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Franchisepreneurship, a 10 Year Case Study

Making it Work. The Course

The first hurdle in developing the franchise program was creating an appropriate course to train students to be small business owners. It required working with mainly traditional business faculty to develop the right class to ensure future success of the student and the program. This was actually more difficult than imagined as only a few of the faculty members had applied experience in small business ownership and limited knowledge of entrepreneurship education in general. Eventually a course was designed and approved. A major requirement of the course is that it would need to be continuously modified as needs are identified by the instructors and past participants. The basic goals and steps in the course are:

1. Provide knowledge of the resources necessary to build an effective business plan for a specific franchise “study” store.
2. Using discipline-based faculty as guest lecturers to cover the “small business” needs of that discipline focused largely on:
 - a. Digital and social media marketing.
 - b. Managing a predominantly part-time workforce.
 - c. Understanding QuickBooks.
 - d. Understanding the financing necessary to succeed.
 - e. How to read and understand a mall or shopping center lease.
 - f. Understanding a franchise agreement.
3. Exposure to successful entrepreneurs (including the philanthropist who created the program).

4. Beginning in year 3, mentorship and support of previous successful graduates of the program.
5. In-store training in an actual franchise.
6. How to write a successful business plan.
7. Preliminary Competition.
8. Completing a one-week internship (for those who get past the preliminary competition).
9. Revising the business plan.
10. The Final Competition.

One might ask, what is the overall purpose of the class and the competition? The answer is, first and foremost, identification of an individual who will work hard (and long) to make the franchise store succeed. It is necessary to ensure the individual has sufficient financial acumen to handle the financial commitments involved in the program. Most important is the ability to pinpoint the individual with a passion to run a business and a plan to be a long-term business owner (but not necessarily of the franchise store). Please recall that the donor's intent is to put students on the field so they can participate. Where it goes from there is mostly within the control of the individual graduate.

One interesting note is that alumni are allowed to come back, take this class, and compete for the franchise opportunity. A few have returned and some of them have won. As one might imagine, this has, on occasion, presented a challenge to the person recruiting students for this program.

Finding the Store

One of the more difficult aspects of the program is the identification of study stores to award to competition winners. Early on, the franchisor had several opportunities available. As the program matured, the number of underperforming stores available to award to competition winners decreased. For the program to be sustainable, the university needed access to franchises that can be purchased at a small enough price that it can be paid off from earnings within five years. Another challenge presented by the success of the program and the decreasing number of franchise options is location. At times, it required a student to move and live in an expensive locale. At other times, it required them to move to a more remote spot. This created some challenges in attracting Midwestern students to participate in the program.

In any given year several stores would be identified as possible candidates. As one might imagine, some of these stores are beyond saving. To ensure a reasonable opportunity of success for the students, an “Entrepreneurship Committee” of the business school’s Executive Advisory Council was formed. The Committee is made up of accountants, acquisition officers, and successful entrepreneurs. For each store proposed, the following information must be submitted to this Committee for evaluation:

- A. A copy of the current lease agreement
- B. Financial information for the store for the past three years (if available)
- C. Proposed sale price of the store

The committee is charged with evaluating this information and may make one of the following recommendations:

- A. Accept the proposal as submitted
- B. Make an offer of a lower purchase price for the store
- C. Reject the store

Training

It might be anticipated that because of the specific nature of a franchise operation, it is necessary to provide training in the operations of such a specific store. This dilemma was solved by the donor opening a franchise store in the community in which the University is located. This became the “training store.” The “trainer” for this aspect of the program has changed over time. Early on it was the co-owner of the store who was a previous winner of the competition. More recently one of the outstanding operators (a previous winner) provides the in-store training over six sessions during the semester. Topics covered in the training include:

1. Point of Sale System
2. Cleanliness
3. Customer service
4. Product display
5. Inventory planning and control
6. Operating a retail establishment

The Business Plan

There is nothing really unique about the process of developing a business plan. The aspect of this program, which is unique, is that the business plan is developed for a specific study store in a specific location (recall that stores awarded are either underperforming franchises or corporate-owned stores). Students are required to sign a non-disclosure agreement and are provided with the financial performance of the store over the previous years, a copy of the current lease agreement for the store, and the location of the specific store. Beyond this, it is a traditional business plan including company, industry and market analysis, identification of

target customers, local competition, a marketing plan, a staffing plan and financial plan including three years of cash-flow projections, Profit & Loss statements, and Balance Sheets.

The Competition – Phase 1

The format for the competition is pretty straightforward. It follows a model of presenting a business plan focused on specifically what the student would do to make the study store a success. For example, as part of the business plan, every competitor generally presents an increase in sales. For the competition, students must explain specifically how they will accomplish that increase.

The competition is a two-phase process. There is a preliminary competition designed to accomplish two things. First, the judges' primary goal is to identify the candidates they believe will be successful small business owner/operators. The second goal is to help those individuals improve their business plans to communicate better underlying assumptions, and implementation ideas to obtain reasonably accomplishable goals. The judges provide feedback to all competitors, even those not passed through to the final competition.

