" of the business. Franchisees are trained to conduct the business along a specific model. The franchisee pays an initial fee and thereafter a fee or a royalty for the right to use the franchisor's business concept (Spinelli et al., 2003:2). Examples of established franchised businesses in South Africa are MacDonald's, Steers, Juicy Lucy, Mica Hardware, Jack's Paints, to name a few (FASA: Franchise Yearbook, 2003).
A franchising model may either take on the form of a business format franchise where the business uses a specific manner in which they conduct business, or a product franchise (Spinelli et al., 2003:2). An example of the business format franchise is a MacDonald's outlet. In this type of franchise outlets the focus is on the manner that the service or product is presented and sold to the public. These firms would decide on a plan of how their products or services are to be delivered. They normally do "something else" that distinguishes them from the competition. This value added component is to be faster, cheaper or more cost effective than that of their competitors. Or the firm may develop a unique way in streamlining a process thereby adding value to the customer in the time that is saved for the customer.

Another form of franchise is the product franchise. An example hereof is a vehicle manufacturer that uses franchised outlets to sell their vehicles. In the latter instance the focus is rather on the product (for example a BMW or Audi) and the product is the focus and not necessarily the manner in which the business is conducted. According to Purvin (1994), it has become more and more difficult to distinguish between product and business format franchises.

An important aspect flowing out of the aforementioned examples is the establishing of the business concept or product in the eye of the consumer. The franchisor holds the right to the insignia and other intellectual property rights on a brand. To use the brand and to grant
licences the franchisees have to obtain the permission from the franchisor. These grants are normally for a specific period and within a certain geographic area (Spinelli et al., 2003:2). The marks or insignia of a franchised outlet distinguishes them from competitors and helps the public to associate them with a specific business model. By association they learn what to expect from a specific brand.

In a business based on a franchise model, there are several different kinds of important relationships. This relationship is made up out of different sub-relationships that have to be managed well and maintained by the parties involved in the relationship to avoid confusion and friction between the franchisor and franchisee. The relationships forming the basis of the franchise model are referred to as the Franchise Relationship Model (FRM). The FRM analyses those aspects that are essential for a solid franchising venture to succeed. This special alliance between the franchisor and the franchisee is normally outlined and described in the franchise agreement and the operations manual. How the relationship is monitored is important for both the franchisee as well as the franchisor because it maintains the brand and ensures that levels of uniformity are upheld across the board of the franchise operation (Timmons & Spinelli & Spinelli, 2004:221).

At the core of the franchise relationship model is the customer and its needs. The needs of the customer in turn are outlined and a plan of action to get the product in the best possible manner to him is described
in the Service Delivery System (SDS). Any changes to the customer or the SDS could have serious consequences for the alliance (Spinelli et al., 2004:18).

1.2 Management Theory

Franchising as a concept is growing in economic and academic importance. Franchising in its essence has a multi-disciplinary nature that draws on disciplines such as economics, law, sociology, psychology and business (Hoy and Stanworth, 2003:1).

Hoy and Shane (1998) describes franchising as an entrepreneurial venture form with distinct differences from the firm or organization. They explain that franchising as a business format takes on the same characteristics as an entrepreneurial process and that there is a strong focus on aspects of entrepreneurship in the franchise model.

A special relationship exists between the franchisor and the franchisee referred to by Spinelli et al (2004:2) as an entrepreneurial alliance.

Underlying this alliance is a special relationship that exists between the franchisor and the franchisee. This alliance between entrepreneurs is governed by the Franchise Relationship Model (Spinelli et al., 2004:17). The franchise relationship model is an entrepreneurial framework that incorporates specific processes and elements that are unique to the
franchise business model. The relationship between the franchisee and the franchisor is governed by the franchise agreement, which is a documented agreement that spells out the different aspects of the relationship.

The Service Delivery System (SDS) focuses on the fundamental means by which customer's needs would be served in the franchise. It consists of all the "bricks" that is necessary to make sure that a strong brand is built and that customers return or recognise the brand and know what to expect. It contains the "ingredients" for the recipe necessary to make a successful enterprise and build a strong brand.

Lastly, it is important to describe which party to the alliance would be responsible for what in the service delivery system. Transactional analysis is used to determine the division of the functions. Transactional analysis refers to the division of the tasks in a SDS between the franchisor and the franchisee. Transactional analysis would be used to identify each of the tasks of the franchisor and the franchisee in the SDS.

1.3 Problem Statement

Many businesses that choose franchising as a means to obtain a bigger segment of the market go about this process haphazardly and without thinking about and understanding what franchising means and what the benefits or disadvantages of franchising would be for a company looking to
expand. These firms very often do not understand the benefits and
disadvantages why a firm would engage in franchising as a method of
expansion (Rodkin 2000:15).

There are many franchise offerings available in the market and franchisees
in June are often unsure about what they should be looking for in a
franchise offering. On the flipside of the coin many franchisors do not
know what a good franchise offering consists of and how to present the
franchise offering to franchisees (Timmons & Spinelli & Spinelli, 2004:
221).

Flowing out from the franchising as a business model there are several
relationships that are crucial for the successful operation of a franchise
chain. One of the most important relationships, namely the one between
the franchisor and the franchisee, is a very complex one and a relationship
that needs to be fully understood by both the franchisor and the
franchisee. One aspect of this relationship is the monitoring of
franchisees. How is the relationship between the franchisor and the
franchisee is monitored and controlled (Bradach in, 2004: 2)? Franchisees
who are not monitored may engage in shirking or free riding to detriment
of the franchise operation as a whole and thereby diminishing brand equity
and undermining the business concept (Spinelli et al., 2004:78; Brickley
and Dark 1987:401).
Furthermore, franchisees and franchisors do not always know what is expected of the other and operate without a clearly defined analysis of tasks. How are these tasks assigned and how are they divided between the franchisee and the franchisor (Spinelli et al., 2004:22)? Unassigned tasks could lead to confusion and misunderstandings between them and the result is often a corporate disaster with the franchisor having to face lawsuits from disgruntled franchisees and eventually face possible financial ruin.

1.4 Research Objectives

The objectives of this study are:

1.4.1 Objective one:
To investigate the meaning of the concepts of franchising, franchisor and franchisee. To show how franchising is essentially an entrepreneurial alliance between two entrepreneurs, namely the franchisee and the franchisor. The reasons why firms engage in franchising are investigated and the benefits and disadvantages of franchising are examined by contrasting it with company owned outlets.

1.4.2 Objective two:
The franchise offering is analysed from the perspective of the franchisee (i.e. what to look for in a good franchise offering) and from the perspective of the franchisor (i.e. what a good franchise offering consists of).

1.4.3 Objective three:
The relationship between the franchisee and the franchisor is discussed against the backdrop of the Franchise Relationship Model. The components of the Franchise Relationship Model are identified and it is shown how the elements of the franchise offering link with the Franchise Relationship Model to build a strong alliance between franchisor and franchisee.

1.4.4 Objective four:
The monitoring of franchisees is discussed and the different tools a franchisor can implement to monitor and supervise franchisees without restricting them and dampening their own creative inputs. The franchise agreement is the document that largely regulates the relationship between the franchisee and the franchisor. The importance of the franchise agreement is discussed and the role that the franchise agreement plays in the relationship between the parties is examined.

1.4.5 Objective five:
The importance of transactional analysis of the service delivery system is analysed and it is illustrated how tasks are divided between the franchisee and the franchisor in order to avoid confusion and a duplicity of tasks.

1.4.6 Objective six:
A conclusion and a summary of the findings of the study are presented.

1.5 Research Methodology

This study follows an extensive literary research with comparisons and analysis to achieve the stated study objectives. Writer found that not too
many academic treatises are published in South Africa on the subject of franchising.

Writer had the pleasure of dealing with and consulting Harvard University’s Business School (HBS) quite rewardingly in this study. Several appealing articles on the subject of franchising were downloaded from their very well organised and accessible website. One of the main sources of the study, *Franchising Organizations* (Bradach, JL: 1998), was ordered telephonically (over a weekend) from the HBS head office in Boston (Massachusetts, United States of America) and reached writer in his office, little less than ninety six hours later! Franchising as a business form has been known in the United States of America since the 1850’s. The result is that many of the older literature sources on franchising originated in the USA. Some very useful older publications on franchising are consulted in this study in order to achieve a balance between contemporary and older literature on the subject.

1.6 **Demarcation of the study**

**Chapter two: The rationale of franchising as a business concept:**
The definition of franchising, franchisee and franchisor is investigated in this chapter and how franchising is an entrepreneurial alliance between the franchisor and the franchisee. There are distinct differences between company owned outlets and franchised outlets. These two forms are discussed and the strengths of both these business models examined. The
main reasons are deliberated why businesses franchise and what benefits and disadvantages it holds in store for franchisees and franchisors. The franchise offering is examined from the perspective of the franchisee (i.e. what does a prospective franchisee has to look for in an offering) as well as from the perspective of the franchisor (i.e. what elements do a franchisor need to address when compiling a franchise offering).

Chapter three: The franchisee/franchisor relationship: The dynamics of the relationship between the franchisee and the franchisor is considered in this chapter against the backdrop of the franchise relationship model, described by Spinelli et al (2004:22).

Chapter four: The monitoring of franchisees: The monitoring of franchisees is discussed in this chapter. The reasons why it is important for the franchisor to monitor franchisees are investigated as well as the benefits of a good monitoring program for both the franchisee and franchisor. The franchise agreement is discussed as well as the meaning and implication of certain of the key clauses normally found in a franchise agreement.

Chapter five: The Service Delivery System and transactional analysis: An important aspect of the service delivery system is finding a suitable location to operate the franchise business from. The relationship between real estate and the service delivery system is explained in this chapter as an example how tasks in the franchise operation are identified and divided between the franchisor and the franchisee.
Chapter six: Conclusions and recommendations: In this chapter a summary is made of the major findings of the research document. These are then linked to some of the major recommendations flowing from this study.
2. Chapter Two: The rationale of franchising as a business concept

2.1 Introduction

This chapter concerns itself with the definitions of the terms franchising, franchisee and franchisor. The reasons why companies decide to franchise are investigated as well as the benefits and disadvantages of franchising for the franchisee and for the franchisor. There seem to be a polarisation between businesses that choose company owned outlets and businesses that choose franchising as a way to grow their business. Both of these models have very distinct characteristics and benefits that combined, can form a very powerful business format.

