NBER WORKING PAPER SERIES

ARE FRANCHISES BAD EMPLOYERS?

Peter Cappelli
Monika Hamori

Working Paper 13327
http://www.nber.org/papers/w13327

NATIONAL BUREAU OF ECONOMIC RESEARCH
1050 Massachusetts Avenue
Cambridge, MA 02138
August 2007

This article is forthcoming in Industrial and Labor Relations Review. Thanks to David Hsu and Anne Marie Knott for helpful comments. The research in this paper was conducted while the authors were Special Sworn Status researchers of the U.S. Census Bureau at the Center for Economic Studies. Research results and conclusions expressed are those of the authors and do not necessarily reflect the views of the Census Bureau. This paper has been screened to insure that no confidential data are revealed. Financial support was provided by the Center for Human Resources at the Wharton School. Please address comments to the first author at: Department of Management, The Wharton School, University of Pennsylvania, Philadelphia, PA 19104-6370 or Cappelli@wharton.upenn.edu.

Are Franchises Bad Employers?
Peter Cappelli and Monika Hamori
NBER Working Paper No. 13327
August 2007
JEL No. J31,L22

ABSTRACT

Franchise jobs are often described as representing the epitome of the "low road" approach to managing employees: high turnover, little training, deskilled jobs, and little employee involvement, practices often seen as unsophisticated. Research on franchise operations suggests, however, that the basic operating principles and practices of franchises tend to be more sophisticated than those of equivalent independent operators. We might therefore expect their employee management practices to be more advanced as well, challenging the stereotype of franchise jobs. We use data from a national probability sample of establishments to examine the relationship between franchise status and employment practices. While descriptive statistics suggest that franchise operations use low road practices, once industry, size, and other control variables are included in the analysis, franchise operations appear on important dimensions to offer better jobs with more sophisticated systems of employee management than similar non-franchise operations.

Peter Cappelli
The Wharton School
Center for Human Resources
University of Pennsylvania
Philadelphia, PA 19104-6358
and NBER
cappelli@wharton.upenn.edu

Monika Hamori
Instituto de Empresa
monika.hamori@ie.edu

Introduction

Franchises are an important part of the U.S. economy. There are an estimated 1,500 franchise companies operating in the U.S. doing business through 320,000 retail units (see International Franchise Association estimates). Our data, described in more detail below, suggests that they represent about five percent of all establishments in the U.S. Franchises represent an alternative to traditional forms of business operations. They signify a legal agreement where the independent franchisee sells a product or service using the brand name and/or operating system of the franchisor, typically in return for a lump sum payment and annual royalty fee (Shane, 1996, Shane & Foo, 2001).

Franchises have a market-like aspect due to the exchange of capital and products between the franchisor and the franchisee; they also have a hierarchical aspect due to the uniform operating procedures set by the franchisor (Norton, 1988). Franchises also represent a hybrid between the attributes of small and large-scale operations in that they function with some autonomy as independent establishments but are also part of a much larger franchise organization. The product or service's image, marketing, and basic operating practices are produced most efficiently in large scale by the parent (Rubin, 1978), while the actual production of the goods and services is most efficient when it is decentralized to the place of consumption (Caves and Murphy, 1976).

The management of employees and work organization issues is central to most franchise operating procedures, in part because franchises are especially common in services where labor content is the crucial component. And the popular image of franchises is that they provide low-quality jobs. We consider the conceptual arguments behind that position and then examine it empirically in the analyses below.

Franchises and Employment Practices:

The descriptive literature on franchises reinforces the idea that franchises provide low-quality jobs (e.g. Zuber, 1997; Matusky, 1998; Schaaf, 1994; Feuer, 1988), although most of that work is anecdotal. Franchise outlets appear to make extensive use of part-time and temporary employees (Leidner, 1993) and do not invest much in recruiting because they do not expect employees to be with the organization for a very long time (Royle, 1998). They also appear to pay low wages. Royle (1998), for example, emphasizes the huge disparity between the US average wage and the starting wage at McDonald's. Benefits like health insurance and sick days are entirely absent at some franchise operations (Leidner, 1993). Franchise operations are marked by a very high rate of turnover that can reach 300 per cent per year (Krueger, 1991).

While the practitioner-oriented literature hails the effectiveness and superiority of training practices of franchises (e.g. Zuber, 1997; Matusky, 1998; Schaaf, 1994; Feuer, 1988), Litz and Stewart (2000) survey 307 hardware stores in a trade name franchise chain and question whether franchises train more than independent stores. Whether workers actually learn much from franchise training is another open question. Wildavsky (1999) asserts that fast food franchise workers learn both job-related skills, such as how to operate a cash register or train others, and general, transferable skills such as teamwork, customer service or getting along with coworkers; Leidner (1993), on the other hand, points out that the training for making French fries, for example, consisted of simply watching a short videotape, and the most skilled job, window work, demanded only three to four hours of total training time (Leidner, 1993).

Among the larger and more sophisticated franchises, such as McDonald's, there is at least a priori evidence suggesting that the basic approach to management – generating standardized "best practices" and transferring them across organizations - bears a great deal of similarity to

that of scientific management. Frederick Taylor's model for organizing production work began by systematically gathering up the tacit knowledge of production held by skilled workers and organizing it into precise, formalized rules that defined the performance of each specific task performed by every individual worker (see Taylor, 1947 for a discussion). The effect of scientific management approaches on worker-level outcomes, particularly skill requirements, is extremely well documented: Because knowledge is built into rules, procedures, and systems, individual workers no longer need to have that knowledge, and job requirements fall. (See Braverman, 1974 for the seminal work and Attewell, 1987 for a review.) Less-skilled workers, who are cheaper, can be hired into these de-skilled jobs and then trained to follow the standardized approaches. Leidner's (1993) ethnography of franchise operations argues that their routinization of work practices leads to tight managerial control, detailed job descriptions, and plenty of specifications and regulations, very much like scientific management.

