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| Vol.XIX, Issue 1 Welcome to this fall issue of **Franchisor Pipeline**®. This newsletter supplements our website: [www.FranchisorPipeline.com](http://www.franchisorpipeline.com).In the sections that follow, we provide you with new insights and developments related to the buying and selling of franchisors.In our **FranLight**® section below, the spotlight is on how to negotiate a multi-unit franchise deal with private equity.In our **FranPost**® section below, learn about the key recent developments that have taken place in “THE Marketplace for Buying and Selling Franchisors,” including:• New listings of franchisors at [**Franchisors4Sale**](http://www.franchisorpipeline.com/franchisors4sale/)®• New press releases and articles at [**Franchisor Equity News**](http://www.franchisorpipeline.com/news/franchisor-equity-news/)®• New private equity ownership and listings at [**FranVestors**](http://www.franchisorpipeline.com/franvestors/)®• New publically-held franchisors at [**Franchisor Folio**](http://www.franchisorpipeline.com/stocks/franchisor-folio/)®• New suppliers to franchisors at [**Brets-List**](http://www.franchisorpipeline.com/brets-list/brets-list/)®• New blogs at [**SellBuyBlog**](http://www.franchisorpipeline.com/blog/sellbuyblog/)®If you have a franchisor for sale – or a franchisor looking for an investor – please contact me confidentially to obtain a free and anonymous listing, or to learn more about our website.We hope that you enjoy this newsletter.***Bret Lowell***Founder, Franchisor Pipeline703-773-4242 (o)202-365-0965 (m)bret@FranchisorPipeline.com |
| **FRANLIGHT®**

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|  | **Private equity acquisition of multiple-unit franchises: 8 likely negotiation points**Private equity firms have historically been interested in owning franchisors. Due to the limited number of franchisors, and the high multiples at which franchisors have been selling, PE firms are increasingly acquiring multiple-unit franchises by transfer from existing franchisees. |

Transfer provisions in franchise agreements usually require that a buyer:1. be approved by the franchisor (based on an existing track record, existing financial statements, and adequate equity ownership)
2. execute the then-current form of franchise agreement
3. provide a guarantee of payment and performance
4. attend training, and
5. execute confidentiality and non-compete covenants.