2.2 A definition and explanation of franchising

Franchising is mostly the product of an entrepreneurial process. The term entrepreneurship has been described as "(the) ability of someone that is able to seize a viable business opportunity and regardless of the resources available, implementing it successfully (Conradie:2002)".

Hisrich and Peters (2002:10) define entrepreneurship as: "The process of creating something new with value by devoting the necessary time and effort, assuming the accompanying financial, psychic, and social risks and receiving the monetary and personal satisfaction and independence".
Hoy and Shane (1998) describes franchising as an entrepreneurial venture form with distinct differences from the firm or organization. They explain that franchising as a business format takes on the same characteristics as an entrepreneurial process and that there are a strong focus on aspects of entrepreneurship in the franchise model.

Spinelli et al (2004:19) come to the same conclusion and also express franchising as a form, or an extension of entrepreneurship. They explain that franchising happens when an entrepreneur, the franchisor, develops a business model and then sells the rights to operate the business system to another entrepreneur who is called the franchisee.

The writers Timmons & Spinelli and Spinelli (2004:221) state that as is the focus of entrepreneurship, so is the focus of franchising the recognition of opportunity and the creation of wealth. They argue further that a franchise offering is a thoughtful system for reshaping and executing a delivery system designed to extract maximum value from the opportunity. Franchising according to them is an entrepreneurial alliance between two organizations, the franchisor and the franchisee. The team then operates in synergy to maintain and build the brand.

It is therefore concluded from the aforementioned definitions by different writers that a franchising operation has the following characteristics:

- It is an entrepreneurial process whereby a viable business opportunity is seized;
• A system is developed to extract maximum value by the franchisor from the opportunity;
• The rights to use the system is sold to a franchisee;
• An alliance between two organizations namely the franchisor and the franchisee is created;
• The opportunity is exploited by both as a team and they work together to build and maintain the brand.

2.3 Why companies decide to franchise their businesses

There are a number of advantages to a firm that decides to franchise. The most obvious of these reasons is the fact that a firm can quickly establish itself as a presence in a market and quickly lock itself in a market position. Another benefit is the initial fees paid by the franchisee and the ongoing royalty fees that are paid in return for support and training (Gompers 2001).

Tikoo (1996) lists several reasons why companies would decide to franchise. They are:

2.3.1 Resource constraints.

The main reason to franchise seems to be the fact that resource restraints can be more easily be overcome. Tikoo argues that firms often franchise because they cannot raise the capital required to set up company owned stores. He also states that a firm may also be restrained in managerial resources to set up a network of company owned stores. In the franchise
relationship the franchisees supply labour and capital to the franchisor and this is lower than a situation where the franchisor would train and recruit managers from scratch.

2.3.2 Specialization/Function benefits.
Franchising provides an effective way to trade off certain functions and thereby minimizing production costs. What is meant hereby is that franchisors are more cost effective when it comes to deal with and execute functions in a fast food business such as mass advertising, new product development and economies of scale. The franchisee on the other hand is more effective on a smaller scale such as in the preparation of food and serving the customer in the shop.

2.3.3 Monitoring costs.
The problem identified by several writers such as Brickley and Dark (1987) and Gompers (2001) is that in company owned stores, monitoring costs are high because the managers tend to engage in "shirking and perquisite taking", "free riding problems", "inefficient risk bearing" and "quasi rent appropriation". The fact that franchisees have invested their money in the business and therefore share risk in the venture. The corporation have to spend considerably less on monitoring costs because the managers (franchisees) are self motivated and entrepreneurs in their own right. They would work hard in order to make their outlet succeed.

2.3.4 Promotion efficiencies.
Advertising and building a brand is crucial to the success of a firm. When a firm has enough visible stores they can reap the benefit of nationwide
advertising. Advertising costs are also spread more evenly between the numbers of outlets.

2.3.5 Risk management.
When opening a new store a franchisor cannot precisely determine the business potential. If a particular store fails, the franchisee bears the risk of the failure. Franchising therefore enables a firm to judge the profitability potential of a particular store or area and not incurring the risk associated with a company owned outlet. In the event of the franchise agreement expiring, the firm can then convert profitable outlets in company owned stores.

2.4 Why are entrepreneurs interested in becoming franchisees?

2.4.1 A proven system.
Espinoza (1990) states that the main reason is that a franchisee buys into a proven system and that the failure rate of franchises is considerably lower than stand alone businesses.

2.4.2 Financial leverage.
Financiers believe that proven systems are less risky than a stand alone business and are prepared to lend money to these prospective franchisees.

2.4.3 Opportunities to build outlets.
If the franchisee proves to be successful, it would be to the benefit of both the franchisor and the franchisee if the franchisee was to open another outlet.
2.4.4 Access to information.

Gompers (2001) also mentions that franchisees have access to information relating to the business format, products and services that they would not otherwise be able to access were they stand alone operators.

2.4.5 Training.

Franchisees have access to training and therefore have a benefit over stand alone operators in that the franchisor would ensure that they are adequately trained to manage an outlet (Gompers: 2001).

2.4.6 Brand name, reputation and goodwill.

The franchisee buys into a business that has a vested brand name in the market and benefits from established goodwill (Gompers: 2001).

2.4.7 Financial requirements.

The financial restraints on the start up costs of a business are a high barrier for a prospective entrepreneur. A franchisee benefits from a lower than normal entry into an established market. It is also a better investment to buy into a franchise because the franchisor's know-how makes it a more efficient use of capital expended (Gompers: 2001).

2.4.8 Marketing.

The franchisee benefits from a bigger promotion and advertising budget and from a national scale of advertising (Gompers: 2001).

2.4.9 Economies of scale.

Franchisors have larger purchasing capacities and franchisees can avail themselves from the bulk purchasing capacities and negotiation capacities of franchisors.
2.4.10 Ongoing support.

One of the characteristics of franchising is that the franchisor commits him to ongoing support to the franchisee. The franchisee therefore has at its disposal access to specialised and highly skilled knowledge of the franchisor. There are also field supporters in many of the established franchised firms who travel between franchisees and supply them with service and knowledge (Mendelsohn, 1982:24).

2.5 The disadvantages of franchising for the franchisee

The following are the disadvantages of franchising to the franchisee as described by several of the sources consulted:

2.5.1 Imposition of controls.

Franchising inevitably entails the imposition of control by the franchisor on the franchisee (Mendelsohn, 1982:24; Gompers (2001). These controls are imposed to regulate the quality of goods sold or services rendered.

2.5.2 Payment of fees.

The franchisee will have to pay the franchisor for its services provided for the use of the system, marketing and support (Mendelsohn, 1982:24).

2.5.3 Difficulty of assessing the quality of the franchisor.

A franchisor's offering may not amount to a sound business offer and the franchisor may be unable to maintain the standards of ongoing services such as training and support (Mendelsohn, 1982:24; Vaughn 1982:67).

2.5.4 Restrictions on the sale of the business.
The franchise agreement may contain restrictions on the resale of the business (Mendelsohn, 1982:25).

2.5.5 Dependency.

The franchisee may get too dependent on the franchisor. The effect thereof is that the franchisee may not achieve the levels of motivation that is necessary for him to build his business (Mendelsohn, 1982: 25).

2.5.6 Mistakes of policy.

The franchisor may make a bad business decision that may adversely affect the whole franchise chain Mendelsohn, 1982: 25).

2.5.7 Diminishing of the brand.

The franchisee does not have as much control over the protection and preservation of the brand as he would have in his own business (Vaughn, 1982:67).

2.6 The disadvantages of franchising for the franchisor

Mendelsohn (1982:28) lists the following as disadvantages to the franchisor:

2.6.1 Independence of the franchisee.

If the franchisee's business is running smoothly and he becomes more independent from the franchisor, he may develop an attitude of not requiring the franchisor in his business. This can cause big problems for the franchisor if this situation is not handled carefully.

2.6.2 Maintaining levels of quality.
The franchisor should at all times ensure high levels of quality, service and support. The franchisor should always remember that the franchisee operates his business independently from the franchisor and that he cannot use and impose "company policy" on the franchisee to get the required results. The franchisee has to be coaxed into believing that the system described by the franchisor is the most sensible in his particular circumstance (Gompers: 2001).

2.6.3 Lack of trust.
There may occur a lack of trust between the franchisee and the franchisor out of the incompatibility of some of the franchisor's field personnel (Gompers: 2001).

2.6.4 Competition.
The franchisor may believe that with all the training put into a franchisee, he might be creating a future competitor.

2.6.5 Suitability.
The franchisor should take great care in selecting franchisees, due to the great responsibility placed in the hands of franchisees to build and protect the franchisor's brand.

2.6.6 Communication.
This is a vital aspect of the relationship and great care should be given by the franchisor that there is always a clear and unambiguous channel of communication available to the franchisee to resolve problems.

2.6.7 Not disclosing gross income.
Franchisees may understate their earnings by not disclosing all their revenue when they pay royalties based on their monthly turnover.
2.7 *Company owned stores vs. franchised units*

A discussion of the reasons why companies decide to franchise or not would not be complete unless the benefits of company owned stores and franchised units are discussed.

