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INTRODUCTION AND LEARNING OUTCOMES

The purpose of this chapter is to give the reader an understanding of the history of franchising, looking back to the origins of the word and discovering how franchising has developed into the business expansion system we have come to associate with the term in current usage.

The reader will be able to:

- Understand how franchising was conceived and how it has been modified.
- Understand the importance of the concept throughout history and its importance in today's business world.

Franchising is not a new concept! However, its origins are a matter of much debate and discussion. Some authors would have readers believe that it is a wholly American concept, devised in the mid-1800s to help American businesses establish an efficient distributor network. As we shall see over the next few pages, this notion does have some limited foundation and it was certainly the origins of business-format franchising, but the concept of franchising was undoubtedly in existence considerably earlier than when Christopher Columbus first set foot on the American continent!

The foundation of the franchising system probably lies closer to the Roman Empire as it existed in the early years of the New Testament than the commercial empires of businesses that have utilized this phenomenally successful business development model. Even the word franchise has its roots in the languages of central Europe, rather than the English language, though its precise origins are unclear.

FRANCHISING – THE EARLY YEARS

In ancient times, there was a Germanic tribe called the Franks, who derived their name from their weapon of choice – a spear. These Germanic warriors were given their name by their immediate neighbours, because this tribe was renowned for standing up for its rights in a vigorous manner (usually in battle, and using their trusty spears) so their name came to mean 'free' or 'the defenders of freedom', from which we get the phrase 'to speak frankly, or freely'. The country name France comes from the same root, meaning the place where one can be free. Indeed, prior to the French Revolution, the currency of France was the *écu d'or* in Louis IX's time (*écu* means 'shield', which featured on the coins, bearing a coat of arms, though it may be a reason why the French were firmly in favour of calling the currency currently called 'the euro', the European Currency Unit, or ecu for short), or the *Louis d'or*, which was first minted in 1640 during Louis XIII's time. In 1795, having removed the aristocracy, the French Revolutionary Council introduced the silver decimal franc, meaning 'free money' or coinage minted after the freedom from the oppressive monarchy.

In the Middle Ages in England, the word franchise had come to be associated with citizenship and the freedoms that being a citizen brought, specifically the right to vote, and this is where the word disenfranchised enters the language, meaning those who have lost their citizenship rights, particularly the right to vote. Therefore, some would argue that, in deriving from the old French word '*franc*', meaning 'free', we can assume that the original concept of franchising is the granting of certain rights to those who deserve (or can afford) a specific right to be granted, which in a positive sense is precisely what franchising does; the word franchise actually means freeness.

Nevertheless if one goes back to the early Roman Empire, where the lingua franca was Latin, there was the verb '*frango*', meaning 'to break into pieces', and it may be that the roots of the word 'franchise' can be traced back to here.

Originally, when the legions of Rome colonized what has become known as the continent of Europe, the senate appointed a Governor to control the newly acquired settlement. The Governor had the responsibility of protecting the land and the people that inhabited it, to introduce Roman law, and to establish a level of governance that was intended to establish both freedom and a level of authority in the conquered land.

The cost of establishing a protectorate was to be met by the imposition of taxes, which were collected by the Governor from the inhabitants of the state. Any expenses were deducted from the taxes collected, including a percentage which the Governor retained as his remuneration, and the balance was sent to Rome to swell the Roman treasury. So we can see that the Roman Empire was comprised of many semi-autonomous states, each holding allegiance to Rome, and controlled by an appointee of the Senate in Rome, whose task was to gather revenue (taxes) from the populace and after defraying costs of providing services (governance), would send the balance to the Rome.

When transposed over the business format model, we can see many similarities: the Roman Senate (franchisor) appoints a Governor (franchisee) to a dependent state (territory) where his task is to maximize potential and revenue and, after deducting his expenses, submit the balance to the Roman treasury (fees). Consequently, the concept of franchising potentially has its roots more in the task of collecting taxes than in any commercial enterprise, but the step forward to a mercantile arrangement was both simple and rational.

On a commercial footing, the Governors of Rome's far-flung dependent states quickly identified that sourcing all the needs for their local governance directly from Italy was both cumbersome and time-consuming, so they appointed local craftsmen and tradesmen to supply the needs of their administration – from chariots and weapons for the legions, to food and other provisions for their administration, each was sourced locally. The suppliers of these essential needs received their patronage from the Governor; they were licensed to supply their goods and services, and in return for their licences, they would pay the Governor a fee.

