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STRATEGIC PLAN ON FRANCHISING SERVICES IN THE CARICOM SINGLE MARKET AND ECONOMY (CSME)

A Concept Paper prepared for the CARICOM Secretariat

By
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Introduction

This Concept Paper on the development of franchising of services within the CARICOM Single Market and Economy has been prepared in accordance with the “Guidelines and Expected Outcomes” of a Contract of Service between G. L. Sydney Simmons of No. 11 Hope Park, St. George, Barbados, and the CARICOM Secretariat.

G. L. Sydney Simmons, the Executive Chairman of Global Development Services Corporation (GDSC), during the preparation of this Paper, has also been advised by international franchising expert Alexander S. Konigsberg, Q.C., of LaPointe Rosenstein of Montreal, Quebec, Canada; and assisted by research associate Hadlee Sobers.

The Paper, while adhering to the agreed “Guidelines and Expected Outcomes”, seeks to design and present a practical and pragmatic concept for franchising in the Region that draws from the current and historical CARICOM experience with franchising. The view then is a Concept that can be applied as an **entrepreneurial development project** within the targeted member states of the CSME.

The Conceptual Model presented herein provides the CARICOM Secretariat with a practical Pilot Project and a framework within which technical developmental assistance can be provided to businesspersons who may be willing to invest in the development and building of franchising capability; first within the Common Market, and then as a strategic method for developing exports outside of the region, over a 5–7 year period.

The Concept Paper has fashioned this Model for CARICOM Franchise Services Development after examining the experiences of Caribbean businesspersons who have for several years produced under license, using

established international Brand names, Trademarks, Patents, and other private labels, processes or Intellectual Property.

Emphasis has not been placed on businesses which are/were wholly owned subsidiaries of extra-regional or transnational/multinational corporations, or petroleum distribution; beverage manufacturing and bottling; lodging /accommodation; quick service/fast food restaurants; catering; or accounting professional establishments.

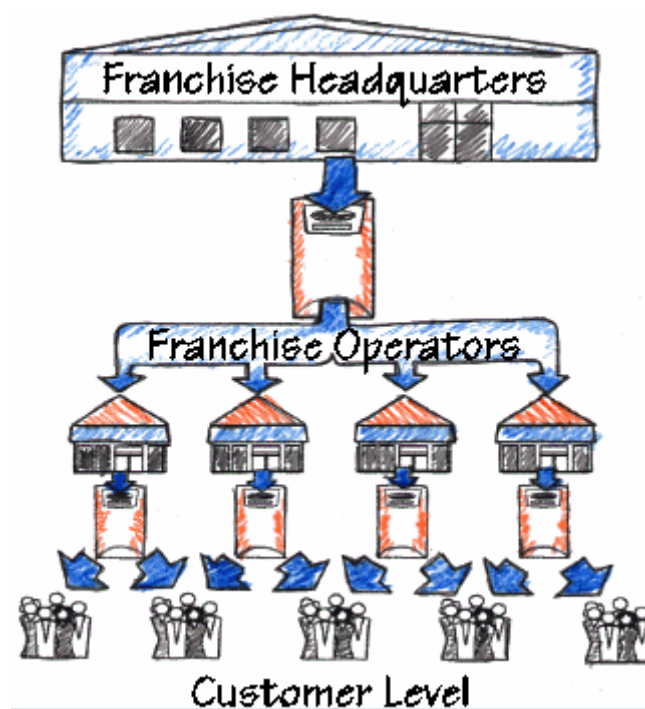
This approach has been adopted because these establishments do not and have not demonstrated either (1) the willingness, or (2) the intention to build national entrepreneurial capacity in any country where they operate, or where they have facilitated licensing or licensee-type arrangements. In other words, these companies have an inward focus *only* and do not enable franchisees to develop entrepreneurial skills, or acquire transferable business management skills.

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Mr. Simmons has worked as an International Marketing Management Expert; Project Analyst; International Development Consultant and Business Development Advisor throughout the Caribbean Region, Europe and North America.

The views herein expressed are drawn from his expert experience in global export development.

