



## Franchising Glossary

**Acknowledgement of Receipt:** The last page of the FDD (Franchise Disclosure Document), which is signed by recipient to show receipt by a certain date.

**Advertising/Marketing Fee:** An ongoing fee paid by franchisees, usually a percentage of gross revenues, enabling franchisors to develop and purchase national advertising. This fee is not a component of every franchise; if it is required it is typically paid in addition to the royalty fee.

**Agreement:** The contract signed with the franchisor, this document governs the relationship between the franchisor and franchisee. Also called the Franchise Agreement.

**Arbitration:** A very common mediating process used to resolve disputes between franchisors and franchisees. When using arbitration, a neutral third party hears both sides to the dispute and makes a binding decision.

**Area Developer/Master Franchisee:** The right granted to a franchisee by franchisor to open several franchise locations in a specific area. This opportunity may include a requirement to develop a certain number of locations within a specified timeframe, and/or may also include the right to sell franchises within the specified area.

**Broker:** An intermediary who works with franchisee candidates and franchisors to facilitate a franchise purchase. Brokers can represent either sellers or buyers.

**Business Format Franchise:** A type of franchise where the franchisor grants the franchisee the use of the franchisor's trademark and product or service and provides all business procedures, which can include marketing, sales, inventory and accounting.

**Business Plan:** A plan developed by the franchisee that provides the objectives of a business and the steps necessary to achieve those objectives.

**Capital Required:** The amount of liquid assets a potential franchisee is required to have to provide for the start up and initial operation costs of the business.

**Company-owned Outlet:** A business which is operationally similar to a franchise entity, but owned directly by the corporation.

**Conversion Franchise:** A franchisor who allows existing businesses to convert to the franchisors brand for the purpose of being part of the franchised system.

**Designated Supplier:** Approved supplier of products and services that meet the requirements of a particular franchisor.

**Default:** A failure to perform the requirements of the franchise contract.

**Distributorship:** A right granted to a person or business to sell the products or services of another business or wholesaler. Although most distributorships are not considered to be franchises, some arrangements may qualify and will require pre-purchase disclosure.

**Earnings Claims:** Claims made by the franchisor regarding the past performance of franchisees or to the potential financial performance of a franchisee. If given, claims must be disclosed in item 19 of the FDD.

**Entrepreneur:** A person with the desire to create his own career opportunity and who is willing to assume the responsibility, risk and rewards of starting and operating a business.

**Exclusive Territory:** A designated area or geographic boundary granted to the franchisee by the terms of a franchise agreement. The franchisor agrees to not to open another franchised or company-owned business of a similar nature within the franchisee's protected territory. Also known as Protected Territory.

**Federal Trade Commission (FTC):** The agency of the U.S. government that regulates franchising in the United States.

**FPR:** Financial Performance Representations, See Earnings Claims

**Franchise:** A privilege or right officially granted to offer specific products or services under explicit guidelines at a certain location for a declared period of time.

**Franchise Agreement:** A written contract that sets forth the mutual obligations of both the franchisor and franchisee.

**Franchise Disclosure Document:** Also known as the FDD, this background and contractual information is a requirement by the FTC and given to potential franchisees by franchisors. It contains information such as terms, royalty payments, existing franchisees in the system, any litigation and other pertinent data. Prior to a change in 2008, this was called the Uniform Franchise Offering Circular.

**Franchisee:** A person or entity who holds a contract to conduct one or more businesses using the name, trademark and operating system of a franchise company.

**Franchise Fee:** The initial fee paid to a franchisor, usually due at the signing of the contract, for the right to use the franchisor's name, trademark and business system.

**Franchising:** A long-term cooperative relationship between two individual companies - a franchisor and one or more franchisees - based on a legal agreement in which the franchisor provides a licensed privilege to the franchisee to do business.

**Franchisor:** A company that grants to an individual or entity the right to use its name, trademark, and system of business operations for distribution of a product or service, in return for a fee and other considerations.

