

Five Franchising Faux Pas

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FIVE MOST COMMON FRANCHISING MISTAKES

1. **Making Excessive Comments.** All franchise agreements are franchisor-biased! Raise only the most critical issues.
2. **Relying on Anything Outside of the Franchise Agreement.** The “entire agreement” clause in the franchise agreement negates everything outside of the franchise agreement.
3. **Ignoring the Effect of a Short-term Franchise.** Do you want to pay the fees and incur the expense to develop a franchise that can be taken away in five years? If the franchisor does not renew the franchise, do you want to be bound by a noncompetition agreement?
4. **Personally Guaranteeing all Franchise Obligations.** Creates “backdoor liability” to circumvent the liability shield of your limited liability company or corporation.
5. **Failing to coordinate multiple obligations.** Avoid becoming obligated for leases, etc. that are not contingent on effectiveness of the franchise agreement.

GENERAL START-UP BUSINESS MISTAKES

1. **Starting Business without a Limited Liability Entity**
2. **Failing to Document Owners’ Rights & Responsibilities**
 - Business divorce & impasse resolution
 - Transfer restrictions and rights of first refusal
 - Capital contribution obligations & vesting
 - Withdrawing owner’s equity & purchase rights
 - Deceased owner’s equity
 - Drag-along & co-sale rights
3. **Taxes, Taxes and More Taxes – hire an accountant!**
4. **Securities Laws Violations** - noncompliance gives each investor a “put” personally guaranteed by you
5. **Litigation**

GENERAL RECOMMENDATIONS

1. “The E-Myth Revisited” by Michael Gerber.
2. Learn basic business law principles through classes or books. There will be exceptions to the general principles but knowing the basics can help you determine when to seek legal help.
3. Review available resources including:
 - <http://www.sos.state.tx.us/corp/related.shtml> - discusses licensing and other new business issues
 - www.irs.gov – IRS web site for tax information & audit guides
 - <http://www.inc.com/articles/2002/10/24780.html> – Striking Out on Your Own (Inc!)
 - <http://www.inc.com/articles/2000/01/14880.html> - 10 Common Mistakes of Prospective Franchisees
 - Trade associations
4. Hire professionals (Attorney and CPA) and find a good banker.
5. Read your legal documents and ask “what if” questions – it’s the only way to make sure that you and your attorney are correctly reflecting your desires.