



April 2003

Representing the interests of small business franchisees nationally.

American Franchisee Association
53 W Jackson Blvd, Suite 205 — Chicago, Illinois 60604
(312) 431-0545 www.franchisee.org

MARK YOUR CALENDAR!!

AFA Franchisee Leadership Summit

Leadership Summit ...

- April 29 in Chicago
- 9 am to Noon
- Guest speaker

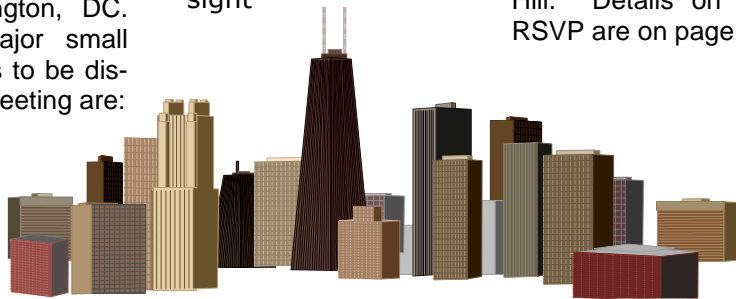
W. Timothy Locke

The Smith-Free Group

The Board of Directors of the American Franchisee Association (AFA) is holding a Franchisee Leadership Summit from 9 am to 12 noon on Tuesday, April 29th in Chicago. Also attending the Summit is W. Timothy Locke, Senior Vice President of The Smith-Free Group, a Washington, DC-based lobbying firm. Mr. Locke will explain what it takes to accomplish political agendas in Washington, DC. Among the major small business issues to be discussed at the meeting are:

- Health Care and Association Health Plans
- Payroll Taxes
- Minimum Wage
- Accelerated Depreciation
- Regulatory Reform
- Federal Trade Commission (FTC) Oversight
- Non-Compete Clauses
- Mandatory Arbitration Requirements
- Repeal of the Estate Tax.

We hope that you will choose to join us in order to forge a unified franchisee presence on Capitol Hill. Details on how to RSVP are on page 6.



RISING HEALTH INSURANCE COSTS TOP DOMESTIC AGENDA

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Franchisees are beginning to see the real impact of rising health insurance costs on their profitability. In response to member requests, the American Franchisee Association (AFA) has taken steps to address this issue. The AFA has been working to develop a program that

will result in reduced health insurance costs for both franchisees and their employees by "pooling" AFA's buying power.

In November 2001 the American Franchisee Association (AFA) began a dialogue with AON Corporation regarding the crea-

tion of a "health benefit program." We organized a working group of AFA members associations to spearhead the programs development. This working group had its first formal presentation on "health and welfare benefits programs" in April of

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RISING HEALTH INSURANCE COSTS TOP DOMESTIC AGENDA

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2002 at AON Corporation's headquarters in Chicago.

Finding ways to reduce the cost of health care is also a top priority item for the Bush administration. One of the cost reduction methods being discussed in Washington and elsewhere is the use of association health plans (AHPs). AHPs will allow small businesses to pool their buying power and negotiate lower health insurance premiums. These plans could

reduce premiums for small businesses by an average of 13% according to the Congressional Budget Office (CBO).

AHP legislation has now been introduced in both the House and Senate. Both bills will allow small businesses to band together to buy health insurance through a national trade association or professional society. This legislation could greatly assist AFA in its efforts to provide low cost health insurance for franchisees.

WANT TO REDUCE YOUR HEALTH INSURANCE COSTS?

In order to develop a successful "franchisee pool" we need the input of as many franchisees as possible. We invite your franchisee association to join AFA's Health Insurance Committee. If you are interested contact Samuel Crawford at 312-431-0545 or sjcrawford@franchisee.org

AFA ARCHIVES

To commemorate the 10-year anniversary of the AFA, we bring you yet another vignette from the AFA's history. This installment of the AFA Archives focuses on the AFA's success in 1996 at influencing the U.S. Small Business Administration (SBA) in introducing a "supplemental agreement" for franchisors whose franchisees receive SBA loans.