Hierarchical and bureaucratic forms of supervision and control have an independent effect on limiting the autonomy of employees by transferring decision making up the hierarchy (e.g., Perrow 1972; Edwards 1978). The franchise model, where the design and control over operating procedures lies at the franchisor headquarters, very much resembles a bureaucratic control system. Bureaucratic systems of control through hierarchy are also part of the scientific management approach, as the design and control of jobs is separated from the execution of work and transferred to layers of industrial engineers and supervisors. In the case of highly specialized jobs, for example, it is difficult for workers to coordinate their work with others on their own because they often lack the knowledge and the links to do that. Further, highly specialized work is less intrinsically motivating, which again increases the need for hierarchical supervision

(Lawler, 1988). The practices of scientific management and the practice of hierarchical control systems both limit the autonomy and control of employees.

Scientific management implies different outcomes for franchise *management* jobs, however, as managers may need greater skill to execute the operating practices. Parcel and Sickmeier (1988) highlight how McDonald's simultaneously uses a secondary labor market for front-line workers with low entry criteria, low wages, low degree of autonomy and little employment stability, and an upper-tier labor market with high wages and benefits and clear lines of promotion to attract managers with the knowledge, skills, and abilities to develop and maintain these routines.

One argument reconciling why franchises could have more sophisticated management practices in general *and* apparently unsophisticated low road employment practices would be that they rely on these scientific management principles. The poor employment outcomes for front-line workers could be part of an intentional strategy. A great deal of contemporary research in human resources and industrial relations, however, has emphasized the considerable advantages for employers of "high commitment" or "high performance" work systems associated with greater worker involvement and participatory decision processes (e.g. Berg, 1999; Berg, Kalleberg and Appelbaum, 2003). High performance work practices, which focus on employee involvement and team work arrangements, also tend to be accompanied by supporting programs such as worker training (Osterman 1994). Wages for workers employed in high commitment systems are higher than those employed by traditional organizations, especially for managers, supervisors, and technical workers in unionized establishments (Black, Lynch and Krivelyova, 2004). While the early studies on high commitment work systems showed benefits associated with individual performance, the more recent studies demonstrate effects associated with firm-

level outcomes in services as well as the more typical manufacturing settings (e.g., Combs, Liu, Hall and Ketchen, 2006; Preuss 2003).

If the essence of franchise management is to identify effective management practices, standardize and distribute them across franchise outlets, then it is not obvious why franchise operations would not also include high performance work practices in their portfolio. Further, it is not obvious that the descriptive literature on franchise jobs is definitive. Most of the studies that point out the poor quality of employment practices at franchises focuses on fast food outlets, especially McDonald's (e.g. Love, 1985; Parcel and Sickmeier, 1988; Leidner, 1993; Royle, 1998 and 2000). Many of the characteristics of jobs at those franchises appear to be common to all fast food jobs. The franchises that were examined in these studies also tend to be relatively small operations, and small firms often lack the resources to develop human resource practices like training (Kalleberg et al, 1996; Litz and Stewart, 2000). Vickerstaff (1992) found, for example, that smaller firms lacked both the training infrastructure (training specialists and budgets) and the training capacity (employees' time and training skills) to implement training programs. To truly understand the workplace practices that characterize franchises, it is necessary to control for these other attributes that are associated with typical franchise operations as they may well confound any association between job quality and franchise status.

The few studies that control for these factors carefully are those that compare franchisee-owned establishments to company-owned establishments, often in the same chain, e.g., a franchisee-owned Burger King store compared to a company-owned Burger King (e.g., Krueger, 1991 and Bradach, 1998). This approach is very helpful for examining the effects of ownership structure per se, but it cannot examine the effect of franchise operating practices because the basic operating models are the same in company-owned and franchisee-owned operations within

the same chain. The nature of the relationship between franchise operations and employment practices therefore demands further examination, which we turn to below.

Hypotheses

Our central question, based on the conflicting implications of the literature cited above, is whether franchises offer lower quality jobs than do non-franchise operations. The perception that they do is widespread, but whether that apparent association is due to confounding factors is an important empirical question. Research suggests that franchises in general are more sophisticated in their management practices than equivalent non-franchise operations, which might lead one to hypothesize that their workplace practices would also be more sophisticated and not necessarily the "low road" approach with which they are associated.

Asking this question requires first establishing criteria for deciding the quality of jobs: What constitutes a good job? One approach, for example, might be to compare the perceptions of workers themselves in franchise and non-franchise operations: Which ones are more satisfied with their jobs? The difficulty with this approach is that interpreting differences in attitudes across jobs is very complicated because satisfaction levels are in part influenced by expectations, and representative attitudinal data across operations is extraordinarily difficult to obtain. A more straightforward approach is to examine the attributes of jobs directly. Kalleberg, Reskin and Hudson, 2000 focus on three factors to measure job quality: wage level, pension benefits and health insurance. Other aspects of jobs no doubt are important as well, such as promotion prospects, the specific aspects of individual tasks as they relate to principles of job design,

relationships with superiors and other aspects of interpersonal dynamics, etc.[2] Many of these are complicated to measure (or even to define) and, unfortunately, are beyond the scope of the data that we know to exist. We believe most observers would agree that important measures of job quality include aspects of the rewards from work (pay and benefits), employer investments in employees (training programs), and, especially in the context of franchises, work organization practices that affect employee involvement along the lines of high performance systems.

An important caveat to the notion of assessing job quality is that the distinction between good jobs and bad jobs is somewhat arbitrary. In fact, job quality is likely to represent a continuum that depends on which attributes of jobs are being examined. And the fact that workers may have different preferences with respect to these attributes (e.g., some prefer part-time work) makes even a continuum complicated to construct.

Methods and Data

To address the questions above, we need data that can compare the employment practices of franchises to equivalent non-franchises in order to control for possible confounding relationships. To do so, we turn to the National Employer Surveys (see Cappelli 2001 for a description). Conducted by the U.S. Bureau of the Census, the National Employer Surveys are representative surveys of all private sector, for-profit U.S. establishments with more than 20 employees (excluding corporate headquarters). The 1994 National Employer Survey sampled over 4000 of these establishments. The survey was administered via Computer Assisted Telephone Interviewing to a target respondent of the plant manager in manufacturing establishments and the local business site manager in service establishments. The survey also obtained information from multiple respondents where the target respondent thought those

[2] One could imagine controlling for the attributes of individuals holding those jobs as well in order to determine whether jobs are better than one would expect given the quality of the workers. This approach answers a slightly

responses would be more accurate. It asked about establishment characteristics, work organization practices, and human resource practices. The overall response rate was 72% with no apparent differences between respondents and non-respondents on dimensions such as industry type or size. The 1994 public use data file that resulted contains data on 3173 establishments.

