

Important Things To Know About Franchise Royalty Fees

From fast-food restaurants to tire and lube shops, one thing is shared in common by all franchisees under all brands in all industries - the royalty fee. Ongoing royalty fees are the financial backbone of franchising. It's how and why franchisors exist, and it is the driving force behind every marketing campaign or new product and service.

What is It?

The royalty fee is a percentage of the gross revenue of the individual franchise that must be paid to the franchising company for use of the company's business model, as well as use of its trademarked name, products and services. Though the percentage charged varies widely from franchisor to franchisor, the nation average is around 7%.

It isn't uncommon to hear franchise owners express some degree of displeasure at being required to turn over a substantial part of their earnings to the franchising organization. It is important to keep in mind that it is this fee that allows the owner to continue operating a successful and well known business in the community in the first place. Without the franchise name and business plan, the owner would have had to claw his or her way up from scratch to establish the business's reputation in the community and ensure its longevity.

What Do Royalty Fees Pay For?

While all franchisees hope that their franchisors will actively work toward growing the brand and thereby making it more profitable for all involved, there is never a guarantee of this. There certainly isn't any guarantee, either stated or implied, in the agreement concerning royalty fees. The payment of royalty fees simply grants the right to continue to use the company name, business model, products and services, whether or not the franchising organization flourishes or fails.

Does this mean that the franchisor has no obligation to develop the brand? Not exactly. If a franchisor wants to be successful, then they want that 7% to be constantly higher amongst its franchisees.

What is the Franchisor's Role?

The franchisor, if they are a solid and viable company, will most certainly act to grow the brand and increase revenues for the franchisees. This growth is not a "service" bought by the franchisee by the royalty fees, it's simply good business. What is good for the franchisee is good for the franchisor.

Since royalty fees are paid as a percentage of revenue, in most cases, it is in the best interest of the franchisor to make its franchisees as profitable as possible. They do so by wide-spread marketing campaigns, and by developing the products and services of the brand to make their franchises more competitive in the marketplace. Just as in other businesses, some franchisors succeed and flourish, others fail and fade away.

What to Look For?

If you are thinking about investing in a franchise and want to know if the brand you are looking at has a trademark worth paying for, then look at their marketing and growth. Has its recent marketing been effective or ineffective? Is the brand growing or has it reached a plateau? Are they consistently coming out with new products or services, or are they dead in the water? Researching your potential brand's history can give you an idea of where they are most likely heading.

About the Author

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