Nice Ice

Gary Brunswick
Northern Michigan University

Brian Zinser
Northern Michigan University

ABSTRACT

The case involves a proposal for a scalable regional business (fictitious) which provides a turnkey solution to bars, restaurants, and other institutional businesses which need a regular supply of ice. The entrepreneur who is considering launching this business is attempting to fine tune his business plan, and is encountering some key strategic decisions which will determine the future success of the company.

Keywords: Business-to-business services, services marketing, entrepreneurship, marketing strategy, franchising, subscription-based services

Note: This is a fictitious case. All information contained herein was fabricated by the author(s). Any similarity contained herein to actual persons, businesses, events, etc. is purely coincidental

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Introduction

"Argggh !, not again. Wouldn't it be nice if this #&%! ice machine worked and I didn't have to worry about running out of ice" shouted Skip Longwaite, owner of the Do Drop Inn, a local watering hole where Jack "Buzz" Ogaldorf was sitting, enjoying his favorite beverage. Jack wondered what Skip was upset about now, and after a brief moment realized that the ice machine was not working again, which appeared to happen quite frequently at the Do Drop Inn. While Skip was instructing one of the wait staff to go to the local convenience store to buy 10 bags of ice, Jack had an inspirational idea – what if business owners like Skip had the option of leasing their ice making equipment, along with a service contract and possibly an unconditional guarantee of never running out of ice ? Would there be a market for this type of service ? How big is the market ? How would the pricing work ? Would the business be profitable ? Jack finished his drink, and decided to go back to his home office to begin drafting a business plan for a company he might launch under the name of Nice Ice, which was inspired by Skip's shouting a few minutes earlier.

The Market For Ice

After some quick research on the internet, Jack quickly realized that a small business owner can spend a lot of money on the front end installing an ice machine which will fill the needs of that specific bar, restaurant, or institutional service provider (e.g., hospitals, nursing homes, schools, universities, etc.). Prices of ice machines range from $1,000 to well over $ 5,000, and then installation costs would add to that total (plumbing and electrical costs related to a commercial installation scenario). Additionally, there would be periodic emergency situations involving repairs to the machine, etc., which invariably happen at the "worst" time.

Over recent years, Jack also noticed that there was an emerging trend, in both the consumer market (B2C) and also in the industrial or business-to-business (B2B) market, involving subscription-based services. Netflix is a prime example of a highly successful subscription-based services in the B2C market, while in the B2B market, companies such as Caterpillar and John Deere are putting hardware sensors on all of their products and charging a subscription fee to use their product vs. the customer owning the product outright. Cintas is another example of a firm which has been very successful in the B2B market providing various subscription-type services for bars, restaurants, and other retailers; Cintas provides uniforms, rugs and mats, and fire protection services to these types of business on a continual basis (i.e., Cintas picks up dirty uniforms, rugs, mats, etc. and replaces them with newly cleaned items on a systematic basis). The more Jack thought about subscription-based services in the B2B market, the more examples he was able to come up with, and in a way it reminded him of several college courses he took as an undergraduate where the classic "make vs. buy" or "buy vs. lease" decisions were covered in case studies.

Starting Up: Go or No Go ?

After doing considerable research, and talking with possible B2B customers of all types (bars, restaurants, hotels, institutional food service operators such as schools, universities,

hospitals, etc.) Jack started to develop some quantitative estimates related to possibly starting up Nice Ice.

In terms of specific startup costs, here is what he initially came up, including a range of starting inventory of various sized ice machines (including ice storage bins):

Small machine (250 - 500 lb capacity) = $ 1,500 per unit (20 units to start up)
Medium machine (500 – 750 lb capacity) = $ 2,500 per unit (20 units to start up)
Large machine (750-1,000 lb capacity) = $ 3,500 per unit (20 units to start up)
Extra large machine (1,000 – 1,250 lb capacity) = $ 4,500 per unit (20 units to start up)
Jumbo machine (1,500+ lb capacity) = $ 5,000 per unit (20 units to start up)

Jack also estimated that average installation costs (per unit) would be about $ 1,000, and assumed these would be covered by the customer, although he considered waiving these fees if the customer signed a long-term contract (minimum of 5 years). A reasonable assumption was that 25% of the customers would pay the $ 1,000 fee in the first year.