The 1996 National Employer Survey interviewed a sub-sample of the establishments from the 1994 survey and also asked whether the establishment was a member of a franchise organization. The response rate for the 1996 survey was 75%. By matching the data from the 1994 survey to the franchise question from 1996, we have a data set with 2136 observations that identifies organizational and work practices for a national sample of franchises and non-franchised establishments.[3]

Cross-sectional data of this kind creates obvious difficulty in establishing causal relationships. That concern is mitigated in this context, however, because the direction of causation seems clear on logical grounds. It is straightforward to see how the decision to become a franchise drives work practices because the use of specific operating procedures is typically required by the franchise agreement. These, in turn, either define the employment practices or drive employment outcomes. It is much more difficult to imagine the reverse case, where employment outcomes exogenously cause an establishment to become a franchise or a

---

different question, though, whether jobs offer a market premium as opposed to whether they are good per se.

[3] Establishments do switch status from franchise to non-franchise and visa versa, although such changes are rare – Peterson and Dant (1990) found that the number of franchisees that have *ever* been an independent operator, e.g., was only 6.7 percent. The rate of change over a short period like 1994 to 1996 is likely to be insignificant for the purposes of empirical analyses. We know so little about what causes franchise status to change in either direction that it is difficult even to speculate as to possible relationships with the other variables. Not all franchise agreements are the same. The important distinction is between "trade name" franchises, where the franchisee acquires the right to sell a particular product and manage its operation with considerable autonomy (e.g., a gas station's relationship with an oil company) versus "business unit" franchises, where the operations are highly structured according to prior agreements (e.g., most fast-food chains). While we might expect relationships with work practices to be stronger for business unit franchises, we cannot distinguish the two in our data.

franchise to switch to a different ownership form. Further, the type of work practices and outcomes we are considering are in no way unique to franchise status, so there is no reason to believe that having these practices would require that a firm take the franchise form.

A different concern with respect to estimation is whether franchise status and work practices are determined simultaneously. Simultaneous observations could bias OLS estimators asymptotically, although OLS estimation may still be preferred over other forms (e.g., by being more robust). Again, the process through which franchise operations take place suggests that franchise status occurs first and then work practices follow. While they may appear to be simultaneous in the sense that most franchise firms begin operations with their work practices in place, the actual process is invariably that operators decide to become a franchise and then roll out the operating procedures, which include work practices.

Variables and Analyses

The arguments above at least satisfy the requirement of Granger Causation and suggest that simple regression models are sufficient to establish the estimates of the relationship between franchise status and work practices and associated outcomes. Among the primary variables to consider in deciding whether franchises offer good jobs are wages, which we measure separately for managerial and non-managerial (typically front-line) workers.[4] This measure is for full-time workers. It would be useful to have similar data for part-time workers as well but such data is unavailable. We also include a count of how many among 10 important benefits the establishment offers its employees. All of these benefits add fixed costs to employment and are typically seen as practices that help create attachment between firms and employees. Not all

benefits are equal in terms of value or cost, of course, and there is a wide range of possible analyses one could conduct to examine relationships with benefits. This approach at least has the benefit of parsimony.[5]

Another important variable is the extent of training offered to employees, which we measure with three variables: First, whether the establishment has a written training program or policy in place, second, the percentage of employees who receive formal training each year, and third, the number of hours of formal training employees receive each year. The last two variables are measured separately for managerial and non-managerial employees.

One way to capture the extent of pay, benefits, training, and other expenditures on employees is with a single measure of total labor costs. This variable comes from the 1997 National Employer Survey, which asks about expenditures for 1996, the year for which the franchise question is collected. [6] We also include other measures of job quality – the percentage of workers who have part-time status, the average education level of the workforce (measured separately for management and non-management employees), and a proxy for turnover and tenure. Actual turnover measures are not available, only the percentage of the workforce with less than one year of tenure. This measure is important in its own right as an indication of the extent of new hires in the workplace. It should vary directly with turnover, but it, like all measures of tenure, can be confounded by employment growth: Growing companies, other

[4] The original question in the survey asked for average hourly pay, but because not all establishments had compensation data in that format, they were allowed to report it as weekly, monthly, or hourly pay. The reports were therefore converted to a standard metric of annual salaries based on 40 hour workweeks and 52 week years.
[5] The benefits are: pension, severance pay, health insurance, dental insurance, life insurance, sick pay, paid vacations/holidays, family leave (this was before the Family and Medical Leave Act), grievance/complaint procedures, and stock options.
[6] The size control variable helps to adjust for difference in labor costs based simply on having more employees. Per employee measures have important caveats, though, in that establishments may differ in their use of part-time labor and overtime hours. If franchises make greater use of part-time workers, e.g., then their labor cost per employee measure should be understated compared to the true expenditure per unit of labor.

things equal, have lower tenure independent of turnover rates. Because employment growth rates are not available, it is important to recognize that this measure is an imperfect proxy for turnover.

We also have two measures for high performance work systems that have been used in previous studies. The first is the percentage of the workforce involved in regularly scheduled meetings to discuss workplace problems. This measure captures something about the extent of employee participation in the workplace, but it is also fair to say that it is an imperfect measure as we do not know how much involvement employees truly have in these discussions. The second measure is whether the establishment has a total quality management program. Hackman and Wageman's (1995) study of TQM practices found that problem-solving teams, a central aspect of high performance systems, was the most common attribute of TQM programs.

In addition, we control for establishment size (measured as the logarithm of the number of employees working at the establishment in 1996) and the industry that the establishment operates in (measured by ten binary variables, the omitted category is "Other manufacturing"). Table 1 presents a description of the ten industries.

We do not have detailed measures of the human capital and demographics of the employees in these establishments other than their average education level. The focus here is on the jobs per se, but attributes of the employees would allow us to answer other questions as well, such as whether franchises disproportionately employ younger workers or whether they pay a premium for equivalent workers as compared to non-franchises.

The analyses below begin with difference-of-means tests for franchise and non-franchise establishments followed by regression models that control for the most important characteristics of establishments that may be spuriously associated with the franchise form. Because the

analyses are examining the possible effect of the franchise form on various practices and aspects of employment, each such aspect in measured by a different dependent variable and is therefore essentially a separate model. Whether each equation should have a unique model specification based on its own theoretical underpinnings is an important question. Without an established literature to define what such models should look like in each case, however, it is not obvious what characteristics or management practices other than industry, size, and establishment age are truly exogenous to franchise status and therefore should be controlled for in the equation. There are also advantages of consistency in using the same model across equations.