Background – An Introduction to Franchising



According to the International Franchise Association's (IFA) Educational Foundation, a franchise is

¹. "The agreement or license between two legally independent parties which gives:

- a person or group of people (known as "the franchisee") the right to market a product or service using the trademarks or trade name of another business
- the franchisee the right to market a product or service using the operating methods of the franchisor
- the franchisee the obligation to pay the franchisor fees for these rights
- the franchisor the obligation to provide rights and support to franchisees"

www.franchise.org

Types of Franchises:

There are basically two (2) types of franchises.

1. *Product Distribution Franchises*
2. *Business Format Franchises*

Product Distribution Franchises

Under this type of franchise arrangement the franchisee simply sells the franchisor's products; there is basically a supplier – dealer/retailer relationship.

The franchisor has permitted the franchisee to use, under license, his logo and trademarks. There is no management support or system for running the business.

Business Format Franchises

On the other hand, the Business Format franchisee not only uses the franchisor's product, logo and trademarks, but is also provided with a complete system of conducting the business itself. This system will include total management guidance, such as marketing plans and full operational manuals.

This is the most common type of franchise in the USA, Canada and the UK; and is the type best suited for the CARICOM situation.

The Current Franchising Sector in CARICOM

The Franchising Service Sector in CARICOM is dominated by American petroleum, fast food/quick service restaurants, lodging/accommodation, and Business Services. Names such as Shell; Texaco; KFC; Hilton; Marriot; Hyatt; TGIF; Ace Hardware; Esso/ExxonMobil; Coca-Cola and Pepsi are virtually household names in most of the Member States.

In addition to these there are many other licensed products being manufactured or processed in the Region, using the brand names or trademarks of extra-regional producers, distributors or marketers.

Among these are *Van Heusen; Levi's Jeans; Clayton's Kola Tonic; Scheppe's Bitter Lemon and Tonic Water; Phensic; Valrico; Chefway; Victoria Secrets; and Bath & BodyWorks.*

Notwithstanding the fact that it can be assumed, through the process of executive judgment, that these franchised businesses make a significant direct contribution to the CARICOM economies, there is no statistical information being collected across the region. Consequently, data such as the number of establishments, payroll, jobs (direct & indirect employment), and output are not available at this time.

This unavailability has a direct negative impact on planners and policy makers who may wish to consider incorporating franchising into any entrepreneurial development or export development model, or Pilot Project.

A clear, comparative example of this impediment can be seen when a look is taken at statistics of franchising in the USA (Table I)

2. **Table 1:**

FRANCHISED BUSINESS GROWTH COMPARED TO ALL BUSINESSES

2001–2005

	2001		2005	
	Franchises	All Businesses	Franchises	All Businesses
JOBS	9,797,117	132,040,682	24,074,800	136,709,071
PAYROLL (USD billions)	\$229	\$4,567	\$279	\$5,268
OUTPUT	\$625 Billion	\$16 Trillion	\$881 Billion	\$20.1 Trillion
ESTABLISHMENTS	767,483	24,074,800	909,253	27,891,770

From this (Table 1 data) analysts were able to compare growth, employment generation, payroll movements and growth in the number of establishments over a specific period. Since no such data exists for CARICOM analyses, assessments and recommendations have to be based on ‘intimate knowledge’ or executive understanding of specific sectoral issues; or performance of individual franchises in any one Member State.

One of the major problems facing CARICOM is the lack of a “*franchisor culture*”; typically the Region has been seen only as an expansion area for foreign franchises (in most instances product/service distribution). This has had, and is still having, a negative impact on the growth of franchising in the Region.

In one Member State there is at least one local international-standard fast food outlet where the owner & management team are expressly reluctant to consider even establishing a wholly-owned subsidiary in any other Member territory.

By contrast, in another Member State, the owner of another indigenous food operation is willing to consider franchising as an expansion option; however, there is currently no supporting technical assistance readily available in the Region.

This lack of assistance to enable the development of franchisor capacity has also been felt by a regional fast food restaurant operator, who sold a franchise to a businessman in Barbados, but did not have well-developed management training or operational systems to pass on as part of franchisor support.

Eventually the operation closed after three (3) years of opening its doors – under the Brand name which is well established in the franchisor's territory.