He also wondering about limiting his trading or coverage area. Should he limit the coverage area to approximately 1 hour (one way) driving time (for his technicians), which would be approximately 50 miles, or should that be extended to 2 hours (again, one way) driving time, or approximately 100 miles ?

Beyond the ice machines and storage bins, Jack estimated the following would also be needed in order to start up Nice Ice:

Plumbing and electrical supplies, including some spare parts inventory (necessary for initial installations) = $ 5,000
One service van (for installations, service calls, etc.) = $ 40,000
Monthly cost of insurance, gas, maintenance for service vans = $ 500
Monthly office rent = $ 1,000
Monthly telephone and internet access = $ 400
Annual cost for one administrative assistant (including fringe benefits) = $ 40,000
Annual cost for 1 service technician (for installations, service calls, etc.; includes fringe benefits) = $ 80,000
Annual cost for office supplies, other consumables = $ 10,000
Initial office startup costs (furniture, phones, computers, etc.) = $ 5,000
Annual marketing budget (including digital forms of advertising) = $ 20,000
Start up working capital (for various permits, licenses and unforeseen expenses) = $ 10,000

Jack needed to look at what the total amount of startup costs (in dollars) would be for Nice Ice (i.e., the total $ amount for year 1). Jack also assumed that he would be the primary salesperson for Nice Ice in the initial year(s), with some assistance from the administrative assistant that will work for Nice Ice. Jack was a licensed electrician and plumber, and would envision also helping the service technician which Nice Ice would hire when the workload would require more than 1 technician. Finally, Jack assumed he would not draw any type of salary from Nice Ice in the initial year(s) of operation.

Next, based upon various interviews with potential customers and other factors, Jack estimated the following pricing for each of the 5 sizes of ice machines (including storage bins):

Small machine (250 - 500 lb capacity) = $ 145 per month
Medium machine (500 – 750 lb capacity) = $ 195 per month
Large machine (750-1000 lb capacity) = $ $ 225 per month
Extra large machine (1000 – 1250 lb capacity) = $ 255 per month

Jumbo machine (1500+ lb capacity) = $ 300 per month

Jack wanted to develop 3 different "what if" scenarios based upon possible annual streams of revenue, given the suggested pricing he came up with:

Scenario 1 – Optimistic = all machines are rented within the first year

Scenario 2 – Reasonable = 75 % of all machines are rented within the first year

Scenario 3 – Pessimistic = 50 % of all machines are rented within the first year

Bottom line: Jack wanted to estimate whether or not Nice Ice would generate a profit (before taxes) based upon the estimated cost and revenue numbers, given each of the 3 scenarios. Is the decision "Go" or "No Go", Jack wondered to himself.

Additional Thoughts

Jack had taken a course in services marketing when he was a college student, and wondered about whether or not a service guarantee would be meaningful to his potential customers. One thought he had was to have an unconditional service guarantee, such as "Nice Ice guarantees that you will never run out of ice", but he wondered about the pros and cons of offering such a guarantee, and whether or not it would be both reasonable and possible for Nice Ice to make such a statement. Another idea Jack had was to offer a specific result guarantee, such as "Nice Ice guarantees to respond to any equipment failure within 2 -3 hours of being notified (depending upon location)". This type of specific result guarantee might be more reasonable to offer, depending upon the travel time involved. In the case of any type of service guarantee, Jack assumed that either he or his technician would need to be on call during "normal" business hours and be able to respond to any customer invoking a service guarantee. Jack also assumed that the service technician would be able to bring several hundred pounds of ice with on any service guarantee-based service call, in order to meet the immediate need for ice, and would also bring a replacement ice machine along with, just in case an on premise repair could not be made immediately. For a customer operating a bar, restaurant, or any other business that requires a reliable source of ice, having a solid service guarantee would seem to be an important selling point, or so Jack thought that potential customers would like the idea of never having to worry about the reliability of their ice supply ever again, period.