In addition to direct effects, franchise status may also have indirect effects on the dependent variables considered here through relationships with other variables. For example, greater use of part-time jobs may reduce average education levels. If the goal is to see what the net effect of franchise operations is, then it is sufficient to examine the reduced form of what are no doubt more complicated relationships: By leaving out possible control variables that could be endogenous to franchise status, all of the possible indirect effects appear together in the franchise coefficient. This approach is sufficient to address the question as to whether franchises are associated with good jobs. The caveat is that it does not answer the more complicated question concerning why franchise jobs might be better or worse.

Results

Table 1 provides descriptive detail on some of the characteristics of franchises in the U.S. by size and industry classification. Smaller establishments (with less than 100 employees) contain a slightly greater proportion of franchises than in the overall population (8 versus 5.4 percent). Mid-size establishments (between 101 and 435 employees) have about the same proportion of franchises as in the economy as a whole, while larger establishments

(establishments with more than 435 employees) have about half as many franchise organizations as in the overall economy (3 versus 5.4 percent). Franchises are quite rare in manufacturing. They represent 2.2 percent of organizations in the manufacturing sector versus 5.4 percent in the whole economy. The distribution of franchise organizations in the service sector is twice as great as in the economy as a whole (10.9 vs. 5.4 percent), and franchises are disproportionately concentrated in retail (31.1 percent), in hotels and restaurants (29.7 percent) and in business services (11.8 percent). They are roughly in proportion to the economy as a whole in most of the other service industries. As one would expect, franchise status appears to be related strongly to other important attributes of employers.

-- Insert Table 1 about here –

The difference-of-means tests in Table 2 show that in terms of human capital, franchises pay lower wages and salaries both to their non-managerial workers (20.5 vs. 24.7 thousand USD, $p<.001$) and to their managerial employees (40.6 vs. 49.1 thousand USD, $p<.01$). They employ three times as many part-time workers (6 vs. 18%, $p<.001$) and twice as many employees who have less than one year of tenure with the organization (27 vs. 14%, $p<.001$). The results seem consistent with the stereotype of "bad" jobs, although franchises are significantly more likely to have a formal training policy (72 vs. 58%, $p<.01$) and, on balance, they may provide more training both in terms of the percentage of employees trained and total training hours. What we cannot know from these results is the extent to which the differences in Table 2 are driven by franchise status per se or other attributes that are associated with franchises.

- Insert Tables 2 &3 Here -

The regressions presented in Table 3 control for industry and the size and age of the organization. The results are strikingly different from those in the difference in means tests. There are no significant differences with respect to pay or benefits for franchises; the signs of the variables actually point toward higher pay and benefits for franchises. The results for training are consistent with the idea that franchises provide more extensive and intensive formal training to their employees than do non-franchise operations. Franchise operations are more likely to have a formal training policy (ß=.45, p<.1), they train a significantly higher percentage of their non-managerial workforce (ß=9.34, p<.05) and they provide more training hours per employee (ß=.4, p<.05). And overall, labor costs per employee are higher in franchise operations. There is no support for the idea that franchises pursue a strategy of lower expenditures on employees. Franchises also appear to make greater use of work organization practices associated with employee involvement, such as work-related meetings (ß=2.26, p<.1) and TQM practices (ß=.56, p<.01).

On the other hand, franchises do employ non-managerial employees with fewer years of education (ß=-.19, p<.1), they have a higher percentage of part-time workers (ß=.03, p<.05), and have a higher percentage of employees with less than one year of tenure on the job (ß=4.43, p<.01) than do non-franchise operations.

The size of the coefficients on the control variables remind us just how important basic factors like industry and establishment size are in determining employment outcomes. Consistent with the argument that larger employers provide better working conditions (Brown, Hamilton and Medoff, 1990), large-sized establishments in this sample are also significantly more likely to have higher labor costs, provide higher pay for their managers and for their non-managerial staff, make more investment into the training of their employees, and hire employees

of higher human capital. But the effects associated with franchise status are also sizeable: Controlling for industry and employment levels, for example, franchises spend $170,000 more per year on employees than do non-franchises.

From among the industry controls, the comparison of the "Franchise" variable with the "Hotels and restaurants industry" and "Retail" controls provides useful insights, given that most of the franchises examined in the extant literature operate in these two industry classifications (e.g. Bradach, 1998; Leidner, 1993; Royle, 2000). The predictor "Franchise" often has the opposite coefficient than the predictors "Hotels and restaurants" and "Retail", showing that franchises do take a different approach to managing their employees than establishments in the hotels and restaurants and retail industries per se. In separate analyses, available on request, we examine the interaction between the hotel/restaurant industry variable and franchise status. The coefficient of the interaction variable across the models in Table 3 generally suggests that franchises in that industry provide better employment outcomes, although the results are significant in only about one-third of the cases, possibly because the number of observations in that industry (101) is relatively small.

Finally, the control variable that measures the establishment's turnover rate is significant in all but three of the equations where it is included. Establishments with a higher turnover rate provide lower pay and fewer benefits both to their managerial and non-managerial employees. Their managers and non-managerial employees have lower education levels, and fewer of them are involved in work-related meetings. Such establishments are also less likely to have TQM practices.

Discussion and Conclusions

This study is the first to use nationally representative data to examine franchise operations and their work practices in detail. The basic question we investigate is whether franchise forms of operation are associated with lower quality jobs. The results above suggest that this bad jobs stereotype in franchises may have been based on confounding attributes associated with franchises rather than franchise status per se. Franchises are concentrated in smaller establishments, which have fewer resources, and in industries like hotels and restaurants, which have lower-quality jobs. But within those sectors, franchise operations appear to offer more sophisticated management practices and to make greater investments in their employees. Once we control for size and industry, we find little evidence that jobs are worse in franchises and considerable evidence that they are better than in equivalent, non-franchise operations. While there is some evidence that franchises may hire less qualified workers (in terms of education) and use more part-time roles, they spend more on these workers, offer them more training, and are more likely to engage them in employee involvement-related work systems than do non-franchise establishments. A fair assessment might be that franchise jobs offer more to lower-quality workers.

