Franchise Fees: How 4 Types of Fees Can Lead to Growth

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Your current franchise fees enabled your brand to get to where it is today — but will they get you to the next level?

While many franchisors are hesitant to increase franchise fees, there are proven benefits to both the franchise organization and individual franchisees. Higher fees can ultimately boost revenue, give you a competitive advantage, and grow the value of your brand. Below, we explore in detail how four types of franchise fees can lead to growth.

1. Initial Franchise Fees

Initial franchise fees vary from company to company. These fees, typically collected in a lump sum payment when the franchise is granted, allow franchisees to license the brand and gain access to the organization's best practices and intellectual property.

Some franchise brands assume that requiring lower fees will help them stay competitive and open up the door to more potential franchisees — especially those who are seeking affordable options. Other brands take the position that higher fees lead to increased revenue, which attracts higher quality franchisees. However, the majority of franchise brands simply align their fees with others in their sectors.

But being like everyone else won't help you win market share, will it?

Research shows a surprising correlation between franchise fees and revenue. Brands that charge franchise fees of about $40K realize 2.5 times more revenue than those that charge $25K — in total, about $1.5 million per store. And the higher potential for revenue, the more franchisees are willing to pay a higher franchise fee.

So ultimately, by increasing your initial franchise fees, you have the opportunity to increase revenues, attract more franchisees, and grow the value of your brand.

2. Royalty Fees

Royalty fees extend beyond the initial franchise fees. Franchisees pay these fees for ongoing rights to participate in the franchise.

The majority of franchise organizations — 94 percent — charge a royalty fee. Most charge a percentage of revenue, but a small number charge a fixed dollar amount. The average royalty fee for all verticals is 6 percent of monthly revenues.

How can royalty fees lead to growth? Since most franchisors already collect royalty fees, the strategy here isn't to necessarily increase these fees — but rather, to look for opportunities to increase or reinvest the dollars you collect through *other* fees (which we cover below). Ultimately, this will allow you to profit from your royalty fees, rather than allocating those dollars to growth initiatives.

3. National and Local Marketing Fees

Requiring franchisees to pay a national advertising fee can help build brand awareness, create programs for franchisees, and provide the ability to rally resources if necessary — for example, if there is a major competitive intrusion.

Most franchise organizations (72 percent) currently charge a national advertising fee. Of those brands, 89 percent charge a percentage of sales, while 11 percent charge a fixed dollar amount. Across all verticals, the average national advertising fee is 2 percent of monthly revenues.

Fewer franchise brands require a local marketing spend. Just over half of franchise organizations — 55 percent — require this fee, while 45 percent do not. Of those that do require it, 79 percent require a percent value of revenue, rather than a fixed dollar amount.

To grow your franchise brand, you must ask yourself: Do your current fees allow you to effectively compete in your vertical? Based on our research, 80 percent of survey respondents say the marketing fees they currently charge are not enough to allow them to compete. Consider a new approach to these fees that provides the resources to effectively compete on national and local levels.

4. Technology Fees

Some franchise organizations also require franchisees to pay a technology fee, which contributes to the purchase or licensing of software, hardware, and networking equipment necessary for store operations. Only 61 percent of franchises collect technology fees, and typically, they charge a flat rate, rather than a percentage of revenue.

Are you undermining your system by foregoing this fee and not investing in technology?

If so, you may be missing a major growth opportunity. Half of franchisees say that technology tools are among the top value that a franchisor can provide. And franchise organizations that charge technology fees are likely to grow 36 percent faster over a two-year period than those that do not charge a technology fee.

Consider McDonalds, for example: The franchise recently began implementing technology in their drive-throughs that uses artificial intelligence and personalization to make menu suggestions from a customer's order history. This has the potential to increase order size, speed up the ordering process, and provide a better customer experience.

However, without technology fees, your franchise brand likely won't be able to afford this kind of cutting edge technology — which can make you lag behind the competition. Appropriate technology fees can equip your franchisees to be more efficient, deliver better service, and compete more effectively with others in your vertical.

Increasing your franchise fees won't scare away potential franchisees. In fact, appropriate franchise fees can attract more highly qualified franchisee candidates — because they will recognize that your franchise is primed for growth.

For a deeper dive into franchise fees, listen to the webinar replay, "Franchise Fee Structures That Strangle Your Growth."

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