

# Buying a Franchise

## A Franchise Accountant's Perspective

The process of buying a franchise is not an easy one. In fact it is usually fraught with difficulty. It will usually take more time than you expect and it will often be confusing. The process is made much easier if you use professionals who are experienced in franchising. These professionals are likely to include your bank manager, a franchise consultant, a solicitor and an accountant.

I have advised many people to buy (and not to buy!) a franchise. Nearly every potential franchisee wants to know what role an accountant can play in helping with the purchase of the franchise. So this article describes the role of a franchise accountant in the process of purchasing a franchise.

I like to break down the process into three stages

1. The business identification stage
2. The business evaluation stage
3. The business purchase stage

Each of these stages in turn involves three sub stages

### 1. Business Identification Stage

You have decided that you want to buy a franchise, but don't know much more than that. How can a franchise accountant help?

#### 1a. Direction

At this stage an experienced franchise accountant can point you in the right direction. I can tell you where you might start looking – for example franchise directories, the internet or print media - and I can supply details of other franchise specialists you might need to talk to. So I can set you on the right path and give you some direction. What I am not able to do is answer the question "Which franchise should I buy?" That is not my role.

#### 1b. Education

Not surprisingly, most of the potential franchisees I see have little knowledge of the franchising industry or how it is regulated. Often my initial role is that of educator rather than accountant - explaining about franchising regulation, documents and operations. Do you know that all franchise agreements have a fixed term like a lease? What happens at the end of that term? What documents should be provided to you? What extra information must be provided and what information can you request?

McClean Delmo works with other franchise professionals to run regular seminars for potential franchisees. Other organisations do these seminars as well. Naturally, I find that the more informed you are about franchising and its operation, the better the decision you are likely to make.

## 1c. Finance

Unless you are going to pay cash for your franchise you are going to have to borrow money to buy it. You therefore need to know how much you can borrow and who will lend you the money.

How much you can borrow will depend on two main factors – (1) your assets and (2) whether or not the franchise is accredited with a bank or other financial institution. All major banks in Australia have franchise divisions and franchise specialists and the banks are the major source for franchise finance. But there are other financial institutions that provide franchise finance.

Once I know what your assets are and what franchise you are thinking of buying, I can give you a good indication of your borrowing capacity. It is wise to establish this at an early stage. I quite often talk to people who are thinking of buying a franchise but they are simply not aware that they will not be in a position to borrow the required amount. You can of course also discuss this with your bank or financial institution and it is certainly a good idea at this early stage to talk in principle with your financial institution about what you intend to do.

## 2. The Business Evaluation Stage

At this stage you have identified a possible franchise opportunity. How can a franchise accountant assist you now?

### 2a. Information required

Proper evaluation of your franchise opportunity will require proper evaluation of numerous documents. What these documents are will depend on your particular opportunity. They will include a franchise agreement and disclosure document. They might also include other documents such as prior year's financial statements, income tax returns, franchise audit report and leases.

These documents may need to be reviewed and evaluated. Unless you have particular expertise in this area, you will need assistance from a franchise accountant and solicitor to interpret and understand these documents and the key issues that arise from them. This is perhaps the most important step of all.

### 2b. Projections

The information that you have gathered will help you make qualitative (non financial) decisions about the franchise and its purchase. You also need to make the quantitative (financial) decision as to whether to purchase the business or not. So I will help you use the information gathered to prepare the profit and loss and cash flow projections. Profit and loss and cash are not the same for most businesses. When you sell an item you make a profit (hopefully). There is no cash in the bank until you have been paid for that item - which for some business is not for 30, 60 or 90 days – or perhaps never if the debt becomes bad. It is necessary therefore to prepare both profit and loss and cash flow projections. Banks are particularly interested in the cash flow projections because they get repaid by cash flow not profit.

These profit and loss projections should be prepared on a month by month basis for at least the first twelve months.

I will help you prepare the projections in such a way as to help you evaluate the franchise opportunity and also in a form suitable for a bank application. Occasionally I work with franchises that have the expertise to prepare their own projections. Even in those cases, most franchisees find it useful for me to play the devil's advocate in reviewing those projections.

### 2c. Decision time

Now it is decision time. Do you buy the business or not and if you do how much should you offer for it (because you should not necessarily pay the price that the seller is asking)? Everything you have done up until now has been leading to this point – do you buy or not? My role is to help in that decision but the final decision must always be yours.

### 3. The Business Purchase Stage

Well done! You have made the decision to purchase - but there is a fair bit to be done yet.

#### 3a. Business plan

You have decided that you want to purchase the franchise, but will the bank lend you the money? A formal application will need to be made to your bank and it will require the preparation of a business plan. My preference is for you to prepare your own business plan with assistance from me as necessary. I can provide an outline of the plan and its contents but it is better if the plan comes from you. The most important part of the plan is the profit and loss cash flow projections which have already been prepared as part of the business evaluation stage.

#### 3b. Business structure

You need to determine how you are going to run your business - as a sole trader, in partnership with somebody, or using an entity such as a trust or company. There is no universal structure that suits everybody – in my practice I have franchisees using each of these structures. What you aim to do in choosing a structure is (1) minimise risk, (2) minimise income tax and capital gains tax and (3) have flexibility. My role is to advise you on the most appropriate structure taking these factors and your particular circumstances into account.

#### 3c. Business regulation

Once the business structure has been chosen and set up, there are many registrations to be done – including applications for tax file number, goods and services tax registrations, Australian business number, pay as you go tax, workers compensation and superannuation guarantee. Your franchisor may help you with some of these items as part of your training but, if not, it is my role to ensure that all appropriate registrations are done.

And so, finally, you are up and ready to go. Congratulations! You have reached the end of the beginning.

Now it is time to create and maximise profits and wealth. And as your accountant, I should have a major role to play in that process. But that is the subject of another article.

**If you are thinking about buying a franchise or are interested in more information, please contact Jamie Bishop on 9018 4666 or [Jamie.bishop@mcleandelmo.com.au](mailto:Jamie.bishop@mcleandelmo.com.au).**