Brickley and Dark (1987:401) suggest that there may be merit in combining franchised outlets and company owned stores in a single business structure. They argue that it makes sense to franchise outlets if they are far from the head office because the monitoring costs are low. The writers also argue that the type of business plays a role in the decision to have company outlets or franchised units. As an example they use a fast food business close to a busy highway without many repeat customers and suggest that if this outlet was a company outlet, then the owner manager would not have a big incentive to adhere to stern quality maintenance standards. Therefore, a company would rather retain ownership of such a store. In a business where there are repeat customers, it is more likely that they would be franchised units. Brickley and Dark (1987:410) further suggests that factors favouring franchising over company owned stores are low investment risk on the part of the franchisee, low incentives for free riding by both the franchisor and the franchisee and low investment in firm specific assets.
Bradach, JL (1998:33) lists some of the main characteristics of company and franchise arrangements. In his discussion he refers to "chain operator", with this term the writer means that it could refer to either the franchisor in a franchise relationship or the employer in an employment relationship. For the ensuing discussion this term would also be used intermittently. Bradach (1998:2) criticises Brickley and Dark's model and conclude that there should be a mix of company owned outlets and franchised outlets, but they do not suggest how this system should be managed. Bradach's own model is based on what he calls a "plural form" (Bradach, 1998:4). The plural form entails that the advantages of both company owned outlets and franchised outlets are combined in the plural form to create a much stronger organizational form. Bradach (1998:10) argues further that the chain operator should strive to strike a balance between similarity and innovation. If there is too much similarity, it diminishes variety and too much variety diminishes similarity across the chain. Although Bradach's model can be a complete separate study in franchise operations the following are according to him "the building blocks of chain organisations:

2.7.1 Contractual relationship

The labels employee and franchisee imply two different relationships vis-a-vis the operator of the business. It entails two different agreements. One is an employment contract with company personnel, the other one is a business agreement with franchisees. Employees are subordinates to the operator of the business, while franchisees are partners of the operator. In an employee agreement, the subordinate would accept
decisions and orders from his superiors and carry it out. In the franchise agreement it is a partnership agreement between the owners, with a different assignment of duties to each of the partners. Underlying this agreement is the franchise agreement, a normally voluminous document that sets out the expectations and the rights of the parties in great detail. Macauley (1963) however, states that it does not fully reflect the entire relationship between the parties.

2.7.2 Chain operators' economic benefit

In a company operated arrangement, the company invested capital and receives the net income, while in a franchise arrangement, the franchisee provides the capital and pay royalties and thereafter receives the income from the unit. The franchise arrangement can create a potential problem for franchisees in the following manner: Franchisors benefit from royalties and higher turnover from franchisees. Franchisors can therefore engage in behaviour that boost revenue, but cut down on profits. An example of this is where the franchisor sells two franchises close to one another. The sum of the revenue would be higher but both the franchisees' profit will not be high. Similarly a franchisor can introduce a product that generates high volume and turnover but with little profit margin.

2.7.3 Local operator rewards and orientation

Company managers are normally rewarded by a fixed salary and promotions. A franchisee's reward comes from income generated by its units. Managers ensure that standards are met and kept high. This is a consequence of the reward system. By contrast the franchisee's reward is determined by how well his outlet performs on a financial basis. The
franchisee bears a lot of personal risk in the venture and they know they have to make it work. Maintaining operating standards matter to them but the central challenge is to make profit by competing effectively in their local market.

2.7.4 Source of chain operator influence

In an employment relationship people are “told” what to do. There is a direct line of authority. In the franchise relationship there is a different approach. The franchisor has to sell ideas rather than dictate them. The entrepreneurial partner has to be convinced that a certain decision is the right one.

2.7.5 Architecture of information

The information captured by the company arrangement is transparent from top to bottom but opaque from bottom to top. By this it is meant that in a company arrangement, the chain operator receives a lot of information from the bottom. In a franchise operation the chain operator receives very little information from the bottom, while the information from the top is very clear to the franchisee.

Bradach concludes this discussion of the differences between company owned outlets and franchised units by arguing that the typical company arrangement was a typical hierarchy, while the franchised units were held together by formal contracts and informal relationships and that it formed a federal structure. He suggests that there are benefits to be extracted from both these models and he suggests a so called plural form, which is a hybrid between franchised and company owned outlets.
2.8 The franchise offering

The following discussion focuses on what is put forward in a franchise offering. To look at it from the perspective of the franchisee: *What does a good franchise offering consist of?* The elements described in this chapter are normally located and described in the franchise agreement and in the operations manual supplied to the franchisee by the franchisor. The following are the elements of a good franchise offering, according to Timmons & Spinelli & Spinneli (2004:220):

2.8.1 The Service Delivery System (SDS)

Once an opportunity has been identified some thought has to be given to the way in which the product or service would reach the customer in the most effective way. The Service Delivery System (SDS) is the fundamental means by which customers will be served. The way in which the SDS is presented to the public can create the competitive advantage between competitors in a specific market (Timmons & Spinelli & Spinelli, 2004: 227). The SDS is also referred to by some writers as the business format or as a “franchise package” (Vaughn: 1982, 88) or as a “blueprint” (Seltz: 1982, 35).

Mendelsohn (1982:66) also points out that a principle aim of what he refers to as the “concept” (of a franchise) should be distinctiveness from its competitors and that each franchise has at its core an innovative concept that sets it apart from competitors.
Some examples of a well defined SDS are the “drive through windows” at a fast food restaurant, or the bi-level facilities in oil change facilities. (Spinelli et al., 2004:20).

The SDS is the essence of the franchise offering and should be described and perfected to the finest detail. It is suggested that the business model and by implication the SDS should be kept simple and that the overall aim should be to simplify control, reduce paperwork and to make the system as foolproof as possible (Mendelssohn, 1982: 65). The planning and the development of the concept require meticulous planning and great care and anticipation should be given to different needs and problem areas.

Morse (2003) states in an article that one should never franchise a concept. A successful model should first be established. Mendelssohn (1982:68) and Seltz (1982:35) suggest that a pilot operation should be used as a prototype operation. The franchisor and the franchisee would benefit from a prototype operation in the following manner:

• A pilot operation is a proving ground for the concepts, methods and techniques that the franchisor intends to use in the franchised operation;

• It is a secondary training centre for the development of corporate administration and operational personnel;
• It is an additional operation to provide the necessary income, expense and profit documentation required for every successful franchise offering;
• It is also an additional research and development centre for the testing of concepts, promotional campaigns and advertising programs.

Although the writers Spinelli et al. (2004) and Timmons & Spinelli and Spinelli (2004) do not deal specifically with the operating benefits of having a pilot operation in their discussion of the system delivery system, it is suggested that this is a safe route and advisable route into franchising. The benefits of having a pilot store outweigh any disadvantages.

After the franchisor has identified and developed a pilot store, he can proceed with the analysing and the detailing of the franchise program, or to use Spinelli’s term, the Service Delivery System.

In the final chapter of this dissertation, the Service Delivery System would be revisited and the different aspects thereof would be examined and examples given. The differentiation between the tasks for the franchisor and the franchisee will also be looked at.

2.8.2 Training and operational support

The trade name and the trademarks are the most valuable assets in a franchise system (Timmons & Spinelli and Spinelli et al., 2004: 228). In
order to protect and build these intangible assets, it is critically important for franchisors and franchisees to engage in training sessions regularly.

Training of franchisees occurs on two levels. Firstly, there is basic business training such as bookkeeping skills, administration, documentary systems and staff management. The second aspect of training relates to the providing of operational skills of a franchisor’s business (Mendelsohn, 1982:107). Espinoza (1990) argues that if an operation is well defined and well developed, he can do with a hardworking franchisee that has few business skills, while if the system is not so well developed, he needs to recruit franchisees that are highly skilled. The implication thereof, is that a well developed operation requires less training and support than a less developed operation. The opposite is unfortunately the position in practice (Espinoza:1990).

Stevens (1968:277) specifies certain criteria to which a franchise training program needs to conform to:

- The program must be easily administered;
- The program must be self paced and individualized;
- The program must be economical;
- The program must be continuous.

Seltz (1982:153) suggests that another benefit of training is that it ensures franchisee self confidence.
Operational support relates to the operational aspects of the business. Espinoza (1990) lists the following as further examples in which areas a franchisor can give operational support to franchisees:

- Assistance with site selection;
- Trade mark or logo;
- Established reputation;
- Accounting and quality control;
- Purchasing power in buying and advertising;
- Sharing of advertising costs;
- Managerial advice research and development, new product introductions;
- Assistance in obtaining finance;
- National and regional meetings to exchange information and experience.

It is suggested therefore that a franchised organization should engage in regular and continuous training and provide extensive and continuous operational support. It is a positive sign and a sign of commitment to prospective franchisees if there is a solid training programme and a commitment to training by the franchisor. It would benefit both the franchisor and the franchisee to invest in continuous and relevant training programs. By investing in continuous training and support, the franchisee/franchisor alliance would continue to add value to the brand, not diminish brand equity and work together towards the strengthening and building of the brand.
2.8.3 Field support

Field support is closely related to training and operational support. This normally takes on two forms, one where the franchisor’s representative visits the franchisee location in person and the other where the franchisor would retain resident experts in each of the managerial disciplines for consultation at the corporate headquarters (Timmons & Spinelli and Spinelli: 2004, 229).

One of the disadvantages of field support according to Mendelsohn (1982:24) might be that the franchisee sees the support as being restrictive and that controls are imposed on him. It is to be remembered that the franchisee functions as an entrepreneur in own right but do so under the license of the franchisor. It is important for the franchisor to exercise control over the franchisee to maintain standards. Timmons & Spinelli & Spinelli (2004: 229) refers to some franchisors that utilise the field support function as a “diplomatic or a pejorative exercise rather than for training and support”.

2.8.4 Marketing, advertising and promotion

Marketing programs are normally developed on three levels (Timmons & Spinelli & Spinelli: 2004, 229).

2.8.4.1 National advertising marketing and promotion.

Typically controlled by the franchisor, the franchisees contribute a percentage of their turnover to the fund;

2.8.4.2 Regional advertising, marketing and promotion.
Typically controlled by the franchisor, structured around an area of dominant influence or in a specified region;

2.8.4.3 Local advertising, marketing and promotion.

At this level the franchisee is normally contractually required to make direct expenditures on advertising. The franchisor normally gives certain guidelines in the franchise agreement relating to the boundaries of local marketing or advertising.

