



Pros and Cons of Buying a Franchise with Unprotected Territories

When it comes to investing in a franchise, vocabulary terms like “Franchise Disclosure Document,” “royalty fee,” and “franchise agreement” may all sound a bit foreign at first. But as you wade through the franchise-speak, pay close attention to one term in particular: “protected territories.”

“A protected territory provides a franchisee with some protection against the franchisor putting another franchised or company-owned unit on the next block or very close by,” explains franchise attorney Harold Kestenbaum. It’s a term that you’ll come across often in your research, since most small and midsized franchises grant some kind of protected territory, according to franchise attorney [David Cahn](#). But what about those that don’t? We asked Kestenbaum, Cahn, and franchise attorney Andrew A. Caffey for their thoughts on the advantages and disadvantages of investing in a franchise that offers *unprotected* territories. Here’s what they had to say:

Advantages:

- *Competition may be healthier:* “Direct competition is healthier than artificial impositions by franchisor planning,” says Caffey.
- *The franchise system has room for flexibility:* “Territories are artificial and inefficient for all concerned,” says Caffey. “Territories lock in the franchise system at a frozen point in time, and prevent the system from reacting and responding to changes in the market. A system without those restrictions can be more nimble over time.”
- *Certain franchisees can greatly benefit:* “For service businesses in which sales and customer service are paramount, the lack of territorial restrictions can be of great benefit to a ‘go-getter’ who is entrepreneurial and creative,” says Cahn.
- *Franchisees are forced to focus on building a strong core for their business:* “The franchise owner focuses on the operation of the business to build business value rather than relying on a protected territory as an inherent value of the business,” says Caffey.
- *Allows for a more modern marketing strategy:* “Recognizing the realities of Internet, social networks, and modern media,” says Caffey, “marketing the brand is not compartmentalized and stunted by artificial territories.”

Disadvantages:

- *While some franchisees are helped, others are hurt:* “The lack of territorial rights typically leads to intensive intra-brand competition and inhibits franchisee cooperation and collaboration for the good of the brand,” says Cahn. “So, while the lack of territories may be good for consumers in terms of price options, it can harm the cohesiveness of the franchise system and of course the less assertive franchisees.” Kestenbaum agrees, saying, “You will be competing with other franchisees of the same brand, so fighting for market share may be a real challenge.”
- *Marketing efforts can be weakened:* “Marketing activities in a franchise system without territories may be poorly focused,” says Caffey, who adds that franchisees may not focus local promotion in the proper market area.
- *Franchisor/franchisee trust may be affected:* “Franchisees without clearly defined territories may feel threatened by franchisor marketing decisions,” says Caffey. “Franchisors and franchisees have different interests when it comes to the decision regarding building the brand. A new location may greatly increase brand awareness - a plus for the franchisor - while at the same time reducing the revenues of the franchisee - a minus for the franchisee.”
- *Legal problems may arise:* Says Caffey, “The franchisor may adopt territory ‘policies’ that are complicated and difficult to enforce and that may lead to litigation over their application.”

In the end, it will be up to you as the investor to look at the whole picture. "Don't assume that the lack of a defined territory will weaken the value of your franchised business, but make sure you understand the policies put in place by the franchisor regarding franchise expansion," says Caffey, who directs potential investors to Item 12 of the Franchise Disclosure Document for detailed information. "Talk to existing franchisees to see how territory issues are handled in the system."

Industry Issues

Trying to determine whether the whole issue of unprotected territories will be an issue as a franchisee?

Cahn advises potential investors of *retail* franchises with unprotected territories to consider:

- whether securing a prime location would be sufficient to keep competitors at bay
- whether there is a strong, captive audience, such as a large office building that will provide regular business.

For those considering a *service* franchise, Cahn recommends:

- gauging how aggressive you are and thereby getting a good sense of how successful you would be in pursuing/attaining business
- determining whether existing franchisees in the area have already developed the brand, in which case it might be difficult for you to be successful in business development and establishing yourself

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