Another idea that Jack was considering involved possibly franchising the business model behind Nice Ice, perhaps after several years of successful operation. During his college years, Jack became familiar with the concept of franchising in several of his marketing courses, and realized there were two primary sources of revenue from the franchisor's viewpoint: the one-time franchise fee, and then the monthly royalty payments. What would a prospective franchisee be willing to pay for a Nice Ice franchise ? What would be an appropriate royalty fee (monthly, assuming it would be a percentage of $ sales generated by the franchisee) ? What would be the starting up costs associated with franchising ? What about marketing-related costs ? On-going training costs ? Franchising is a fast way to expand geographically, but would Jack be better off retaining corporate ownership of various Nice Ice locations if he were to expand. Might some competitor's emerge over time, using the same business model ?

Heading Back To Where This All Started

A few weeks had passed, and Jack was still thinking, from time to time, about all of these issues surrounding the business model behind Nice Ice. As Jack was driving, he thought it might

be a good idea to head back to the place where all of this started – the Do Drop Inn – to again enjoy his favorite beverage and catch up with the bar's owner. Upon his arrival back at the Do Drop Inn, Jack sat down at his favorite bar stool, and waived to the owner, Skip Longwaite, who seemed to be in an exceptionally good mood that day. Since Skip was in a good mood, Jack thought this would be a good opportunity to "pick" Skip's brain about his current thinking and ideas for Nice Ice, and have Skip play the role of "devil's advocate", attempting to "punch holes" in Jack's overall strategy and the specific tactics and elements he had developed related to Nice Ice. After about an hour or so of deep conversation, Skip had agreed with Jack that there was some merit in the idea behind Nice Ice, and even commented that perhaps one day, when (hopefully) Nice Ice and Jack are well-known, he (Skip) could say that he had some involvement in the early days behind Nice Ice. Jack thanked Skip for his feedback, thoughts and idea, and then headed out the door of the Do Drop Inn, still wondered whether or not he should launch Nice Ice. As Jack drove back to his home office, he thought perhaps another look at the numbers would help him make a final decision on Nice Ice. Jack had been successful working for many years as a licensed plumber and electrician, and had accumulated enough money to easily launch and fund Nice Ice for several years, but should he move forward with this business idea ?

NICE ICE TEACHING NOTE

Case Description

The case involves a proposal for a scalable regional business (fictitious) which provides a turnkey solution to bars, restaurants, and other institutional businesses which need a regular supply of ice. The entrepreneur who is considering launching this business is attempting to fine tune his business plan, and is encountering some key strategic decisions which will determine the future success of the company.

Case Synopsis

Jack "Buzz" Ogaldorf is visiting one of his favorite "watering holes" known as the Do Drop Inn, and as he is enjoying his favorite beverage, the owner of the Do Drop Inn (Skip Longwaite) is expressing frustration over the ice machine breaking down once again. While watching the bar owner scramble to respond to this problem (which appears to happen all too frequently), Jack has an idea for a subscription-based business that would provide an ice machine, storage bin, and the necessary installation and repair services to bar owners, restaurants, and other institutional users of ice. Being a licensed plumber and electrician by trade, Jack also took some business-related courses when he was in college, including courses in marketing, and as such he develops a listing of startup and ongoing costs for this business, which he names Nice Ice. Similarly, he develops three different revenue scenarios, based upon a range of 5 different sized ice machines and storage bins. Jack also wonders about offering a service guarantee through Nice Ice, so customers will never have to worry about ice machines breaking down again. An additional consideration which Jack thinks about has to do with expanding this business over time; would franchising be a good way to grow the business, vs. outright corporate ownership of different geographic locations for Nice Ice.

Notes To Instructors

This case can be used in a variety of classroom settings, including an introductory marketing course, introduction to business course, entrepreneurship course, or as a case early in a course related to marketing strategy or marketing management. Students, working individually or in teams, can be assigned the possible case teaching questions discussed below. The case is a good example of how an entrepreneur may approach the decision to possibly launch a new business, and the case uses basic analyses including break even, scenario analysis, and aspects of services marketing and the possibility of franchising.