These three (3) references, although the operations have not been explicitly identified herein, are all typical of the indigenous franchise sector; a sector which can boast of only one indigenous franchise that is, according to industry information, actively exploring the possibilities of securing franchises in more mature extra-regional markets (in this case North America).

The CSME Member Territories remain predominantly a franchisee area, where some businesspersons are seeking to be Master Franchisees for the Region.

Policy Framework

Legislative Framework – Harmonization

There is currently no established or harmonized regional legal environment for franchising. In fact, to date, Barbados is the only Member State in the Common Market which has enacted specific Franchise Legislation (**The Barbados Franchises Registration and Control Act Cap.179A**) (*see Attachment I*)

In other Member States, since there is no specific legislation, franchising is regulated under other laws which address general business registration and operation (e.g. The Antigua and Barbuda Business Licenses Act, 2004).

In itself the Barbados Legislation has its' primary focus on protection of local business interests, rather than wider entrepreneurial development or export development; and so cannot in any way serve as a viable model for other Member States who may wish to employ franchising as a part of their export development strategy over the next few decades.

When compared with legislation designed to facilitate the use of franchising as a viable business option, such as the *UNIDROIT Model Law* discussed hereafter, the Barbados Franchises (Registration and Control) Act CAP. 179A clearly does not in any way cater to the development of franchising in the country.

The Act deters non-citizens of Barbados from operating a franchise without permission from the Minister. It does not seek to encourage even citizens to acquire franchises as a means of developing international competitiveness capability.

Legislative Framework

Based on the foregoing conclusion, it would seem advisable that the Member States should consider establishing common legislation which would be applicable to both regional and extra-regional (potential) franchisors and franchisees.

Such legislation could be based on an International franchising Act/Convention, such as the “Model Franchise Disclosure Law” of the **International Institute for the Unification of Private Law (UNIDROIT)**. This recommended legislation states in its’ Explanatory Report that

- i. The Model Law is intended to encourage the development of franchising as a vehicle for conducting business. As a pro-commerce document, it recognizes that franchising offers the potential of increased economic development, especially among countries seeking access to know-how*

- ii. The Model Law is a disclosure law. A disclosure law may be considered to be a means to create a secure legal environment between all the parties in a franchise agreement. To that end, the Model Law ensures that the prospective franchisees who invest in franchising receive material information about franchise offerings, thus permitting them to make an informed investment decision. In addition, the Model Law brings security to franchisors in their relationships with franchisees, administrative authorities and courts.*

These explanatory notes relate both to domestic (intra-regional) and international (extra-regional) franchising, where the Model Law will also apply to different types of franchise agreement, such as

- (1) Traditional unit agreements
- (2) Master Franchise agreements
- (3) Development agreements

It is anticipated that the Model Law will also cover any new forms of franchise agreements that might develop in the future.

The Model Franchise Disclosure Law focuses entirely on the franchisor, the franchisee, the franchise itself, training programmes, terms of franchise, preparation of financial statements, enabling information, etc.

This Model Law provides a serious developmental approach, and focuses on all aspects of franchising. It would certainly be an extremely useful and appropriate decision if Member States adopted this approach as a model on which harmonized CSME Franchise Legislation should be based.

Trademarks and Intellectual Property Registry

To facilitate international competitiveness it will absolutely necessary to establish a single regional Trademark and Intellectual Property Registry, where both regional and extra-regional data will be recorded and accessible to all franchisors and franchisees.

This will simplify doing business within the CARICOM Single Market, and remove the often onerous necessity of having to register trademarks, licenses, patents, designs and other proprietary marks in each individual Member State that the franchising party might seek to operate in. This would not only decrease the level of bureaucratic hindrances to entering the market, but also significantly reduce the costs of doing business in the Region; since a single fee can be charged rather than 15 (one in each Member State).

The revenues collected can then be used by the Registry to assist with the financing of its operations.

Regional Franchising Model

At present the Caribbean Region is not ready to undertake franchising as a viable export strategy or development option. In the Regional Public Sector there is no supporting or enabling institutional environment in place, in the private sector there is unit franchising experience but no collective history or experience to facilitate or form the basis for the development of an export model. Consequently it is being recommended that serious consideration be given to a Pilot Model Franchising Development Project.

