

SIGNIFICANCE OF FRANCHISE BUSINESS IN CONTEMPORARY ECONOMIC CONDITIONS

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ABSTRACT: Franchising is a way of business cooperation of legally and financially independent enterprises. Development strategy of business entities, which is referred to as franchising, had a huge success in the whole world. There were two similar enterprises that have sold hamburgers in the USA in the 1950's of the previous century: White Castle and McDonalds. The first enterprise was significantly better-known and it had 27 restaurants, while the other enterprise had only one restaurant. In the middle of 1980's, the situation is drastically changed. The number of McDonald's restaurants has grown to over 8000, and White Castle had 167 restaurants. The reason is simple. McDonald's started with franchising then, while White Castle has remained with the same number of restaurants. It is about a classical form of restaurants spreading, along with the spreading of own enterprise on one hand, and extremely effective business approach, which is referred to as franchising, on the other hand.

KEY WORDS: franchising, franchise business, forms of franchise compositions, franchise possibilities...

1. INTRODUCTION

Definition of franchising, which is set forth in the Code of Ethics of European Franchise Federation and accepted by European Union as well, is the following:

„Franchising is a composition of goods marketing and/or realization and/or technology, which is based on close permanent cooperation between legally and financially separated and independent enterprises, franchisors and individual franchisees (giver and recipient of franchise), in which case the franchisor gives its franchisees the right to operate in accordance with franchisor's concept“.

This right authorizes and obliges individual franchise recipient to use franchisor's trade name and trademark or the mark of service activity, business or technical method, composition of procedures and other rights in direct or indirect exchange. They come from industrial and intellectual property, which supports a constant providing of business or technical support, in implicit and time framework of the written franchise agreement, which was concluded by both parties with that purpose.

Business form of franchising is an operating mode, where the owner of the recognized business system, franchise giver, gives another entrepreneur the right to found a similar enterprise. In exchange for a payment and a promise to accurately follow the instructions and quality standards, the franchise recipient thus obtains a right to use franchisor's trademarks [1]. In addition, he thus obtains the support in marketing, equipment and raw materials.

That definition includes three main elements:

- Franchise giver,
- Franchise recipient and
- Franchise composition.

Franchising implies a close business relationship between two relatively independent entrepreneurs, it includes the giver and recipient of franchise package and franchise composition.

Franchising requires a particular ownership of associated enterprises – franchise, and thus it ensures a direct support to independent entrepreneurs, through the instruments of training in the elimination of problems and assistance in financing by the franchisor, which has extensive entrepreneurial experience. It also includes both help and work in business management, trading, accounting, personnel training...

Franchise is not any kind of goods, because it is not sold to any buyer. The heart of franchise compositions is growing quality of products and services of every enterprise, the franchise recipient [3]. Franchises are based on simple availability and speed of action; they are characterized by moderate price, by which confidence and reputation are created. All of that are the marks linked with protected and well-known name of franchise composition.

Franchise givers also take care of raw materials suppliers, who are the input components in the unit of their composition, so that the franchise givers are „benefactors“ in development sense as well.

2. FORMS OF FRANCHISE COMPOSITIONS

Classical classification of franchise compositions consists of four forms:

- Manufacturers and wholesalers (industrial franchise) – manufacturers provide raw material, i.e. semi-product for the franchise recipients in a particular field. They develop a final product from it and sell it to the retailers, i.e. distributors. Franchise of Coca-Cola, Pepsi-cola, Schweppes, was formed by syrup producer, so that he determined a procedure of making juices, their bottling and distribution in the particular field. In our country, that category might partially include manufacturers of candy and cakes, who sell it through other food shops, stores...
- Manufacturers and retailers – the emergence of modern franchise reaches the fields of developing and distributing the products such as motor vehicles, oil derivatives, water, etc. Car manufacturer forms a franchise network for sale (ordering, delivery, payment) of his cars. For example, we have gas stations, which are leased to individuals

(Jugopetrol) by the manufacturer of oil and oil derivatives, and they are very close to such an arrangement, and in a combination with appropriate trade houses (such as in OMW gas stations) they are very close to the business format of the franchise.