It should also be noted that Nice Ice is a fictitious company, but the issues and examples used in the case reflect a range of research and experiences developed by the case author(s) over time. Any questions regarding the case can be directed to the case author(s)

Possible Case Teaching Questions

1. Comment on how profitable is this business might be at some point within the first year of operation based upon the startup and on-going costs cited in the case vs. the 3 different "what if" scenarios that were given (i.e., Scenario 1 – Optimistic = all of the

machines are rented within the first year), Scenario 2 – Reasonable = 75% of all machines are rented within the first year, and Scenario 3 – Pessimistic = 50% of all machines are rented within the first year.

Starting inventory of various sized ice machines (including ice storage bins):
Small machine (250 - 500 lb capacity) = $ 1,500 per unit (20 units to start up) = $ 30,000

Medium machine (500 – 750 lb capacity) = $ 2,500 per unit (20 units to start up) = $ 50,000

Large machine (750-1000 lb capacity) = $ 3,500 per unit (20 units to start up) = $ 70,000

Extra large machine (1000 – 1250 lb capacity) = $ 4,500 per unit (20 units to start up) = $ 90,000

Jumbo machine (1500+ lb capacity) = $ 5,000 per unit (20 units to start up) = $ 100,000

Total investment in ice machines (including storage bins) = $ 340,000

Note that Jack would be able to purchase all of these ice machines (including ice storage bins) using his own capital, along with self-funding any additional startup costs for the first year (which will be discussed later in this teaching note).

Jack also estimated that the average installation costs (per unit) would be about $ 1,000.00, and assumed these would be covered by the customer, although he considered waiving these fees if the customer signed a long-term contract (minimum of 5 years). Assume that 25 % of all customers do not sign a 5-year contract, and end up paying $ 1,000 for each installation.

He also wondering about limiting his trading or coverage area. Should he limit the coverage area to approximately 1 hour (one way) driving time (for his technicians), which would be approximately 50 miles, or should that be extended to 2 hours (again, one way) driving time, or approximately 100 miles ? More will be discussed regarding the trading area for Nice Ice and possible service guarantees later in this teaching note.

Beyond the ice machines and storage bins, Jack estimated the following would also be needed in order to start up Nice Ice:
Plumbing and electrical supplies, including some spare parts inventory (necessary for initial installations and any repairs) = $ 5,000

One service van (for installations, service calls, etc.) = $ 40,000

Monthly cost of insurance, gas, maintenance for service vans = $ 500 per van x 12 = $ 6,000

Monthly office rent = $ 1,000 x 12 = $ 12,000

Monthly telephone and internet access = $ 400 x 12 = $ 4,800

Annual cost for one administrative assistant (including fringe benefits) = $ 40,000

Annual cost for 1 service technician (for installations, service calls, etc.; includes fringe benefits) = $ 80,000
Annual cost for office supplies, other consumables = $ 10,000
Initial office startup costs (furniture, phones, computers, etc.) = $ 5,000

Annual marketing budget (including digital forms of advertising) = $ 20,000

Start up working capital (for various permits, licenses and unforeseen expenses) = $ 10,000

Overall start up and annual costs not including ice machines and ice storage bins = **$** 232,800

Total start up and annual costs including ice machines and ice storage bins = $ 572,800

Next, based upon various interviews with potential customers and other factors, Jack estimated the following pricing for each of the 5 sizes of ice machines (including storage bins):

Small machine (250 - 500 lb capacity) = $ 145 per month x 12 = $ 1,740

Medium machine (500 – 750 lb capacity) = $ 195 per month x 12 = $ 2,340

Large machine (750-1000 lb capacity) = $ 225 per month x 12 = $ 2,700

Extra large machine (1000 – 1250 lb capacity) = $ 255 per month = $ 3,060

Jumbo machine (1500+ lb capacity) = $ 300 per month x 12 = $ 3,600
Total potential annual revenue if one size of each of the ice machines and storage bins are rented or leased by a customer = $ 13,440

Jack wanted to develop 3 different "what if" scenarios based upon possible annual streams of revenue, given the suggested pricing he came up with:

