



Franchises in Alberta

This publication is intended to provide general information only and is not a substitute for legal advice.

August 2007

HIGHLIGHTS

1 WHAT IS A FRANCHISE?

1 WHAT IS THE LAW IN ALBERTA?

4 BEFORE YOU BUY A FRANCHISE

7 FRANCHISE FRAUD

8 FOR MORE INFORMATION

**Government
of Alberta** ■

WHAT IS A FRANCHISE?

A franchise is a business arrangement. A franchisee (buyer of a franchise) buys the right to market particular products and services from a franchisor (seller of a franchise). The franchisee buys those rights for a specific period of time in a particular location.

What the buyer and seller of the franchise are entitled to receive depends on their arrangement. In some cases the franchisee buys an entire system: buildings, equipment, supplies, bookkeeping, uniforms, training, etc. This ready-made set-up is also known as a turnkey operation. Fast-food chains are good examples of a turnkey operation.

This tipsheet will provide you with general information about franchises, regulations regarding the sale of franchises in Alberta and franchise fraud warning signs.

WHAT IS THE LAW IN ALBERTA?

The *Franchises Act* and *Franchises Regulation* outline the requirements for disclosure of information that will assist prospective franchisees in making informed investment decisions as well to provide civil remedies to deal with breaches of the legislation.

Disclosure Document

Franchisors must give prospective franchisees a copy of the franchisor's disclosure statement. The disclosure document must comply with the requirements of the legislation and contain copies of all franchise agreements and financial statements.

Every prospective franchisee must receive a copy of the franchisor's disclosure document at least 14 days before any agreement relating to the franchise is signed, or the payment of any consideration relating to the franchise, whichever is earlier.

If this does not happen the franchisee may cancel all the franchise agreements. The franchisee must give notice of cancellation within

60 days after receiving the disclosure document or within two years after the franchise has been granted, whichever occurs first.

Franchisors are permitted to use disclosure documents acceptable under franchise legislation in jurisdictions outside Alberta. However, if the documents do not include all the information required under Alberta legislation, this must be provided as an addendum to the documents.

The disclosure document must include specific information about the franchisor such as:

- The name, address, and the name under which the franchisor does or intends to do business
- The principle business address of the franchisor and, if the franchisor has an attorney for service in Alberta, the name and address of that person
- The business form of the franchisor
- The length of time the franchisor has conducted a business of the type to be operated by the franchisee
- The length of time the franchisor has offered franchises for the same type of business as that to be operated by the franchisee
- Whether the franchisor has offered franchises in other lines of business including
 - a description of each line of business
 - the number of franchises sold in the previous five years in each other line of business, and
 - the length of time the franchisor has offered franchises in other lines of business
- The names of the directors, general partners and officers of the franchisor who will have day-to-day management responsibilities relating to the franchise (each person's principal occupation and employers during the five years preceding the disclosure statement must be included)
- Details on convictions and pending charges (previous 10 years), bankruptcy (previous six years), civil litigation and liabilities, administrative proceedings and existing orders against the franchisor, its associates, directors, partners and officers who have management responsibilities relating to the franchise.

In addition the document must contain all material facts relating to the franchise including information on fees to be paid, investment requirements, financing arrangements, working capital needed to sustain the operation, earnings claims, restrictions relating to purchase or sale of the products and services by the franchisee, rebates or other benefits to the franchisor, obligations of the franchisee, a list of existing franchisees, outlets, the territory granted the franchisee, and what is required to terminate, renew or transfer the franchise.

The disclosure document must also include a certificate (set out in Schedule 2 of the regulation) that states the disclosure document contains no untrue information of material fact, or that the required information has not been omitted or misrepresented. If a franchisee suffers a loss because of a misrepresentation, the franchisee has a right of action for damages against the franchisor and every person who signed the disclosure statement.

Financial statements must be prepared in accordance with generally accepted accounting principles. The Franchises Act Exemption Regulation exempts certain franchisors from the requirement to include financial statements in their disclosure documents.

If you are thinking about buying a franchise, have all documents reviewed by a lawyer who is up to date on the legal aspects of franchising.