- Wholesalers and retailers – it is about a similar arrangement as in case of manufacturers and retailers, so that the franchise giver is wholesaler who is supplied by goods from more different manufacturers or other traders. Wholesaler forms franchise trade in such a way to determine the internal order and external layout of the store, export of goods and its order, service mode...
- Retailers – the majority of so-called franchises of „business format“ can be classified there, which implies the offer such as: copying, printing, towing service...

3. FRANCHISE POSSIBILITIES

Franchising is a repetition of successful operations, where within franchise trade chains and distribution of goods and services they take place within a strategic plan, which is based in such a way to significantly reduce the costs of the complete distribution and to increase the quality of work and products.

As a means for rapid and profitable growth of enterprise, the method of entrepreneurship is extremely attractive. Due to a relatively higher security of investment, franchising also represents a simple way for winning over other people's investments in unfavourable market conditions. Significance of franchising for the general economic and social development of countries in transition is primarily in the transfer of business, managerial and technical knowledge, in spreading the quality standards, good business habits and growth of production compositions, which are particularly included in franchising, as raw materials suppliers.

The principles proclaimed by European Franchise Federation are such that the franchisor, as the initiator of a particular franchise network, is proclaimed for its long term protector. In addition, they explicitly require that franchisor needs to test a particular business concept by him and test it in one testing unit before he sells his first franchise. Besides, he needs to be the owner or he must have the legal right to use the trade name of the network, trademark or other identification signs. He needs to determine the initial training of franchise recipient and he must determine a permanent business or technical assistance for the duration of franchise agreement.

4. FRANCHISING IN EUROPE

Today in Europe, especially Central and Western Europe, the fast food franchises, trade franchises, etc, are widely spread. In addition, the franchises for accounting, personnel, administrative, technical and other tasks started to develop rapidly, and thus for the market saturation with classical forms of franchise, there are also less-known forms introduced, such as: mobile franchises for helping the drivers, housework, water and food refreshments...

In Europe, apart from Great Britain and Spain, domestic franchise compositions prevail. Franchising has firstly began in the field of trade, fast food, car rental.

As for the international franchising in Europe, American compositions that come to Europe via Great Britain are leading. Differences between American and West European franchising come from specific cultural and economic characteristics, as well as from internal heterogeneity and

relatively smaller market content than it is the case with American. Classical American franchise content is more centralized and vertically linked, while for contrast, the European is different and it is more similar to the type of corporative enterprises, where the franchise recipients would directly be included into strategic decision-making in the enterprise. [4,5,6]

The competition in the field of development of distribution channels, which was also reflected in Europe in a larger specialization and emergence of always new ideas, and one of them, operates through franchising. In Europe, there is a small number of franchise compositions that operate, so that the American franchise compositions are dominant, which resulted in that modern forms of franchising were developed in Europe after the arrival of American franchises.

Today, there is a more recent business form of franchise enterprise, where it is about original, complex, high quality and proven knowledge. Precisely that form of franchising has led to its glory more than the first generation of franchise compositions.

5. ROLE OF THE FRANCHISE AGREEMENT

Agreement between the giver and recipient of the franchise is the agreement that regulates the entire relationship between both partners.

For that reason, it is necessary to precisely reflect various ownership rights of the giver provide the penetration and control and provide the recipient with the security in functioning, development and selling of a part of equipment.

Franchise agreement contains the following chapters:

- Definition and protection of ownership interests of franchisor,
- Use of trademark and other marks, allowed name next to the giver's brand,
- Location and territory of franchise,
- Duration of the contract,
- Determination of tasks that are agreed by franchise giver in the beginning and later on,
- Additional and permanent obligations of the recipient (purchase of raw materials, technology, equipment, paying the membership fees and part from the sale),
- Rights of franchise recipient,
- Operational control of what the giver performs over the recipient,
- Sale of the unit and giver's rights,
- Cessation of franchise from one side or the other,
- Arbitration,
- Cessation of franchise agreement and consequences.

Apart from these chapters, franchise agreement also includes the following elements:

- Name and address of the giver,
- Name and address of recipient,
- Location,
- Number of units,
- Membership fee (amount without taxes),
- Date of signing the agreement,
- The effective date of the agreement,
- Mark, labels,
- Allowed name next to the giver's brand,

- Type and description of activity,
- Duration of the agreement,
- Current, periodic amounts of payment as a share from sale, general, advertising...
- Signatories,
- Signatures.