Spinelli et al (2004:94) discusses the reasons why marketing is important in franchised organizations. These factors are:

- Marketing states the system’s promise to the customer.
  
  If the franchisor has identified the customer, then he has to convince them to buy into his concept. Through marketing a promise is made to the customers that their needs would be fulfilled. When the sale is made and this is true to the promise made in marketing, then the service delivery system is validated and the brand is built.

- Marketing sells franchises and raises capital.
  
  A strong and well known brand is not only important in attracting customers but also helps in selling franchises and to obtain finance for the franchisees.

Scott (1990) refers to brand identity (in addition to a well developed system for doing business) as “probably a franchisor’s most important
stock in trade”. The brand must also be a planned, strategically focussed and integrated process throughout the franchise offering.

Spinelli et al (2004:102) warns against marketing in franchise organizations as it seems to be a contentious issue and often the subject of litigation. The franchise agreement should very clearly specify and outline all fees and expenditures mandated by the franchisor (this aspect would be discussed in greater detail when dealing with the franchise agreement and the components thereof). The writers also warn of free riding risks of franchisees. Free riding refers to franchisees who buys into a strong brand and capitalize on the brand while contributing little to the marketing budget or do little or no local advertising.

Brickley and Dark (1987:401) also list free riding as a problem frequently experienced by franchisors. They refer to the fact that franchisors can free ride on their franchisees. An extensive marketing campaign can be very costly and the franchisor is responsible for the costs thereof, while the benefit of the value goes into the individual outlets. Unless franchisors have the incentive to open more units, receive continuing revenue from the franchisees and owns certain of the units, franchisors have an incentive to default on their responsibility to protect and build the brand through advertising.

2.9 Conclusion
It is concluded from the aforementioned definitions by different writers that a franchising operation has the following characteristics:

- It is an entrepreneurial process whereby a viable business opportunity is seized;
- A system is developed to extract maximum value by the franchisor;
- The rights to use the system is sold to a franchisee;
- It is an alliance between two organizations namely the franchisor and the franchisee;
- The opportunity is exploited by both as a team and they work together to build and maintain the brand.

Several benefits have been discussed as to why a company would consider a franchising model and it appears that the main reasons a company would franchise are mainly to gain access to economies of scale, to expand rapidly or to gain a quick entry into a market and be a presence there without going through all the growing pains.

Several disadvantages were also described. A franchisor has to ensure that quality is controlled throughout the franchise system. It can be very costly to implement a monitoring program. The franchisor may also invest a lot of time, effort and money in franchisees and there exist a risk that they may use the system to compete with the franchisor.
Franchisees might be interested in franchising because it gives them access to a tried and tested business formula, it creates the security of buying into an existing brand name and to have accessibility to marketing exposure that they would otherwise not have been able to afford.

It follows from the discussion that one of the main disadvantages of a franchised system to the franchisee is the fact that a certain measure of control is still exerted by the franchisor in the franchisee. Entrepreneurs who are very independent may be restricted in a franchise system. Another disadvantage to the franchisee is that he may not get the required support of the franchisor or that there may be disputes relating to marketing and the payment of fees.

Bradach (1998) discusses the difference in approach between company owned arrangements and franchised arrangements and come to the conclusion that there exists a good basis that a firm that combines the two forms in a so-called “plural” form, can extract the best characteristics of both models and combine it in a single business format that is stronger than only a franchised operation or company owned operation.

It is clear from the aforementioned that both the franchisee and the franchisor can benefit from a concept that has been well established and clearly defined. The relationship between the franchisor and the franchisee is described as an entrepreneurial alliance and also that they would function in a team. Each item in the franchise offering depends on
both the franchisor and the franchisee operating as an allied force. Franchisors should offer prospective franchisees the training and support before they start the operation and thereafter do so on a continuous basis. The main aim of the franchisee/franchisor team should be the protection and building of their most valuable asset: the brand of the business. Franchisees should view franchise offerings that neglects to spell out how training and support be conducted very carefully and they should also be cautious of franchise offerings that does not have a clearly defined marketing and advertising program.
3. Chapter Three: The franchisee/franchisor relationship

3.1 Introduction

The next step is to look at the underlying relationship between the different elements discussed in the previous chapter and how it is integrated in the franchising relationship model.

3.2 Definition of the Franchise Relationship Model (FRM)

The underlying relationship between the different players in the franchising model may never be ignored. It was argued in chapter two that there appears to be a special type of alliance between the franchisor and the franchisee. In securing this alliance between two entrepreneurs there has to be a viable business opportunity in which both parties acknowledge the possibility to create wealth for themselves, as well as for the other key players such as the investors, employees and the community in which the business operates.

The franchise relationship model (FRM) takes the elements of a franchise offering discussed in chapter two and connects these elements with one another to provide a framework for the franchisor to show how he can most effectively construct a franchise company. It is also a framework for the franchisee to illustrate whether a business is suitable for his needs. Each of the principles interacts with the others to form a powerful
interlocking business concept that solidifies itself as the links are implemented more efficiently.

3.3 Figure 3.1: Franchise Relationship Model

The process starts with the customer in the centre of the FRM. Thereafter it moves to the Service Delivery System. Any changes in the target customer or the SDS, has consequences that would affect the franchise alliance.

The value of the FRM is that it enables one to identify the nature of the consequences. Once the causes are identified, the franchise can be
improved by realigning the transaction responsibility and reassessing the financial well-being and reliance on each of the franchise partners. The FRM is best explained along the lines of the following questions (Spinelli et al., 2003:18).

3.3.1 The Customer: How does opportunity recognition work in franchising?

It was discussed as part of the definition of franchising that it is essentially an entrepreneurial venture and that it therefore entails a valid business opportunity. As the customer is the centre of the FRM, the franchisor needs to develop a manner in which the customer can best be served and by the same time makes money for the franchisor and the franchisee.

Once a market and a demand are established for one's goods or products, the potential of the size of the market has to be measured. This is done as follows:

\[ \text{Target customer} \times \text{estimated revenue per transaction} \times \text{Transactions per year by each target customer} = \text{Revenue} \] (Spinelli et al., 2004:19)

Projecting revenue is a process of calculating the size of a customer base and the result of selling products and services to each member of the market. The customer base is projected as a percentage of the primary target audience. Then it must be realistically calculated how many products would be sold in the market, how many add on sales would occur
and how many times per year would a sale be made. With a projected figure of annual revenue in mind the business can then move on to the next level.

3.3.2 How is the service delivery system established?

The SDS or the business format is a proprietary design, discussed in detail in Chapter two. This is the fundamental means by which the customers’ needs would be fulfilled. It is also the manner in which the business describes how resources used in the business would be organised and arrayed to create a competitive advantage over competitors.

3.3.3 Transactional analysis: How are responsibilities divided between the franchisor and the franchisee?

Spinelli et al (2004:22) explains that the sum of all the transactions in the franchise relationship model constitutes the brand equity of the franchised business. The transactions for which the franchisor and the franchisee are responsible are documented in the franchise contract and the operations manual. In setting up the franchise offering the franchisor should detail what all the different transactions are to deliver the product or service to the customer. The tasks or transactions are then distributed between the franchisor (national) and the franchisee (local) level. The franchisor’s tasks normally include those actions that relate to economies of scale such as franchisee training, national advertising or the purchase of bulk material. The franchisee’s transactions normally include those tasks that have to be implemented in the local market such as hiring of employees and sourcing of local material. Some tasks may also be shared between the franchisor and franchisee.
3.3.4 Financial structure: How does the financial model work?

The financial concept flows forth out of the customer and the SDS. The customer definition in the franchise relationship model relates to revenue. The resources needed to establish the SDS relates to the costs involved to establish the business.

It is important to note how different individual transactions play a role in the financial structure of the franchised business. The different transactions have to be analysed and the question posed how each transaction can be most effectively incorporated in the SDS.

3.3.5 Agency issues: How to find the right partner

In South Africa, unlike in the United States of America it is not yet compulsory for franchisors to make disclosure of their financial statements, operating manuals or other information available that would enable franchisees to make an informed decision about buying into a franchise or not. Parker (2004:175). If however the franchisor belongs to the Franchising Association of South Africa (FASA), it is compulsory for its members to hand in a disclosure document, agreement and operations manual in with their application. Belonging to a body such as FASA is also a positive sign of a franchisor in South Africa, because he is willing to conform to FASA's principles of ethical franchising. A franchisee should investigate the offering very carefully and spend considerable time asking questions and visiting existing outlets. Espinoza (1990) states that at a minimum, the franchisee should ascertain whether he would receive a good measure of personal enjoyment from the franchise business that he
wishes to join. In addition to the offering the franchisee should also give
careful consideration to the following elements to decide whether a
franchise is suitable for him or not:

3.3.5.1 Capital.
Some franchises require a substantial input or rely on the fact that the
franchisee has some financial support to help him through the initial
stages of the business. Other franchisors may help finance their
franchisees in their businesses.

3.3.5.2 Skills and support.
The franchise should provide an extensive program of franchisee support
and investment in developing the franchisee's skills.

3.3.5.3 Operational flexibility.
The franchisee should consider whether he fits into the system and that he
does not find it restrictive to his own skills and approach. If the franchisee
has a high need for autonomy, he should not buy a franchise from a
franchisor that has a rigid format for doing business. Franchisors are
realising that strict standardization and excessive management can
distract the focus on the most important element of the relationship
model, namely the customer. Such conditions could hamper innovation
and creativity of the franchisees.

Scott (1999) also points out that a prospective franchisee should in
addition to what has already been discussed, try to talk to as many
owners as possible to form a clear picture of what to expect in the field.
From a franchisor point of view the selection may be a little more difficult. According to Spinelli et al (2004:26) franchisors tend to sell franchises rather than cultivate long term relationships. A franchisor should be sure that the person he selects as franchisee has the capabilities to conform to the business system and be motivated, especially in the early stages of the relationship. If there are not effective and open channels of communication, two of the biggest problems in the franchise relationship, shirking and free riding may occur. Shirking occurs when franchisees neglect to perform a specific task or duty outlined in the franchise agreement. A typical example is where franchisees substitute ingredients in food with less, or less expensive ingredients and thereby lowering the quality of the food and effectively undermining the brand equity and eroding the offering. Free riding occurs where a franchisee does not contribute his share towards for example local advertising but rely on the national advertising by the franchisor and thereby getting a "free ride" (Brickley and Dark, 1987:405).