Using the previous analogy to interpret the actions of various parties, we can now see that, as well as holding the franchise from the Roman senate, the local Governor was now acting more in the role of franchisor in handing out licences to local tradesmen, and so we can also see where the concept of the master franchisee was born; that is, the franchisee who has the authority to issue licences to sub-franchisees.

This system of tax collection under franchise was so successful that it was adopted by most of the victorious powers down the ages. Certainly, when William the Conqueror arrived in England in 1066, he imposed a similar system of tax collection and created the role for local governors, though in William's administration, these were more localized, often being restricted to the area of a county or large city. William called his governors Sheriffs (coming from *scir* and *gerefa*, an ancient word for the royal authority in a shire) and we can therefore see that the much hated Sheriff of Nottingham from the Robin Hood fable was probably one of the first master franchisees in Britain!

One of the ancient rights bestowed by the Sheriff on the population was the privilege of holding fairs in the town, and many of these fairs still exist today (for example, the Nottingham Goose Fair). The fair was held on land owned by the state and controlled by the Sheriff, and in return the tradesmen who set up stalls at the fair paid a percentage of their takings to the Sheriff, often a tenth, or a tithe, as it was called.

The title of Sheriff still exists today as the representative of the monarch in some regions of England, but the role is now only a ceremonial title, as the role of tax collector has since devolved to central government, following the rule of Oliver Cromwell and the rise of Parliament. However, the concept of tithing continued. Gradually, the Church obtained more and more property and land, and those who worked on the Church estates were obliged to tender a tithe to the Church for God's bounty in giving them work. Naturally, the Church could not indulge in commercial activities, residing as it did on a far higher spiritual plane, but in order to meet its expenses, it had to raise capital and tithing was a legitimate route to fund-raising. Even today, in some religions, the expectancy of tithing still exists.

Moving away from matters religious and the funding of the Church, some would lay claim that franchising originated in the twelfth century with the ancient guilds of London. Certainly, there is evidence that a form of franchising was adopted by these august bodies, which would charge members an affiliation fee set by the guild and there would be a large fee payable for membership and annual payments to retain that membership. Some guilds charged a percentage of turnover as their fee, while others a set monetary amount. Membership of the guilds brought wealth and prosperity to the merchant classes – the name 'guild' comes from the ancient Anglo-Saxon word *gilden*, meaning 'to pay'.

THE BREWING CONNECTION

Moving forward to the early part of the nineteenth century, we find ourselves in the time when alcohol was starting to play an increasingly significant role in the lives of Britons and in other European states.

It has been suggested that business format franchising was originally conceived by the German brewer, Späten, who gave the rights to sell their beers to certain taverns, but the emergence of a single German brewer in this field alongside a number of British brewers who at the same time used this approach, might suggest that this form of franchising originated in Britain rather than in Germany, but there is little to support this hypothesis other than the quantity issue.

Wherever it started, at this time, the manufacture of ale was very much a more local affair than it is today; most hostelries made their own ale, and ale houses were spreading throughout the country. These ale houses brought with them other social problems and it soon became clear that some sort of regulation was needed. The government of the time decided that the taxation of ale manufacture would significantly reduce the number of ale houses, and consequently the inherent problems associated with them. Faced with financial ruin, however, the proprietors of these ale houses joined together and formed breweries, where the ale could be

