# TABLE OF CONTENTS

Executive Summary........................................................................................................... 1
Survey Questions ............................................................................................................... 3
Factor Structure of Breakout Criteria............................................................................... 12
Analysis and Results ....................................................................................................... 14
Conclusion ....................................................................................................................... 16
Franchise Performance Index™ .................................................................................... 17
Resources ......................................................................................................................... 18
Disclaimer ......................................................................................................................... 18
About FranchiseGrade.com ............................................................................................. 19
EXECUTIVE SUMMARY

The purpose of the Franchise Grade® Franchise Expert Survey was to:

1. Validate specific variables that comprise components of the Franchise Grade Franchise Performance Index™ (see page 17)
2. Determine the value and level of importance franchise industry experts place upon franchisee performance indicators and related franchise system attributes.

The Franchise Performance Index is a proprietary analytical system that was designed by FranchiseGrade.com to evaluate, rank and measures the performance of individual and franchise sector performance. It differs from other franchise ranking systems in that the variables are not limited to the size of the franchise network and system growth but rather a number of measures. By conducting this survey we were able to determine that the variables used in the FPI™ were appropriate and applicable. Moreover, since the information in the FPI is gathered from Franchise Disclosure Documents subjectivity is virtually eliminated.

In order to perform the survey, participants were asked to respond to questions specifically related to franchise performance. In addition, they were asked to rank and compare the specific items contained in the questions. The survey factor structure and the methodology is explained in further detail on pages eight and sixteen respectively. Several hundred recognized franchise professionals with extensive franchise careers and backgrounds were solicited to participate. The respondent’s names were kept confidential. The result was that 158 respondents representing a cross section of franchisees, franchisors, franchisor and franchisee attorneys and franchise consultants participated. The survey questions were drawn from the Franchise Performance Index™, information contained in Franchise Disclosure Documents and franchise operational practices.

As expected, some respondents tended to differ in their responses depending upon their particular role in the franchise industry. For example, franchisor and franchisee attorneys could be expected to differ somewhat in certain responses and rankings. More detail is provided below in Conclusions.
Some of the more interesting survey results included:

- Franchisee satisfaction survey results were considered slightly more important than an Item 19 disclosure
- Negative franchise outlet growth was ranked more important than positive franchise outlet growth and whether or not the franchisor operated corporate locations
- Franchisee lawsuits were ranked less important when compared to both franchisor lawsuits and franchisor executive bankruptcies
- A franchise agreement providing an additional franchise renewal term was ranked slightly more important than the granting of an exclusive territory
- 47% of respondents stated that franchisees only sometimes understand the Franchise Disclosure Document

The responses to the survey questions provided valuable feedback on the importance and applicability of particular franchise practices.

We thank all franchise experts who participated in the survey.
SURVEY QUESTIONS and RESPONSES

How best would you describe your role within the franchise industry?

- 25% Franchisor
- 22% Franchisee
- 41% Franchisor lawyer only
- 6% Franchisee lawyer only
- 4% Franchisor and franchisee lawyer
- 1% Consultant
- 1% Accountant
Independent franchisee satisfaction data was ranked more important than an FDD providing an Item 19 FPR (Financial Performance Representation).
The respondents ranked negative franchise system growth as slightly more important than positive franchise system growth.
Lawsuits filed against the franchisor were seen as more important than lawsuits against franchisees.
Franchise industry experience on the part of the franchisor leadership group was more important than the number of years the franchisor was in business.
It is interesting to note that territory exclusivity was slightly less important than a minimum of one renewal term.
In your experience, does Item 7 (Estimated Initial Investment) within the FDD provide full disclosure of all expenses and costs related to the successful start up of a franchised business?
When reviewing alternative dispute resolution clauses what do you feel is the most reasonable structure for a balanced relationship?