3.3.6 Relational dynamics: How are tasks best monitored?

According to Spinelli et al (2004:27), a strict enforcement of the franchise agreement would almost ensure conflict and litigation would be inevitable. He suggests that the relationship be regulated both formally and informally. The following chapter focuses on the monitoring of franchisees and the role of the franchise agreement.

In addition to Spinelli's franchise relationship model it is also important to consider a couple of other basic aspects of the franchise relationship.
Vaughn (1982: 165) states that the most important aspects of the franchise relationship are:

- To motivate franchisees to perform at a high level in terms of internal operations and marketing;
- To facilitate the adoption of new ideas;
- To obtain new ideas from franchisees;
- To head off legal problems in the anti trust (called competition laws in South Africa) and trademark and trade name fields.
- Develop procedures to reduce need deficiencies and increase satisfactions;
- Reduce boredom by encouraging successful franchisees to obtain another franchise;
- Initiate and facilitate two-way communication with franchisees through periodic monitoring, franchisee councils and a face to face "open door" policy.

Vaughn's suggestions are centred on human psychology, that if you motivate and invest in someone then he would perform at his best. Emotions and feelings are important in the franchisee/franchisor relationship and are somewhat neglected in Spinelli's clinical discussion of the franchise relationship model.

Another writer on franchising, Seltz (1982:171) discusses his list of the most important aspects of the franchisor/franchisee relationship. He calls it the "Twelve Realities":

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• Be professional. Franchisees have rising demands and need professionalism. They expect the franchisor to bring quality marketing strategies into the management of the business. They do not want to settle for incompetence or mediocrity.

• Negotiate equally. The franchisor/franchisee relationship should be one in which the merits of the proposition is sold rather than dictated.

• Institute self improvement programs. Franchisees seek to improve their management abilities and ultimately their profits. Franchisors should look for ways in which to meet this need of franchisees.

• Provide a marketing umbrella. Franchisees want to see their business featured on a local and regional basis. They need the coverage that they could not afford on their own.

• Maintain high franchisor status. The franchisee expects the franchisor to maintain a high level of reputation. A reduction of the franchisor's status reflects adversely on the franchisee and can affect his or her substantial investment.

• Establish constant communication flow. Franchisees want to participate in future plans of the franchised business. They want to be consulted and they want their advice to be considered in planning the company's future.

• Plan for growth potential. Franchisees like to see their company expanding. Innovation is required and ways have to be identified to assist in this need of franchisees.
• Plan for diversification. Franchisees seek diversification for add on profits and earnings and to ensure that the business is constantly upgraded to meet current needs. Both the franchisor and the franchisee should actively seek new ways in which to serve customers’ needs better and more efficiently.

• Suggest immediate tax benefits. If the franchisor provides tax guidelines and show the franchisee on the tax benefits of their investment in the franchise, this could be an added service or benefit to the franchisees.

• Help the franchisee see “money now”. Some franchisees want money “now from the business. They want to see capital gain on their initial investment. The franchisor should assist in this need of franchisees.

• Provide strong leadership. Franchisees have their own way and ideas of how a business should operate. It is important that the franchisor has strong leadership skills to show the way and prevent that franchisees lose sight of the business format.

• Help a franchisee to become a community VIP. Franchisors should assist franchisees in this aspect so that they can become respected members of their community and a recognised face in the community.

3.4 Conclusion
The customer is at the core of the franchise relationship model and the service delivery system has to be perfected to best serve the customers needs and to exploit the business opportunity completely. In chapter two, it was discussed that franchising is a strategic alliance. In the execution of duties it is important that both parties communicate with one another, knows what it is expected from one another and work together to make the venture work. It is a symbiotic relationship in which both parties have to assist one another and take the needs of one another into consideration and work together to make the franchise model work.
4. Chapter Four: The monitoring of franchisees

4.1 Introduction

It has been discussed in chapter two, that the relationship between a franchisor and franchisee is a partnership or an alliance. It is not an employment relationship. Therefore, are terms like manage or “give orders” not taken kindly by franchisees in general. They are independent business people in their own right. Another approach has to be cultivated, one where franchisees are monitored instead of formally managed. The question that arises is how does a franchisor maintain standards and ensure uniformity across the franchise operation? What must a franchisor do to stimulate a culture of innovation amongst the franchisees and to make them feel that they are valued and respected as independent business people? This chapter focuses on the monitoring function of franchised businesses and how the monitoring of franchisees can help with these questions.

4.2 Why franchisees should be monitored

Brickley and Dark (1987:401) argue that the operation of units in a business system can be very costly because it is expensive to develop systems for controlling employee behaviour, especially if the units are dispersed over a wide area. As a result of expensive monitoring, each of the problems identified has a significant influence on the revenue of a franchised outlet and ultimately also on the franchisor's revenue. Spinelli
et al (2004:82) argue that the main reason why franchisees are monitored is that a certain level of service is promised to customers. Accordingly it is important that the brand should be protected by ensuring that the SDS is executed properly.

The most common problems in the franchise relationship according to Brickley and Dark (1987:401) are:

- inefficient risk bearing,
- shirking and perquisite taking,
- quasi rent problems; and
- Free riding.

The abovementioned franchisee behaviour has been affirmed by Spinelli et al (2004:79). As background to the topic under discussion let us consider and define the problems franchisors may encounter from franchisees:

4.2.1 Inefficient risk bearing.
This problem occurs where the franchisee under invest in certain areas of the business such as local advertising or the investing in extra equipment. The franchisee might be concerned about the risk of the investment, and not make the investment, despite the fact that it may have a positive effect on his revenue.

4.2.2 Shirking and perquisite taking.
Brickley and Dark (1987:401) conclude that it would not be in the interest of a franchisee to shirk because it would affect his own revenue more than a manager in an owner operator store. It does however occur that
franchisees engage in shirking by lowering the quality of their products by using substandard ingredients.

4.2.3 Free riding.

It has been found in franchises where repeat customers are low, such as fast food outlets alongside major travel routes, that the franchisees have an incentive to provide lower quality products. The problem is that the customer will not return to any of the other outlets again. The cost is therefore borne by the whole franchise chain. Another example is where a franchisee has little incentive if his local advertising leads to revenue in another outlet. These examples illustrate that franchisees may take a "free ride" on other franchisees or on the entire business operation.

4.2.4 Quasi rent appropriation.

Where a building has been erected with distinct features of the franchised store (such as a MacDonald's outlet) the franchisee may engage in opportunistic behaviour. An example hereof is where the franchisee refuses to pay the agreed rent due, and offer to pay a lower amount. Due thereto that the franchisor has the risk of the mortgage, he would consider it for that reason and because enforcing the contract would entail larger expenses than benefits.

4.3 Management challenges of the franchise operation

In addition to the aforementioned "problems" of franchisors with franchisees, Bradach (1998:21) suggests that there are several
"challenges" facing the management of a franchise chain. These challenges are:

- Growth by adding units;
- Uniformity;
- Local responsiveness;
- System wide adaptation.

The franchisor wants to maintain the SDS and the brand by making sure standards are kept up and to prevent that franchisees engage in behaviour described above. Several tools exist and are described that enable the franchisor to maintain standards, assuring uniformity, implementing and maintaining system wide adaptation, preserve the brand and guard against franchisees shirking or free riding. The tools described by Spinelli et al (2004: 84) and Bradach (1998) that has to be implemented in the franchise operation to ensure compliance with the business methods of a franchisor are:

- Field support;
- External service audits;
- Peer review;
- Analytical tools;
- Customer feedback;
- Mystery shopping;
- Management information systems

These tools are described as follows:
4.3.1 Field support

Many franchised companies use support personnel to act as a liaison between the franchisor and the franchisee. Field personnel's main responsibilities include:

- Evaluating franchisees;
- Identifying potential problems;
- Implementing corrective actions

When a company develops and implements a field support system, there is usually a rating system against which franchisees can benchmark their performance relative to other franchisees. There has to be a balance between the number of field support staff and the franchised outlets. The more field support staff is employed, the higher the monitoring costs.

Bradach (1998: 197) describes how a typical field visit works in a franchise operation: "Typically after sitting down in the franchisee's restaurant, ordering something, and eating, the franchise consultant asked to take a look around, which meant looking behind the counter of the franchisee's restaurant. During the course of several tours of restaurants, I never heard a consultant tell a franchisee or their employees to do anything, even if a deviation was observed. The consultant might ask them about an item—which of course drew attention to it—but there was no analogue to the manager to in the manager in the company unit saying: "do this; fix that". The franchise consultant sometimes explained a new marketing program or the operation of a piece of equipment, but it was always done..."
in a non directive way. The entire conduct of the field visit reinforced the understanding that this as the franchisee's business.”

Bradach (1998) goes further and argues that the purpose of a field visit is that the franchisee is treated and respected as an independent businessman. He also suggests that these field visits are formally documented in a business letter. This letter would confirm the visit, the findings, recommendations, obligations and concerns. This action provides both parties a valuable paper trail that is very useful if the relationship ends in litigation.

4.3.2 External service audits and peer review

In order to curb the costs of monitoring franchisees, some franchised businesses make use of outside consultancies to monitor franchisee operations. An example of how an outside agency might perform this function is the so called “mystery shopper”. The consultancy would have a brief wherein it is specified what to look out for in a franchisee. A member of the agency visits an outlet and sends a report to the franchisor about his findings. The limitations of this method are however that the “mystery shopper” is subjective and does not understand the business as well as the franchisor or the franchisee.

Bradach (1998:99) submits that mystery shopping is a method of monitoring more frequently used in company owned operations. His findings were that franchisees are generally not opposed to mystery shopping, unless they are not informed thereof and it is used to evaluate
and compare them to other franchisees. Bradach’s findings in this regard are in line with the submission made earlier that franchisees don’t want to be managed as such by the franchisor.