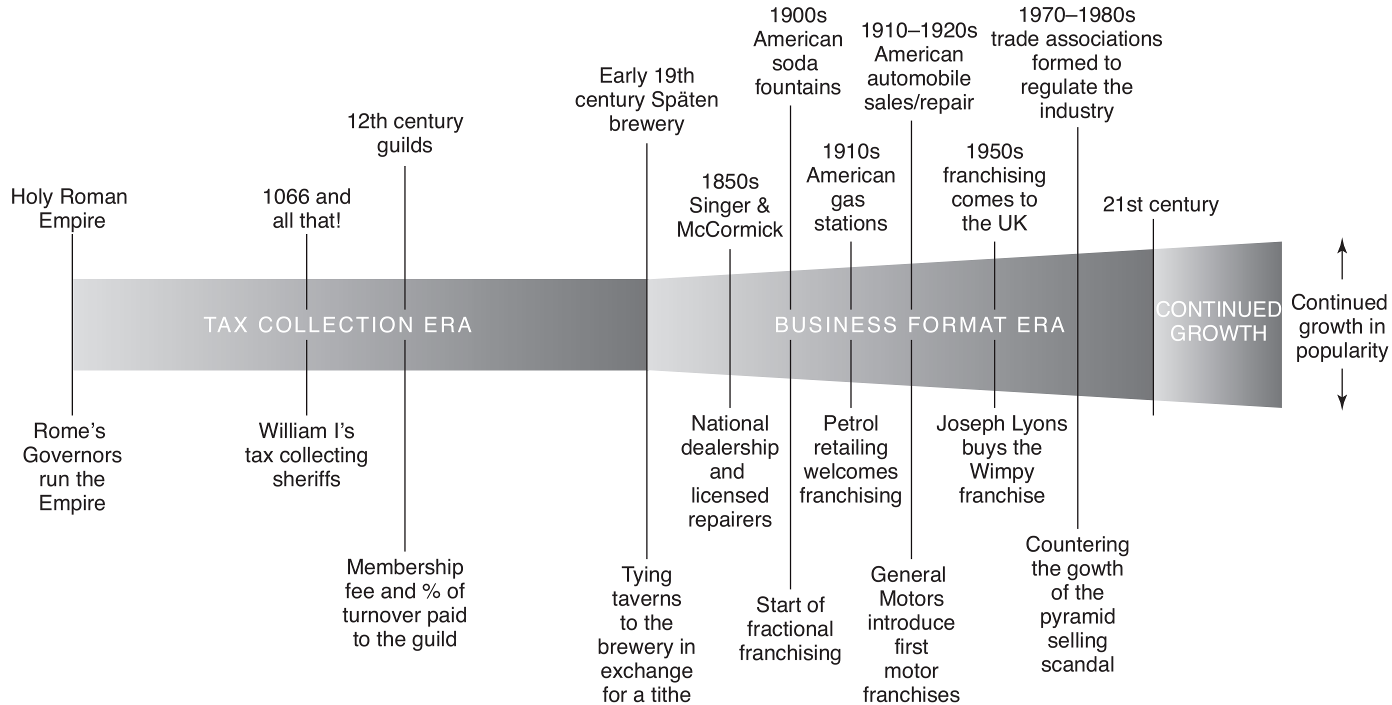

Figure 1.1 Timeline of franchising

brewed centrally and distributed to the ale houses that formed part of the brewing group. The landlords bought their ales from the brewer and in addition paid a tithe which covered the cost of the brewing tax. The brewer collected the tithes and dealt centrally with the tax-collecting arm of the treasury.

So we can see that, even at this late stage, relatively speaking, the franchise issued by the brewer was more concerned with the collection of taxes than being an ongoing commercial business, though the brewer derived its profit from the mark-up on the ale it was selling. The tithed houses soon became known as tied houses, and the term still exists today, where public houses are tied to a particular brewery, to which a percentage of the profits are paid.

The higher level of the franchising concept survives to this day – one will often hear it said that the government has awarded the franchise to do something to a particular company. In effect, charging a commercial operation for the right to carry out some task in exchange for revenue (or tax) paid to the Treasury. This notion is at odds with the definition of business format franchising, as we shall see, but within the general definition of franchising, and certainly within the guidelines of the original understanding of franchising, it is legitimate.

Readers will have noted that a qualification has just been introduced in respect of franchising to which they may be, as yet, unfamiliar. *Business format franchising* is the method of adapting the franchising model to the version to which most of us are accustomed and which we associate most frequently with the idiom 'franchising'. The history of franchising is summarized in Figure 1.1.

BUSINESS FORMAT FRANCHISING

It has never been entirely clear who was the originator of the business system that grew into business format franchising, but general consensus suggests that it happened in America and was either the founder of Singer Sewing Machines, Isaac Merritt Singer, or Cyrus Hall McCormick, the inspirational father of mechanical reaping and harvesting, as both systems appeared at about the same time, 1850–1, way before the American Civil War; but whichever got past the winning post first, both were instigators of a great tradition that has developed and changed the world of business in the following 160-odd years.