Scenario 1 – Optimistic = all 100 machines are rented within the first year

Small machine (250 - 500 lb capacity) = $ 145 per month x 12 = $ 1,740 x 20 = $ 34,800

Medium machine (500 – 750 lb capacity) = $ 195 per month x 12 = $ 2,340 x 20 = $ 46,800

Large machine (750-1000 lb capacity) = $ 225 per month x 12 = $ 2,700 x 20 = $ 54,000

Extra large machine (1000 – 1250 lb capacity) = $ 255 per month = $ 3,060 x 20 = $ 61,200

Jumbo machine (1500+ lb capacity) = $ 300 per month x 12 = $ 3,600 x 20 = $ 72,000
Total potential annual revenue = $ 268,800 (note: also assume $ 25,000 in revenue for installations, given that some customers would not sign 5-year contracts) so the total would be $ 293,800.
Scenario 2 – Reasonable = 75 % of all machines are rented within the first year (15 machines per category)
Small machine (250 - 500 lb capacity) = $ 145 per month x 12 = $ 1,740 x 15 = $ 26,100

Medium machine (500 – 750 lb capacity) = $ 195 per month x 12 = $ 2,340 x 15 = $ 35,100

Large machine (750-1000 lb capacity) = $ 225 per month x 12 = $ 2,700 x 15 = $ 40,500

Extra large machine (1000 – 1250 lb capacity) = $ 255 per month = $ 3,060 x 15 = $ 45,900

Jumbo machine (1500+ lb capacity) = $ 300 per month x 12 = $ 3,600 x 15 = $ 54,000
Total potential annual revenue = $ 201,600 (note: also assume $ 18,750 in revenue for installations, given that some customers would not sign 5-year contracts; $ 18,750 is 75% of the $ 25,000 in installation revenue cited in Scenario 1) so the total would be $ 220,350.
Scenario 3 – Pessimistic = 50 % of all machines are rented within the first year (10 machines per category)

Small machine (250 - 500 lb capacity) = $ 145 per month x 12 = $ 1,740 x 10 = $ 17,400

Medium machine (500 – 750 lb capacity) = $ 195 per month x 12 = $ 2,340 x 10 = $ 23,400

Large machine (750-1000 lb capacity) = $ 225 per month x 12 = $ 2,700 x 10 = $ 27,000

Extra large machine (1000 – 1250 lb capacity) = $ 255 per month = $ 3,060 x 10 = $ 30,600

Jumbo machine (1500+ lb capacity) = $ 300 per month x 12 = $ 3,600 x 10 = $ 36,000
Total potential annual revenue = $ 134,400 (note: also assume $ 12,500 in revenue for installations, given that some customers would not sign 5-year contracts; $ 12,500 is 50% of the $ 25,000 in installation revenue cited in Scenario 1) so the total would be **$** 146,900.
In summary:
First year startup and operational costs combined = $ 232,800 + $ 340,00 = $ 572,800
Scenario 1 (100% of machines rented) total revenue = $ 293,800
Scenario 2 (75% of machines rented) total revenue = $ 220,350

Scenario 3 (50% of machines rented) total revenue = $ 146,900

Overall conclusion: Nice Ice will not be profitable in the first year under any of these scenarios. However, things will be different in year 2, as the next question illustrates, given that some one-time costs will not be relevant in year 2 and subsequent years.

2. How might 2nd year profitability be different for Nice Ice vs. 1st year profitability ?

Students need to realize that a number of one-time costs associated with the first year of operation would not be incurred in the 2nd year. For example, given that Jack already paid for these ice machines (including storage bins) these costs would not be repeated in year 2 and beyond, although it is important to also recognize that the payback on the $ 340,000 investment in ice machines and ice storage bins needs to be paid back in a reasonable amount of time. If demand exists, Jack could purchase additional ice machines in year 2 and beyond (and students could be tasked with additional scenarios along these lines).