A related question is whether franchise operations appear to be closer to the scientific management model or the high commitment model for managing employees. The bad jobs argument, especially directed at fast food companies like McDonald's, emphasizes deskilled jobs based on approaches that look much like scientific management. On the other hand, the fact that franchises are generally seen as more advanced in their management practices than equivalent non-franchise operations suggests that they would be more likely to use high performance work practices than non-franchise operations. Franchises do hire less educated front-line employees,

as one would expect from scientific management, but the fact that they spend more money on their employees is certainly inconsistent with the goal of scientific management, which is to lower employee costs by deskilling jobs. We also find no evidence that franchises use better paid and educated managers, as scientific management implies.[7] But the most compelling evidence that franchises are closer to the high performance model is that they make greater use of systems associated with employee involvement and teamwork. Data that could measure more precisely the tasks individual workers perform and the aspects of their job design would be helpful in establishing more clearly the extent to which franchises make use of scientific management as an organizing principle. Additional data on the attributes of the employees might also make it possible to tell whether franchisees treat equivalent workers better and whether, for example, they offer efficiency wage levels of compensation.

One conclusion to be drawn from the results above is that jobs cannot necessarily be classified easily into categories of good and bad. The particular choice of attributes and the mix of outcomes across them suggest that we might need a much more sophisticated system of classifying to reveal how they stack up for workers.

Several important puzzles remain about franchises and work practices, though. An obvious question is why franchises invest more in training but also appear to have higher turnover at least as measured by more low-tenure workers because training investments are lost when workers leave. Franchise training and other arrangements could be structured to earn a return in a shorter time period; it is also possible that turnover at franchises is actually lower than one would expect given the characteristics of the workers they hire (e.g., less educated). But this

[7] An alternative that we cannot examine is that franchises concentrate management skill requirements at headquarters where the operating systems are designed, allowing them to use lower quality, lower paid managers in the establishments.

explanation leads to the more general question that has yet to be answered clearly: What is the comparative advantage of franchises? Spending more per employee than non-franchise operations would appear to put franchises at a considerable cost disadvantage that somehow has to be offset – possibly through superior productivity or some other method of adding value. It is clear, though, that the competitive advantage of franchises is not based on a model of spending less on its employees. The fact that they continue to exist and at least in many areas thrive against non-franchise forms suggests that they must be able to offset the labor cost disadvantage in other ways.

A logical explanation for the above would be that franchises have productivity advantages over non-franchise forms. Unfortunately there is little research on this issue, due to the difficulty of accessing data on franchise financial performance in part because most franchise chains are privately owned (Combs, Michael and Castrogiovanni, 2004). The papers that do look at financial performance compare the performance of the various franchisee-owned outlets (Combs, Ketchen and Hoover, 2004; Darr, Argote and Epple, 1995; Hennessy, 2003), or the franchisee- and company-owned units of the same chain (Sorenson and Sørensen, 2001; Thomas, O'Hara and Musgrave, 1990). The financial performance of franchises vs. non-franchise forms remains for future research to examine. The place to begin would be with the hypothesis that the greater use of practices such as TQM and training in franchises drives higher performance and offsets the labor cost difference.

References

Attewell, Paul.1987. “The deskilling controversy.” *Work and Occupations*, 14(3):323-46.

Berg, Peter. 1999. “The effect of high performance work practices on job satisfaction in the United States steel industry.” *Relations Industrielles,* 1: 111-134.

Berg, Peter; Arne L. Kalleberg and Eileen Appelbaum. 2003. Balancing work and family: The role of high-commitment environments. *Industrial Relations,* 42(2): 168-189.

Black, Sandra E., Lisa M. Lynch, and Anna Krivelyova. 2004.”How workers fare when employers innovate.” *Industrial Relations,* 43(1): 44-66.

Bradach, Jeffrey L. 1998. *Franchise Organizations*. Boston: Harvard Business School Press.

Braverman, Harvey. 1974. *Labor and Monopoly Capital: The Degradation of Work in the 20th Century.* New York: Monthly Review Press.

Brisley, Chester L., and William F. Fielder. 1982. “Balancing cost and accuracy in setting up standards for work measurement.” *Industrial Engineering,*14(5): 82-89.

Brown, William. O. 1998. “Transaction costs, corporate hierarchies, and the theory of franchising.” *Journal of Economic Behavior and Organization,* 36: 319-329.

Brown, Charles, Jay Hamilton and James Medoff. 1990. *Employers large and small*. Cambridge, MA: Harvard University Press

Caves, Richard and William Murphy. 1976. “Franchising: Firms, markets and intangible assets.” *Southern Economic Journal,* 42: 572-586.

Cappelli. Peter. 2001. “The National Employer Survey: Employer Data on Employment Practices.” *Industrial Relations*, 40: 635-647.

Combs, James G.; David J. Ketchen Jr. and Vera Hoover. 2004. A strategic groups approach to the franchising-performance relationship. *Journal of Business Venturing,* 19(6): 877-897.

Combs, James; Yongmei Liu; Angela Hall and David Ketchen. 2006. How much do high-performance work practices matter? A meta-analysis of their effect on organizational performance. Personnel Psychology, 59(3): 501-528.

Combs, James G.; Steven C. Michael; Gary J. Castrogiovanni. 2004. Franchising: A review and avenues toward greater theoretical diversity. *Journal of Management,* 30(6): 907-931.

Darr, Eric D; Linda Argote and Dennis Epple. 1995. The acquisition, transfer and depreciation of knowledge in service organizations: Productivity in franchises. *Management Science,* 41(11): 1150-1162.

Dicke, Thomas. S. 1992. *Franchising in America*. Chapel Hill: University of North Carolina Press.

Edwards, Richard. 1979. *Contested Terrain: The Transformation of the Workplace in the Twentieth Century*. New York: Basic Books..

Feuer, Dale. 1988. "The key to cloning your own business." *Training,* 26(6): 25-33.

Forth, John and Neil Millward. 2004. "High-involvement management and pay in Britain." *Industrial Relations,* 43(1): 98-119.

Godard, John. 2001. "High performance and the transformation of work? The implications of alternative work practices for the experience and outcomes of work." *Industrial and Labor Relations Review,* 54(4): 776-805.