Looking at the case put by the founder of the Singer Sewing Machine Company, we learn that Isaac Merritt Singer was producing a range of highly popular sewing machines. Singer's sales force travelled the length and breadth of the country selling these marvellous machines to families and businesses that, until this time, had been sewing by hand. Singer soon became the victim of his own success, however, because while he was able to sell vast quantities of the new machines, bringing them back to the head office for service and repair was both costly and highly cumbersome; moreover, it was occupying too much of his representatives' time and consequently sales were starting to fall.

Singer devised a plan whereby he would develop a network of licensed engineers, who would carry stocks of the most common components and repair the machines locally. The engineers were all self-employed and were paid directly by the customer, but could legitimately call themselves 'official licensed repairers' of Singer's machines; the engineer would buy component stock from Singer and would also pay Singer a small percentage of the invoice price as a fee for being allowed to operate as an authorized repairer. This concept freed up the representatives' time to expand sales and gave their customers a local point of contact for a more efficiently handled repair or service.

Soon these repair engineers began selling replacement machines as the originally purchased machines wore out, and the concept of a true franchised dealer was born. These first franchisees held stocks of the latest Singer machines, which they would sell and repair locally, and they were expected to pay Singer a percentage of their sales turnover as a franchise fee. Consequently, the Singer Sewing Machine Company became the first business format franchisor. As Singer's business grew, it soon became apparent that the franchisees were making a solid living out of their relationship with the company, and Singer was inundated with applicants to become a licensed dealer. It became clear that some sort of selection process was required and the easiest one to implement was a financial entry barrier; if one could not afford to buy into the system, one could not join. Despite this payment being only a few dollars, it quickly sorted the genuine from the opportunistic applicants and allowed for a management structure with adequate training for the franchisee network to be funded independently of Singer's core profit margin. The business was so successful that others looked at the model as a method of expanding their own businesses.

CASE STUDY 1.1

McCormick Harvesting Machine Company – a pioneer franchisor

Cyrus Hall McCormick was an outstanding early American mechanic; he was a man of vision with a passion, and a genius at business development and marketing.

Even though McCormick manufactured reapers for sale as early as 1834, he did not sell any for the next six years, but was undaunted by

➜

CASE STUDY 1.1 *continued*

this. Eventually, he sold two machines in 1840, seven in 1842, and fifty in 1844. The reaper was not suited to the hills of Virginia, where McCormick was based, and the conservative farmers were uncertain about buying expensive new machinery that needed to be repaired by a skilled mechanic.

When McCormick made a trip to America's Mid-West, however, things changed rapidly. He saw his opportunity in the endless and verdant prairies, with hundreds of miles of good rich soil with few trees and fewer rocks. When his fierce rival, Obed Hussey, moved east, Cyrus McCormick moved west and established himself in Chicago in 1847. At that time, Chicago was a small town of little more than 10,000 citizens, but McCormick built a factory there, and manufactured 500 machines in time for the harvest of 1848.

McCormick's skill in marketing resulted in him creating a complex business plan. He sold his machines at a fixed price, and if farmers could not afford the capital cost, they could pay by instalments, and he gave a guarantee of satisfaction.

Recognizing that his machines would be sold throughout the USA, McCormick quickly identified a major problem. His machines were used during the harvest period and if a farmer's machine needed spare parts from the Chicago factory, the crop would be ruined before they could be delivered and fitted. So McCormick set up a system of agencies which would sell his machines, give instruction to the buyers and supply spare parts. This was during the infancy of business format franchising, but it is clear that Cyrus McCormick's innovative approach to business helped to develop its current form.

This industrial revolution set up an arrangement whereby a business system would allow the latest technology to be distributed, sold and serviced over a vast physical area, without the costs of developing a fully owned and operated infrastructure. This system became known as 'business format franchising'.

The next big influence in the development of business format franchising arrived with the big soft-drinks manufacturers in the USA – Coca-Cola, 7-Up and Dr Pepper's Root Beer – when it was quickly discovered that shipping bottles of what was essentially carbonated sweet water around the continent was a phenomenally expensive operation. What was needed was a system whereby water, sugar and carbonation could be added at source to the vital ingredients of these popular drinks. The drinks companies started to produce syrups that could be added to locally sourced water and then carbonated at point of sale, giving rise to the famed American soda fountains. The proprietors of the soda fountains became fractional franchisees, paying a percentage of their soda sales to the drinks companies who were supplying their base syrups. The concept of the fractional franchise arose because most soda fountains were in stores that sold other commodities – from hardware to ice-cream. The proprietors bought their syrups and equipment from the drinks companies and gave a percentage of their soda sales as a franchise fee.