- Binding arbitration with one arbitrator: 10%
- Binding arbitration with three arbitrators: 12%
- Mediation followed by arbitration: 12%
- Mediation followed by litigation: 13%
- No arbitration or mediation requirements: 53%

A Very Interesting Response was 53% of Respondents Favored Mediation Followed By Arbitration. The other Dispute Resolution Requirements were Evenly Divided.
Only 16% of respondents felt that prospective franchisees either always or often understand the Franchise Disclosure Document.
FACTOR STRUCTURE OF EVALUATION CRITERIA

With 20 items from question 1 to question 5 and responses from 158 participants (8 participants were dropped because of their “N/A” responses), we conducted a principal component factor analysis with varimax rotation. Our observations to items ratio for this analysis were 7.90 to 1, which surpassed the typical rule-of-thumb ratio of 5 to 1 (Hair, Black, Babin, Anderson and Tatham, 2006). Loadings of 0.35 or greater were considered meaningful for interpretation and were then assigned to the corresponding factors. After removing one item with high loadings on multiple factors (i.e., Positive Financial Outlet Growth), six factors with eigenvalues of greater than 1 had emerged and explained a total of 63.96 percent of variances. All items had positive loadings greater than 0.56 on their intended dimensions. Please see below for six factors and their corresponding items.

Factor 1, Financial Information, consists of “Franchisor financial statement analysis”, “The FDD has an Item 19 financial performance representation”, “SBA default analysis”, and “The franchisor operating company owned locations”.

Factor 2, Legal Concern, consists of “Lawsuits against franchisees”, “Lawsuits against the Franchisor”, and “Executive or corporate bankruptcies”.

Factor 3, Franchising Capability, consists of “Top Management Team Franchise Experience”, “Years franchising”, and “The size of the franchised network”.

Factor 4, Contract Terms, consists of “Has a minimum of a 10 year initial franchise term”, “Has at least one renewal term”, “Has at least a minimum of a 10 year renewal term”, and “Negative Financial Outlet Growth”.

Factor 5, Exclusiveness, consists of “Has some form of exclusive territory”, and “Has an exclusive territory with no or minimal exceptions”.

Factor 6, Supporting System, consists of “Independent Franchisee Satisfaction Data”, “That the system has an advisory council”, and “That the system has an independent franchisee association”.

Table 1. Description of evaluation criteria ratings of franchisors, franchisees & consultants.

<table>
<thead>
<tr>
<th>Constructs</th>
<th>Factor 1 Financial Information</th>
<th>Factor 2 Legal Concern</th>
<th>Factor 3 Franchising Capability</th>
<th>Factor 4 Contract Terms</th>
<th>Factor 5 Exclusiveness</th>
<th>Factor 6 Supporting System</th>
<th>Sample Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Franchisor (1)</td>
<td>3.88</td>
<td>4.09</td>
<td>4.19</td>
<td>4.19</td>
<td>4.17</td>
<td>3.68</td>
<td>39</td>
</tr>
<tr>
<td>Franchisee (2)</td>
<td>4.29</td>
<td>4.68</td>
<td>4.41</td>
<td>4.51</td>
<td>4.69</td>
<td>4.36</td>
<td>35</td>
</tr>
<tr>
<td>Franchisor lawyer only (3)</td>
<td>4.00</td>
<td>3.86</td>
<td>3.52</td>
<td>4.18</td>
<td>4.14</td>
<td>3.05</td>
<td>7</td>
</tr>
<tr>
<td>Franchisee lawyer only (4)</td>
<td>4.25</td>
<td>4.67</td>
<td>4.83</td>
<td>4.75</td>
<td>4.50</td>
<td>4.17</td>
<td>2</td>
</tr>
<tr>
<td>Franchisor &amp; franchisee lawyer (5)</td>
<td>4.23</td>
<td>4.37</td>
<td>4.47</td>
<td>3.93</td>
<td>3.45</td>
<td>3.70</td>
<td>10</td>
</tr>
<tr>
<td>Consultant (6)</td>
<td>4.18</td>
<td>4.52</td>
<td>4.21</td>
<td>4.22</td>
<td>4.24</td>
<td>3.79</td>
<td>63</td>
</tr>
<tr>
<td>Accountant (7)</td>
<td>3.88</td>
<td>4.33</td>
<td>4.83</td>
<td>3.88</td>
<td>4.25</td>
<td>3.17</td>
<td>2</td>
</tr>
<tr>
<td>Mean/Total</td>
<td>4.12</td>
<td>4.41</td>
<td>4.25</td>
<td>4.26</td>
<td>4.27</td>
<td>3.85</td>
<td>158</td>
</tr>
</tbody>
</table>
ANALYSES AND RESULTS

We conducted analysis of variances to test the differences in factor scores among franchisors, franchisees & consultants.