Hackman, Richard and Ruth Wageman. 1995. “Total Quality Management: Empirical, Conceptual, and Practical Issues.” *Administrative Science Quarterly* 40: 309-342.

Hennessy, David A. 2003. Property rights, productivity, and the nature of noncontractible actions in a franchise system. *Journal of Economic Behavior & Organization,* 52(4): 443-468.

Kalleberg, Arne. L., David Knoke, Peter V. Marsden, and Joseph L. Spaeth. 1996. *Organizations in America*. Thousand Oaks: SAGE.

Kalleberg, Arne L., Barbara F. Reskin, and Ken Hudson. 2000. “Bad jobs in America. Standard and non-standard employment relations and job quality in the United States.” *American Sociological Review,* 65(2): 256-278.

Kaufmann, Patrick J. and John Stanworth. 1995. “The decision to purchase a franchise: A study of prospective franchisees.” *Journal of Small Business Management,* 33(4): 22-33.

Knott, Anne Marie, and Bill McKelvey. 1999. “Nirvana efficiency: A comparative test of residual claims and routines.” *Journal of Economic Behavior and Organization.* 38: 365-383.

Krueger, Alan. B. 1991. “Ownership, agency, and wages: An examination of franchising in the fast food industry.” *The Quarterly Journal of Economics,* 106(2): 75-101.

Lafontaine, Francis, and Emmanuel Raynaud. 2002. “The role of residual claims and self-enforcement in franchise contracting.” NBER Working paper No. 8868

Lawler, Edward E. III. 1988. “Substitutes for hierarchy”. *Organizational Dynamics,* 17(1): 4-15.

Leidner, Robin. 1993. *Fast Food, Fast Talk*. Berkeley, Los Angeles, London: University of California Press.

Litz, Reginal. A. and Alice C. Stewart. 2000. “Trade name franchise membership as a human resource management strategy.” *Enterpreneurship Theory and Practice,* 25(1): 125-135.

Love, John F. 1985. *McDonald's. Behind the Arches.* New York: Bantam Books

Matusky, Greg. 1998. "No train, no gain." *Franchising World,* 30(5): 23-24.

Norton, Seth W. 1988. "An empirical look at franchising as an organizational form." *Journal of Business,* 61(2): 197-217.

Osterman, Paul. 1994. "How Common Is Workplace Transformation, and How Can We Explain Who Adopts It? Results from a National Survey." *Industrial and Labor Relations Review*, 47: 173-188.

Parcel, Toby. L., and Sickmeier, M. B. 1988. "One firm, two labor markets: The case of McDonald's in the fast food industry." *The Sociological Quarterly*, 29(1): 29-46.

Peterson, A., & Dant, R. P. 1990. Perceived advantages of the franchise option from the franchisee perspective: Empirical insights from a service franchise. *Journal of Smal Business Management*, 28(3): 43-61.

Perrow, Charles. 1972. *Complex Organizations: A Critical Essay*. Glenview, IL: Scott, Foresman. .

Pizanti, Inbar, and Lerner, Miri. 2003. "Examining control and autonomy in the franchiser-franchisee relationship." *International Small Business Journal,* 21(2): 131-159.

Preuss, Gil. 2003. "High Performance Work Systems and Organizational Outcomes: The Mediating Role of Information Quality." Industrial and Labor Relations Review, 56(4): 590-606.

Royle, Tony. 1998. "Corporate versus societal culture: A comparative study of McDonald's in Europe." *International Journal of Contemporary Hospitality Management,* 7(2): 52-56.

Royle, Tony. 2000. *Working for McDonald's in Europe. The unequal struggle?* London and New York: Routledge.

Rubin, Paul. H. 1978. “The theory of the firm and the structure of the franchise contract.” *The Journal of Law and Economics,* 21: 223-233.

Schaaf, David. 1994. “Inside Hamburger University.” *Training,* 31(12): 18-24.

Shane, Scott. A. 1996. “Hybrid organizational arrangements and their implications for firm growth and survival.” *Academy of Management Journal,* 39(1): 216-234.

Shane, Scott. A. 1998. “Making new franchise systems work.” *Strategic Management Journal,* 19: 697-707.

Shane, Scott A., and Foo, Maw-Der. 1999. “New firm survival: Institutional explanations for new franchiser mortality.” *Management Science,* 45(2): 142-159.

Sorenson, Olav and Jesper B. Sørensen. 2001. Finding the right mix: Franchising, organizational learning, and chain performance. *Strategic Management Journal*, 22(6-7): 713-724.

Taylor, Frederic W. 1947. *Scientific Management*. New York: Harper and Bros.

Thomas, Wade L.; Michael J. O’Hara and Frank W. Musgrave. 1990. The effects of ownership and investment upon the performance of franchise systems. *American Economist,* 34(1): 54-61.

Vickerstaff, Sarah. 1992. “The management of training in a smaller firm.” *Management Development Review,* 5(4): 32-36.

Wildavsky, Ben. 1989. “Inside America’s largest youth training program.” *Policy Review,* 9(Summer): 30-37.

Zuber, Amy. 1997. “Franchisee training: Preparation for the real world.” *Nation’s Restaurant News,*31(42): 3, 75.

Table 1. Descriptive Characteristics of Franchise Organizations*

Establishment size	Independent Establishments	Franchise Establishments	Percentage franchised
Between 20 and 100 employees	652	57	8.04
Between 101 and 435 employees	687	37	5.11
More than 435 employees	682	21	2.99
Total	2021	115	5.38

* Census concerns about data disclosure require that information about the franchise variable be reported in a categorical form.

