

## **Can franchising be applied to the not-for-profit sector?**

*Jason Gehrke, 2010.*

Franchising as a method of doing business has proven incredibly popular in the private sector since the post-World War II economic boom fuelled the growth of disposable incomes and fast food concepts in the west coast of the United States in the late 1940's.

The private sector has embraced franchising as a way of growing and replicating an existing and successful concept using the energy, enthusiasm and capital of smaller-scale entrepreneurs who invest their money and talent to clone businesses in pursuit of strong returns, a change of lifestyle, or both.

Franchising has thrived in the private sector to the point where the largest franchise brands in the world are held up as testaments to the triumph of capitalism and free markets.

Yet franchising is not the exclusive domain of profit-driven enterprises. For all its appeal as the entrepreneurial innovation of the 20<sup>th</sup> century, franchising in the government sector has existed even longer. When Britannia ruled the waves and spanned an Empire on which the sun never set, its colonies were governed in basically the same way around the globe under a franchise of the British government system. Similarly the ancient Romans conquered new lands and installed the Roman way of government to bring civilisation to the hordes (in return for a taxation royalty stream to Rome).

The franchising of government long precedes the acknowledged prominence of franchising in the private sector, but can this method of business be extended even further into the not-for-profit sector?

The answer is a resounding yes – within reason.

Franchising in the not-for-profit sector (also known as the third sector in relation to the government and private sectors) requires a fundamentally different approach to the principles of franchising adopted by the high-profile brands that appear to dominate the sector.

The key difference - and the one which makes any kind of enterprise in the third sector unique - is that the purpose of the business model is to create social benefit in lieu of profits.

To do good instead of making profits is the mantra of social enterprises which have embraced, or are considering embracing the franchise business model.

This is in contrast to many for-profit “commercial” franchises which deliver some social or charitable outcomes, but which are incidental to their “for-profit” operations and often not their sole reason for being compared to a true social franchise.

Social franchising is a relatively new field of franchising practice, and largely unknown in Australia. Of the 1,1000 franchise systems found by Griffith University's 2008 Franchising Australia survey to be operating in Australia, none are believed to be social franchises.

However identification of social franchises can be difficult.

Like “commercial” franchises, social franchises are not readily identifiable by external observation. A social franchise (like a commercial franchise) may appear the same as any well-branded corporate chain to a casual observer, or even a customer. Due to the social benefit focus of social franchises, these may even be equally indistinguishable from government or charitable enterprises.

Existing social enterprises with highly visible business operations such as the Salvation Army's “Salvos Stores” and the Endeavour Foundation's “Recycled Clothing Stores” are not social franchises as these outlets are understood to be centrally owned and operated.

In the absence of a central and definitive list of franchise systems, the identification of social franchises already operating in Australia is limited by an observer's knowledge of both franchise and non-profit sectors.

While many franchise systems may provide social benefits through their products or services, this may be as a means to commercialise a for-profit enterprise. For example, a tuition franchise delivers a social benefit by enhancing children's literacy and numeracy, but does so primarily to make profits as a return on investment for the operators of such businesses.

Likewise for other education franchises, or other commercial operations which improve quality of life or standards of living (eg. home services for the elderly). These are not social franchises – despite the benefit of such services – as the profits generated are retained for private gain.

*The principal outcome for a social franchise is to create a social benefit in lieu of profits, or if profits are generated in one part of the franchise, they are redistributed to one or more other parts to create other social benefits, rather than be passed to shareholders as dividends.*

By this definition, franchises which donate to or support charitable causes are not social franchises, as their philanthropic endeavours are incidental to their profit motivation, and not the organisation's sole reason for being.

### **Types of Social Franchises**

A review of some of the available literature on social franchising indicates a variety of social franchise models, from those which are entirely donor dependent to others which are completely commercial.

For those social franchises where the social benefit is to provide empowerment and life skills via employment to beneficiaries such as the disabled or disadvantaged, two distinct trends emerge in the commercial model.

One trend is where the social franchise provides high levels of employment for its beneficiary social group, but accepts a lower level of profitability as a result. This is often the case where the social enterprise has developed the franchise model in its own right, and seeks to increase the social benefit by maximising beneficiary participation throughout the organisation.

The primary focus in this instance is employment participation over profit (notwithstanding that the business must still make enough money to cover its costs).

An alternative social franchise model is one where the social organisation acquires a franchise of an existing commercial franchise and employs a lower overall proportion of beneficiaries to maintain the operation. This approach provides a reduced social benefit via participation, but aims to maximise profitability so that the profits can subsidize other social enterprise programs managed by the organisation and which are able to provide greater benefits to stakeholders.

For example, a charitable group in the United States might acquire a local franchise for a national fast food brand. It then includes a number of its beneficiaries in the employment roster, but seeks to operate the business as profitably as possible so that it can continue to fund its other socially-beneficial activities (eg. Hospice care for young cancer sufferers).

For social enterprises where the social benefit is to provide employment for beneficiary groups, the relationship between employment and profit is inversely proportional as illustrated by the figure below.

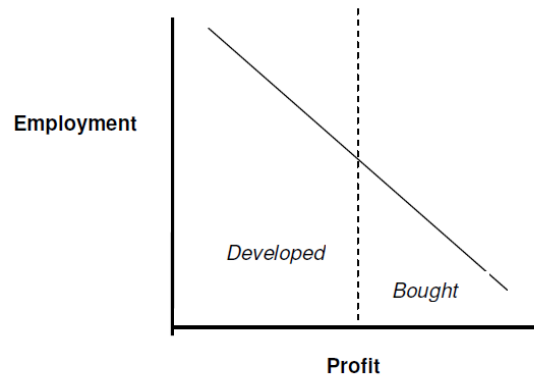


Figure 1: Social Franchising Models

Furthermore, enterprises which have developed their own business operations tend to have a greater focus on employment participation for its beneficiary group than organisational profit, whereas those enterprises which have bought a franchise to operate are more focused on profit than employment.

The development of a franchise concept by a not-for-profit organisation in order to maximise employment or other forms of engagement by its beneficiaries could be referred to as a **socially-developed franchise**, whereas the acquisition of an outlet from a commercial chain by a not-for-profit could be known as a **socially-acquired franchise**.

Socially-developed franchises are likely to be innovative, highly creative and fill a market niche that is either untapped or not well-served by private enterprise. However socially-developed franchises also risk being undercapitalised and lacking in the necessary systems, procedures and disciplines present in commercial franchises.

Socially-acquired franchises on the other hand benefit from the established brand, systems and procedures of a commercial franchise, but are not without challenges, key among which is to be granted the franchise in the first place. Franchisors have an overwhelming preference to grant franchises to owner-operator franchisees, whose profit motivation – usually backed by a sizeable debt to acquire the business - will ensure they remain focussed on achieving the highest levels of performance possible.

By comparison, a social enterprise, which is unlikely to risk losing its house if the business fails, and which may be controlled by a management committee of volunteers may not be so attractive to a franchisor. Then there are further considerations about the maintenance of the brand image and integrity required by the franchisor contrasted against the need to engage beneficiaries such as the disabled or disadvantaged in the franchise' workforce.

Developing or acquiring a franchise may be an important step in increasing the social benefit provided by not-for-profit organisations, but should in all instances be approached with caution, as the costs of failure can be severe. Specialist advice should be sought, as well as consideration of alternative growth strategies that may ultimately achieve the same or substantially similar social benefits.

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