A one-way analysis of variance test indicated that different groups of participants have valued factor 1, Financial Information, differently (F[2, 134]=2.68, p<0.10). Franchisors rated this factor the lowest (M=3.88, SD=1.05), followed by consultants (M=4.18, SD=0.69), and franchisees (M=4.29, SD=0.60). A planned contrast test was performed to compare the ratings of factor 1 for the three groups. Using a two-tail test, the results indicated that franchisors provided lower ratings of factor 1 compared with franchisees (mean difference=-0.40, t=2.17, p<0.05) and compared with consultants (mean difference=-0.30, t=1.84, standard error = 0.43, p<0.10). However, there was no significant difference between the franchisees and consultants (p=0.54).

A one-way analysis of variance test indicated that different groups of participants have valued factor 2, Legal Concern, differently (F[2, 134]=6.38, p<0.001). Franchisors rated this factor the lowest (M=4.09, SD=0.91), followed by consultants (M=4.51, SD=0.76), and franchisees (M=4.68, SD=0.42). A planned contrast test was performed to compare the ratings of factor 2 for the three groups. Using a two-tail test, the results indicated that franchisors provided lower ratings of factor 2 compared with franchisees (mean difference=-0.58, t=3.37, p<0.001) and compared with consultants (mean difference=-0.42, t=2.81, p<0.01). However, there was no significant difference between the franchisees and consultants (p=0.31).

A one-way analysis of variance test indicated that there is no difference in the ratings of factor 3, Franchising Capability, among these three groups (F[2, 134]=1.34, p=0.27).

A one-way analysis of variance test indicated that different groups of participants have valued factor 4, Contract Terms, differently (F[2, 134]=3.02, p<0.05). Franchisors rated this factor the lowest (M=4.19, SD=0.69), followed by consultants (M=4.22, SD=0.63), and franchisees (M=4.51, SD=0.51). A planned contrast test was performed to compare the ratings of factor 4 for the three groups. Using a two-tail test, the results indicated that franchisees provided higher ratings of factor 4
compared with franchisors (mean difference=0.31, t=2.17, p<0.05) and compared with consultants (mean difference=0.29, t=2.20, p<0.05). However, there was no significant difference between the franchisors and consultants (p=0.84).

A one-way analysis of variance test indicated that different groups of participants have valued factor 5, *Exclusiveness*, differently (F[2, 134]=3.90, p<0.05). Franchisors rated this factor the lowest (M=4.17, SD=0.91), followed by consultants (M=4.24, SD=1.00), and franchisees (M=4.68, SD=1.00). A planned contrast test was performed to compare the ratings of factor 5 for the three groups. Using a two-tail test, the results indicated that franchisees provided higher ratings of factor 5 compared with franchisors (mean difference=0.52, t=2.54, p<0.05) and compared with consultants (mean difference=0.45, t=2.42, p<0.05). However, there was no significant difference between the franchisors and consultants (p=0.69).

A one-way analysis of variance test indicated that different groups of participants have valued factor 6, *Supporting System*, differently (F[2, 134]=9.09, p<0.001). Franchisors rated this factor the lowest (M=3.68, SD=0.83), followed by consultants (M=3.79, SD=0.66), and franchisees (M=4.68, SD=0.75). A planned contrast test was performed to compare the ratings of factor 6 for the three groups. Using a two-tail test, the results indicated that franchisees provided higher ratings of factor 6 compared with franchisors (mean difference=0.69, t=3.93, p<0.0001) and compared with consultants (mean difference=0.57, t=3.63, p<0.001). However, there was no significant difference between the franchisors and consultants (p=0.46).
CONCLUSION

Overall, franchisors and franchisees significantly differed in their ratings of these factors, except for factor 3. Franchisors and consultants displayed similar ratings on factor 4, factor 5 and factor 6, but differed in their ratings on factor 1 and factor 2. Franchisees and consultants displayed similar ratings on factor 1 and factor 2, but differed in their ratings on factor 4, factor 5, and factor 6. These findings illustrate that all three groups have placed different weights on these evaluation criteria, suggesting different rankings might be needed for different audiences.

