June 2002

AFA Blast Fax!

Representing the interests of small business franchisees nationally.

American Franchisee Association
53 West Jackson Boulevard, Suite 205
Chicago, Illinois 60604
312-431-0545

www.franchisee.org

Location, Location, Location; Finding a Good One

By Paul M. Sill, President
Forum Analytics, L.L.C.

There are a rare few franchisees fortunate enough to obtain accurate, objective market intelligence during their site selection process. In some instances, the parent company will provide basic information from which primitive assessments can be drawn, however if you're investing your life in a business, you need more than a "gut instinct" or basic market demographics before choosing a location. There are specialized analytic techniques available which will help you estimate your first year sales potential that won't break your bank, but may save your business.

The best approach is to gather as much information about existing franchise locations similar to the one you plan to open. Information can be collected about customer trade area, sales potential, demographics, and competitive importance. You'd be surprised how much information can be gathered with a minimal amount of effort. You'd also be surprised at how little information you need to collect before you can make accurate statistical assessments of your sales potential at any given location. Here's an example where objective market research can really pay off in the long run: *Continued on page 2*

"Franchisees represent strong, entrepreneurial democratic men and women, and if you treat them that way, you have peace in the valley."

-- John R. Neal, 140-unit KFC Franchisee, Nation's Restaurant News, May 20, 2002

AFA Mission Statement

The mission of the AFA is to promote and enhance the economic interests of small business franchisees.

Is a PEO a Viable Option for Your Business?

By Peter J. Kaye
Reprinted with permission from the Pennsylvania CPA Journal, a publication of the Pennsylvania Institute of Certified Public Accountants.

A PEO, or Professional Employer Organization, is a company specializing in human resource management. A PEO will contractually assume responsibility for all human resource-related functions for your business and its employees including interviewing and hiring assistance, payroll management, employee benefit design and administration, and administration of federal and state workplace regulations.

When you hire a PEO, your business and the PEO become co-employers with the PEO effectively becoming your off-site personnel department. This relationship can result in significant cost savings for you and your personnel department by reducing paperwork and human resource administration time.

It is estimated that PEOs currently employ 2-3 million Americans. PEOs exist in every state of the country with approximately 2,000 different PEO companies. The industry is growing 20-30 percent each year.

How PEOs Work

A PEO is an organization that "hires" your employees. The PEO generates paychecks for your employees and administers the filing of all related payroll tax deposits and monthly, quarterly and annual returns. The PEO bills your company for payroll, tax liabilities and fees for health, worker's compensation and unemployment insurance premiums in addition to the PEO's administration fee. With such a large pool of employees from various companies, the economies of scale allow for a vast array of benefits *Continued on page 3*

THE AMERICAN FRANCHISEE ASSOCIATION

Location, Location, Location *Continued from page 1*

There are two sites, identical in size, available for your franchise location,but one site is $20 per square foot and one is $35 per square foot. Your gut instinct may be to sign the lease for the $20 location since it's so much less expensive. However, a comprehensive market analysis reveals that the $35 location is going to yield 180% more revenue, making it a better long term investment for your business. It is generally a good idea to have an expert analyst working with you to perform the assessment and acquire the necessary data. While this analysis may sound complicated or costly, there are a number of resources available that are cost effective. Remember, research is an investment in your business. It can make all the difference between your success and failure and if performed properly can ensure that your business has the best chance for a long and successful life.

Sales Diversion

Sales diversion may be the greatest threat to long-term financial viability for any consumer-oriented business, yet there are few well documented approaches to understanding this complex problem. At all levels of franchising, the ability to forecast with a known degree of statistical certainty what impact new units will have on existing ones would prove to be an invaluable planning tool.

Multi-Unit Operators

For existing franchise networks looking to expand or assess the impact of new units in close proximity, there are two basic approaches that can be implemented to forecast sales diversion. The first involves the use of customer specific data, the second involves the use of statistical probability and the laws of retail gravity. Customer specific data is the preferred and most accurate method for calculating sales diversion. It requires the collection of household level consumer data via one of several methods; credit card data, in-store raffles or drawing, membership data, automobile license audits, or intercept surveys. For smaller franchisees, the data collected from a raffle can prove invaluable to the sales diversion modeling process.

Customer household data can be tracked back to existing units and through the use of geographic modeling techniques, valid assumptions and forecasts can be made about the future of consumer behavior. For example, if you have 500 existing customers in zip code 60647 today, but a new competing unit opened up in zip code 60647, spatial modeling would forecast how many of those 500 customers would be lost to the competing location. A sales per customer ratio can then be assigned to the value of each customer to determine actual sales impact in many cases.

Probability modeling (also known as gravity modeling) is generally used in the absence of historic sales or customer data. Probability modeling assumes that, all things being equal, consumers will be attracted to the closest retail option in direct proportion to the size of that retailer and inversely proportional to the distance from it. By understanding the total potential for a business in an area, gravity models assign a proportion of the total potential to each independent unit. This methodology allows a planner to play what-if scenarios in assessing the impact of new units in different locations.

