Due Diligence in Independent Small Business and Franchising
An Empirical Study from Australia

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Abstract

This research reports an in depth analysis of the type of due diligence activities that prospective independent small business operators and franchisees in Australia undertake prior to purchasing or starting up their business. Although both academic literature and industry publications promote the notion of undertaking ‘proper due diligence’, there is a lack of empirical research into the effectiveness of due diligence on business outcomes. This research attempts to fill this void. A unique contribution of the research is the comparison between independently owned small businesses and those operated by franchisees.

Using a qualitative approach, some 60 currently and formerly operating independent small business owners and franchisees were personally interviewed by the research team. Participants were located across five Australian states and territories in capital cities, regional cities and towns, and remote locations. Respondents were selected from a range of industries representing diverse business experiences. The interviews explored the diversity of approaches to undertaking due diligence prior to entering the business.

The research revealed that differences occur in both the type and amount of due diligence undertaken by independent small business owners and franchisees and highlighted further differences between currently operating participants and those who had exited their businesses. Many participants were unfamiliar with the term ‘due diligence’ or with how to conduct effective research into the business opportunity.

In general, the due diligence undertaken by participants was relatively unsophisticated with few exceptions of rigor and planning. Where prospective independents and franchisees were entering business for the first time their appreciation of business was naïve. A steep learning curve followed during which they often recognized flaws in their initial research. As a result of this qualitative depth research, we present a set of propositions regarding due diligence and a model for future testing on a large sample.

Key words: Due diligence, Expectations, Franchise, Independent small business, Pre-entry, Start-up

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