

If you are looking at expanding your business by permitting third parties to trade under your brand name or otherwise use your intellectual property, you need to determine whether your arrangements will constitute a franchise or a licence.

This guide will provide you with insight as to the key differences between a franchise and a licence, and tips on identifying the right structure for your arrangement.

DOES IT MATTER WHICH STRUCTURE I CHOOSE?

Yes, as the structure you choose will ultimately dictate your obligations. Franchisors are subject to stringent obligations under the Franchising Code of Conduct (Code), whereas licensors are not heavily regulated in Australia.

The difference between a franchise or licence arrangement is based on many different factors.

Under a licence, you give another person the right to use certain things such as intellectual property, a business name, a logo, or certain software which you have the rights to. There are generally no set restrictions on how the licensee may operate their business, so long as the licensee does not cause harm to the reputation of the licensor or its branding. The most commonly understood example is a software licence.

A franchise is similar to a licence, however a franchise commonly gives a franchisor more control over franchisees, and as a result is more heavily regulated than a licence arrangement. An example of the control that a franchisor has, is the right to require franchisees to comply with an operations/marketing manual, which specifies limitations as to how the relevant intellectual property may be used and can also dictate how a franchisee must operate their business. The most common examples are fast food chains.

The Code applies to franchises in Australia and imposes stringent obligations on franchisors, such as limitations around the types of clauses that may be included in a franchise agreement, and an obligation to disclose certain matters to prospective franchisees.

Often businesses will attempt to disguise a franchise as a licence so as to avoid the responsibilities and obligations of franchisors under the Code. However, the Code will apply to licence agreements which meet the definition of a "franchise", even if the parties call it a licence. There are penalties and serious financial consequences for disguising a franchise as a licence and failing to comply with the Code. This is why legal advice is important.

DEFINITION OF "FRANCHISE AGREEMENT" UNDER THE CODE

A franchise agreement is defined under the Code as an agreement under which:

1. a person (the franchisor) grants to another person (the franchisee) the right to carry on the business of offering, supplying or distributing goods or services in Australia under a system or marketing plan substantially determined, controlled or suggested by the franchisor or an associate;
2. the operation of the business will be substantially or materially associated with a trade mark, advertising or a commercial symbol owned, used or licensed by the franchisor or an associate; and
3. before starting or continuing the business, the franchisee must pay or agree to pay to the franchisor or an associate of the franchisor an amount including, for example an initial upfront fee, a payment for goods or services, a training fee or a royalty fee.

The definition of 'franchise agreement' is very broad, and as noted above, the definition does capture many licence arrangements. Regardless of what label you put on an arrangement, if it falls substantially within the definition of a "franchise agreement" under the Code, then the Code will apply.

KEY CHARACTERISTICS OF A FRANCHISE VS A LICENCE

The following table sets out the key differences between a franchise and a licence arrangement. This list is not exhaustive and each arrangement will turn on its own facts, however, it is a useful starting point for determining how you may wish to structure your arrangement.

FRANCHISE	LICENCE
You control the methods and systems used by the franchisee, including uniforms, fit-outs and the types of goods and services the franchisee is approved to sell within a geographical area or territory.	You will generally have no control as to the methods and systems in place for how the licensee decides to market or distribute the licenced goods. The licensee may be restricted from using the licensed intellectual property outside of certain locations.
You require the franchisee to comply with a marketing plan that you control.	Licencees will determine their own marketing plan.
The business is substantially or materially associated with a trade mark or other symbol.	The licensee may or may not use your trade mark/s, and is not necessarily required to carry on their business using your trade mark.
You offer training on how to operate the business. Ongoing support is often also given.	Training and support is limited.
Numerous fees are generally paid by the franchisee, such as an upfront franchise fee, document preparation fee, royalty fee, and a training fee.	Generally only a licence fee is payable, which may be calculated as an annual or monthly fee, and/or a royalty fee.

TOP TIP ENSURING YOUR ARRANGEMENT IS A LICENCE

Establishing a franchise can be expensive, time consuming and involves ongoing compliance. If you do not want your arrangement to fall within the definition of a franchise, often the best way to ensure that this does not happen is to avoid requiring the licensee to operate under a system or marketing plan substantially determined, controlled or suggested by you. This can leave your brand exposed to risk (for example, if a licensee does not operate the business in the way you want them to), however can be worthwhile if you are only looking at entering into one or two licence arrangements and do not want control over how the licensee operates. On the other hand, if you are planning on expanding and wish to maintain control of your brand, a franchise agreement is likely to be the best option for you.

KEY TAKEAWAY

The decision of whether you choose a franchise or license arrangement will depend largely on your future intentions. We have acted for both franchisors and licensors across a number of industries and would be happy to share our insights as to what arrangement might be best suited to your situation and goals. If you require assistance with choosing the right structure for your business or if you need a franchise or licence agreement prepared, please feel free to contact one of our experienced team members today.