



Trademark Licensing

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When Trademark Licensing Looks Like Franchising: Avoiding Legal Risk

If anyone doubted that trademark licensing has become an essential part of brand management, the last Annual Meeting of the International Trademark Association (INTA) would have set them straight. Several high-powered speakers at that event promoted the view that building brands (the goal of every red-blooded American) now also means building partnerships with others who will borrow and help build your brand for you.

You can be sure that 7000 trademark attorneys gathered in one place also noted the biggest risk posed by lending your brand to others: dilution. But no one (at least no one that I heard over the five-day conference) commented on another risk: That trademark licensing with the controls a brand manager demands may subject it to liability as a franchisor.

Licensing vs. Franchising

Historically, trademark licensing and franchising have been very different legal animals. A trademark licensee was a company experi-

enced in its core business but able to use the licensor's brand to its advantage. The licensor chose the licensee because of its experience in manufacturing and selling such products, and did not try to tell the licensee how to run its business.

A franchisee, on the other hand, sought to borrow not just another company's name but its entire business concept, and was willing to share its revenues with the franchisor in exchange for reduced business risk. The franchisor chose a franchisee because it brought financial resources to the deal, but also because the franchisee spared its franchisor the cost of setting up its own business. A condition of their agreement has always been the franchisee's agreement to run its business almost exactly as the franchisor requires.

Given these differences, there has historically been little risk that a license agreement would be confused with a franchise agreement. In a legal franchise relationship, the franchisee must operate its business pursuant to a marketing plan or "system" imposed by the franchisor; the franchisee must pay a franchise fee; and the franchisee's business must be substantially associated with the franchisor's trademark. Imagine the

typical McDonald's restaurant: It operates under rules imposed by the McDonald's Corp., it sends a percentage of all revenues to the McDonald's Corp., and it exists as a business solely under a trademark borrowed from the McDonald's Corp.

In contrast, the typical licensee has had a very different job. Although it, too, sends a portion of its revenue based on the licensor's brand back to the licensor, it has complete freedom in running its own business separate from the licensor.

But these distinctions are narrowing as brand managers grow increasingly excited about the ways that licensing can build their brands. These brand managers invariably want to exert as much control over their licensees as they exert over their advertising agencies, and as they do so, their licensees look more and more like franchisees. One day, such a licensor is going to find itself sued by a disgruntled (or terminated) licensee for violating state and federal franchise laws, liability for which can be extensive.

Avoiding a Franchise Situation

In order to limit the risk of being considered a franchise, a licensor needs to make sure that its oversight of the licensee's marketing efforts remains oversight and does not become control. This will remain difficult so long as trademark attorneys tell clients that they have to review all uses of

