

# HOW MUCH CAN I MAKE BY OWNING A FRANCHISE?



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*The question is on every prospective business owner's mind; the answer can be elusive.*



## ■ A Big Decision And An Important Question

Money is a central factor in any business decision, and it's no different when it comes to franchise ownership. The No. 1 question an accountant who is a prospective owner may have is: "How Much Money Can I Make By Adding a Franchise?"

The question is a good one, especially for accountants looking to add a new revenue stream and customer base. However, prospective franchise owners cannot and will not get an answer from the franchisor. Legally, the franchisor can't make any financial claims about a prospective business. Financial representations can be shared only in one portion of the Financial Disclosure Document that franchisors share with prospective owners. Franchisors can't wave a magic wand and tell you how much you'll make in your first year of business, your second year, or even your 20th year.

Your success will depend on many things — most importantly, you and the choices you make as the business owner to provide additional services to your existing clients and bring in an entirely new customer base.

That doesn't mean you can't paint a picture for yourself of what you may be able to achieve by adding a tax franchise. To do so, you must understand the playing field. What are the track records of tax franchise businesses? Where are the growth areas? You also need to peruse documents, talk with past and present franchisees, and see what the future might hold. As an accountant, you'll likely want to provide additional services to your current clients so you can increase revenue from them. For that reason, you may want to reach out to people like you who found success by combining their accounting business with a franchised business.

You already have a head start because you understand how businesses make money. You know the difference between revenue and profit and understand cash flow and how it can affect your business operation. That understanding and an ability to apply these basics to your franchised business will put you closer to the happy ending you desire.

## ■ The Franchise Business is Good and Growing

Franchise businesses are engines for the economy. A report by the International Franchise Association and IHS Economics found that franchise growth outpaced the U.S. economy in 2016. It was the seventh consecutive year that franchise growth exceeded the overall U.S. economy.

“Franchising is an American success story,” said IFA President and CEO Robert Cresanti. “Establishments are growing faster and creating jobs at a faster pace than the overall economy. They’re getting more sales and growth than other businesses.”

The 2017 report shows that:

- Franchise employment grew 3.5 percent in 2016 and is expected to grow another 3.3 percent in 2017
- Franchise output was up 5.8 percent in 2016 and will continue to grow another 5.3 percent in 2017

## ■ Business Basics and the Bottom Line

Since you’re currently involved in accounting services, you may find it easier to be successful in the tax business because it closely matches services you already provide to your existing customer base. But how much you can make still depends on many factors, including your understanding of basic business principles and their application to your business. Understanding cash flow, for example, is essential. As you are likely aware, poor cash flow is a top reason many new businesses fail.

**Cash flow.** As a business owner, you have lots of expenses, including payroll, lease payments, equipment, and servicing your debt. You also have income from sales and, perhaps, loans. Cash flow is the difference between these two things — the money a business brings in and the money a business spends over a certain period of time. For example, a business will have a certain amount of money in its bank account at the start of a particular month and a certain amount at the end of that month. Cash flow is the measure of that

### *Cash flow statements are generally separated into three parts:*

**Operating Activities** - This section evaluates a business’s net income and losses. By assessing sales and business expenditures all income from non-cash items is adjusted to incorporate inflows and outflows of cash transactions to determine a net figure.

**Investment Activities** - This section reports inflows and outflows from purchases and sales of long-term business investments such as property, assets, equipment, and securities. For example - if your bakery business purchases an additional piece of kitchen equipment, this would be considered an investment and accounted for as an outflow of cash in this section. If your business then sold equipment that was no longer needed, this would be considered an inflow of cash and accounted for in this section.

**Financing Activities** - This section accounts for the cash flow trends of all money that is related to the financing of your business. For example - if your small business was issued a loan from the Microloan Program to assist with start-up funding, the loan itself would be considered an inflow of cash. Loan payments would be considered an outflow of cash, and both would be recorded in this portion of the cash flow statement.

– SBA.gov

change, from the beginning of the month until the end. Good cash flow is essential for a successful business. It will allow you to meet payroll, service your debt, and keep your business open and operating. A cash flow statement can help an owner keep track of revenue and expenses. It can help the business owner see patterns in the business and make plans for future expansion or growth. At its root, cash flow is a simple concept, but it still often poses a challenge for business owners, and not just new owners. A report by the Corporation for Enterprise Development, a non-profit based in Washington, D.C., found that about 37 percent of experienced business owners sometimes have cash flow issues.

**Sales.** Sales equals the money a business receives for services rendered. Sales, or revenue, is the money brought in by your franchise's business activities.