If a dispute arises with a franchisor, speak directly with the company to try and resolve the problem. If the matter is not resolved you may need to seek redress through the courts. You may also have the right to cancel the franchise agreement under civil or contract law.

You can order a copy of the *Franchises Act* and *Franchises Regulation* from the Queen's Printer Bookstore.

10611 - 98 Avenue
Edmonton, Alberta T5K 2P7
Phone: (780) 427-4952
toll-free in Alberta: dial
310-0000 and follow the instructions.

BEFORE YOU BUY A FRANCHISE

Check each franchise opportunity and ask questions about every part of the business.

The Business Link is a not-forprofit organization that provides information to help new and developing small to medium businesses (contact information at the end of the tipsheet).

The product or service

Some questions to consider before making a decision include:

- What is the product or service?
- Will anyone buy this product?
- Is it priced competitively with others in its class?
- What assurance do you have that the suppliers will continue to provide the product?
- Are there any government standards for the product or service, and if so, does it meet those standards?

Find out from your lawyer whether there are any restrictions on the product's or service's use or licensing.

A franchise is a business arrangement.

A franchisee buys the right to market particular products and services from a franchisor. The franchisee buys those rights for a specific period of time in a particular location.

If you are thinking about buying a franchise, have all documents reviewed by a lawyer who is up to date on the legal aspects of franchising.

Trademark

Does the franchisor own the trademark? Does the franchise system have exclusive distribution rights to the trademarked product, or can the product be sold outside the franchise system, either now or in the future?

The company (franchisor)

Before making a decision you should know

- who the directors and managers in the franchisor's company are, their experience in this type of business, and their length of time with the company
- the current number of franchises and whether any have closed or changed hands; as well as when it happened and why
- any limitations that will be imposed on your business operation, including what and where you must buy and sell (e.g. franchises often impose rigid rules about sales, marketing, and quality control)
- if the company has done a feasibility study for your franchise (e.g. traffic counts at various places you might locate the franchise, average income and number of potential customers in the area)

- the franchisor's company's financial history and whether it indicates steady growth and has a growth plan.

Have your accountant review all the financial statements to alert you to any problems.

You should also know what economic and market conditions the franchisor is basing profit margins and projected earnings on.

Get all franchisors' promises in writing and ask for references including: the names and addresses of existing franchisees; financial institutions; and suppliers.

Also talk to existing franchisees about their experiences with the franchisor and confirm that the franchisor met the terms of the contract.

Check the business reputation of the company by asking government departments, bankers, the Better Business Bureau, trade associations (e.g. the Canadian Franchise Association, and the International Franchise Association) for information about the franchisor.

Expect the franchisor to investigate you thoroughly too. Take care when dealing with a franchisor that's ready to sign you up without checking you out. Your success may be of less interest than your sign-up fee.

Check each franchise opportunity and ask questions about every part of the business. The Business Link provides information to help new and developing small to medium businesses.

Money Matters

Most franchises require an investment of at least \$100,000 but there may be additional costs you will have to pay. Confirm who is responsible for:

- advertising, both local costs and payments to national funds
- continuing royalties (a percentage of sales or profits, or a fixed charge per unit)
- equipment
- insurance
- leasehold improvements
- legal and financial advice
- licences
- product or service supply costs
- real estate
- training.

Take care when dealing with a franchisor that's ready to sign you up with-out checking you out. Your success may be of less interest than your sign-up fee.

Have an accountant review your business plan to ensure you have included everything you need to make an informed decision including projected costs and earnings.

Territory and location

Determine who decides the franchise's location within your area and decide whether the location offered suits your needs. Other questions to ask include:

- Must you lease or buy the property? If leased, is the term of the lease as long as that of the franchise agreement? If not, can you renew or extend it?
- Do the premises have to meet certain standards set by the franchisor, such as age of building, street frontage, or minimum size?
- Do you have exclusive rights to the territory and for what period of time?
- What guarantees do you have that another franchise won't be opened in your area? Could you open another franchise outlet in the area?