In the summer of 1996 AFA President Susan P. Kezios received a phone call from the U.S. Small Business Administration's Associate Deputy General Counsel Ron Matzner. Ever since the 1995 White House Conference on Small Business (WHCSB) the SBA had become more aware of and sensitive to franchisee problems such as encroachment, franchisor handling of supply sources, arbitrary terminations and denial of renewal rights. Mr. Matzner explained to Susan that the SBA was exploring a requirement that franchisors attach a supplemental agreement to their form franchise contracts if the franchisors' franchisees sought SBA loan funding. Mr. Matzner was looking for a top dozen list of issues from the AFA to be reviewed by the SBA for inclusion in the supplemental

agreement.

Susan asked Mr. Matzner about the types of provisions the SBA was currently considering for inclusion. He listed franchisees' right to a protected territory and franchi-

Mr. Matzner was looking for a top dozen list of issues from the AFA.

sors' ability to handle franchisees' accounts receivable on a short list. Mr. Matzner said that the overall purpose of the supplemental agreement would be to take the burden off the local SBA loan processors, who had to go through each individual franchise agreement to make sure there were no conflicts with laws, regulations and policies before approving a loan. Susan was, quite frankly, surprised at the SBA's aggressiveness on

behalf of franchisees, but she welcomed the opportunity to protect franchisees' property rights and add the AFA's input.

On subsequent phone calls, Mr. Matzner said the SBA was looking for as much feedback as possible. He asked Susan to recommend

franchise lawyers—both from the franchisee and franchisor side of the fence—to whom he could send a draft of the supplemental agreement. Susan obliged and forwarded to Mr. Matzner a list of both franchisee and franchisor lawyers.

What Susan *didn't* know was that Mr. Matzner sent copies of the draft supplemental agreement

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AFA ARCHIVES

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and a cover letter on SBA letterhead from him that began, "Susan Kezios recommended you as a recipient to review...". She found out about the letter from members of the press. She also found out from members of the press that there was a great outcry from the franchisor lawyer side of the fence regarding not only the SBA's proposal for a supplemental agreement but also about the AFA's input into the process. Where franchisor lobbyists had traditionally held sway, the AFA had made important friends.

In an article entitled, "SBA Borrows AFA Agenda," Neil Simon, Esq., then of Hogan & Hartson said, "Its obvious the AFA has made significant inroads into the SBA. They're trying to get through the back door what they couldn't get in through the front door (through legislation)" (*Continental Franchise Review*, July 12, 1996). In "SBA Proposal Sends Shock Wave" the rhetoric increased, "I'm afraid this will end up being (AFA President) Susan Kezios' rubber-stamped list of approved franchisors," said Jerry Wilkerson (*Franchise Times*, Sept. 1996).

The draft form of the supplemental agreement was a four-page legal document between the franchisor, franchisee and SBA. Included in the original draft were provisions that dealt with renewal, leasing and subleases, sourcing of supplies and encroachment. A

series of meetings in the fall of 1996 were scheduled at SBA headquarters in Washington, DC with franchisee lawyers, franchisor lawyers, bankers and SBA officials to hammer out the details of the supplemental agreement. Each meeting was highly charged with both sides (franchisee and franchisor) openly debating the

"Its obvious the AFA has made significant inroads into the SBA."

issues. The supplemental agreement met with strong resistance from the franchisor side of the fence. They were not interested in meeting franchisee lawyers half way. The negotiation process was at an impasse.

In response to the whining of franchisor lawyers about the "unfairness to franchisors" of the supplemental agreement, Mr. Matzner transmuted the document into a central electronic registry of franchise concepts pre-approved by the U.S. Small Business Administration (SBA) for loans. "As we initially proposed it, franchisees would have been beneficiaries," said Ron Matzner, "As its come out (the registry) satisfies the SBA's requirements. As for the other issues affecting the franchise industry, franchisees are going to have to deal with them in some other way (*Franchise Times*, February 1999)."