The benefits to be derived from the project are:

1. A high level transfer of knowledge of running a successful business with global potential
2. The development of the Region's international business capacity and image, through the high visibility achievable by most world-class franchises
3. The leveraging of a highly trainable, highly educated and highly skilled force of knowledge workers
4. The building of capacity to enable regional businesspersons to offer Caribbean stakeholders a range of high-value services in developing franchising systems
5. The eventual creation of a cadre of franchisors and master franchisees with capacity to establish franchises in Canada, the USA, Europe, South Africa, Nigeria, Botswana, and other selected target markets
6. The capacity to develop regional brands and licenses to stimulate the economies of Member States, increase regional business offerings and foster the growth of innovation.

The Conceptual Development Models

From a preliminary overview of the of the international franchising sector it would seem advisable for a CSME Model Project to initiate discussions with some specific franchisors who already operate very successful international franchises and who would be prepared to assist with a programme to grow an economy and create an entrepreneurial class through

- (1) the transfer of know-how
- (2) in-depth training programmes
- (3) technical management assistance, and
- (4) influencing of public sector development project financing.

Based on the review it would appear that a successful approach could be made to the following franchise operations:

Franchise 1:

A highly successful French franchise company in the business of producing breads and baked goods for its own limited-menu café, bakeries, supermarkets and premium hotels. This French company has successful franchises in France, Japan, South Africa, Indonesia, Canada and the USA.

The company has developed sophisticated high-quality packaging and distribution systems and would certainly be interested in CSME franchisees in Barbados, Jamaica, St. Lucia, Trinidad & Tobago, the Bahamas and Antigua, initially. Other franchise target markets will include the U.S. Virgin Islands, British Virgin Islands (B.V.I.) the Dutch Antilles, St. Maarten, Bermuda, St. Vincent & the Grenadines, and Grenada.

This franchise provides high quality frozen dough for the production of its breads and other baked goods. It is envisaged that the Project can start with importation of dough from one of its factories before the construction of the first production facility in the CSME, possibly in either Jamaica or Barbados.

Franchise 2:

From preliminary analysis it would seem advisable to resist the idea of even considering a project involving any restaurants, catering or quick service food outlets.

Consequently Franchise option 2 should focus on other types of service offerings, such as

- Business Services Centers
- Overweight Packaging & Postage Service at airports
- Large-scale Pharmacies
- Optometrists
- Professional Services
- Car Maintenance
- Convenience Stores
- Private Education

Financing the Sector's Needs (Models):

Franchise Option 1 – Production of French breads and baked goods

This development Franchise Project will have to be carefully structured so as to be able to attract three (3) types of financing

- a. Multilateral Development loan and grant financing*
- b. Commercial Bank loan financing*
- c. Private Equity*

A. Development Financing

Since the identified project franchise is French it should be possible to seek regional developmental grant financing under the Economic Partnership Agreement (EPA) between the European Union (EU) and the Caribbean Community (CARICOM).

This funding will be used to provide the institutional framework and to prepare the initial Prospectus/Project Document, after negotiations with the French franchisors to license Master Franchisees in the Region.

Contingent Recoverable Grant financing can be sought from regional multilateral sources in order to finance training and joint production of the management system (business process) documentation.

B. Loan Financing

It is anticipated that this project will require loan financing for the establishment and initial operations of the franchise in the first one or two CSME Member States.

However, the nature of this franchise service, the output and sales should be adequate to make the Project bankable and attractive to commercial banks, Credit Unions and other loan providers.

There should be no difficulty in obtaining collateralized loan financing for this potentially highly profitable franchise.

C. Equity Financing

This limited-menu café/bakery franchise is quite an attractive project and should offer a fairly competitive rate of return. Therefore it should not be difficult to attract interested persons to invest in the project – however, because of the developmental nature of the Pilot Project it may be necessary to initially have a public/private ownership structure with the public shareholding being offered to the private sector at the end of five (5) years, or perhaps before, if reasonable.

During the first five years of entrepreneurial development through franchising great care will have to be taken to ensure that franchisees understand the developmental and capacity building concepts that underlie the promotion of Business Formal Franchising as a means of acquiring the skills and techniques of managing a successful and profitable Business.

