

Will your trademark license become an inadvertent franchise?

Presented by: Dennis Steinman, Partner, Kell, Alterman & Runstein L.L.P.

Hosted by: Oregon State Bar, Intellectual Property Section

Discussion Outline:

- What is a franchise?
- The inadvertent creation of a franchise
- Best practices for avoiding an inadvertent franchise
- Hypothetical example
- Questions

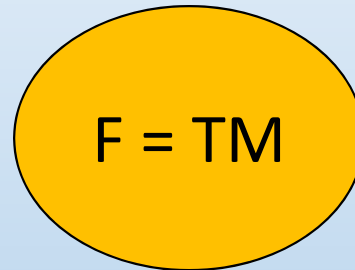
Why does it matter?

- Extensive regulation
 - Federal and state laws
- Cost/delays of regulatory compliance
- Legal consequences
 - Damages
 - Injunctive relief
 - Rescission
 - Potential personal liability
 - Criminal prosecution (felony)
 - Administrative agency remedies
 - Attorney fees

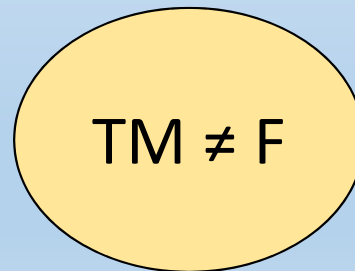


What is a franchise?

- Every franchise is a trademark license



- Not every trademark license is a franchise



Federal Franchise Rule

- **(1)** The franchisee will obtain the right to operate a business that is identified or associated with the franchisor's trademark, or to offer, sell, or distribute goods, services, or commodities that are identified or associated with the franchisor's trademark **[The Trademark License Element]**;
- **(2)** The franchisor will exert or has authority to exert a significant degree of control over the franchisee's method of operation, or provide significant assistance in the franchisee's method of operation **[The Control Element]**; and
- **(3)** As a condition of obtaining or commencing operation of the franchise, the franchisee makes a required payment or commits to make a required payment to the franchisor or its affiliate **[The Payment Element]**.

The Trademark License Element

- Any service mark, trade name, or other advertising or commercial symbol
- Ownership not necessary

The Control Element

- Balancing control and assistance
- Inexperience of franchisee
- Franchisee taking large financial risks
- Methods of operation
- State variation here, AKA “community of interest” or “marketing plan”



The Control Element

- Four factors:
 - a requirement that a franchisee service or repair a product (except warranty work)
 - inventory controls
 - required displays of goods
 - on-the-job assistance with sales or repairs
- FTC policy exemption
 - trademark controls designed solely to protect the trademark owner's legal ownership rights in the mark under state or federal trademark laws (such as display of the mark or right of inspection)

The Payment Element

- Broad
- \$500 at any time prior to or within the first six months of operations
- Mandatory
- Resale or lease
 - Bona fide wholesale prices and reasonable amounts

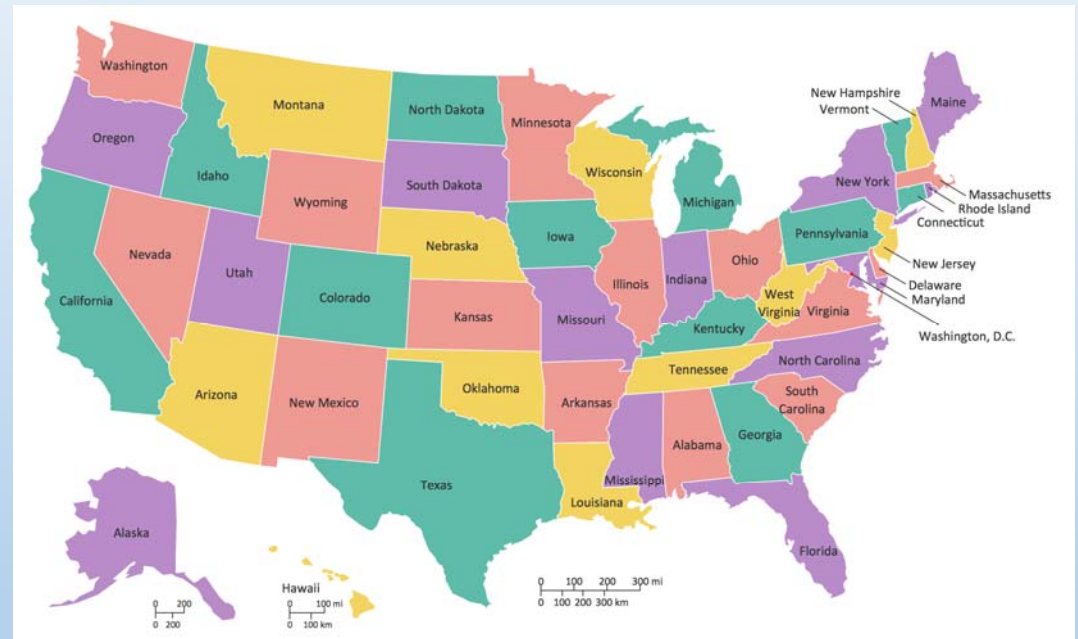


Exemptions and Exclusions

- Scope of relationships
- Single trademark license
- Collateral product licensing
- Licensing agreements entered into during trademark infringement settlement negotiations

State Franchise Regulation

- Variation
- About half of all states
- More restrictive than federal



Disclosure Requirements

- FDD
- Section 5 of the Federal Trade Commission Act

The Inadvertent Creation of a Franchise

- Trademark element easily met
- *Girl Scouts of Manitou Council, Inc. v. Girl Scouts of the United States of America Inc.*
- *To-Am Equip. Co. v. Mitsubishi Caterpillar Forklift Am.*
- *Charts v. Nationwide Insurance Co.*
- *Gentis v. Safeguard Business Systems*

Best Practices

- A rose by any other name
- Avoid the franchise fee
- Keep exemptions and exclusions in mind
- Licensor providing inventory or supplies
- Discovery a violation
- Limit control and assistance



Hypothetical Example

- A local Italian Restaurant, Mama Marinara, has gained national attention for its delicious marinara sauce. Mama Marinara decides to sell bottling rights to Bottlers and allow Bottlers to use the Mama Marinara name in their business. Mama Marinara licenses its top secret marinara sauce recipe to Bottlers, who will then make and sell the sauce according to Mama Marinara's strict standards. Bottlers must buy all the sauce ingredients from Mama Marinara. Mama Marinara also implements advertisements to assist in the sale of the marinara sauce produced by Bottlers. Is this a franchise?



Questions?

Thank you!