**Profit.** As an accountant, you know sales minus costs and expenses equals profit.

## ■ Applying the Basics to the Franchise Disclosure Document

With your knowledge of basic business terms, you can better understand and assess the opportunity presented by adding a tax franchise to your accounting business. You can apply the basics to the Franchise Disclosure Document (FDD) and build for yourself a picture of how your future might look as a franchise owner. By law, the franchisor must provide the FDD to you at least 14 days before you are asked to sign a contract or pay money to the franchisor. A prospective franchisee can also request the document after he or she has received the franchisor's application and agreed to consider it. The FDD is a hefty document. You may look at it and want to look away, but you'd be wise to pull up a chair and study the document, paying particular attention to Item 19 and Item 21. Item 19 includes the Financial information with the information in Items 5, 6, and 7 of the FDD to get a sense of how much the businesses take in and how much they spend on payroll, royalty fees, and more. Looking at the two together will give you a sense of profitability of the pool of franchisees who have been included in the disclosure. Some franchisors offer a range of franchisees, so you can compare the high earners, with the mid-range earners, with the low earners. The key is to remember that this disclosure shows you how others are doing. It does not and cannot project what you may earn as a franchisee. In fact, franchisors must include in Item 19 a warning that a prospective franchisee's actual earnings may differ.



**Financial Statements.** Item 21 is where you'll get a look at the franchise's audited financial statements for the past three years. If you are not familiar with financial statements, it might be wise to have an accountant review the document with you to help you determine if the franchise is financially robust and stable.

**Lawsuits and Bankruptcy.** Items 3 and 4 of the Franchise Disclosure Document will reveal lawsuits against the franchise and bankruptcy issues. It's important to view the lawsuits with some pragmatism. Lawsuits often are a part of doing business, so you may see some in the disclosure.

**Upfront Costs.** Item 7 in the Franchise Disclosure Document will tell you every aspect of the initial investment, including allowances for initial advertising and operating capital reserves. It will give you more of a picture of how much it will cost you to go into business. You can compare these costs with what you've seen in Item 19 to create a clearer picture of revenue and expenses.

# FRANCHISE

## THINGS TO CONSIDER IN THE FDD

**Sample Size.** Suppose a franchisor says that franchisees in its system earned \$50,000 last year. The disclosure document should tell the sample size and the number and percentage of franchisees who reported earnings at the level claimed.

**Average Incomes.** A franchisor may say that the franchisees in its system earn an average income of, say, \$75,000 a year. Remember successful franchisees can inflate the average.

**Gross Sales.** Some franchisors provide figures for the gross sales revenues of their franchisees. These figures don't include actual costs, such as rent and other expenses, or profits.

**Net Profits.** Franchisors often do not have data on net profits of their franchisees. If you get net profit information, ask whether it includes information about company-owned outlets; they often have lower costs because they can buy equipment, inventory, and other items in larger quantities, or they may own, rather than lease, their property.

**Geographic Relevance.** Earnings may vary with geography. The disclosure document should note geographic or other differences among the group of franchisees whose earnings are reported and your likely location.

**Franchisee's Backgrounds.** Keep in mind that franchisees have different skill sets and educational backgrounds. The success of some franchisees doesn't guarantee success for all.

– Federal Trade Commission

## ■ Don't Be Shy: Talk to Current and Former Franchisees

The FDD will give you a good sense of the franchise, but to learn even more about how individual franchisees are doing, you will need to make a few phone calls.

Some franchisors include contact information for current and former franchisees in their disclosure documents. If that information is provided, consider it a gift. Open it and use it.

Call people who are still in the system and ask them the questions that are on your mind. Don't limit yourself to a small pool; reach out to 10 or more current franchisees. Naturally you'll want to know things like:

- 1. How much did it cost you to get the business open?** You will already have a sense of the answer, based on your earlier research and information in the FDD, but the franchisee can share the surprises he or she encountered. The franchisee can tell you how much the business paid for business permits, payroll, marketing, technology, loan interest, and more.
- 2. Were your first-year sales what you expected?** Let the franchisee explain how he or she predicted first-year sales, where he or she was correct, and where the franchisee miscalculated. Let the franchisee tell even more about the first-year experience so you have a clear sense of what you might be in for.
- 3. When did you break even?** With this information, you'll have a sense of how long it took the franchisee to generate enough operating revenue to cover monthly operating expenses and start paying back the initial investment.
- 4. How much can I make as a franchisee?** Of course, the franchisee can't tell you how much you'll make, but the franchisee might be willing to share how much he or she makes in profit.

Call former franchisees and ask some of the same questions, but be sure to ask them why they no longer are franchisees. Some may express anger toward the franchisor, but they may also share how their lack of business basics interfered with the dream of business ownership.

## ■ Adding It All Up

All the information you amass will help you see more clearly the opportunities available to you by adding a tax franchise to your accounting business. Review the information with your lawyer and those who support your dream of expanding your business and adding a new revenue stream. Then, make your decision and embrace it.

If you're interested in learning if adding a tax franchise to your portfolio is right for you, contact us today at [Libertytaxfranchise.com](http://Libertytaxfranchise.com) or call 1-844-895-5621.