Another form of monitoring is peer review. The aim of this method is conducted between franchisees in the same franchise system. Different franchisees visit locations, work in operation, review the back office and interview employees and customers. Franchisees have a vested interest in one another’s performance; a program of peer review can be an effective method of franchisee behaviour. An example of how this method of monitoring could have prevented brand undermining is the following:

A team of Carte Blanche (a local actuality television program) went into various fast food outlets in order to test the quality of the cooking oil and reported their findings. They found that a “Something Fishy” franchise in Durban re-used oil that contained unhealthy levels of poisonous bi-products and was potentially dangerous to consumers. The franchisees of other outlets were outraged by this incident because: “it diminished the brand in the public eye and the whole system suffers because one franchisee did not adhere to the operating manual. People view an isolated incident like that in a very serious light and would never purchase from any Something Fishy outlet again, as a result of such an incident.” Annemarie Velloen (personal interview, 9 October, 2004).

If proper monitoring methods are in place, then a situation like this would not happen. A franchisee’s peers who wish to uphold the standards and
quality would report a franchisee that shirk to the franchisor and call for steps to be taken against such franchisee.

4.3.3 Analytical tools

Another method of monitoring franchisees is to use a set of performance expectations based on the performance of a couple of company stores. Any store that falls outside the expectation report is then visited by the franchisor and the origin of the problem investigated.

4.3.4 Customers

Customers can provide the franchisor with a wealth of information regarding how well the store is meeting expectations. After all it has been discussed the fact that the customer is the centre of the franchise relationship model.

4.3.5 Other methods and benefits of monitoring

Seltz (1982:177) refers to the monitoring of franchisees as “supervision”. Some of the additional methods that the writer mention are:

- Mail contact. In our day and age the power of the internet and email make it possible to be in contact with hundreds of people on a daily basis. This contact form can be used to inform franchisees of news flashes, messages with a motivational slant, self check activity forms where franchisees can highlight the franchisor on a frequent basis with up to date information from the local store;

- Telephonic contact. If franchisees hear from the company executive every now and then in person they feel valued and may act as a motivator;
Seltz (1982:179) also lists the benefits that supervision creates:

- Builds morale;
- Decentralizes head office functions;
- Enables regional control and follow-up;
- Achieves constant and open channels for communication;
- Assures maximum morale and help to eliminate hostility;
- Acts to place franchisees on the right path in the first six months of the franchise operation. Normally the critical period when franchisees can fail irretrievably in their operation.

Bradach (1998:106) discusses two processes whereby a franchise operation that consists of franchised units as well as company units can use to ensure that uniformity is maintained across the board of the outlets. These two processes are described by him as ratcheting and modelling:

- Ratcheting: Franchised outlets and company owned outlets are benchmarked against one another in order to create healthy competition between these two "camps". Legitimate units of measure are given to the two camps. People identified strongly with "their side", thereby creating a situation where the company owned stores would raise their standards to get on par with the franchised outlets, or vice versa.

- Modelling is in some aspects similar as ratcheting. In this regard the most successful store(s) are used as a model to other units whether
it be franchised units or company owned. The argument is that all
the outlets should model their system on the successful outlet.

Despite the fact that costs of monitoring franchisees may be high, it is
very important for the franchisor to fulfil this function. On a business level
it protects and builds the brand. It avoids situations where franchisees
shirk or free ride on the reputation of the franchisor. On a psychological
level an effective monitoring system ensures that the morale of the
franchisees are kept high and that the franchisee feels that he is important
when he knows that the franchisor cares about him and the performance
of his outlet. Franchisees benefits from monitoring because it ensures
that their hard work is rewarded by ensuring that standards are
maintained across the whole franchise operation.

4.4 The franchise agreement

The franchise agreement is probably the most important document that
exists between the franchisor and franchisee because it contains the
description of the rights between the parties and also outlines the

In South African law there is not a separate set of rules pertaining to
franchising but is governed by several legal principles such as copyright,
intellectual property, competition legislation and depending on the
circumstance, several other aspects of law (FASA:2001). In South African
law, the franchise agreement is a binding agreement governed by the same legal principles as any other commercial agreement. Matthewson and Winter (1985) states that the principal ingredient in a franchise agreement is the right to use a national brand name in exchange for a share of the profits to the franchisor.

Rubin (1978:223) states that there are several standard clauses in franchise agreements. He states that the franchisor normally agrees to provide certain assistance and support to the franchisee. The support typical support consists of start-up assistance and training for the franchisee and ongoing support during the term of the franchise agreement. The initial fee provides the franchisor with capital to finance the franchisee's initial training and the ongoing support is paid for by the royalties paid.

Depending on whether one looks trough the glasses of a lawyer or that of a businessman, the emphasis of the franchise agreement's role in the relationship between the parties may differ. Shannon (a lawyer) (1982:221) describes the role of the franchise agreement as follows: "The relationship between a franchisor and franchisee is invariably based on contract."

Macauley (1963) and Macneil (1978) describe the role of the franchise agreement as follows: "The contract sets the expectations of the parties
and creates a framework for the relationship but it does not fully reflect the actual conduct of the relationship.”

Bradach (1998) agrees with the latter view and he concludes that the formal contract between the parties is a limited and sometimes misleading map to understanding how the franchise relationship was conducted in practice.

A contract in the legal sense is an agreement made with the intention of creating obligations by mutual consensus between the parties (Potgieter: 2001). A valid and enforceable agreement however, comes into existence when the following elements have been complied with:

- The parties should have the necessary contractual capacity (i.e. they should be older than 21 at the time of the signing of the agreement);
- The performance must be possible at the time of contracting;
- The contract must have a lawful objective;
- The particular formalities should be observed;
- The contract must be certain, meaning that it should not be vague.

Kurt Illetschko (2002:32) also specifies the following guidelines when evaluating a franchise agreement:

- All the relevant common law and statutory requirements should be observed;
• The agreement should be drafted from a practical point of view. The intention of the parties should always be borne in mind.
• The agreement must be a memorial of the transaction which the parties can read without difficulty and one that does not invite the intervention of the courts.

4.5 Key clauses of a franchise agreement

Here are some of the main clauses one might expect to find in a franchise agreement. It has to be borne on mind that each franchise agreement would differ from the next, so this is only a guideline:

4.5.1 The parties.
An agreement would normally start with a reference to the parties to an agreement. Careful attention has to be given to this clause. Companies, private persons or Close Corporations have to be carefully described with reference to full names, identity numbers, registration numbers, addresses and who represents these entities. At this point the franchisee may want to ascertain that he is doing business with a franchisor that is honest. It is advised that the franchisee should (if he had not done it before); investigate the history of the franchisor.

4.5.2 Definitions.
This clause attempts to give clarity to terms used in the agreement. Definitions should be carefully analysed and properly phrased. Useful definitions would refer to the following and explain it clearly:

• The business system;
• The franchised business;
• Intellectual property (designs, patents, goodwill, copyright, trade dress, trade marks, trade secrets etc.)
• The operating manual;
• The territory in which the franchisee would be functioning;
• The effective date of the agreement and also the commencement date of the business.

4.5.3 Rights granted.
This is a very important clause because this would describe the rights that the franchisor grants the franchisee in relation to the business. This clause would normally refer to the right to:
• Operate the franchised business;
• From premises within the territory;
• Using the franchisor's business system;
• Using the franchisor's intellectual property as defined in the franchise agreement and operating manuals.

4.5.4 Duration and renewal.
Most franchises are granted for a specific period with the provision for renewal. These periods depend from business to business. Brickley and Dark (1987:420) argues that longer term agreements can help to prevent franchisees from engaging in quasi rent appropriation.

4.5.5 Territory.
When exclusive rights are granted for a specific area it is of utmost importance that the territory be described carefully. Market conditions may however change and an additional franchise may be considered in the
area. It is advisable that the franchisee in the territory has a right of first refusal. The selection of suitable premises is of great importance. The assistance with the selection of the premises should be described in detail and the task clearly defined to which of the parties bear the onus of negotiating a lease.

4.5.6 Franchisee obligations

This clause normally deals extensively with the obligations of the franchisee and compliance with the operations manual. The parties should ensure that these obligations are written objectively and not overly in favour of the franchisor. The clause will normally cover the following aspects:

- Operations manual and compliance with it;
- Goods and services that the franchisee are required to use and offer to the public;
- Minimum performance standards;
- Advertising with specific reference to local advertising and regional and national advertising. If it is the case, the contribution from the franchisee to the marketing fund;
- Training. Required training and ongoing training or any refresher training during the period of the franchise agreement;
- Premises. A detailed description of the premises from where the franchisee will conduct the business. This clause would also cover any local authority or governmental requirements. This clause also deals with the session of the lease agreement to the franchisor, thereby ensuring the franchisor to continue with the business should
the agreement expires and the franchisor wishes to continue with the lease.

- Location of suitable premises with specific reference to the locating of the premises, the period in which suitable premises has to be located and then the result of suitable premises not be located within the prescribed time periods.

- Payments. This clause deals with the initial payment and ongoing royalties payable to the franchisor. This clause should be drafted with clarity and precision in order to avoid confusion later.

4.5.7 Payments

This clause deals with the initial payment and ongoing royalties that are payable to the franchisor. This clause should be drafted with clarity and precision in order to avoid confusion later.

4.5.8 Franchisor obligations

The duties of the franchisor may differ considerably from business to business but should normally include the following obligations:

- Disclosure of the business system;
- Delivery of a starter package;
- Disclosure and designation of design, decor and fittings;
- Supply of training, continued support and assistance to the franchisee;
- FASA's consumer code requires the assistance and availability of experienced and key members of staff to be available to the franchisee;

4.5.9 Relationship between the franchisor and the franchisee
The franchisee is an independent operator owner of the franchised business and not a partner, agent or representative of the franchisor. The importance of this aspect is the fact that the franchisor should not be held liable for the franchisee's unlawful conduct. The public should also be warned of this fact by putting up a sign at the franchisee's premises to indicate that the franchisee is a proprietor in own right.