Notwithstanding the need to influence or manage franchise selection, it will be advisable to ensure that no legal, institutional, protectionist, bureaucratic barriers or impediments be placed in the way of persons who have adequate equity financing to enter into franchising arrangements. In fact, such should be encouraged rather than obstructed and all appropriate means of promotion should be employed to facilitate the growth and expansion of both regional franchisors and franchisees.

D. Venture Capital

Most Venture Capital providers in the region are publicly financed. Even though some governments offer tax incentives to corporations which invest in these vehicles, there has been an aggressive rush from private sector companies and institutions either to invest in or to offer Venture Capital directly to entrepreneurs.

In addition, regional small and medium entrepreneurs have been expressing a preference for loan financing, since there is usually no requirement for the kind of oversight and terms of investing which venture capitalists and venture capital providing institutions insist on as a condition precedent to investing; even though the requirement may simply be a seat on the Board of Directors, or a quarterly trial balance report or in extreme cases a joint signatory on cheques.

Nonetheless, Venture Capital is still an excellent vehicle for the financing of franchises and franchise entrepreneurial development. This method will offer the Venture Capitalist, the franchisor and the serious-minded franchisee an efficient and effective method of financing the venture.

There are, within several of the Member States, at least one or two public sector and or private sector institutions offering Venture Capital windows through which financing for franchising may be obtained.

E. Commercial Banking Sector

Traditionally the Commercial banking sector has had a conservative and cautious approach to financing Small and Medium Sized Enterprises (SME's) which have no history or track record. Any lending to this sector has had to be financed, secured or collateralized.

There is little likelihood that there will be any significant shift in lending policies by this sector since most franchises will be unit franchises and the tendency has been to evaluate the borrower as well as the project. However, it maybe possible to provide a Business Format Franchise scheme which offers a guarantee through a multilateral Funding institution or a Central Bank or some Government Authority or Business Development Agency.

Any such scheme, although it may seem to be pandering to the Commercial Banking Sector's policies of non-developmental intervention, could influence an individual Commercial Bank to be more supportive of a franchise unit.

In order to provide some impetus toward change in the policies of this sector it may just be possible to negotiate a Special Franchise Financing Arrangement with a Commercial Bank that operates in several or all Member States. Such an approach will provide the Commercial Banking Sector with an incentive to join development support institutions in a partnership for development.

Incentives

Recognizing that franchising is playing an ever-increasing role in a wide range of natural economies, to effectively employ it as a twofold strategy of a) growing economies and b) simultaneously developing an entrepreneurial Class within CSME, Member States would have to consider the granting of packages such as:

- (1) Fiscal incentives
- (2) Training/Know-How acquisition assistance packages
- (3) Critical legal/negotiation assistance
- (4) Assistance with development or negotiation of trademarks, patents, service-marks, copyright and other intellectual property.

Opportunities from Trade Agreements

As indicated earlier in this Paper, there are possibilities of developing an effective Franchising Model through a relationship with a French franchisor. In addition Canada offers considerable scope for acquiring franchises and developing franchising relationships.

Under the EPA between Europe and CARICOM (as part of CARIFORUM) there are possibilities of developing mutually profitable relationships in the franchising sector. Although France has been identified as an initial target, Germany has developed a number of “green” eco-labels under the *Blaue Engel* (*Blue Angel*) mark. These, along with *Nordic Swan* and other European labels offer possibilities of licensing or use. However the terms and limitations of this Concept Paper do not allow for amplification and exploration of these possibilities herein.

Sustainable Franchising Services

Although there may not be many franchise-ready projects currently within the CSME it is quite likely that with appropriate institutional support, regional unit franchisors and master franchisees could maintain internationally competitive businesses, even in the currently turbulent and uncertain economic climate.

In fact, unit franchises can have a greater component of survivability than many other small or medium-sized local production or service units, due to the strength derived from their internationally-recognized name and associated brand image/implied quality – if profitably managed.

Sustainability and longevity will ultimately require institutional promotion and support; but this is achievable, and so the question of sustainability rests squarely on the shoulders of franchisors and franchisees living up to the demands of a growing market that is becoming more sophisticated day by day.