One- or Two-Unit Operators

For the smaller franchisee, looking to protect one or two locations from a parent company's encroachment, the techniques described above can also be applied. In every case however, data collection is critical. The more data collected, the more accurate the encroachment assessments. When possible, leveraging franchise associations with many hundreds of members is a great way to collect data for a large sample of locations that will assist in the accuracy of the encroachment analysis for all franchisees.

Any consumer-based business can benefit from the use of slightly more advanced analytic techniques when planning their growth and future. These techniques are highly cost effective when weighted against the losses associated with selecting sub-par retail locations, over-saturation of a market place, or poor planning for the impact of encroaching businesses.

Welcome!
New Association Members

Dairy Queen Operators Association (DQOA)

Independent Organization of Little Caesar's Franchisees (IOLCF)

How PEOs Work *Continued from page 1*

and services at a significantly reduced cost.

Interestingly enough, the Internal Revenue Service views the PEO as the employer of record and is liable to pay the federal income and unemployment taxes, whether or not the client company pays the PEO. Most (but not all) states recognize the PEO as the responsible entity for payment of state unemployment taxes. PEOs also provide employees with coverage under all employment laws and regulations including federal, state and local discrimination laws. This includes Title VII of the 1964 Civil Rights Act, Age Discrimination in Employment Act, ADA, FMLA, HIPAA, Equal Pay Act and Cobra.

Advantages and Disadvantages of a PEO

There are several advantages to entering into a business relationship with a PEO. Some of them are 1) potential significant cost savings in hiring a PEO versus a full-time employee, 2) significant reduction in paperwork volume, 3) a wider array of employee benefits, 4) full-time compliance of payroll, EEOC, etc. and 5) worker's and unemployment claims management.

According to the National Association of Professional Employer Organizations (NAPEO), "NAPEO members report an average of 14 worksite employees per client company with an average gross pay of $19,659. The average annual cost of regulation, paperwork, than 500 employees is about $5,000 per employee, and tax compliance for firms with fewer comp ared with $3,400 per employee for firms with more than 500 employees. The average small business owner spends between 7 percent and 25 percent of his or her time handling employee related paperwork."

The disadvantages of a PEO include having an employer's potential perceived loss of control of his or her employees. Although the employer continues to have the ultimate authority in maintaining employee efficiency and output, the PEO shares and retains the right to hire, reassign and fire the employees. This sharing of responsibility may make an employer feel that he or she has lost some control in the management of his/her workforce.

Another consideration would be the employee's perception of the change seeing the PEO's name on a paycheck. This may make the employee feel that he or she is now working for a different company. These types of and concerns must be addressed when examining the PEO relationship.

Would Your Business Benefit from a PEO?

In examining the potential benefits of a PEO and whether this type of relationship would be right for your company, you must consider several factors. For instance, does your company need a PEO to perform these human resource tasks? In answering this question, consider whether your company suffers from a high turnover rate. Do your employees frequently complain about the company's "below average" benefit plan? Do you spend a significant amount of time handling unemployment and worker's compensation claims and administration? If you answer "yes" to these questions you should research the possibility of hiring a PEO to handle the human resource function for you. A PEO may offer you significant cost savings via reduced personnel requirements and reduced paperwork.

AFA Affiliate Member Peter Lagarias, Esq. joined AFA President Susan P. Kezios last month for a series of meetings on Capitol Hill in Wahsington ,D.C.

AFA Blast Fax!

The American Franchisee Association (AFA) is urging Congress to pass the Kyl/Graham Amendment which would permanently repeal the estate tax. We urge all AFA members to contact their Senators to vote in favor of permanent repeal of the estate tax. For more information contact Samuel Crawford, Director of Public Policy: 312-431-0545 or SJCrawford@franchisee.org.

THE AMERICAN FRANCHISEE ASSOCIATION

May 29, 2002

Honorable Jon Kyl
United States Senate
SH-730 Hart Senate Office Building
Washington, DC 20510-0304

Dear Senator Kyl,

I am writing to you on behalf of the 30,000 small businesses that are members of the American Franchisee Association (AFA), a national trade association of small business franchisees. We want to thank you for your support of the nation's small business owners by seeking permanent repeal of the estate tax through the Kyl/Gramm amendment.

AFA members employ over 350,000 workers and generate hundreds of millions of dollars in revenue. They are the men and women who pay upfront fees to a franchisor and invest their capital to establish the local franchised small business. Like all small business owners they hire the employees, pay the taxes and contribute to their local communities in a multitude of ways.

My members are very concerned about the negative effect the estate tax has on their businesses, their families and the U.S. economy. The estate tax actually punishes these small business owners for having been successful entrepreneurial risk takers. The estate tax taxes an entire family on acquired income that has already been taxed once. It robs small business owners of revenue that could be reinvested in their businesses by forcing them to engage in expensive "estate planning." The estate tax is a disincentive to saving, business expansion and job creation.

We strongly support the Kyl/Gramm amendment and we thank you for your leadership in seeking permanent repeal of the estate tax.

Respectfully,

Susan P. Kezios
President

OVER 30,000 OUTLETS STRONG

53 West Jackson Boulevard, Suite 205, Chicago, Illinois 60604
TEL 312-431-0545 FAX 312-431-1132

MEMBERSHIP DOES NOT COST, IT PAYS

THE AMERICAN FRANCHISEE ASSOCIATION