

Buying An Existing Franchise – A Two Step Process



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When you are buying an existing franchise business it is a two step process. A person must evaluate both the franchise investment opportunity (the franchisor/franchisee relationship) and the existing business opportunity (the seller/buyer transaction). This involves two very different steps that need to be taken.

STEP ONE Evaluate The Franchise Opportunity

In the same manner that you would evaluate any franchise investment opportunity, you need to validate this franchise opportunity. You should speak with existing franchisees of the system (the full list of the franchisees and contact info is an exhibit to the FDD and found in the Table of Contents of the FDD) and learn about

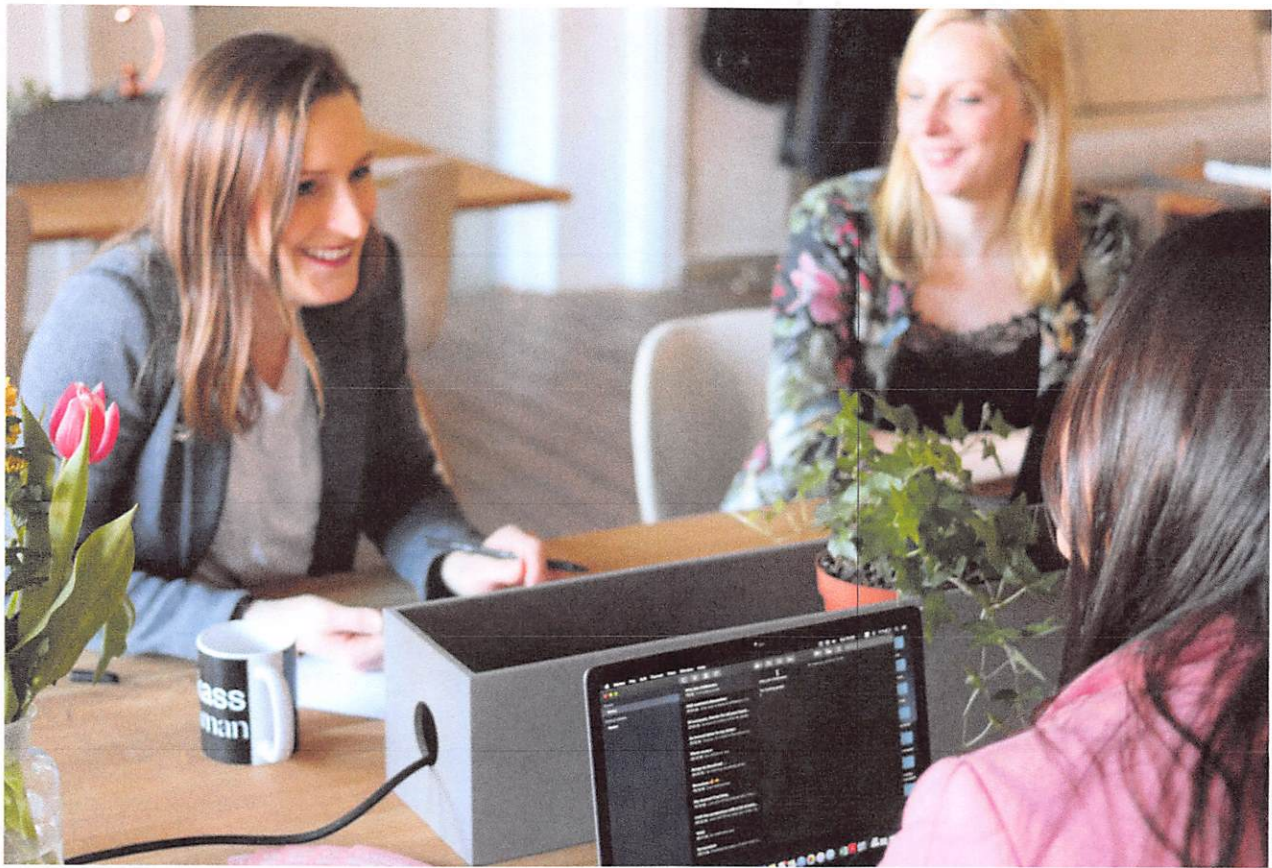
their experiences with the franchisor. You do not need the franchisor's consent to call the franchisees. In another blog post I have listed my top 10 favorite questions to ask existing franchisees (see Top Ten Questions to Ask Existing Franchisees). Talk to as many franchisees as you have time to call as they are the people running the business and working with the franchisor and will be most knowledgeable about the system. Next, read the 23 Items of disclosure that are in the front section of the FDD. They are required by federal law to be written in Plain English and represent important information that you should know before investing in a franchise. I also strongly recommend that you evaluate (or have

an accountant evaluate) the financial statements of the franchisor to ensure that the franchisor is financially strong enough to support the system in place and the growth that is anticipated. The financials will be an exhibit to the FDD (listed in the Table of Contents) and the number of locations and growth can be found in Item 20, tables 1 and 5. Once you have done that independent evaluation, the experienced franchise attorneys at Lanard and Associates can review the franchise agreement and any other documents you will be required to execute with the franchisor.

STEP TWO Evaluate The Business That Is Being Sold

If you are buying an existing franchise business, you need to ensure that the business itself makes sense financially, that the assets are free of claims by creditors and that the party signing on behalf of the seller has the authority to bind the seller, among other things. This means evaluating (or having your accountant evaluate) at least 3 years of tax returns for the business and all other financial information about the business. You should have an experienced attorney review the lease for the business (assuming





it is a brick and mortar business) and determine if the lease has sufficient years remaining to be an asset of the business. If there is only a short term remaining on the lease, it is possible that you may have to find another location or renegotiate the lease terms, which may be financially, and in other ways, less favorable than the current lease. You should also review all outstanding contracts of the business, and evaluate the condition of all the hard assets. Any Purchase Agreement that you enter into should protect you with sufficient warranties from the seller that you can be sure that you are obtaining clear title to the assets and that all the assets are in good working order. You should also obtain warranties and representations that the individual signing on behalf of the seller has the authority

to represent the seller and sign the documents. There are many other issues and concerns when buying an existing business that need to be addressed. For example, in some states you will need to get tax clearance or bulk sales clearance from the state in which the business is located in order to ensure that you do not inherit any tax liabilities. Retaining experienced counsel to assist you with this important process is critical to ensure you do not make any mistakes that will be costly in the future.

CONCLUSION

As you can discern from the discussion above, buying an existing franchise business (a resale) is a two part process. Both parts – evaluating the franchisor/franchisee relationship and documents, and evaluating and negotiating

the sale documents and all accompanying documents and assets (along with ensuring the assets are transferred properly and clear of liens) is critical to the success of a prospective franchisee buying a resale of a franchise business. Neither aspect is more important than the other; they should be reviewed carefully by an attorney who is both familiar with franchise law and handling acquisitions. The attorneys at Lanard and Associates have the expertise to help you with this important acquisition.

ABOUT THE AUTHOR

Nancy is a franchisee attorney who represents individuals investing in a franchise, sets up the entity and reviews and negotiates the lease for their business, along with the legal documents for resales of franchises. Contact Nancy at 215-392-0030 or nlanard@lanardassociates.com lanardandassociates.com