Cross-Sectoral Linkages

Franchising in itself as a means of production, distribution or retailing does not offer any significant cross-sector linkages. This strategy and marketing technique will certainly offer some minor inter-sector and cross-sector linking but it is unlikely that there will be enough activity in any one sector across the region to have any significant economic or sociological impact.

Notwithstanding the above, any well-established franchisor or franchisee will be very competitive and will force others within the sector to improve across all operational areas of business. This is already noticeable in the restaurant/quick service sector in the Caribbean, where a high level of competitiveness is required for all new entrants, whether domestic or international.

International franchises in the fast food/quick service sector have established such a high level of presentation, health standards, food handling, advertising, and overall operations that domestic entrants and other competitors are forced to meet at least the benchmarked levels of international franchises.

Human Resource Requirements

Across the Region, in all the CSME territories there are several trainable persons who can be provided with specialized skills as is required by the particular unit franchises.

Franchise-specific training can be provided by franchisors at training institutions or on-the-job at operational units where specific training centers are not available.

Training manuals, DVDs and other instructional materials on the specifics of a particular franchise are normally provided by franchisors.

A fairly large pool of persons is available for management, operations and ancillary staff. The Region's tertiary-level institutions; Universities, Community Colleges and Polytechnics; provide a number of graduates annually, equipped with the basics in many disciplines. These graduates can form the basis of the new cadre of businesspersons, professionals, knowledge workers and technocrats with highly specialized, world-class business skills.

Access to and Use of Technology

Franchisors in Business Format franchises will provide access to and training in specific technologies which may be needed for operating the business of the specific unit franchise.

Other basic technologies with universal applications, such as computers, e-technologies and office equipment, are readily available in all Member States. Any specific proprietary technologies, patents or copyrights are usually made available under special agreements with the franchisors.

Recommendations

In order for franchising to be employed successfully as a regional developmental tool it will be necessary to provide a regional supporting mechanism that is effective and efficient, within a non-protectionist framework. To achieve this it is recommended that the following be considered:

- I. The establishment of a single **CSME Franchising Registry**, located in one Member State. This would facilitate both regional and extra-regional registration of trademarks, patents, copyrights, etc.
- II. Should recommendation I. not be feasible or practicable it is recommended that Member States then agree to a Single Regional Registration framework which would enable international and domestic franchisors to register in any territory using a Harmonized Regional Registration form.
- III. A single harmonized law be adopted by Member States, and that this Law draw on the approach of the *Model Franchise Disclosure Law*, as developed by UNIDROIT in Rome, 2002. The Model Law's preamble states that

“This Law applies to franchises to be granted or renewed for the operation of one or more franchised businesses within the [state adopting this Law].”

- IV. The CARICOM Secretariat should actively consider and implement a **Special Franchise Development and Enabling Project**.

The Secretariat should explore the possibility of financing this proposed Project within the facilitating mechanisms of the Economic Partnership Agreement (EPA).

- V. If the Secretariat accepts the recommendation that franchising could be used as a mechanism to foster entrepreneurial and economic growth, efforts should be made to influence the establishment of a regional franchising body, possibly within an existing private sector organization.

 - VI. The Secretariat should seek ways to regularize and standardize the collection of data on franchising within the Region. This would be extremely valuable in assessing the contribution to regional economies.
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A Final Thought

Economic development is a challenge to small communities across the world. A central question that arises is how to stimulate a remote and small economy. One method is to allow local entrepreneurs to open service businesses. The problem with this approach is that the skill base and training in opening and managing businesses is often missing from the community and from the people who most need it. Franchising may help in this respect.

Franchising has long been touted as a method of development for small economies. Franchising brings to a local economy a wealth of expertise and a system of doing business that may not be available otherwise.

Among the economic impacts are job creation; output creation tax revenue creation; economic clustering; economic modernization; entrepreneurship development; labour force improvements; as well as increases in innovation, competition, and efficiency.

In a recent study of the US franchise sector conducted for the International Franchise Association, Franchise Recruiters Ltd (2003, p.2) concluded that "franchising is a foremost force in the creation of the US entrepreneurial revolution that continues to fuel the lethargic economy, producing new business owners and jobs."

- Ilon Alon (2006)

Service Franchising – A Global Perspective