

LICENSING vs. FRANCHISING

[Including “How to Sell Licenses”]

A White Paper and short discussion about greatly lowering the cost of business expansion through low cost licensing rather than investing in the huge expense of franchising.

By

Robert Townsend, Attorney At Law.

bob@townsend.net

Tel. 310 207 0180

Direct Line (cell): 310 592 6294

What You Have to Know

- **There are Many Ways to “Skin a Cat”**. This paragraph is the most important idea of this article; i.e. the “many ways to skin a cat” idea. Though this particular article discusses “licensing versus franchising” as methods of expanding a business, it is important to note that these are just two paradigms that can be used. There are many other methods to use, and each factual situation will dictate the best possible expansion avenue to pursue. **Maybe more than half of my clients pursue something other than licensing or franchising once they learn what is available...** and usually *at least* one-fifth of the costs in legal fees compared to franchising.

Why Consider “Licensing”?

- ***Licensing is Lower Cost and Can Be Done Quickly***. If you are thinking about expanding your operation through franchising, licensing may be an alternative because (1) it is substantially less expensive (*sometimes one-twentieth of the cost of franchising*), and (2) it takes about ten to fifteen business days to complete rather than months and months for franchises. As to costs, just the franchise registration fees paid to the States *aggregate* somewhere around \$6,000 (*Almost the cost of a license agreement or a set of license agreements.*). Licenses have no registration fees. So if you qualify for licensing, the legal fees are almost the same as the filing fees paid to the States for franchising.

- ***Avoid Complex Government Regulation***. There is little or no government regulation in licensing, and there is substantial and complex government regulation in franchising. **One such regulation which may prohibit immediate franchising is the requirement to have three years of financial records, and this may at least delay many from franchising until they can obtain the required financial records and incur the accounting and auditing fees:**

The FTC Disclosure Statement requirements include: “*A balance sheet (statement of financial position) for the franchisor for the most recent fiscal year, and an income statement (statement of results of operations) and statement of changes in financial position for the franchisor for the most recent 3 fiscal years. Such statements are required to have been examined in accordance with generally accepted auditing standards by an independent certified or licensed public accountant.*”

- ***You Can Begin Licensing Immediately while with Franchise You may have to Wait several months, a year or more***. Before you begin franchising, you may (a) have to wait for the completion of three years of operations in order to obtain the financial records discussed above, and (b) you must have a registered trade name or trademark which usually takes one year to eighteen months to complete if you do not have one at the time you wish to start franchising. Licensing, with its limitations that franchising may not have, can be used to test the franchise market at a substantially lower cost; i.e. see if licensing works before you go “franchising”.

- **Existing Businesses as Potential Licensees.** Existing businesses often buy a license and add the product or service to that existing business; this allows the licensee to keep his “bread winner” business going while he tests the licensing operations and thus reduces the risk on the acquiring the license.
- **Much Less Work on Daily Basis.** The day-to-day business operation of a licensor is customarily much less work and complex than the business of being a franchisor. If you become a franchisor, you generally have to give up the operations of your own business and enter the full time business of being a “franchisor”.
- **Licensing More Effective in Difficult Economic Times.** In a time when America’s work force is being down sized, in many businesses the market for selling licenses is correspondingly expanding, because these displaced people need a way to replace their lost “living wages. Additionally, there are more qualified and desirable people available on the market to become licensees which makes business expansion quicker and more effective. In essence, the market for selling licenses in many businesses is actually expanding in difficult economic times. And when you add in the fact that licenses are often easier to get into because of a lower purchase price and quick set up, licensing is usually superior to franchising for the new licensee. Licensing is also superior to franchising for the Licensor because of the (a) quick set up, and (b) the substantially lower cost in legal fees.

A Quick Overview of Licensing

- Licensing is a business structure and method of expanding the distribution of goods and services.
- As in franchising, in licensing *under certain circumstances* there can be (i) an initial upfront fee, (ii) continuing royalties, (iii) monthly license fees during the term of the agreement, (iv) exclusive territories, and (v) long or short term agreements.

Difference between Franchising and Licensing

- Franchising and licensing as a means of expanding a business are often confused with one another. However, franchising and licensing come from two distinct areas of the law. Franchising is based on securities law and licensing is a form of contract law.