

LEGAL AND ACCOUNTING APPROACHES OF FRANCHISING OPERATIONS

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Franchise, as a form of marketing goods and services, meets an emphasized extension due to the multiple advantages for the parts involved in the transaction, but also for the economies in their economical, social and fiscal plans. In specialty literature franchise meets different definitions depending on the issues considered most important in this transaction, by various authors. Franchise in our country is defined as "a system of marketing based on a continuing collaboration between natural or legal person, independent in financial terms, by which a person called franchisor, granting to another person called beneficiary, the right to exploit or develop a business, a product, or a service.

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A. Legal regulation of the franchise.

Legal basis of operations of a franchise is represented by the **franchise contract** whose main elements are the ones in the following content:

1. The contracting parties

These are named franchisor and franchise. Legally and financially, they are independent entities. The **Franchisor** is a merchant who: is a holder of rights over trademarks; has the right to exploit or develop a business, a product, technology or service; ensures the beneficiary the initial training for exploiting registered trademark. He personally uses financial means to promote his brand, his research and innovation, ensuring the development and viability of the product. The **beneficiary** is a merchant, individual or legal, selected by the franchiser, who adheres to the principle of uniformity of franchise network. **Franchise network** includes all contractual relationships between a franchisor and more beneficiaries in order to promote a technology, a product or a service and to develop production and distribution of a product or service.

2. The contract work object

It is represented by the good and contract services according to which three categories of franchise are distinguished:

- Franchise of **products**, in two forms:
 - **Manufacturer franchise**, in which the franchiser has as objective product selling but also related services;
 - **Distribution franchise**, in which the franchiser selects the products manufactured by various suppliers, buys the products, they pay for them, then resell them to the beneficiary (pilot units are created);
- **Service franchise**, in which products are not sold but services, various dues: hotel franchise, consultancy franchise etc;
- **Industrial franchise**, in which the franchiser builds a factory in order to be franchised, he gives the license, the patterns, the trademark, he forwards the technology, assures constant technical assistance, and the beneficiary produces and sells the products under the name of the franchiser.

Franchisors may be:

- Manufacturers of goods, who signed franchise contracts in the country or abroad for the sale of manufactured products;
- Wholesalers merchants, who perform a selection of goods that we buy in large quantities, establish exclusive supply catalogs which are sold through the franchise;

- Service suppliers, whose activity consists in the original discovery of ideas and practical methods of profitability: hotel chains, car rental locations, construction of houses etc;
- Industrial people, who form the industrial franchise, the most modern form of the franchise and the most usual in international relations.

Beneficiaries may be:

- merchants, companies that are organized in various ways;
- non-professional people (those who either have never worked in industry either did not have any trade).

3. Price of the franchise

As any other economic activity, the franchise has a price which for the franchisor is the income, and for the beneficiary is the cost. The price of the franchise must cover its costs so that the franchise activity to be profitable. Usually the price of the franchise consists of two elements: entrance fee for the franchise network and royalty.

The entrance fee represents the franchisor's remuneration for granting the right to use the trademark and its way of work, whose development required a variety of expenditures, for example: prior studies to implantation, costs for searching and arranging a certain location, supplying stocks and specific equipment to the franchise; elaborating professional experience (know-how), franchise marketing (participation in fairs and exhibitions) etc. So, the entrance fee is considered as the price of business admission, its size varying on the importance of the business and its prospects. Depending on size, it is provided a certain selectivity of beneficiaries. The entrance fee can be calculated using different methods based on franchise profitability calculation and it is established so that it doesn't have the effect of possible beneficiaries shift to other competing networks. Usually, the entrance fee has values between 5-10% of the total cost of the franchise. If the franchisor proposes signing an exclusive contract and if it is cashed an entrance fee, then on signing the contract, the exclusive rights (exclusive fee) that were calculated proportionally with the entrance fee will be added next to the entrance fee.

The exclusive tax may be dedicated to cover a part of the expenses needed to implement the franchise and/or to delimit the area and/or for the transmitted know-how.

Royalty represents remuneration of the services which the franchisor provides permanently to franchise during the contract, as the following: improving personal experience (know-how), assistance during the period of contract, expenditure on training the staff permanently, expenditure on advertising etc. Usually, royalty rate is calculated in percentage to the turnover, but in some cases it may be established a lump royalty. Sometimes forms of fee assessment can be used, determined by the object of the franchise contract. For example, in hotels royalty may be set according to the number of rooms. It is important that the size of the fee, determined through negotiation, to motivate both sides: a great fee determines the franchisor to be less interested in increasing the sales, and a small fee determines that the majority of the profit to belong to the franchisor, leading to a loss of development sources of the franchisor.

4. The rights and obligations of parties

They represent the important elements of the franchise contract, one of them being directly or indirectly at the base of organizing franchise accounting. Among these we mention:

For the franchisor:

- To provide the beneficiary a process of manufacturing, distribution and marketing of a product or service or to put such a process that would ensure a high turnover and a high yield;
- To sell the beneficiary his experience, components of intangible assets (franchisor's trademark and the know-how);

- To ensure technical assistance to the beneficiary, material assistance and sometimes financial assistance both before making the transaction but during the transaction;
- To provide the beneficiary goods (merchandise) directly, or by selecting some good providers;
- The right to control over the way business is developing, these respecting the conditions imposed by the franchisor.