Susan Kezios, President of the AFA minced no words when she

said, "(Matzner) has rolled over on us. All the registry does is enshrine the very inequities we're trying to get rid of." Franchisee attorney Eric H. Karp charged that the SBA created "an anemic set of procedures which pretend the franchisee is not even a party to the transaction (*Franchise Times*, February 1999)."

Although the supplemental agreement did not survive, the SBA's Franchise Registry exists as a direct result of the AFA's public

policy work in those early years. Today franchisors that exert an inordinate amount of control over their franchisees are denied listing on the registry. As a result, many of them have been known to regularly change their franchise agreement provisions in order to be included. A small victory, but a victory nonetheless for the American Franchise Association (AFA).



Membership does not cost, it pays!

LEGAL BRIEF

SUBWAY'S TRAIN STOPPED A Case Study By Marc N. Blumenthal, Esq.

In late December 2002 I was contacted by a multi-unit Subway franchisee to enlist my services. In a nutshell, his problem was encroachment. Knowing the lack of encroachment protection in Illinois for franchisees, I advised that this was an uphill battle, and that the case law would not favor his position. The Subway franchise agreement, not unlike many other fast-food franchises offers no territorial protection. Common sense would dictate that placing one like brand too close to the next might be poor business judgment. Unfortunately, common sense does not usually prevail in these situations.

After advising the fight would be costly, and no guarantees would be given that a successful outcome would result, the soon to be encroached upon franchisee retained me. In our early discussions, I learned that the prospective encroaching franchisee would be seeking a special use permit from the zoning agency, and the matter was scheduled to be heard by the zoning board. Armed with this information, I decided a two-pronged approach would be the best strategy. Given that the prospective Subway was to be located less than three blocks away, on the same street, in the downtown of a large metropolitan area suburb, and realizing that my client's store had been there for over ten years, I

drafted a long and informative letter to Subway, alerting that company of the mistake it, and its development agent was about to make. This spawned an investigation to determine feasibility--so we were informed. We were quite surprised when we were promptly informed that Subway determined there would be no real impact and that brand awareness would increase! In its rejection letter, Subway said, "the Site Review Committee carefully reviewed all the information submitted and decided to move forward with the proposed location." Knowing this was not what we wanted to hear, Subway stated, "I hope you were nevertheless pleased with the overall site review process," and that "the objective had been met in this case." They really got that one right. Subway, verbally, however, assured me that if my client got hurt, Subway would make amends. What compassion! To paraphrase an old adage, thank goodness there is more than one way to thwart the greedy plans of a franchisor.

Fortunately, this was not the end of the line. The local zoning board was scheduled to take up the application at their next meeting, which prompted my second letter. Understanding that competition could not be considered, I reviewed the locality's standards, studied the prospective franchisee's application, and appeared at

the hearing with other restaurant owners who agreed to support the opposition. On the other side of the table was the landlord, Subway's development agent and the prospective franchisee, who was willing to agree to almost every restriction the zoning board and councilmen wanted to place on his special use grant. This included picking up garbage three or four times a day, within 250 feet of the store in all directions. I pointed out how impractical that was, since that distance would take him into a park, onto a college campus, and in front of countless other restaurants and stores.

Given the opportunity to cross-examine the applicant, I pointed out that certain parts of the application raised some questions. I also informed the gathered board members that the applicant could not possibly guarantee he could be there for five years, since his existence as a sub-tenant and franchisee would be subject to compliance with the franchise agreement. Finally, I pointed out that the only reason we were even discussing this matter was the absence of an encroachment law, and to consider placing another restaurant of the same brand less than three blocks in a suburb was preposterous. Notwithstanding further arguments related to what amounted to a

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SUBWAY'S TRAIN STOPPED

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"negative cumulative effect", by increasing an already intolerable garbage problem, on a street that had become a "food court" the zoning board unanimously approved the special use, with many restrictions. With our hopes partly shattered, and having been turned down by the franchisor, and now the zoning board, we felt we were too far invested to give up.