Reference of Factors:

Factor 1, Financial Information, consists of “Franchisor financial statement analysis”, “The FDD has an Item 19 financial performance representation”, “SBA default analysis”, and “The franchisor operating company owned locations”.

Factor 2, Legal Concern, consists of “Lawsuits against franchisees”, “Lawsuits against the Franchisor”, and “Executive or corporate bankruptcies”.

Factor 3, Franchising Capability, consists of “Top Management Team Franchise Experience”, “Years franchising”, and “The size of the franchised network”.

Factor 4, Contract Terms, consists of “Has a minimum of a 10 year initial franchise term”, “Has at least one renewal term”, “Has at least a minimum of a 10 year renewal term”, and “Negative Financial Outlet Growth”.

Factor 5, Exclusiveness, consists of “Has some form of exclusive territory”, and “Has an exclusive territory with no or minimal exceptions”.

Factor 6, Supporting System, consists of “Independent Franchisee Satisfaction Data”, “That the system has an advisory council”, and “That the system has an independent franchisee association”.

© 2014 FranchiseGrade.com | reports@franchisegrade.com | 1 800 975 6101
FRANCHISE PERFORMANCE INDEX™

Unlike other franchise rankings methods, which are primarily based on the size and growth of an individual franchise system, the Franchise Grade Franchise Performance Index™ utilizes a number of franchise performance factors in addition to new franchisee growth. This provides a ranking based upon the same variables taken from each Franchise Disclosure Document.

A survey performed by FranchiseGrade.com resulted in responses from a cross section of over 158 franchisors, franchisee and franchisor attorneys, franchisees and consultants, who validated the importance of the variables utilized in the FPI™.

In addition to our FranchiseGrade.com statistician and research team the design of the FPI™ included Asst. Professor, Richard Chan of the StonyBrook University Business School, and Ed Teixeira, President FranchiseKnowHow,LLC.
REFERENCES


DISCLAIMER

This report product has been supplied by FranchiseGrade.com Inc. (‘FranchiseGrade.com’) for the sole use by subscribers and purchasers. No portion of this report may be reused, reproduced or distributed in any form without prior written consent.

All information contained within this report is obtained by FranchiseGrade.com from sources believed by FranchiseGrade.com to be reliable and accurate. Any forecasts, calculations or predictions contain within this report are believed to be accurate as the data and methods will allow. Due to the possibility of human or mechanical error, the information within this report is provided "as is" and no warranty of any kind is provided.

FranchiseGrade.com makes no representation to any person or entity with regard to the completeness or accuracy of the data and information contained herein, and it accepts no responsibility and disclaims all liability for loss or damage whatsoever suffered or incurred by any other person resulting from the use of, or reliance upon, the data or information contained herein.

Copyright of this publication is owned by FranchiseGrade.com Inc. All rights reserved.
ABOUT FRANCHISEGRADE.COM

FranchiseGrade.com is the leader in competitive market research and objective analysis for the franchise industry.

Our franchise assessment, grading and standardized reporting tools provide industry stakeholders with critical data driven metrics to support the growth of successful franchise systems. Our motivation is simple: we want to raise the bar in franchise industry market research and build a stronger franchise community.

FranchiseGrade.com provides custom research for greater understanding of franchise systems in this, or any, sector of the franchise industry. For more comprehensive reports and further interpretation of our research please contact us for a custom report or visit http://reports.franchisegrade.com

Contact us at:

1288 Commissioners Road West Suite 204 London, Ontario N6K 1E1 Canada

P: 1-800-975-6101 F: 1-800-975-6014 E: sales@franchisegrade.com