**FTC Rule 436:** The law passed in 1979 that regulates the franchise industry. It set forth disclosure requirements and prohibited franchisors from making earnings claims.

**Gross Sales:** Revenue generated before any expenses are deducted.

**International Franchise Association (IFA):** Founded in 1960 as a membership organization of franchisors, franchisees and suppliers with the purpose of providing help and guidance to the entire industry.

**Initial Investment:** An estimate of the initial cash investment required to buy and open a franchise business. This estimate includes the franchise fee and other initial start-up costs, but not necessarily the total cost of operating the business.

**Liquid Capital:** Assets held in cash or in something that can be readily turned into cash.

**Master Region/Master Franchisee:** A large territory acquired by a franchisee with the intent to subdivide and resell individual franchise locations.

**Multi Unit Franchise:** The franchisee acquires the rights to develop more than one unit. Also known as Area Developer/Master Franchisee.

**Net Worth:** Total assets minus total liabilities.

**Non-Compete Clause:** Restrictions on competing with the franchised company upon termination of a franchise agreement by either the franchisee or franchisor.

**Offering Circular:** see Franchise Disclosure Document

**Operations Manual:** Comprehensive document(s) containing all of the information necessary for the franchisee to be able to operate the business.

**Personal Guaranty:** A non-standard requirement to secure a business loan where the lender asks a corporation's owner(s) to personally guarantee the debt should the corporation default.

**Product Format Franchise:** A type of franchise where the franchisor grants the franchisee the ability to sell a particular product where that product does not constitute all that the franchisee sells. Similar to distribution networks yet the franchisor is able to control the way the dealer company operates by restricting the sale of competitive products or the type of marketing that it can do.

**Pro Forma:** A financial picture of the franchisor including a balance sheet, profit and loss or cash flow statement that estimates income and expense sources, assets, liabilities, and net worth. Pro forma statements issued by the franchisor to the franchisee should be based on actual operating results of the franchisor's units or franchise establishments.

**Protected Territory:** A designated area or geographic boundary granted to the franchisee by the terms of a franchise agreement. The franchisor agrees to not to open another franchised or company-owned business of a similar nature within the franchisee's protected territory. Also known as Exclusive Territory.

**Qualification Questionnaire:** A form to be completed by the prospective franchisee which allows the franchisor to assess whether or not the prospect has the motivation, skills and financial resources necessary to become a successful franchisee.

**Registration:** A requirement in several states that franchisors supply specific information for approval by state regulatory authorities before franchises may be offered in that state.

**Renewal:** The signing of a new franchise agreement upon the expiration of the old one. Many franchisors issue 5 or 10 year agreements which have renewal rights if all conditions are met. A fee is normally associated with renewing a franchise agreement.

**Royalty:** An ongoing payment made by franchisee to franchisor, usually a percentage of gross sales, made throughout the term of the franchise agreement.

**Single Unit:** A franchisee owns and operates one unit of a franchise.

**Start Up Costs:** The amount of money the franchisor will require the franchisee to have available to invest in the franchise in order to get it up and running. Often referred to as Initial Investment.

**Total Investment:** An estimate of the amount of money needed by a franchisee to start a business, including the initial fee, the working capital, and the cost to set up the business which may include site build-out, equipment, inventory, marketing and advertising, and most (but not necessarily all) items considered necessary to create a fully operational business.

**Trademark:** A symbol, name, or other distinctive characteristic which identifies a product that has been officially registered and is legally restricted to the use of the manufacturer or owner.

**Turnkey:** A franchise opportunity where most all aspects of a business prior to opening are provided to the franchisee by the franchisor. Also referred to as "Business in a Box," a turnkey business means the franchise buyer shouldn't need to do much more than "turn the key" in the door to start the business.

**UFOC:** Uniform Franchise Offering Circular, see Franchise Disclosure Document