The judging panel for the preliminary competition has remained consistent since the beginning of the program. This group is a representative sample of members of the business school's Executive Advisory Board and several successful entrepreneurs from the community. This group provides significant advice to all the candidates based upon their experiences. The faculty member who teaches the class is present and provides input to the judges but does not vote on whether to pass candidates through to the finals or eliminate them. Over the years, this judging panel has become more aware and focused on the qualities needed for success. As a result, fewer students are getting passed through to the finals. Part of the reason for this phenomenon stems from the fact that not all awardees have historically been successful.

Although small in number, the impact of a failure can be significant to the future of the program and the franchisor.

The Internship

Each of the competition finalists is required to complete a one-week internship in the store of a previous winner. The store owners endeavor to give the interns a good look at what it means to own and operate a franchise. They are asked to conduct a full inventory during the internship, making the intern the lead. Every intern is required to open the store, close the store, and work during peak business hours. The goal is to have them experience the level of work required to succeed. Although it is difficult to demonstrate in a week, the hope is to leave them with the idea that it is not a “40-hour work week.” Owners are asked to review their first year with interns and outline the problems and challenges of owning and operating the store. Staffing and motivating staff are the two most consistent issues raised by the previous winners.

The Celebration Dinner

Early in June, after the semester has ended, there is a celebration dinner for the program. All current students in the class and all former winners are invited. Invitations are sent to all members of the business school’s Executive Advisory Council, all current and former judges, program sponsors, plus business and political leaders in the community. This dinner takes place the night before the final competition and includes an introduction of each of the finalists.

The dinner also serves as a celebration of the success of the current owners. Recognition of those who paid off their loans during the year is always a great event. Owners who have added additional businesses are also recognized. Every other year, winners of awards from the franchiser are recognized (this particular franchisor holds bi-annual conventions for its owners).

Also in attendance at the dinner are the judges from the finals. Over the years, this has included several members of the management team of the franchisor, the benefactor who proposed the program, representatives of other franchise organizations, past winners, the University President, and members of the business school's Executive Advisory Council.

The Final Competition

The judges arrive in the morning to a light breakfast and a brief discussion of the day. The first finalist is normally scheduled to arrive starting at 9:00 a.m. The competing student is instructed to spend no more than 15 minutes on their presentation at which point they sit down and respond to questions from the judges. Questions range from specific questions about the proposed business plan to where the student plans to be in five or ten years. Several of the finalists are married or have significant others who will contribute to the success of the overall plan either by working in the store or by working in a professional position contributing income to the family. These contributions help the awardees continue in business even if predicted sales increases do not occur as planned.

Over the years, the number of finalists who have received a franchise has ranged from 1 to 4. It was in those years where four stores were awarded that the potential weaknesses in the program were exposed. In recent years, the maximum number awarded an opportunity has been reduced.

After the winner(s) is/are selected, they proceed to mandatory franchisee training at the company's training facility. Costs of attending this training can be covered by part of the start-up funds students can request.

Financing

Clearly the greatest challenge to helping any traditional college graduate or recent alum is financing. Early in the program, some of the stores sold for as little as \$36,000. As previously mentioned, because of the reduction in available franchises, investments of more than \$100,000 have been required. Needless to say, financing future stores is a challenge.

Early in the program, the benefactor financed the stores awarded to winners. This worked well until the years when more than two finalists were awarded stores. After the program generated some successful owners, the franchiser was convinced to help with the financing stores each year. Financing for a store typically included the following:

- A. The purchase price for the store
- B. Up to \$15,000 for inventory acquisition
- C. Up to \$10,000 for start-up and relocation costs
- D. Up to a \$10,000 line of credit for the first year to cover any equipment failures requiring significant investment.

The financing vehicle used was a loan secured by the assets of the business. The loan was typically on a five-year amortization although for a couple of the more expensive acquisitions this was extended to seven years to ensure sufficient cash flow to cover payments. Winners were required to put together a plan for the use of their “start-up” funds before any distribution was made.

Conditions of the Financing

The total costs of this program are not insignificant in this time of reduced funding from State Legislatures. So, one might ask, what does the School get from this program beyond some good publicity? The benefactor who developed the program asks that every winner signs an

agreement to do three things in addition to operating the store and paying their loans and bills.

The three things are:

- A. Return to the Campus (or other designated location), at their own expense each year for the first five years after winning.
- B. Contribute back to the University each year based upon the sales they achieve.
- C. Attend an annual “Owners’ Meeting.”
- D. Although not required, many of the winners have worked closely with the Director to market the program to other students.

Over the years winners have done a reasonably good job of meeting these obligations and contributions back to the School have exceeded \$230,000.