4.5.10 Use of intellectual property rights

It has been discussed that the use and the authority to use the franchisor's intellectual rights is one of the most important aspects of the relationship. It is important to properly describe the different intellectual property rights to avoid confusion. These rights include the right to use the franchisor's get-up, trademarks, trade secrets, copyrights, patents and other distinctive features. The following should be clear from this clause:

- That the franchisor's intellectual property rights are not misused by third parties;
- Compliance with the South African Trade Marks Act;
- A list supplied to the franchisee of all the intellectual property rights and where possible diagrams or photos of the rights;

4.5.11 Improvements to intellectual property

Disclosure should be made from time to time to the franchisees of improvements or changes to the intellectual property rights.

4.5.12 Transfer of title

It is important that the franchisee cannot dispose of the business without giving notice to the franchisor and the franchisor approving the prospective new franchisee.
4.5.13 Death or incapacity of the franchisee

This clause deals with the transfer of the business after the death or incapacity of the franchisee. It should provide for interim arrangements to protect the business and ensure that the business does not suffer any damage as a result thereof.

4.5.14 Restraint of trade

This is a very important clause because it protects the franchisor against a franchisee applying the know-how, in another business in competition with the franchisor. The clause should however be drafted carefully by the franchisor so that it is not unreasonable towards the franchisee. If a court finds that a restraint of trade clause is too restrictive and unreasonable, the whole clause could be null and void and the franchisee may potentially be able to cause serious damage to a franchisor's business.

4.5.15 Warranties

This clause would normally call upon franchisees (if they are legal personae) to bind themselves as co-principals and debtors with the legal person

4.5.16 Dispute resolution

The Consumer Code of Franchising makes provision for mediation and arbitration process but the parties are free to decide what manner of dispute resolution they want to follow.

4.6 Conclusion
Despite the high costs of monitoring franchisees it is an important and necessary function in a franchise organisation. Franchisees generally do not want to feel managed and rightly so, because they are businessmen in their own right. The importance of monitoring is to protect the brand, maintain standards across the franchise operation and to ensure that levels of service and uniformity are adhered to by all the franchisees. Monitoring does not only benefit the franchisor, but benefit the franchisee as well.

In the monitoring function, the franchise agreement is an important document in the franchisee / franchisor relationship and should be carefully drafted, preferably by an attorney specialising in franchise law. Although the franchise agreement is a complex document dealing with a variety of legal issues, it should be drafted clearly and the points made must be crisp and no confusion should be invited by writing a complex document making the interpretation thereof impossible. The franchise agreement is important but a holistic approach should be taken, taking the whole relationship into account and not focussing on one or two minor breaches of the agreement. The franchisor should use the franchise agreement as a last resort to bring franchisees breaching the relationship, in line.

The spirit of the franchise agreement should reflect the fundamentals of the relationship, namely an entrepreneurial alliance and it should be an
extension of the alliance, rather than a whip to crack at the slightest contravention.

It is also important that when interpreting an agreement the "bigger picture" is borne in mind and a common sense approach is practical to ask oneself whether the agreement is a fair reflection of what the parties intend to document.
5. Chapter Five: The Service Delivery System and Transactional Analysis

5.1 Introduction

This chapter illustrates how the transactional analysis of the franchise's service delivery system works. The importance of the SDS has been discussed and the importance that the franchisor and the franchisee know exactly what is expected from them to deliver the service or the product to the customer. When the SDS is analysed into different categories and each transaction analysed and the tasks apportioned, the strategic alliance between the partners in franchise relationship becomes a well oiled and well organised operation.

It falls outside the ambit of this study to investigate each and every aspect of the SDS and the transactional analysis of each of the underlying tasks. As an example, it will be described in detail how the real estate function (i.e. the location and development of a business site) functions in the SDS and how the tasks are divided between the franchisor and the franchisee. As further examples, the service delivery system of other aspects of the franchise would be given at the end of the chapter.

5.2 The SDS and real estate

Real estate is valuable for a franchise operation if it provides the platform for the delivery of the product or service to its customers. The investment
that is made in the real estate is validated when the market demand is fulfilled (Spinelli et al., 2004:53). Franchisors in South Africa, according to Rodkin (1996:49), rank good location higher than the service or product they are offering. In South Africa the retail market is dominated by large shopping centres. These shopping complexes attract large volumes of customers with influential purchasing power.

5.3 Platform for the SDS and the influence of buyer behaviour

The main feature in establishing where a business would buy or rent premises, are dictated by the behaviour and the location of its customers. According to Spinelli et al (2004:53) the franchisor should investigate the type of buying behaviour his customers and categorise it as follows:

5.3.1 Spontaneous buying behaviour.
This is where a purchase is made without thinking too hard about it. The items in this category are for example: petrol, coffee or a daily newspaper. In spontaneous buying it is of paramount that an outlet is located very conveniently for the customer to make a purchase.

5.3.2 Semi planned purchase behaviour.
This type of buying behaviour consists of two stages namely, a trigger to make a purchase. Secondly there is a time gap between when the problem is identified and when the purchase is actually made. An example of this type of buying behaviour would be the purchase of paint to paint a house. Real estate in this regard should be selected to optimise cost and
benefit. The aim is to minimise cost for the retailer and to optimise location benefits for the customer.

5.3.3 Planned purchase behaviour.
In this instance care is taken by the consumer before a product is purchased. Examples of these purchases are electronics, luxury goods or motor vehicles. Prime retail sites are not a pre requisite for these purchases.

5.4 How to select real estate
Ernst and Young (1997) published a study regarding the common practises in assessing retail markets and site selection. Their finding were that retailers should change their emphasis from the quantity of stores to the quality of stores that they open. They point out that the three criteria for selecting are:

- Projected sales potential
- Population
- Geographic location.

Spinelli et al (2004:57) describes the real estate process as comprising of three steps:

- Selecting the site profile based on primary target audience demographics;
- Finding the trade area that best matches this profile. A trade area is the area within which by a rule of thumb, 70-80% of customers will
come from. Trade areas may be more attractive than others if there are other anchor shops and shopping malls;
• Assessing the attractiveness of both the trade area and the actual site.

Spinelli et al (2003:58) lists some of the most important considerations when locating premises for a prospective franchisee. These aspects are of course not a closed list and writers such as Seitz (1982:71) supply similar considerations for the obtaining of premises.

5.4.1 Density of the primary target audience.
If a target audience has been effectively captured, then a business spends the first year building the brand and thereafter expand the business into the secondary and tertiary target markets.

5.4.2 Traffic volume
Another element in determining the attractiveness of a site is the traffic volume that passes the site. This is often measured in the amount of pedestrians or vehicles that pass a site within 24 hours. The data is also segmented between weekday and weekend operations.

5.4.3 Site visibility
Visibility of key aspects of the store's location is important. Convenience is important to semi planned and planned purchases and crucial for spontaneous buying behaviour. Enough time must be allowed for customers to recognise the site and locate safe parking close to the store.

5.4.4 Zoning
Aspects relating to the zoning are important to take into account when identifying a site. Some sites are perfect for a particular business but may not be capable of zoning or business rights due to municipal ordinances.

5.4.5 Traffic flow to the site
Properly managed traffic flow to a site can maximise throughput of volume in and around a site, which will maximise revenue inside the building. Entrances and exits to and from the site are very important in this aspect of site selection.

5.4.6 Complimentary versus contradictory neighbours
This deals with clustering of different businesses. Certain businesses make sense close to one another. As an example it makes sense to place a fast food outlet next to a video store. The opposite can also be true.

5.4.7 Traffic patterns
This aspect relates to the pattern of traffic passing a site with specific reference to inbound and outbound sides of the street. Other aspects are for example whether the site is situated on a corner, normally a positive indicator for a site. Inbound or outbound traffic flow is important depending on the type of business one wants to establish. A convenience store is normally better when it is situated on the homebound side of the street.

Understanding the aforementioned criteria adds the structure and the objectivity required to compare different site and to select the most beneficial site for a business. Seltz (1982:74) and Spinelli et al (2004:62) suggests a site location work sheet to compare different sites objectively.
Miller (1997) gave in addition to the aforementioned criteria, certain "X factors" that he argues are often overlooked when choosing a site. His "X factors" are:

- **Employee base.** Sometimes an excellent site is found but is situated badly in terms of potential employees. Employees suited for the business may typically be from lower middle class regions and the site is located in an upmarket, difficult to reach location.

- **Green acre syndrome.** This occurrence is where a business owner spots a piece of land on the fringes of a developing area. The business may initially capture the market but as the development grows, new competitors move in and competition levels and costs rise.

- **Current and future traffic patterns.** Future traffic plans are often overlooked when locating a site. A proposed new road could alter traffic patterns detrimentally to or from a site.

### 5.5 Transaction analysis

The importance of transactional analysis lies therein that by examining the different tasks of the franchisee and the franchisor, the exact source of a system's competitive advantage is identified and the tasks can be allocated to the party that does it best. Training becomes more focussed and efficiency increases (Spinelli et al., 2004:108). Transactional analysis "deconstructs the service delivery system in different layers. The aim of
the dissection should be to assign the tasks cost effectively and to make the execution thereof as easy as possible.

In the first part of the chapter the importance of real estate is examined and the criteria along which a decision of site location has to be based. The whole process of site acquisition entails certain transactions or tasks. Examples are the compilation of the work sheet that refers to the different site criteria. Someone has to physically perform these tasks. It is important that when a franchisor develops a transactional analysis that he and the franchisee work closely together and discuss the assignment of tasks in order to set proper expectations.