Starting inventory of various sized ice machines (including ice storage bins):

Small machine (250 - 500 lb capacity) = $ 1500 per unit (20 units to start up) = $ 30,000

Medium machine (500 – 750 lb capacity) = $ 2500 per unit (20 units to start up) = $ 50,000

Large machine (750-1000 lb capacity) = $ 3500 per unit (20 units to start up) = $ 70,000

Extra large machine (1000 – 1250 lb capacity) = $ 4500 per unit (20 units to start up) = $ 90,000

Jumbo machine (1500+ lb capacity) = $ 5000 per unit (20 units to start up) = $ 100,000

Total investment in ice machines (including storage bins) = $ 340,000

Beyond the ice machines and storage bins, Jack estimated the following would also be needed in order to start up Nice Ice, however not all of these costs would be relevant in the 2nd year and beyond:

Plumbing and electrical supplies, including some spare parts inventory (necessary for initial installations and any repairs) = $ 5,000 (Note: it is reasonable to assume these would be annual costs)

One service van (for installations, service calls, etc.) = $ 40,000 (1-time cost covered in year 1)

Monthly cost of insurance, gas, maintenance for service vans = $ 500 per van x 12 = $ 6,000

Monthly offices rent = $ 1,000 x 12 = $ 12,000

Monthly telephone and internet access = $ 400 x 12 = $ 4,800

Annual cost for one administrative assistant (including fringe benefits) = $ 40,000

Annual cost for 1 service technicians (for installations, service calls, etc.; includes fringe benefits) = $ 80,000
Annual cost for office supplies, other consumables = $ 10,000
Initial office startup costs (furniture, phones, computers, etc.) - $ 5,000 (1-time cost covered in year 1)

Annual marketing budget (including digital forms of advertising) = $ 20,000

Start up working capital (for various permits, licenses and unforeseen expenses) = $ 10,000 (1-time cost covered in year 1)

Overall annual costs for year 2 = $ 177,800

Based upon the significantly lower operating costs in year 2 (and moving beyond year 2), Nice Ice would be profitable under both scenarios 1 and 2, and these profits could be used to pay back the initial $ 340,000 investment in the ice machines (including ice storage bins) and eventually Jack could begin to draw a salary from the business
Scenario 1 (100% of machines rented) total revenue = $ 293,800 – $ 177,800 = $ 116,000 gross profit
Scenario 2 (75% of machines rented) total revenue = $ 220,350 - $ 177,800 = $ 42,550 gross profit
Scenario 3 (50% of machines rented) total revenue = $ 146,900 - $ 177,800 = $ 30,900 loss

If 100% of the machines are rented, payback on the initial $ 340,000 investment in the ice machines and ice storage bins would be achieved by the end of year 3 of operation for Nice Ice.

Note that if sufficient demand exists, Jack could purchase additional ice machines in year 2 and beyond (assuming 100% of the existing inventory of ice machines and storage bins are rented or lease), and students could be tasked with additional scenarios along these lines.

3. Should Jack and Nice Ice consider offering an unlimited service guarantee (i.e., customers will never run out of ice) or more of a specific result service guarantee (i.e., we promise to fix your nice machine within 2-3 hours or we will replace it immediately). Which option would you select and why ? What should the “trading area” or service coverage area be for Nice Ice ?

Offering a service guarantee of some type would be attractive to customers of Nice Ice, and this issue ties in with what the trading area should be for the firm. It is suggested that a 1-2 hour driving limit (one way) should be put into place whereby any customer beyond that range would not be able to invoke the service guarantee. Both Jack and the one service technician would need to be “on call” 24/7 in order to honor the service guarantee, and some potential problems might emerge if 2 or more customers experience problems at the same time, although with brand new ice machines being

installed the likelihood of this happening would seem to be relatively low, at least for the first several years of operation.

Another issue to consider would be adding a price premium to different levels of service guarantees. An unconditional guarantee of never running out of ice might be attractive to some customers, who in turn would be willing to pay a monthly surcharge (say $ 10-20 more per month) to have this level of service. Customers who would not opt for the unconditional guarantee would still have some coverage, but it might be phrased in a way whereby Nice Ice promises to be there to make the repair within 2-3 hours, depending upon location. Students could do some "what if" analysis with the additional revenue generated from customers (say 10% up to 25%) who would be willing to pay the surcharge for the unconditional guarantee.