Again, soda fountains became popular, and soon there were more applicants than there were 'territories' available, so the system of paying for a franchise was implemented, to include equipment, uniforms, training and a marketing package. Very soon, soda fountains moved into the mainstream and dedicated stores began to operate.

This was all around the time of the expansion of America's love of the motor-car, and with motor-cars came the need for petroleum spirit on which to run them. Owning vast numbers of petrol retailing outlets was prohibitively expensive, even for the wealthy American oil giants, so a system of franchised operators was introduced. A garage operator would buy the franchise for Standard Oil (Esso), or Texaco, or one of the other numerous oil producers, and the operators were supplied with petrol pumps in the oil company's livery, a sign to hang on their forecourt and other dedicated products from their chosen supplier. The franchising concept allowed for exceptional growth of outlets at minimal cost to the oil companies, and the race was on to get the widest coverage in the quickest time.

Similarly, as more and more cars appeared on American highways, so the need for competent local salesmen and repairers grew; after several motor manufacturers joined forces in 1910 under the banner of General Motors, so the concept of franchising extended to vehicle sales and repairs. Some say that General Motors emulated the Singer model of franchising; while others will suggest that they looked to Belgium and the rival business of Adam Opel (who, incidentally, came under the GM banner in 1929) for their inspiration. Opel, before manufacturing cars, had made sewing machines and it is said that Opel had adopted Singer's model and refined it for the European market; whichever story is true, General Motors set up hundreds of franchised automobile dealerships in a very short period of time and left the rest of the industry playing 'catch-up'.

The franchising model of business development proved so successful that it became the preferred method of retail expansion in America in the early part of the twentieth century; and despite wars, recessions and the mob, franchising flourished.

Following the success of the wartime cartoons featuring a muscular, spinach-eating sailor by the name of Popeye, and his friend, Wimpy, Joseph Lyons in England identified a strong American trademark and niche product and subsequently bought the non-US global rights to the Wimpy brand of hamburger restaurants, and with the rights to the brand brought the concept of business format franchising to mainstream fast food in the UK. Growing the business through franchising was so successful that Lyons very quickly applied the model to his other business divisions, and the jingle of the Lyons Maid ice cream franchise was soon to be heard throughout the nation.

Pyramid selling: *a practice adopted by some manufacturers of advertising for distributors, and selling them batches of goods. The first distributors then advertise for more distributors, who are sold subdivisions of the original batches at an increased price. This process continues until the final distributors are left with a stock that is unsaleable except at a loss.*

Many other businesses followed Lyons' franchising model and now the world has a vast number of franchised businesses, but success did not come without some problems. In the 1970s the commercial world was rocked by the shame of the pyramid selling scandal; unsuspecting 'pyramiders' were offered the opportunity of vast wealth merely by introducing friends to the pyramid. As the new pyramiders paid their entry fees to the person who introduced them, the fee was passed up the line, being diluted increasingly until the organizer of the pyramid scam received a vast quantity of small remunerations, making him or her exceedingly wealthy.

Like most scams, this had no real basis for success, but there were some slight similarities to business format franchising, and consequently the franchise industry was tainted by the scam. It was clear that there needed to be some control over the industry, and in many countries regulatory legislation was introduced. Following the British tradition of self-regulation, several franchisors joined forces to create the forerunner of the British Franchise Association, and in the USA a similar organization was formed, with global aspirations, under the banner of the International Franchise Association.

With the growth of the European Union, the BFA and other European national franchising bodies affiliated under the European Franchising Federation, each retaining its own identity but all subscribing to a European set of principles and a code of ethics that would create a level playing field for franchising throughout Europe.

Therefore, we can see that what started life as an efficient method of collecting taxes from the distant corners of empires has developed into a highly successful business expansion model and as business opportunities evolve, one can be sure that franchising will develop in more refined forms to meet the needs of commercial evolution.

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Notes: **bold** = extended discussion or term highlighted in text; f = figure.