Due to the structure and nature of PE firms, these requirements can present hurdles to buyers that are PE firms, and a franchisor may use the PE firm’s inability or refusal to fully satisfy these requirements as a basis to try to deny consent to transfer.For example, the entity proposed by the PE firm to be the franchisee is likely to have no track record and no prior financial statements and to be highly leveraged. Also, it is unlikely that anyone at the PE firm will be ready to – as the then-current form of franchise agreement will probably require – provide a guarantee of the franchisee’s obligations under the franchise agreement, have (as to both the owner and potentially the manager) an unencumbered minimum equity stake, attend training, or personally sign confidentiality and non-compete covenants. However, after weighing the legal and practical consequences of such a denial, franchisors will often negotiate their traditional approaches to these provisions and be flexible about their policies in order to facilitate a transaction with a PE firm.Legally, if a franchisor unreasonably withholds its consent, an existing franchisee may bring claims for breach of contract, breach of the covenant of good faith and fair dealing, or tortious interference. While the claims for breach would belong only to the selling franchisee, both sellers and buyers have sought to bring tortious interference claims.**Advantages and disadvantages of negotiating with a PE firm**From a practical perspective, and beyond the general desire to avoid litigation, there are often advantages and reasons why a franchisor should be willing to negotiate with a PE firm and thereby bend when it comes to its usual requirements and policies pertaining to transfer. There can also be disadvantages to providing this flexibility.On the advantage side, PE firms have the potential to infuse significant capital into the franchisor’s system through the renovation of existing units and the construction of new units. In turn, such investment can enhance the brand in a way that leads to greater overall system revenue and royalties and higher resale values system-wide.On the disadvantage side, there are a number of unfavorable aspects to private equity involvement. PE firms generally have a short-term strategy (about seven years) through which they seek to return investor money and earnings. And, because they are driven almost exclusively by financial returns, PE firms may close marginal units without regard to brand, development obligations or breaches of the franchise agreements.**Likely negotiation points**To overcome these differences, franchisors and PE firms typically need to negotiate and modify owner/operator, training, confidentiality, financing, non-competition, transfer, guarantee and cross-default requirements. Specifically, PE firms are likely to negotiate:**Owner/operator requirements.** As PE firms generally have a unique ownership structure not suitable for standard franchise agreements, they may need to modify owner/operator equity requirements.**Training requirements.** Private equity executives are unlikely to be willing to attend the training (or at least extensive training) typically required under standard franchise agreements.**Confidentiality requirements.** Confidentiality obligations may need to be tailored in a manner that allows private equity executives to oversee other portfolio companies that may operate in a same or similar field.**Financing requirements.** Provisions and policies requiring franchisor approval of franchisee financing arrangements likely will need to be changed so that, at most, the franchisor will receive notification of new franchisee financings.**Non-competition requirements.** PE firms are likely to want to do “bolt-on” acquisitions of businesses that they can add to their franchise portfolio (eg, other franchises from within the same system), and, more contentiously, may desire to acquire other businesses that operate in the same or a similar space.**Transfer requirements.** A “not unreasonably withhold consent” qualification on a franchisor’s approval rights may provide the PE firm with the comfort it needs to transfer the franchises according to its exit strategy, but even more unrestrained freedom to transfer may be requested. Of potentially greater concern to a PE firm would be provisions in the franchise agreement that restrict minority transfers, transfers of beneficial interests (ie, interests in the fund that owns the portfolio company franchisee) and provisions calling for franchisor approval of heirs and representatives of such persons upon death or disability.**Guarantee requirements.** In lieu of a guarantee from the PE firm of the portfolio company’s obligations to the franchisor, the franchisor may instead be willing to receive a letter of credit, or simply rely upon a strong balance sheet that remains above certain minimums.**Other requirements.** If multiple franchise agreements contain cross-default provisions, and it is the intent of the PE firm to shutter certain non-performing units, the PE firm may seek franchise agreement changes that allow for such closures without risking a default under franchise agreements other than the one that corresponds to the closure.**PE firm ownership: a trend likely to continue**In sum, PE firm ownership of multiple-unit franchises is a trend that is likely to continue at a significant pace. The process of acquiring such a franchise is similar to the transaction in which a PE firm acquires a franchisor (ie, entailing a bidding process; a Memorandum of Understanding; a purchase agreement, including representations, warranties and schedules; due diligence, including of franchise aspects; and a closing). Unlike such franchisor transactions, the acquisition of a multiple-unit franchise entails not just the assignment and assumption of existing franchise agreements but also the negotiation and entry into non-standard franchise agreements with the franchisor that reflect the special circumstances that PE firms present.***Bret Lowell delivered an earlier version of these comments at the American Bar Association’s 41st Annual Forum on Franchising.*** |

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| Key developments in the franchisor marketplace were recently reported on [**Franchisor Pipeline**](http://www.franchisorpipeline.com/)**®**.  Please visit: * [**Franchisors4Sale**](http://www.franchisorpipeline.com/franchisors4sale/)**®** for these seller additions:
	+ Casual BBQ Franchisor
	+ Pet Services Franchisor
	+ Healthy Casual Dining Franchisor
	+ Casual Dining Franchisor
	+ Women’s Fashion Franchisor
* [**Franchisor Equity News**](http://www.franchisorpipeline.com/news/franchisor-equity-news/)**®** for these news additions:
	+ Jimmy Johns Goes 2 Inspire Brands
	+ Gigi’s Cupcakes Goes 2 Elite Restaurant Group
	+ Papa Murphy’s Goes 2 MTY
	+ Blackstone acquires Servpro
* [**FranVestors**](http://www.franchisorpipeline.com/franvestors/)**®** for these private equity additions:
	+ The Halifax Group, which now owns Pirtek
	+ TPG**,** which now owns Club Pilates
	+ Levine Leichtman Capital Partners, which owns Mountain Mike's
	+ Argosy Private Equity, which now owns Rita's
* [**Brets-List**](http://www.franchisorpipeline.com/brets-list/brets-list/)**®** for these supplier additions:
	+ Yodle, under *Advertising*
	+ SMB Advisers, under *Franchise Consultants*
	+ FranConnect, under *Software*
	+ Franchise Architects, under *Franchise Consultants*
* [**Franchisor Folio**](http://www.franchisorpipeline.com/stocks/franchisor-folio/)® for these new publicly-held listings:
	+ **Bento**
	+ **Burger King, Popeye’s**
	+ **Freshii**

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