Creating Success

How do you create a successful program which allows 22- 26 year old college graduates to own and operate a business with no savings behind them? Fortunately, the answer to that question was identified early in the program. Support of a core group of people was developed for the program. This includes a program director who is responsible for recruiting students, working with the franchiser to identify opportunities, coordinating the activities of the Entrepreneurship Committee, planning and executing the Celebration Dinner, monitoring progress of the winners, attending all store openings, arranging in-store training, internships and internship travel, identifying problems needing to be addressed, and many other details. This is a full-time staff person who, in addition to all the administrative duties arranges all the outside speakers for the class and attends every class session. The salary for the director is funded by the School within its budget.

The program also employs a part-time financial advisor who is responsible for receiving and evaluating quarterly financial reports from the winners for their first three years in operation. This person is responsible for identifying financial issues or problems ranging from inappropriately allocated purchase price in the balance sheet to failure to pay sales taxes. Providing an early alert to these issues is critical. This part-time financial advisor is on an annual contract and is paid from foundation funds provided for the program.

Even with these two dedicated individuals, there is still a need for a corps of volunteers. Some of these volunteers are faculty members, some are former winners, and some are retired entrepreneurs. When either the program director or the financial advisor identifies a significant problem, the dean and program director meet to develop a solution. Solutions range from weekly telephone calls between the owner and the financial advisor to sending a volunteer to the store for a week or more to provide on-site support and direction. Frankly, this has been a critical success item for this program. The School, through foundation funds, pays for the support people to travel to the store and covers costs while they help. This is also true for opening week, when often one or more volunteers attend the opening and help get the store ready. More than one owner has attributed their early success to this support system. As the program has grown, more and more of the support is being provided by previous winners over the phone or during a visit.

Making it Sustainable

The greatest challenge to the program is making the financial support for the program sustainable. Clearly the program cannot depend upon the financial support of one donor. The franchiser recently decided to no longer finance the acquisitions leaving a significant challenge for the program. One remedy was owner financing, where current store owners from outside the

program sell their existing stores to competition winners. Somewhat surprisingly, several have been willing to finance but generally have requested unfavorable terms (e.g., sales price, interest rates, repayment period) from students for this to be a viable option.

Another option explored was to develop a trust that can be used as “loan guarantees” for the winner(s) each year. To support one to two winners each year given current purchase prices, the fund will need to be approximately \$1,000,000. Obviously to expand to more winners or to more expensive franchise opportunities, more funding will be necessary.

The solution for the program was to partner with a regional bank that would allow current University investments to collateralize the loan without having to move any funds. The key to this solution is the decision to partner with a regional bank. As mentioned previously, the stores awarded in this program are generally underperforming which allows students to purchase the store at a fair market price (often lower than the net asset value). Traditional financing is almost impossible because on paper (i.e., every financial document) these stores carry a huge default risk. We found that a regional bank has more flexibility in its financing decisions to allow for a mutual partnership. Overall, the agreement allowed the loans to be guaranteed for students with them only having to pay an interest rate set at the Prime rate. From the perspective of opportunities, the future is bright. Over the past several years other franchise companies have attended the competition and have seen the results.

Ten Years of Success

As we evaluate the program for its impact on the winners, the franchiser, the School and the economy, we conclude it has been a success. To date, 91 students have participated in the newly named Applied Business Ownership course and 30 stores have been awarded by the competition. Some winners still own their original franchise, others own non-franchise

businesses, and more than a third have multiple business ownership. Franchise ownership has expanded to five different franchises and several of the earlier winners have successfully acquired loans for additional business acquisitions. Overall, the winners of the franchise competition now own 38 stores in nine different states and employ more than 319 employees. Their combined annual sales exceed \$11.8 million with payroll of over \$2.08 million.

Potentially the greatest success of this program is the “family” of store owners it has created. These individuals support each other without equivocation. They have supported each other through new store buildouts (some even financially), family expansion (marriages and new babies), and problem solving for their stores. It is amazing to be with this group during their annual Owners’ Meeting to share the camaraderie and success.

Conclusion

This unique program which we call “franchisepreneurship” has proven successful. Recall that the primary intent of the donor was to put these students onto the field by owning their own business. It is not a program easily duplicated. The program requires a significant institutional commitment from the perspective of staffing, to financial support of the financial advisor, to financial support for the travel, and lodging of the volunteers.

One last observation must be made. In truth, the driving force behind this program has been the donor. Not only has he stepped up and loaned several of the winners the money to purchase their stores, he spends significant time with the owners helping them to succeed. He has financially supported several of them to travel to the annual Owners’ Meeting. He has opened his home for periods of time for new owners to live with him when a store was located near him. He is always available to discuss new opportunities with previous winners. He is truly

committed to helping these graduates create a sustainable track of business ownership so they and their families will be self-sufficient and pay it forward to future winners.

In the recipe for success for providing franchisepreneurship opportunities, it takes a village with a dedicated captain who is willing to commit. The legacy left behind by this captain should serve as an example for others to follow.