

# Don't Give Away the Store: Site Selection and Leasing Issues in Franchising



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Presented by:  
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## Outline

- Territory allocation
- Site specific selection
- Leasing strategies
- Offer to lease
- Lease rider
- Other legal issues to consider



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## Assumptions

- Bricks and mortar
- Franchisor is NOT purchasing the land or building
- Location is important
- Examining issues from franchisor's perspective



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### Franchisor's Objectives

- Limiting exposure to liability
- Successful location
- Control over location
- Competing objectives?



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### Limiting Exposure to Liability

- Site Location Assistance:
  - Franchisee acknowledgement re responsibility for selecting the site
  - In the form of a site acceptance agreement
- Lease:
  - Require franchisee to enter into a lease directly with the landlord



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### Two Types of Analysis

- Territory allocation
- Site specific selection



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### Territory Allocation

- Exclusive vs. non-exclusive grants
- Determine the right size of the territory:
  - Too large?
  - Too small?
- Reservation of rights
- Encroachment policies
- Disclosure issues



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### Objectives when Establishing Site Criteria

- Penetrate market areas to:
  - Maximize sales/profits
  - Pre-empt competition
  - Expand exposure to the brand
- Ensure that franchisees have a sufficient revenue stream
- Avoid undue cannibalization of other franchisees



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### Factors that Affect Site Performance (1)

- Where are the competitors?
- Tenant mix - competition within centre, anchor tenants
- Retail synergies
- Density of population
- Traffic count - Pedestrian estimates



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**Factors that Affect Site Performance (2)**

- Size & Zoning
- Visibility from street level or exposure in mall
- Access to:
  - public transportation
  - traffic signals
  - adequate parking

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**Sources of Information (1)**

- Review demographic profile - census data
- Shopping centre data
- Consumer expenditure data

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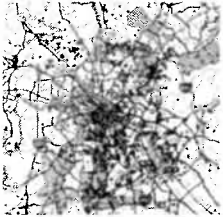
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**Sources of Information (2)**


- Statistical algorithms -software with predictive analytical tools to develop proactive, long-term network growth strategies



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### Site Selection Suppliers

- Jones Lang LaSalle – Toronto
- Mapping Analytics – Rochester, NY
- Javelin Solutions - Englewood, CO



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### Site Selection Strategies (1)

- Establish and codify site selection criteria
- Conduct site selection analysis
- Franchisor should apply its own site selection criteria consistently and in a timely manner
- Explain process in DD/Operations Manual



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### Site Selection Strategies (2)

- Disclaim liability in FA
  - Acknowledgment that franchisee must find an acceptable site
  - Limit liability where franchisor assists franchisee
  - Site Acceptance Agreement



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### Site Plans & Good Faith

- Country Style Food Services Inc. v. 1304271 Ontario Limited, 2005 (ON C.A.)



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### Failures in Site Selection

- Al-Harazi v. Quizno's Canada Restaurant Corporation, 2007 (ON S.C.)



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### Control over Location

- Lease negotiations
- Signage, menu boards and trade dress
- Franchisor constructs the unit itself



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### Conditions re Franchisee Construction

- Franchisee may be permitted to construct its premises, provided that it uses franchisor's:
  - designated signage
  - approved design plan and complies with franchisor's trade dress requirements
  - architects, construction personnel etc. and pays a management fee to ZOR



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### Who is the Tenant?

- Franchisor's objectives will dictate whether landlord directly leases with:
  - Franchisor and sublets to franchisee
  - Franchisee
  - Franchisee but with lease rider in favour of franchisor
- Establish separate leasing entity



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### Direct Lease btwn Landlord & Franchisor - Pros

- Increased control over premises and franchisee
- Quicker transitioning of weak franchisees
- Enhanced bargaining power
- Broader remedies available to franchisor
- Non-competition covenant more easily enforceable



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### Direct Lease btwn Landlord & Franchisor - Cons

- May be forced to rectify franchisee's defaults under the lease and to operate the franchise
- Exposure to liability
- Franchisee has certain rights vis-à-vis franchisor



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### Offer to Lease/Lease (1)

- Operating name
- Permitted use
- Exclusive use
- Patio, seating areas or drive-through areas



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### Offer to Lease/Lease (2)

- Reduce financial obligations to franchisee
  - Basic and additional rent
  - Tenant inducements - Rent free periods, tenant allowances
- Consider any additional payment obligations
- Reserve rights re signage
- Exclude or minimize any radius restrictions



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### Offer to Lease/Lease (3)

- Insurance
- Relocation



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### Offer to Lease/Lease (4)

- Assignment or sublet exemptions re change of control scenarios (to affiliated entities) and to approved franchisees:
  - Without landlord's consent
  - Reserve right to assume control on a temporary basis
  - Limit assumption by franchisor of any liabilities of franchisee
  - Release from any covenants and guarantees



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### Lease Rider Provisions if Franchisee has Direct Lease

- 3-party agreement; or
- Third party beneficiary language in Lease consented to by the landlord



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**Lease Rider Provisions (1)**

- Right to receive sales reports submitted to landlord
- Right to inspect leased premises



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**Lease Rider Provisions (2)**

- Right to require de-identification of leased premises upon termination of FA
- Assignment or sublet to approved franchisee
- Assignment on franchisee's default but at franchisor's option



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**Lease Rider Provisions (3)**

- Landlord to provide written notice of renewal to franchisor and franchisee has no right to renew without franchisor's written consent
- Co-terminus terms of lease and FA



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### Lease Rider Provisions (4)

- Franchisee prohibited from assigning or subletting premises to a competitor
- No right to amend the lease without franchisor's consent
- Notice of default with opportunity to cure
- Assumption of lease not to relieve franchisee of its obligations under the lease



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### Lease Rider Provisions (5)

- Bankruptcy/insolvency not to trigger termination
- Estoppel certificate from landlord
- Rider supersedes any inconsistent provisions in the lease



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### Lease/Sublease Negotiations

- Franchisor counsel should negotiate lease
- Franchisee counsel should review and approve the lease



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### Timing re Execution of Lease

- Before franchisor finds a suitable franchisee?
- Consider financial risks involved



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### Other Legal Issues

- Where franchisor has not secured a location at time of the delivery of the DD
- Details of lease payments and obligations in DD
- Duty of Good Faith



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### Factors Impacting Bottom Line (1)

- Fees in addition to basic and additional rent:
  - % rent
  - Community service events
  - Loyalty programs, gift certificates
  - Administration fees
  - Merchants association dues
  - Advertising payments



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### Factors Impacting Bottom Line (2)

- Common area expenses:
  - LL's remodelling/alterations
  - Replacement of roof & resurfacing of parking lot
  - Relocation of stores/new building construction
- Avoid duplication of costs



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### Cross Defaults

- Cross default provisions in lease/sublease and FA
- To prevent a franchisee from occupying a premises following termination of each agreement



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### Concluding Remarks



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Questions?



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