### 5.5.1 Table 5.1: Transactional analysis for real estate

<table>
<thead>
<tr>
<th>Transaction</th>
<th>Franchisor</th>
<th>Franchisee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Site criteria</td>
<td>Define the key elements of a location, obtain relevant information to best serve a customer in the target audience</td>
<td>Apply the site criteria to the local market</td>
</tr>
<tr>
<td>Site acquisition</td>
<td>Advise the franchisee on lease and purchase agreements and offer lease and purchase agreement templates</td>
<td>Negotiate and execute the lease or purchase agreement</td>
</tr>
<tr>
<td>Zoning and planning</td>
<td>Advise the franchisee regarding zoning laws and suggest professional contacts such as lawyers and engineers</td>
<td>Manage the local zoning process by meeting with local boards and hiring professional consultants</td>
</tr>
<tr>
<td>---------------------</td>
<td>-------------------------------------------------------------------------------------------------</td>
<td>-------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Construction</td>
<td>Prepare and supply blue prints. Create standardised contracts. Provide management support</td>
<td>Obtain local government approval. Solicit bids from local contractors. Handle day to day management of the contractor relationship.</td>
</tr>
<tr>
<td>Equipment purchase</td>
<td>Negotiate national contracts</td>
<td>Establish purchase timing and installation and make payments</td>
</tr>
<tr>
<td>Building or leasehold improvement</td>
<td>Create standardised plans and blue prints and manage the contractor</td>
<td>Modify plans for local building codes and monitor the contractor relationship</td>
</tr>
<tr>
<td>Inventory purchase</td>
<td>Establish efficient inventory level and order quantities. Negotiate national</td>
<td>Place local orders and manage unit level inventory.</td>
</tr>
</tbody>
</table>
### Table 5.2: Transactional analysis for ongoing outlet operations

<table>
<thead>
<tr>
<th>Transaction</th>
<th>Franchisor</th>
<th>Franchisee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating manual</td>
<td>Develop the business model and document a manual for use by the confidentiality</td>
<td>Adhere to the business model and maintain its confidentiality</td>
</tr>
</tbody>
</table>

By using transactional analysis for every major aspect of the franchise operation the SDS can be maintained and the brand expanded and strengthened.
<table>
<thead>
<tr>
<th>Category</th>
<th>Task Description</th>
<th>Role</th>
</tr>
</thead>
<tbody>
<tr>
<td>Training manual</td>
<td>Create a training department for operations R&amp;D and the development of training manuals and videos</td>
<td>Train employees</td>
</tr>
<tr>
<td>Advertising manual</td>
<td>Create and advertising program working with an advertising and public relations firm and local promotions</td>
<td>Purchase local media and execute through the media purchase and local promotions</td>
</tr>
<tr>
<td>Location inspecting/monitoring</td>
<td>Write evaluation criteria based on the operations manual. Field support personnel visit stores and consult with franchisees. Cooperate and communicate with the franchisor. Discuss operational problems and solutions</td>
<td>Cooperate and communicate with the franchisor. Discuss operational problems and solutions</td>
</tr>
<tr>
<td>Research and development</td>
<td>Operate company outlets and share knowledge with the franchisees</td>
<td>Problem solving and communication. Sometimes acts as a test location for new products or procedures</td>
</tr>
<tr>
<td>Inventory</td>
<td>Establish, review and approve product specifications and</td>
<td>Develop local vendors for non national contract supplies and</td>
</tr>
</tbody>
</table>
5.5.3 Table 5.3: Transactional analysis for advertising and public relations:

<table>
<thead>
<tr>
<th>Transaction</th>
<th>Franchisor</th>
<th>Franchisee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brand definition or message</td>
<td>Develop the advertising theme or message</td>
<td>Provide advice and feedback on experience in store</td>
</tr>
<tr>
<td>Material development</td>
<td>Manage marketing material production by managing the advertising agency</td>
<td>Contribute the contractually agreed upon amount to the advertising fund</td>
</tr>
<tr>
<td>Regional marketing</td>
<td>Provide input to and exercise voting rights in regional advertising councils</td>
<td>Contribute to the regional advertising fund and participate in cooperative governance</td>
</tr>
<tr>
<td>Media placement</td>
<td>Make the national advertising (TV and radio) purchases utilizing the national advertising fund</td>
<td>Make regional media purchases through the cooperative and local media purchases individually. Use franchisor developed creative materials</td>
</tr>
<tr>
<td>Promotions</td>
<td>Develop national promotional events and provide advice on local promotions</td>
<td>Evaluate participating store consent for national promotions. Create local promotions.</td>
</tr>
</tbody>
</table>

5.5.4 Table 5.4: Transactional analysis for product supply:

<table>
<thead>
<tr>
<th>Transaction</th>
<th>Franchisor</th>
<th>Franchisee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Product specification</td>
<td>Prioritize product usage and detail specification</td>
<td>Provide feedback on product performance</td>
</tr>
<tr>
<td>Approved suppliers</td>
<td>Investigate vendors who meet specification criteria</td>
<td>Introduce new suppliers for franchisor approval</td>
</tr>
<tr>
<td>Supply contract development</td>
<td>Negotiate national buying contracts</td>
<td>Purchase for local needs and make payment</td>
</tr>
<tr>
<td>Research and development</td>
<td>Field test new products, report of new product introductions, make appropriate changes to the operations manual.</td>
<td>Field test new products, communicate product success and failure and recommend product needs and changes.</td>
</tr>
</tbody>
</table>

5.6 Conclusion

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The real estate aspects of an operation are very important for the continuing success of the business. Careful attention has to be given to the location of premises and aspects such as traffic volume, traffic flow, visibility and the density of the primary target audience.

The transactional analysis holds many benefits in for the franchisee as well as the franchisor. These benefits are aimed at the improvement of the SDS and the preservation and the expansion of the brand. In a true entrepreneurial alliance this should be the aim of both sides. If everyone knows what it is expected from him, then confusion is avoided and wealth is created in the franchise operation.
6. Chapter Six: Conclusion and recommendations

6.1 Conclusion

Franchising as a business format can be described as having the following characteristics:

- It is an entrepreneurial process whereby a viable business opportunity is seized;
- A system is developed to extract maximum value by the franchisor;
- The rights to use the system is sold to a franchisee;
- It is an alliance between two organizations namely the franchisor and the franchisee;
- The opportunity is exploited by both as a team and they work together to build and maintain the brand.

There are several benefits to the question as to why a company considers a franchising model for its operations. It appears that the main reasons a company would franchise are to gain access to economies of scale, to expand rapidly or to gain a quick entry into a market and be a presence without going through all the growing pains of a small business.

Franchisees are interested in franchising because it gives them access to a tried and tested business formula; it creates the security of buying into an existing brand name and to have accessibility to marketing exposure that they would otherwise not have been able to afford. It also gives
entrepreneurs the opportunity to work for themselves and to experience the freedom of owning and operating an own business.

A franchising model can be successfully combined with company owned outlets. The differences in approach between company owned arrangements and franchised arrangements can be combined in a so called "plural" form, and a business can benefit from the best characteristics of both models that is stronger than only a franchised operation or company owned operation.

The relationship between the franchisor and the franchisee was described as an entrepreneurial alliance functioning as a team. Each item in the franchise offering depends on both the franchisor and the franchisee operating as an allied force. A good franchise offering consists of franchisors offering prospective franchisees the training and support before they start the operation and thereafter on a continuous basis. The other main ingredients in a franchise offering are a solid marketing strategy, a well defined and executable service delivery system and ongoing support to franchisees.

The main aim of the franchisee/franchisor team should be the protection and building of their most valuable asset: the brand of the business. Franchisees should view franchise offerings that neglects to spell out how training and support be conducted very carefully and they should also be cautious of franchise offerings that do not have a clearly defined
marketing and advertising program and that do not adequately support franchisees or lack in a well defined training program.

The service delivery system has been discussed and it was shown how the customer is at the core of the franchise relationship model and the service delivery system has to be perfected to best serve the customers' needs and to exploit the opportunity completely. In the execution of duties it is important that both parties communicate with one another, knows what it is expected from one another and work together to make the venture work. It is a symbiotic relationship in which both parties have to assist one another and take the needs of one another into consideration.

Monitoring franchisees is a necessary element of a good relationship between the franchisee and franchisor, despite the high costs thereof. Generally, franchisees do not want to feel managed and rightly so, because they are businessmen in their own right. The importance of monitoring is that it benefits both the franchisee and franchisor if standards are maintained across the board of the franchise operation, the protection of the brand, and to ensure that levels of service and uniformity are adhered to by all the franchisees. Monitoring does not only benefit the franchisor, but benefits the franchisee as well.

In carrying out the monitoring function, the franchise agreement is an important document in the franchisee / franchisor relationship and should be carefully drafted, preferably by an attorney specialising in franchise
law. Although the franchise agreement is a complex document dealing with a variety of legal issues, it should be drafted clearly and the points made should be crisp and no confusion should be invited by writing a complex document whereof the interpretation is almost impossible. The franchise agreement is important but a holistic approach should be taken, taking the whole relationship into account and not focussing on one or two minor breaches of the agreement. The franchisor should use the franchise agreement as a last resort to bring franchisees breaching the relationship, in line. The spirit of the franchise agreement should reflect the fundamentals of the relationship, namely an entrepreneurial alliance and it should be an extension of the alliance, rather than a whip to crack at the slightest contravention.

It is also important that when interpreting an agreement, the "bigger picture" is borne in mind. A common sense approach is to ask oneself whether the agreement is a fair reflection of what the parties intend to document.

Lastly, the importance of the transactional analysis was discussed. The transactional analysis holds many benefits in for the franchisee as well as the franchisor. The benefits achieved by defining the underlying tasks contained in the service delivery system and appointing different tasks to the franchisor or franchisee are aimed at the improvement of the SDS and the preservation and the expansion of the brand. In a true entrepreneurial alliance this should be the aim of both sides. If everyone
knows what it is expected from him, confusion is avoided and wealth is created in the franchise operation. As an example the real estate aspects were discussed and it was shown how the transactional analysis would look for the real estate aspects of a generic franchise. Careful attention has to be given to the location of premises and aspects such as traffic volume, traffic flow, visibility and the density of the primary target audience. Careful attention has to be given to the location of premises and aspects such as traffic volume, traffic flow, visibility and the density of the primary target audience.
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