Implementing Change in Franchised Restaurant Systems

By Edward (Ned) Levitt*

Change is inevitable; change is good; change costs; change too slowly and you are left behind; change too often and you confuse your customer. When you own your own restaurant(s) you can change whenever and whatever you want. When you want to change how your franchisees operate **THEIR** restaurants, that is a horse of a different colour.

Decades ago the marketplace evolved over many years. Today, shifts in any number of important areas can take place seemingly overnight. Anyone heard of trans fats 2 years ago? A franchisee looks to the franchisor to be on top of such changes in the marketplace, to investigate what needs to be done and the best way to implement the changes. This is one of the great values in being a franchisee in a good system. Franchisors need to have the ability to implement necessary changes through their network of independent franchisee operators as thoroughly and efficiently as possible.

Serious problems and conflicts arise when the changes are for the advantage of the franchisor, not in reaction to some marketplace issue. For public franchisors, increased head office profits often translate into increased share prices; the goal of most CEO's of publicly traded franchisors. Unfortunately, while some changes produce such benefits for franchisors by increasing profits for franchisees as well, other changes increase profits for franchisors at the expense of franchisees.

A properly drafted restaurant franchise agreement gives the franchisor the right to require franchisees to implement changes to the system as required by the franchisor from time to time. However, there are both common law and statutory restrictions on the unfettered exercise of such rights to the unjustified detriment of the franchisee. There are also situations where the courts have sided with franchisees in finding that the contractual language did not permit the exercise of the power the franchisor thought it had. In recent years, we have witnessed a number of cases, some of them class actions, which have been decided against a franchisor who tried to force franchisees to makes such changes.

A change that demonstrably lines the pocket of the franchisor at the expense of the franchisees is unlikely to be supported by the courts. Most of the litigation in this area, however, has involved fact situations that were much less clear. Is it a justifiable change to require franchisees to add a product line with low or no margin to increase traffic? Can a franchisor force franchisees to invest significant capital in new equipment that may not show a net return for years? Rising costs, changing buying habits, demographic issues and much, much more are putting increasing pressure on restaurant businesses generally to change and bringing to the surface the inherent barriers to change in franchised restaurant chains.

Once these issues reach the courts, the facts, motives and actions of the franchisor are viewed, dissected and analysed with the brilliant clarity of hindsight. Franchisors can dramatically increase their chances of successfully implementing change and defending such change in court, if necessary, by adopting all or some of the following approaches:

1. Invest in solid third party research on the impact of the change on the franchisees and the system as a whole;

2. Invest in solid third party research on the impact on the franchisees and the system as a whole of not doing the change;

3. Bring any franchisee advisory council or association into the development and implementation stages as early as possible;

4. Spend the time and resources necessary to explain to the franchisees the reasons for and benefits of the change;

5. As much as possible, adopt any modifications that the franchisees may reasonably suggest and let it be widely known that the franchisees had an impact on the decision and nature of the change;

6. Ensure that internal communications at head office do not misstate the franchisor’s motives and business case for making the change;

7. Support the franchisees as much as possible in making the change and document that support thoroughly; and

8. Maintain statistics on the direct and indirect results of the change for individual franchisees and the system as a whole.

It should be kept in mind that, for the franchisor, change is a business issue, not an emotional one, but not all of the franchisees will react in a purely business minded way. The franchisees in most franchise systems come in all shapes and sizes, with varying personalities, attitudes and capacity for change. Often, how change is approached in a franchised restaurant system is as important as what is being changed.

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