In accordance with that, the certificate provider confirms that he was authorized by company's owner to enter into agreement, as well as to surrender its activity onto determined locations, within composition, which includes the sign of the trade name and other labels, logotypes and identification materials for publishing, advertising, style and significance of the equipment and physical planning...

Franchisee wants to obtain the right to use the allowed name by the franchisor, so that he could freely operate in his unit, which would include all the subjects that he solves, as well as the constant assistance of the franchisor in that job.

Franchise agreement cannot be a compensation for mutual confidence and common desire for success. First of all, it is important in the beginning with the building up of franchise composition and with concluding a business relationship. Because of that, in case of franchising, because of a large and long-term mutual dependence, the adjusted interests of both partners are of a crucial importance. [7]

In accordance with the provisions of franchise agreement, the franchisor is obliged that he will offer a permanent help to the franchisee, which is also the constituent part of the principle of European Code of Ethics, for the field of franchising. Without such a help, there is no franchising. Precisely for that reason, that help has become one of the main forms of activity, which the franchisor does not offer, but he sells it to the franchisee as an important own product.

The main forms of assistance that the franchisor sells to the compositions are the following:

- assistance in securing the permits,
- education program,
- assistance and advices of franchise manager,
- operational manual,
- ensuring bookkeeping and accounting knowledge and appropriate computer, program equipment,
- technical assistance,
- advertising,
- assistance with searching financial funds,
- choice of location,
- various forms of financing,
- space and arrangement of departments,
- assistance before and after opening the franchise,
- research and development,
- supply of consumable material,
- regular or occasional personal contacts,
- supply of fixed assets,
- visits of franchisors and problem-solving,
- obtaining business agreements,
- e-commerce,
- enabling or ensuring various forms of insurance.

Relatively inexperienced entrepreneurs, who access the franchise agreement, need to have certain knowledge about them, the franchising and about that what they need to know before they decide to run for or sign the franchise agreement.

Before he enters the franchise business, the franchisor needs to:

- understand the essence of franchising,
- be motivated for a particular form of entrepreneurship,
- be, as a person, mentally and physically ready for such a job,
- be able to tolerate the authority of a particular franchisor,
- own the innovation and to be adaptable,
- be aware of its own personal business maturity,
- be financially capable to carry out a particular job,
- be mentally strong so that he could cope up with the problems, risks and losses,
- that he has cleared up with himself whether the franchising will satisfy his aspirations,
- that he is willing and prepared for difficult and often overtime work and for giving up the social and personal requirements that are not related to work,
- that he has the support of the family, as well as the environment...

In order to enter the franchise business, the franchisee needs to be well-informed about franchising, as well as of the giver of the franchise that is interesting to him. In order to do that, he needs to gather as much information before he decides to sign the franchise agreement, and those are the following:

- what is the content and special value, excellence of franchise business in particular composition (description of product, work),
- market and stability of the market, as well as the competition,
- business plans, expansion of franchise network, growth,
- qualification of people in the head office,
- height and way of paying the membership fee, division of turnover, leasing arrangements, financing...,
- required investments in space, equipment, reserves and activity,
- selection and arrangement of location, territorial rights and constraints and exclusivity of location,
- obligation and terms of purchasing goods, services of franchisor, necessary for franchise functioning,
- how much time he already sells the franchise and in what kind of relations is the franchisor with other franchisees, whether there are legal problems, of what kind are they and where do they appear,
- what about the ownership of the space where the franchisee will operate,
- what kind of activities does the franchisee do, what part of business activity is franchising to him,
- how many own and franchise units has he,
- address of the other franchisees,
- which are the successes, failures of particular units,
- is there a brochure about franchise composition and what does it contain,
- value of the names and marks of the franchisor,
- criminal and civil proceedings in which the composition or its executive managers were or were not involved,
- financial profile and operating of the franchisor, profitability, indebtedness, losses, financial projections,
- methods, forms and types of control that are performed by franchisor,
- method and payment of training the franchisee and his employees in various fields,
- who pays and how much he pays for drafting marketing research, advertising...,

- assistance in exceptional cases with franchisee (illness, death...).