Industry	Independent Establishments	Franchise Establishments	Percentage franchised
Food and tobacco	98	6	5.77
Transportation equipment, machinery and computers, and instruments	242	9	3.59
Other manufacturing: textile and apparel, lumber and paper, printing and publishing, chemicals and petroleum and Primary and fabricated metals	871	12	1.36
Construction	101	3	2.88
Transportation, communication, utilities and wholesale trade	286	16	5.30
Retail	61	19	31.15
Finance and insurance	142	6	5.41
Business services	75	10	11.76
Health services	74	4	5.13
Hotels, restaurants	71	30	29.70
Total	2021	115	5.38

Table 1. Continued: Means, standard deviations and Pearson correlations for key variables in the analyses

Variable	Mean	St.d.	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
1. Franchise	0.05	0.47	1.00														
2. TQM	51.8	50.0	.00	1.00													
3. Meetings	49.7	42.1	.03	.18	1.00												
4. Educ, managers	14.3	1.55	-.06	.15	.10	1.00											
5. Educ, non-mgr.	12.4	1.11	-.03	.03	.10	.43	1.00										
6. Pay, managers	48.6	20.5	-.10	.13	.08	.22	.13	1.00									
7. Pay, non-mgr.	24.5	11.4	-.09	.12	.08	.26	.28	.43	1.00								
8. Benefits	6.85	2.08	-.06	.36	.19	.30	.21	.25	.32	1.00							
9. % part-timers	6.80	14.7	.19	-.07	.01	-.07	-.02	-.24	-.21	-.14	1.00						
10. % w. low tenure	15.1	17.0	.16	-.10	-.04	-.14	-.06	-.26	-.30	-.24	.22	1.00					
11. Training policy	58.7	49.3	.07	.02	.14	.08	.09	-.01	.06	.22	.09	.03	1.00				
12. %manager trained	48.8	37.2	-.01	.26	.19	.05	.05	.07	.12	.26	-.04	-.06	.21	1.00			
13. Lg hour, manager	2.17	1.42	.03	.30	.19	.10	.10	.08	.13	.33	-.02	-.04	.26	.67	1.00		
14. %non-mgr trained	50.5	38.8	.01	.30	.25	.14	.07	.12	.14	.30	-.08	-.06	.25	.50	.51	1.00	
15. Lg hour, non-mgr	2.13	1.52	.02	.30	.22	.14	.11	.11	.18	.33	-.08	-.10	.26	.45	.66	.73	1.00

Correlations higher than .06 are significant at $p<.05$. Correlations higher than .07 are significant at $p<.01$. Correlations higher than .09 are significant at $p<.001$.

Definition of the variables

1. The establishment is part of a franchise (1. Yes; 0. No)
2. Establishment adopted a formal Total Quality Management program (1. Yes; 0. No)
3. Percentage of non-managerial employees involved in regularly scheduled meetings to discuss work-related problems
4. Average number of years of completed schooling for managers
5. Average number of years of completed schooling for non-managerial employees
6. Annual pay for managers (thousand USD)
7. Annual pay for non-managerial employees (thousand USD)
8. Count of provision of ten employee benefits: pension plan, severance plan, health insurance, dental care benefits, child care subsidies, family leave, formal grievance procedures, life insurance, sick pay, paid vacation/holidays and stock options
9. The number of permanent part-time employees at your establishment.
10. The percentage of current permanent employees who have been with the establishment for less than one year
11. The establishment has a formal/written training policy (1. Yes; 0. No)
12. The percentage of managers who received formal training during the past year
13. Natural log of manager's hourly pay
14. The percentage of non-managerial employees who received formal training during the past year
15. Natural log of non-managerial hourly pay

Table 2. The Employment Practices of Franchise and Non-franchise Establishments: Means, standard deviations and difference of means t-tests

Employment Practices	Franchise		Non-franchise		
	Mean	s.d.	Mean	s.d.	t-test
TQM	52.63	50.15	51.77	49.98	0.18
Work-related meetings	54.77	41.48	49.41	42.18	1.34
Education, managers	14.86	1.90	15.27	1.80	2.28*
Education, non-managerial employees	12.06	1.80	12.47	1.32	2.42*
Average pay for managers	40,585	22,341	49,070	20,354	3.48**
Average pay for non-managerial employees	20,492	12,342	24,743	11,264	3.26***
Provision of ten benefits	6.50	2.30	7.03	1.96	2.43*
Percentage of part-time employees	18.72	23.96	6.14	13.68	5.58***
Percentage of employees with the organization for less than a year	26.57	27.41	14.45	15.98	4.69***
Percentage of organizations with a formal training policy	72.17	45.01	57.91	49.38	3.29**
Percentage of managerial employees trained	48.06	35.68	48.93	37.25	0.23
Average number of training hours for managerial employees	62.23	124.86	34.11	56.08	2.13*
Percentage of non-managerial employees trained	36.68	34.23	28.18	28.17	2.38*
Average number of training hours provided to non-managerial employees	55.55	88.42	50.60	92.95	0.47

Total N = 2136; Franchise N = 115; Non-franchise N = 2021
*** p < .001 ** p < .01 * p < .05

Table 3. The effect of franchise membership on employment outcomes

	DV: Labor costs OLS regression	DV: Pay, non-managers OLS regression	DV: Benefits OLS regression	DV: Education, non-managers OLS regression	DV: Percentage of part-timers Tobit estimates	DV: Percentage of employees with less than 1 year on the job OLS regression
Variables	Coeff (st. er.)	Coeff (st. err)	Coeff (st. er.)	Coeff (st. er.)	Coeff (st. er.)	Coeff (st. er.)
Franchise	170026.6** (57721.92)	.63 (1.15)	.12 (.17)	-.19+ (.11)	.03* (.01)	4.43** (1.59)
Size	62474.41*** (7519.8)	1.71*** (.19)	.61*** (.03)	.10*** (.02)	-.01+ (.00)	.02 (.26)
Food industry	111684.5** (41046.4)	-3.41** (1.16)	.06 (.18)	-.16 (.12)	.00 (.01)	5.48** (1.66)
Machine	-3928.24 (28670.86)	-1.01 (.80)	.17 (.12)	.16* (.08)	-.01 (.01)	-2.37* (1.14)
Construction	40128.45 (42080.24)	10.94*** (1.21)	-.88*** (.17)	.26* (.11)	.01 (.01)	5.65** (1.64)
Transportation	50749.21 (32917.54)	7.17*** (.79)	.55*** (.11)	.67*** (.07)	.04*** (.01)	-1.36 (1.08)
Retail	-11185.34 (87642.33)	-4.77*** (1.43)	.10 (.20)	.28* (.13)	.34*** (.01)	12.70*** (1.92)
Finance	28154.49 (55043.5)	4.66*** (1.19)	1.20*** (.15)	.99*** (.10)	.06*** (.01)	1.70 (1.43)
Business services	-12182.94 (61179.11)	9.18*** (1.43)	.03 (.20)	1.24*** (.13)	.10*** (.01)	15.20*** (1.84)
Health	-33133.02 (58409.18)	-2.06 (1.56)	.05 (.20)	.40** (.13)	.21*** (.01)	7.40*** (1.88)
Hotel and rest.	-26180.53 (68330.58)	-4.49*** (1.21)	-.42* (.19)	.51*** (.13)	.16*** (.01)	19.56*** (1.71)
Est age		.02+ (.01)	.01** (.00)	-.00 (.00)	-.00 (.00)	-.10*** (.01)
% low tenure		-.17*** (.02)	-.02*** (.00)	-.01*** (.00)	.00** (.00)	
Constant	-281691.3*** (45178)	16.03*** (1.12)	3.68*** (.16)	11.70*** (.11)	3.29*** (1.6)	15.48*** (1.52)
	N = 654 F = 8.34*** R2=.13	N =1627 F = 39.3*** R2 = .241	N = 2055 F = 71.2*** R2 = .31	N=1930 F = 18.6*** R2 = .11	N=2055 Chi2 = 853.21*** Ps. R2 = .41	N=2055 F= 35.2*** R2 = .17