For the beneficiary:

- To obtain authorization for the functioning of the unit of provision or services under the franchisor's brand. The license accorded in this context specifies both the location of sales and the precise location of the sales unit which refers at: the use of the franchisor's name and distinctive signs, of work techniques and operation methods;
- To purchase goods (merchandise) from the franchisor, or from the agreed suppliers;
- To sale the good (merchandise) and the services forwarded by de franchisor by respecting strictly the contractual conditions;
- To pay the cost of the franchise to the franchisor (entrance fee and royalty) and other elements as: initial inventory (equipment, accessories), the initial stock of merchandise (necessary for opening the franchise), rent premises, public services etc.

B. The accounting operations of the franchise.

In the accounting of the franchisor:

1. The assets available for the beneficiary refer to intangible assets in constant mark of the franchisor (the manufacturing, commerce, services) and know-how. They remain the property of the franchisor because he does not sell them, but "gives" them for temporary use in order to be exploited.

The purchase of the assets specified by the franchisor can be done through purchasing or owning. If the trademark and the know-how are purchased from a third party, these are evaluated at the cost of acquisition and recorded in the account 205 "Concessions, patents, licenses, commercial trademarks and similar rights".

If the trademark and know-how are created by the franchisor, these are counted as any investment in its own meaning: the expenses made in this purpose are collected as they are performed in their accounts of expenditure in class 6, and at the reception, the obtained immobilization is recorded in the cost of production in account 205 "Concessions, patents, licenses, commercial trademarks and other similar rights" according with 721 account "Income from production of intangible assets"

The use of 721 account "Income from production of intangible assets" for the recording of the intangible assets realized in its own is made to avoid the distortion of the exercise by which these are obtained.

2. The expenditure of the franchisor are grouped in the periods in which the sequence is done, in the following categories:

- costs of establishing the franchised companies;
- expenses for the launching of the franchised companies (cost for advertising models, costs for presenting on different showrooms, etc);
- expenses on the beneficiary's technical assistance;
- expenses for administrating the franchise network.

As a rule, the expenses are recorded in the expenses accounts from class 6 according to the exercise these were engaged. In the case where some expenses regard the next exercises to which they were engaged, they are recorded in account 471 "Expenses recorded in advance", so at the end of each exercise the related expenses to be organized in the expenses accounts from class 6.

3. The income specific to the franchisor are grouped in 2 categories:

- direct revenue from the franchise operation which includes revenue from the entrance fee and royalty income;
- income from selling goods to the beneficiary, or the provision of services or execution of papers.

Revenue from entrance fee is considered an accessory-income that is recorded in the account 708 "Revenue from various activities". The right for claiming for the franchisor arises in the moment of signing the franchise contract. Payment may be made in full at the time of signing the franchise contract or staggered through negotiation. In this second case the income from entrance fee is initially booked as income in advance in the account 472 "Income recorded in advance", and that after each staggered collection to be emphasized the current income in the account 708 "Income from various activities".

The income from fees. It is the main income of the franchise which is registered in 706 account "Income from fees, locations and rent management". Calculation, collection and accounting of fees is done periodically, usually monthly, the basis of calculus being the turnover. If at the closing the exact fee income for December is not known, it can be proceeded to estimate the fee income and recording the claims in the account 418 "Clients – bills to be drawn". Later, after the calculation of the turnover based on the drawn bill, the certain claim will be recorded and the difference between income tax and the VAT will be solved in one of the next :

- either by canceling the initial operation (with estimated data) and simultaneous recording of the actual size of dept and VAT.
- or by recording the actual size of claims and by adjusting the differences between income and tax, by amounts in black for the differences in addition to the estimations and amounts in red for the differences in minus.

Income from selling own goods to the beneficiary are ordinary operating income of the franchisor which are registered in the corresponding revenue accounts: 701 "Revenue from finished products", if the franchisor is the manufacturer, 707 "Revenue from selling the goods" if the franchisor is the merchant, 704 "Revenue from performed work and rendered services, if the franchisor is a service provider.

In the accounting of the beneficiary

The franchise operations generate to the beneficiary both expenses specific to the franchise and ordinary expenses and income for any company. Specific expenditure refers to the entrance fee and the royalty that are to be paid to the franchisor, and the ordinary income and expenses relates to the cost of sold goods, general expenses, income from selling goods and so on.

1. The entrance fee expenses are registered at signing the franchise contract in account 628 "Other expenses with the services performed by third parties" if their value is not considerable. Either the entrance fee value can be included in the current expenses, being accounted initially as an advance expense in account 471 "Expenses registered in advance"

When the franchisor makes tangible investment on the beneficiary using the entrance fee (for example the endowment of a business) or offers the beneficiary the right to use the elements of intangible assets (the trademark and the know-how), the entrance fee is accounted partially or totally as a component of the acquisition cost of tangible assets (for example account 213 "Technical installations, vehicles, animals and plantations") or intangible (account 205 "Concessions, patents, licenses, trademarks and other rights and similar values").

2. The royalty costs are accounted as exploiting expenses in account 612 "Expenses regarding royalty, management locations and rentals".

3. The rest of expenses and income are accounted as usual in the expenses and income accounts from classes 6 and 7.

To conclude, being a form of marketing goods and services, franchise meets an emphasized extension because of its multiple advantages for the parts that are involved in the transaction, but also for the economies in their economical, social and fiscal plans.

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