Responses to all those questions can be acceptable for franchisee, but the franchisor is the one who has the final saying. The success of entire composition depends on the proper choice of franchisee. It also occurs that a less reputable franchisor concludes a contract with someone who was rejected by a more reputable and successful franchisor. Different compositions look for different people. The success of its entire composition is based on that about which a reputable and successful franchisor examines the candidates for purchasing a franchise, which he does not want to sell to anyone.

6. DEVELOPMENT VIEW OF FRANCHISING IN CENTRAL EUROPE

There are three factors in development of franchising, and those are the following:

- franchise association, which emerges with its informative, educational and advisory role,
- public interest that is partially enabled by the state with its encouraging, constraining role, primarily of its regulations and political and economic, as well as developmental function,
- brokerage and consulting when introducing foreign franchise compositions.

Each of the above mentioned factors contributes to the correctness of ethical franchise approach, which helps the healthy growth of national economy.

Franchising represents a long-term business cooperation, which comes from a durable market advantage, exceptional selling concept of the franchisor. That concept is related with gained reputation of market name, i.e. trademarks. The precondition for secure and stable incomes to the franchisee is the consistent use of statements and decisions from franchise agreement, as well as multiple support of the franchisor to the franchisee. One of those basic categories in Central Europe is the national code of franchise ethics. [2]

Franchise Association has a task to help the franchisees to the best extent, starting from the definition of franchising, what is its business philosophy, to assist the mutual relations between the franchisors and other associations and observation of the frequent non-understanding or abuse of franchising concept. Respectable and business ethics-based franchise compositions within associations determine his proper place within national and international franchise associations. In this case, the decisions that refer to the appropriate review of franchise prior to its commercial use, as well as determination of appropriate assistance of franchisors to franchisees, are very significant. The existence of association disables greater abuses of franchise concepts.

Within that framework, it is especially important to respect the rules of national code of franchise ethics. It should correspond to the European code and the relationship between both franchise partners should be regulated. Such a code represents an act of autonomous regulation of franchising, which is, in the opinion of European Franchise Federation, by far better than state regulations, especially those that would regulate the fields of franchising. [8]

Membership in franchise association represents a sign of introducing high business ethics in demanding segments of various parts of national economy, which sometimes appears to

be subordinately, but it provides the breakthrough of such ethics into other economic fields as well. Membership in association implies that franchise enterprise has understood the significance of constant growth and fulfilment of franchising, and thus harmonized its operating with the rules of society. Franchise association is interested in respecting and preserving the reputation of franchising as a special form of entrepreneurial activity.

National strategic developmental objectives of the countries in Western Europe imply the training of economy for successful competing in international markets, which are, by elimination of market obstacles, no longer the markets in other countries, but increasingly better domestic markets. In national programs, the national priorities should be clearly expressed, both when conditioning the arrival of foreign franchise compositions, and the supports to the development of domestic brains in encouraging and assistance in growth and development of competition of domestic franchise compositions.

In recent past, in each of transition countries there appeared a large number of successful entrepreneurs, as well as in our country. Great majority of them has a poor knowledge of franchising and problems of overcoming and financing the growth. For some of those enterprises, the best choice would be to accept the role of franchisor and for the others to join the franchise compositions as the franchisees. Apart from that, the enterprises, which have developed franchising as a supporting activity, would in that way contribute to the development of domestic entrepreneurial spirit, talent and the best organic growth of national economy.

According to their organic emergence, franchise compositions in domestic economic field would not even exist and thus the arrival of foreign franchise compositions would be an impulse for franchising development within national economy. When we speak about introducing foreign franchise compositions, it is necessary to indicate one of the dangers, and that is introduction of small and yet unverified foreign franchise compositions. It is usual that franchise composition firstly gets tested and affirmed in local environment, and then it spreads into a wider region within domestic economy. The internationalization is chosen not before the success in local and regional field. In addition, I wish to warn that overgrowth of franchise composition is a sign of a great appetite of franchisor for collecting membership fee, and at the same time it is unable to offer an appropriate support to the franchisees.

In Great Britain the knowledge about such problems is a public secret, and it relies on data that the majority of small franchise compositions are not any safer from entrepreneurial risk and failure than other independent entrepreneurs are. Those franchisors who do not reach a critical mass of franchisees in the first five years (around the number 15), they do not have great possibilities for long-term survival. With the deterioration of franchisors, the franchisees also fail.

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