4. Assuming Jack can achieve a good level of profitability for Nice Ice after several years of successful operation, should he consider franchising the business, vs. expanding the business with corporately-owned locations ? What are the +/- of franchising from the viewpoint of the franchisor ? From the viewpoint of the franchisee ? From a quantitative and cash flow viewpoint how would expansion using franchising compare to expansion using corporately-own locations ?

Students should be asked to prepare a list of advantages and disadvantages of franchising, from the viewpoint of both the franchisor as well as the franchisee. Various sources on franchising are available online, including the following:

https://smartasset.com/career/the-pros-and-cons-of-franchising

https://www.forbes.com/sites/jaredhecht/2019/02/27/the-pros-and-cons-of-buying-a-franchise/?sh=290984831198

https://smallbiztrends.com/2020/05/pros-and-cons-of-franchising.html

Some typical +/- of franchising from the two perspectives (Franchisor and Franchisee) include the following:

Franchisee Advantages:

Relatively small investment vs. starting a similar business with strong brand equity "from scratch"
Well-known brand name(s) (could be both goods and/or services)
Standard procedures and skills (achieved through front-end and ongoing training)
Well-developed business model and operating plan
Cooperative marketing programs benefit all franchisees
Exclusive territorial selling rights
Volume purchases results in lower per unit costs

Franchisee Disadvantages:

Potential oversaturation – too many franchises are being sold in areas, resulting in cannibalization of sales
Tying agreements require franchisees to only buy from selected suppliers
Cancellation provisions exist, and could terminate the franchisee's operations
Royalties are tied to sales, not profits

Franchisor Advantages:

Very fast way to grow (vs. opening corporately-owned stores)
Improved cash flow (again, vs. opening corporate-owned stores, almost the opposite in terms of cash flow)
Franchisor has some control in selecting qualified franchisees
Franchisor has the ability to enforce strict regulations over operations
Franchisees are motivated by ownership; this benefits the franchisor in terms of higher royalties
Franchisor can gain additional revenue every time an existing franchise is sold to a new franchisee

Franchisor Disadvantages

Image is impacted by everyone; negative publicity from one franchisee can impact all franchisees
Sale and resale values are influenced by whether or not revenue is increasing, stable, or decreasing
Potential lack of uniformity across franchisees can exist if operating standards are not enforced

Students should be encouraged to do some external research on what a typical one-time franchise fee would be for a company such as Nice Ice, and what the royalty structure would be. As a starting point for analysis and discussion, consider the following:

One-time franchise fee = $ 40,000 (includes front-end training and on-going support from franchisor)

Royalties = 5% of sales

If Nice Ice sold 50 franchises in a single (first) year, and if each franchise generated revenue or sales of $ 300,000 per year, the following revenue would be achieved by the franchisor:

One-time franchise fee = 50 x $ 40,000 or $ 2,000,000 (note: these are 1 time sources of revenue)

Royalties = 50 x $ 300,00 = $ 15,000,000 x .05 = $ 750,000 (note: these are ongoing sources of revenue)

It should be noted that Nice Ice would also incur various types of ongoing operational costs as the Franchisor, including:

Legal fees associated with developing the franchise agreement
Initial training costs for new franchisees
Ongoing training and monitoring costs for existing franchisees
Expansion of franchisor corporate office staff to handle increased communications with franchisees
Increased travel costs for franchisor
Increased promotional costs for franchisor

5. What should Jack do ? Go ahead and launch Nice Ice, or not launch Nice Ice. Grow via corporately-owned locations, or grow via franchising ?

Students individually, or in teams, could prepare a brief presentation for the rest of the class to argue for their recommendation, including whether or not a service guarantee should be offered, and whether or not franchising is something which Nice Ice should consider after several years of successful operation (vs. Nice expanding on their own with corporately-own locations). The faculty member, at some point in the case discussion, might ask if students looked online to see if any similar businesses currently exist. At the time of the writing of this case, an example business would be a company called "Easy Ice" (see easyice.com).

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https://smartasset.com/career/the-pros-and-cons-of-franchising
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