Premises

You should also ask how tightly the franchisor controls the appearance and layout of the premises. Some questions to ask:

- Will you have to buy a particular brand of furnishings and equipment? If so, can you choose the distributor who will give you the best price or do you have to buy from a specific source?
- If you have to buy or lease from the franchisor, who is responsible for repairs?
- Are there any warranties?

Operations manual

Before you enter into any franchise contract, ask if there is an operation manual. Read this manual carefully. It will tell you what standards of operation the franchisor expects of the operators. You may have to sign an agreement to keep the manual contents confidential.

Training

You should get training in the franchisor's products or services, day-to-day business operations and the operating standards you will be required to keep. Find out what training the franchisor will give you. Some questions to ask:

- Will you learn by hands-on experience at another franchise outlet? If so, how long will you be expected to work?
- Will you be paid while you are training?
- Are you the only one to be trained or will other employees be given training too?
- What type of ongoing training or support is available if problems arise?

Advertising and promotions

Some franchisors have advertising and promotional funds and franchisees often have to contribute to these funds based on a percentage of their sales. Find out whether franchisees have a say in spending this money. Some questions to ask:

- Will the full amount collected be spent on advertising?
- How much will be spent in your trading area?
- Will advertising be national, regional, or local?

- Do you need the franchisor's consent to advertise independently?
- Must you take part in other advertising or promotional campaigns?

Franchise Agreement

The franchise agreement sets out the terms and conditions of your franchise arrangement. The contract should:

- specify your rights and responsibilities and those of the franchisor
- cover every verbal or written promise agreed to
- specify the conditions under which the agreement will be renewed and the cost to renew
- specify conditions under which an agreement can be cancelled by either side and the amount of notice needed
- specify whether the franchisee can sell or transfer the franchise or, in the event of death or disability, what could happen.

Have your lawyer review the contract. Once you sign the contract you must honour it.

FRANCHISE FRAUD

Be aware of signs that could indicate a possible franchise fraud.

High pressure sales tactics

Shady promoters demand quick decisions. They don't allow investors time to investigate profit claims or consult with lawyers or accountants.

Promises of sky-high profits

Honest promoters don't guarantee clients a return on their investments, much less astronomical profits of 100 percent or more. Legitimate operators qualify their success stories by stating the percentage of participants who have earned big money.

Unjustified start-up fees

Examine the inventory, training course, and sales kits promoters insist you buy and whether promoters are asking for more than fair market value for these start-up items.

Evasive answers and failure to reveal information

If the promoters don't answer your questions directly or refuse to provide details, don't go any further. Remember that your chance to succeed depends on the sellers' full cooperation and assistance.

If you suspect that an offer is a swindle, share your suspicions with the authorities, even if you decide not to invest. Contact the police and the Better Business Bureau if you suspect any fraudulent business activity. Your warning can help protect other investors.

If you suspect that an offer is a swindle, share your suspicions with the authorities, even if you decide not to invest. Contact the police and the Better Business Bureau if you suspect any fraudulent business activity. Your warning can help protect other investors.

FOR MORE INFORMATION

Consumer Contact Centre

Edmonton: (780) 427-4088

Toll-free in Alberta: 1-877-427-4088

www.servicealberta.ca

Canadian Franchise Association

- a resource for franchisors and franchisees
- sells publications and a Membership Directory

Toll-free: 1-800-665-4232

www.cfa.ca

International Franchise Association (IFA)

Phone: (202) 628-8000

www.franchise.org

The Business Link

A not-for-profit organization supported by the Government of Canada and the Government of Alberta

Edmonton: (780) 422-7722

Toll-free: 1-800-272-9675

www.cbsc.org/alberta

Better Business Bureau of Southern Alberta

Calgary: (403) 531-8780

Toll free in Southern Alberta 1-800-661-4464

www.betterbusinessbureau.ca

Better Business Bureau of Central and Northern Alberta

Edmonton: (780) 482-2341

Toll free in Canada: 1-800-232-7298

www.edmontonbbb.org

A current version of this and other consumer tipsheets are available at the Service Alberta website www.servicealberta.ca. Most public libraries have Internet access if you don't have access at home.

If you need more copies of this tipsheet, you have permission to photocopy.