# McDonald's franchisees not leaving brand despite tension

Aug. 9, 2013

**Mark Brandau**

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The company disputes claims of a "revolt" as operator concern about cash flow grows.

**What is in this article?:**



Officials from McDonald's Corp. pushed back against reports of mutiny among its owner-operators this week after public comments from McDonald's franchisees revealed ongoing discussions with the franchisor over its rent structure, value strategy and remodeling program.

An Aug. 6 article on Bloomberg.com said two groups of California franchisees were "going rogue" by having meetings, listing grievances and suggesting negotiations with McDonald's to Lee Heriaud, a Phoenix-area franchisee who chairs the National Leadership Council for all domestic McDonald's owner-operators. The report also speculated that McDonald's franchisees would be less likely to open new restaurants or remodel existing ones.

However, McDonald's spokeswoman Heather Oldani said that the franchisee groups holding meetings is "not unusual" and did not constitute a "brewing franchisee revolt," as suggested in the Bloomberg story. "To characterize this as a revolt is the wrong picture," she said.

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A copy of a memorandum obtained by Nation's Restaurant News, which operators in the Pacific Sierra region drafted after a June 6 meeting in Stockton, Calif., lists several points of contention the franchisee group has with McDonald's Corp. The memo is addressed to Heriaud and Kevin Hern, an Oklahoma-based franchisee who chairs the franchisee-franchisor joint

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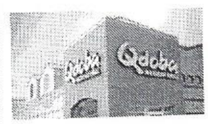

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Operators also wrote that the pace of reimaging stores mandated by McDonald's — calling for all remodels to be complete by the end of 2016 — was too fast, and that the franchisees did not have enough flexibility in how they remodeled their stores. The Pacific Sierra memo suggested McDonald's slow the pace of remodels and decrease the décor mandate to a minimum standard that franchisees could "plus up" however much they wanted.

Johannesen responded that, as with the negotiating process for rent agreements, franchisees work with the System Economic Team "to make sure we're looking at the same numbers and understanding how the economic pie between the company and owner-operators is looking."

Heriaud added that flexibility around the initiative was discussed at the last meeting of the National Leadership Council in June. "We had dialogue around flexibility of timing for each operator, as well as sequencing," he said. "Maybe they can bite off different pieces at a time, like maybe the dual drive-thru opportunity, before addressing the rest of the building. I think we're arriving at a good spot."

McDonald's more than 2,500 owner-operators run about 90 percent of the chain's more than 14,000 restaurants in the United States.

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### Cash-flow pressure

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Franchise consultant Gordon added that, in addition to rent eating up incremental sales dollars at franchisees' restaurants, a "witch's brew" of the other grievances listed in the Pacific Sierra operators' memo put pressure on their cash flow. He agreed that a marketing strategy heavy on value strains profits, making investments in McDonald's reimaging program harder to afford.

The Pacific Sierra operators explicitly said in their memo that they do not share the sentiment given by chief financial officer Pete Bensen in McDonald's first-quarter earnings call, when he said the chain would sacrifice margins to gain market share in an anemic economy.

"Owner cash flow is already eroding ... and heavy discounting is also shrinking the bottom line," they wrote.

Heriaud responded that franchisees would continue to work with McDonald's and exert their influence on value marketing strategy through OPNAD. "It's the owner-operators who decide that through a national voting process," he said. "The company can't determine value when, at the end of the day, the OPNAD vote comes from the operator community."

At the end of 2012, for example, OPNAD approved new $1 items like the Grilled Onion Cheddar Burger but rejected a move to sell hamburgers and cheeseburgers for 69 cents and 89 cents, respectively.



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