+p<.1, *p<.05, **p<.01, ***p<.001

Table 3 continued. The effect of franchise establishments on employee management

	DV: Meetings Tobit estimates		DV: Existence of TQM Logit estimates		DV: Existence of training policy Logit estimates		DV: Log of training hours to non-managers Tobit estimates[8]		DV: Percentage of non-managers trained OLS regressions	
Variables	Coeff	(st. er.)	Coeff	(st. er.)	Coeff	(st. er.)	Coeff	(st. er.)	Coeff	(st. er.)
Franchise	2.26+	(1.18)	.56**	(.23)	.45+	(.23)	.40*	(.17)	9.34*	(4.31)
Size	1.16***	(.18)	.42***	(.037)	.34***	(.04)	.17***	(.03)	4.60***	(.70)
Food industry	-.28	(1.16)	-.11	(.23)	.06	(.22)	-.09	(.18)	-2.63	(4.57)
Machine	.78	(.82)	.39*	(.16)	-.15	(.15)	.02	(.12)	1.97	(3.05)
Construction	1.36	(1.14)	-.83***	(.24)	-.16	(.22)	-.53**	(.18)	-14.39**	(4.29)
Transportation	.60	(.75)	-.67***	(.15)	.41**	(.15)	-.18	(.12)	-7.17*	(2.88)
Retail	-.08	(1.32)	-.55*	(.27)	1.12***	(.29)	-.30	(.21)	-10.75*	(5.28)
Finance	4.94***	(1.17)	-.59**	(.20)	.41*	(.20)	.36*	(.17)	16.66***	(3.93)
Business services	-.23	(1.28)	-.37	(.26)	.36	(.25)	-.63**	(.20)	-19.84***	(5.01)
Health	.96	(1.30)	.09	(.26)	1.26***	(.29)	-.15	(.22)	5.29	(5.30)
Hotel and rest.	3.14**	(1.28)	-.56*	(.24)	.70**	(.25)	-.40*	(.19)	-17.36***	(4.65)
Est age	.00	(.01)	-.01*	(.00)	-.00+	(.00)	.00	(.00)	-.01	(.04)
% low tenure	-.03*	(.01)	-.01**	(.00)	8.95e-06	(.00)	-.00	(.00)	-.01	(.06)
Constant	7.76***	(1.09)	-1.77***	(.22)	-1.57***	(.22)	1.29***	(.17)	28.35***	(4.19)
	N= 1998 Chi2(13) = 73.6*** Pseudo R2 = .01		N = 2040 Chi2(13) = 260.8*** Pseudo R2 = .09		N = 2037 Chi2(13)=139.5*** Pseudo R2 = .06		N = 1567 Chi2(13)=93.1*** Pseudo R2 = .02		N =1675 F = 10.61*** R2 = .08	

+p<.1, *p<.05, **p<.01, ***p<.001

[8] Tobit estimation was used because some establishments report no training of employees, and in those cases, the variable is missing.

Table 3 continued. The effect of franchise establishments on employee management: Evidence for managerial employees

	DV: Pay for managers OLS regression		DV: Education for managers OLS regression		DV: Log of training hours for managers Tobit estimates		DV: Percentage of managers trained Tobit estimate	
Variables	Coeff	(st. er.)	Coeff	(st. er.)	Coeff	(st. er.)	Coeff	(st. er.)
Franchise	1.34	(2.23)	-.05	(.15)	.37*	(.17)	1.23	(1.95)
Size	2.49***	(.36)	.25***	(.03)	.19***	(.03)	3.05***	(.34)
Food industry	-2.09	(2.44)	-.02	(.16)	.03	(.17)	-1.28	(2.01)
Machine	1.07	(1.68)	.29**	(.11)	.14	(.12)	.03	(1.42)
Construction	5.11*	(2.20)	-.19	(.16)	-.39*	(.16)	-4.54**	(1.74)
Transportation	1.13	(1.50)	.13	(.10)	.15	(.11)	1.19	(1.30)
Retail	-13.31***	(2.74)	-.15	(.19)	.04 .	(19)	-.03	(2.21)
Finance	.52	(2.10)	.94***	(.14)	.29*	(.15)	6.16**	(1.98)
Business services	-1.99	(2.58)	1.04***	(.18)	-.05	(.19)	-1.48	(2.03)
Health	-7.21**	(2.58)	1.08***	(.19)	-.08	(.19)	.53	(2.28)
Hotel and rest.	-16.94***	(2.42)	-.11	(.18)	-.07	(.18)	1.63	(2.17)
Est age	.00	(.02)	-.00	(.00)	.00	(.00)	.00	(.02)
% low tenure	-.21***	(.03)	-.01***	(.00)	-.00	(.00)	-.01	(.02)
Constant	39.71***	(2.18)	13.05***	(.15)	1.18***	(.16)	4.12*	(1.84)
	N = 1531 F (13, 1517) = 20.9*** R2 = .15		N = 1930 F (13, 1916) = 19.08*** R2 = .11		N = 1623 Chi2 (13) = 82.87*** Pseudo R2 = .01		N = 1741 Chi2 = 126.58*** Pseudo R2=.03	

+p<.1, *p<.05, **p<.01, ***p<.001