The next step was the committee that hears these applications, after the zoning board approves them. That committee, unlike the zoning board is made up of members of the council, the real decision-makers in this locality. I had begun to lobby one of the key members of the council, whom I learned was undecided. This gentle lobbying continued throughout the process. I also sent the councilmen a letter to explain the situation, trying to stay in the forefront. At the first committee meeting, the prospective franchisee, believing victory was at hand, looked at me and said, "I did not think I would see you again." Having been bloodied in franchise battles before, I told him that "we did not give up that easily."

The purpose for the first committee meeting was to hear from the applicant and any opposition. Since the transcript from the zoning board hearing had not been completed, the meeting was shortened. Before the meeting ended, one of the councilmen told the applicant that Subway's development agent must come to the next meeting, since he had some concerns. I disclosed that the

arrangement with the development agent and Subway was one of the reasons for him to push this application, and the prospective franchisee. This peeked their interest. At the next meeting, the Subway development agent answered the councilmen's questions, and confirmed my disclosure which did not help the applicant. At this meeting, the committee was required to decide whether to introduce the application to the full city council. After extensive discussion, and an unexpected appearance by the senior councilmen who practically called for a moratorium of these types of permitted special uses, the committee decided it would introduce the application, but not present it for a vote which was to take place in two weeks. I sensed a crack in the support, and believed there might be a chance to get a rejection. I immediately signed up to address the entire city council at its meeting later that evening. In my televised presentation, I stressed the affect this extra Subway would have, and that it would add nothing new, it would not help the environment related to the garbage problem; it would have a negative cumulative effect, and that the senior councilmen had railed against it, even calling for a moratorium of these types of uses.

The final meeting date arrived. The vote would be taken, and this long process would come to an end. The room was tense. The applicant had now been in the pipeline for many months. Subway had approved the site, and turned down my client's plea. The zoning board had unanimously approved the applicant, albeit with

restrictions. The committee had agreed to introduce the application to the full city council. Then, something happened. The atmosphere changed. The councilman I had been lobbying began to make a case for rejection. The next councilman to speak did the same, and within 30 minutes a motion was unanimously passed to reject the application. I was dumbfounded and gratified at the same time. My client was getting excited. We knew there was one more hurdle to get over, as the full city council has almost twice as many members, and could have approved the application. In a vote of 8-1, the full city council voted against the application, rejected the special use permit, and brought Subway's train to a screeching halt. An enlightened city council made the right decision for the right reasons. The encroachment was prevented, and the current Subway franchisee can continue to grow his business without the threat of another Subway store to cannibalize his efforts.

Before undertaking an effort such as this one, however, check your franchise agreement to make sure this type of protest is not prohibited. I recently reviewed the franchise agreement for Dunkin' Donuts, Baskin Robbins and Togo's where the exact activity described above—contesting the right of a prospective franchisee to obtain a zoning variance for the development of another location as proposed by the franchisor—is a material breach of the contract (both during the contract term and for 2 years after its expiration!)

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312-431-0545
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Franchisee Leadership Summit

Tuesday April 29, 2003 — 9:00 AM - Noon
 53 West Jackson Blvd., Suite 826
 Chicago, Illinois 60604

Meet W. Timothy Locke, VP
The Smith-Free Group

- Help prioritize top small business issues for franchisees.
- Help determine franchisees' political and legislative agenda.
- Help shape franchisees' political and legislative strategy.

PLUS

Learn How to Save 20% on Health Insurance

RSVP to Samuel Crawford
312-431-0545
sjcrawford@franchisee.org

For those arriving in Chicago on Monday night the AFA has reserved a block of rooms at the Hyatt on Printers Row, 500 South Dearborn, one block from the meeting location, 312-986-1234. Tell them you are attending the Franchisee Leadership Summit to receive a rate discount.



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