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Allen S. Joslyn

LEGISLATIVE DEFINITIONS OF THE FRANCHISE RELATIONSHIP

*ALLEN S. JOSLYN**

The term "franchise" is applied to a variety of relationships, varying from the fast food franchise that grills its own burgers to the automobile dealer that resells products manufactured by its franchisor. Regulation of the franchise relationship arises from a perceived imbalance in bargaining power between the franchisor and franchisee.[1] While the franchisor and franchisee have closely-allied interests—beyond an ordinary dealership or supplier relationship—in marketing the product, there is no sharing of profits. The franchisee has made a substantial investment in the business, it is known primarily by the franchisor's trademark, and its business would lose much or all of its value without the franchise relationship. In a sense, the franchisee is investing its own funds in the franchisor's business without receiving any long-term ownership interest and may suffer an overnight loss of that investment by its franchisor's decision to terminate the relationship.

The legislative response to this risk of loss has taken two forms. Some state statutes, such as New York's,[2] provide only for disclosure of a written prospectus to the prospective franchisee,[3] leaving the franchisee otherwise to rely on caveat emptor. Other states go further to regulate the franchise relationship itself, primarily in the context of termination or renewal.[4] It is with this type of statute that the symposium will chiefly be concerned. A great deal can depend on whether the statutory definition of a franchise is satisfied. If it is not, the would-be franchisee is relegated to the common law, an area noted for its reluctance to imply limitations on the right to terminate business dealings in the absence of an explicit contractual provision.[5] On the other hand,

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* B.A. Haverford College; B.A. Oxford University; LL.B. Harvard Law School. Member, Cahill Gordon & Reindel.

1. *See generally* 62 AM. JUR. 2D *Private Franchise* § 4 (1972).

2. N.Y. GEN. BUS. LAW §§ 680-695 (McKinney 1984 & Supp. 1988).

3. *Id.* § 683 (McKinney 1984).

4. *See, e.g.*, CONN. GEN. STAT. § 42-133f (1987); DEL. CODE ANN. tit. 6, § 2552 (1975); N.J. STAT. ANN. § 56:10-5 (West Supp. 1987); WIS. STAT. §§ 135.03-135.04 (1985-86).

5. *See, e.g.*, Finlay & Assocs. v. Borg-Warner, 146 N.J. Super. 210, 369 A.2d 541 (Law Div. 1976) (where distributorship agreement did not contain requirement for economic dependency, and distributor's business did not operate under name of any franchisor, Franchise Practices Act did not apply, and distributor could not recover against manufacturer for alleged wrongful termination of distributorship), *aff'd*, 155 N.J. Super. 331,

a statutory franchisee may be able to obtain fairly extensive protection against its franchisor. For example, under the Wisconsin statute,[6] a franchisee must be given ninety days' notice of termination and an explanation of the reasons; it must be given an opportunity to cure any defect in its performance; termination may only be for "good cause;" and any change in "competitive conditions" is treated as a termination subject to such provisions.[7] As might be expected, the statute has proved a fertile source of litigation.[8] Under the South Dakota statute, a manufacturer of farm implements that had been losing $1 million per day could be found to have violated the statute (which would be a misdemeanor) when it withdrew from the business entirely; only misconduct or shortcomings on the part of the particular dealer would excuse termination of the dealer's supply.[9]

Apart from such general purpose statutes, many states have statutes applicable to particular industries—automobile dealerships and gas stations being the most common.[10] Notably, federal regulation of franchise termination is limited to these two industries,[11] while federal

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382 A.2d 933 (App. Div. 1978); Ziegler Co., Inc. v. Rexnord, Inc., 139 Wis. 2d 593, 407 N.W.2d 873 (1987) (dealership may fail to renew dealership agreement without good cause if the aggrieved party is not a dealer within the meaning of the Wisconsin Fair Dealership Law).

6. WIS. STAT. §§ 135.03-135.04 (1985-86).

7. *See* Les Moise, Inc. v. Rossignol Ski Co., 122 Wis. 2d 51, 361 N.W.2d 653 (1985) (the use of a nonconforming written notice to terminate dealership by ski supplier was a violation of the fair dealership law; as such, it gave the sports equipment retailer a presently enforceable right of action on receipt of such notice); White Hen Pantry v. Buttke, 100 Wis. 2d 169, 301 N.W.2d 216 (1981) (where reason for termination of dealership was nonpayment of sums due to grantor under dealership, the grantor must provide dealer with at least 90-days' prior written notice).

8. *See, e.g.*, Moore v. Tandy Corp., 819 F.2d 820 (7th Cir. 1987); Ziegler, 139 Wis. 2d 593, 407 N.W.2d 873 (1987); Les Moise, 122 Wis. 2d 51, 361 N.W.2d 653 (1985); Martino v. McDonald's Corp., 101 Wis. 2d 612, 304 N.W.2d 780 (1981); White Hen, 100 Wis. 2d 169, 301 N.W.2d 216 (1981).

9. Groseth Int'l Inc. v. Tenneco, Inc., 410 N.W.2d 159 (S.D. 1987).

10. *See, e.g.*, MINN. STAT. §§ 80E.01-80E.18 (1987) (in motor vehicle franchise relationships, manufacturer must act in good faith and cannot terminate dealer without proper notice and good cause); N.J. STAT. ANN. §§ 56:10-13 to 56:10-24 (West Supp. 1987) (requiring a motor vehicle franchisor to give notice to an existing franchisee of its intent to grant, relocate, reopen, or reactivate a franchise in the same line as franchisee within the relevant market area, and creating a motor vehicle franchise committee in order to decide disputes arising under the statute); N.Y. VEHICLE AND TRAFFIC LAW §§ 460-471 (McKinney Supp. 1986) (referred to as the Franchised Motor Vehicle Dealer Act and defining in pertinent part unfair business practices by automobile manufacturers/franchisors); R.I. GEN. LAWS §§ 5-55-1 to 5-55-9 (1987) (regulating motor fuel distribution by placing a duty of disclosure upon the franchisor to the prospective franchisee).

11. 15 U.S.C. §§ 1221-1225 (1982) (allowing an automobile dealer to sue the manufacturer/franchisor for failing to act in good faith pursuant to the terms of the franchise agreement or for improperly terminating, cancelling, or not renewing the franchise); 15 U.S.C. §§ 2801-2806 (1982) (regulating the franchise relationship among refiners, distrib-

provisions of general applicability govern only disclosure requirements promulgated by the Federal Trade Commission.[12] At the state level, a "franchise" may be defined differently by a state's disclosure statute and by its termination statute.[13] Related state statutes, such as those regulating "business opportunities" (for example, the ownership and lease of pinball machines) where no trademark is involved,[14] and unfair trade practice statutes, may also be interpreted as extending to commercial dealings.[15]

Generally, the elements of the statutory definition of a franchise, also referred to as a dealership, are the existence of an agreement;[16] substantial association with the franchisor's trademark;[17] either a grant of a right to engage in business under a marketing plan substantially prescribed by the franchisor[18] or a "community of interest" in the operation of the business;[19] and, finally, the payment of a franchise fee.[20]

EXISTENCE OF AN AGREEMENT

In a few states, the franchise agreement must be written;[21] however, most statutes specify that it may be oral or written, express or

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utors, and retailers).

12. 16 C.F.R. §§ 436.1-436.3 (1987).

13. *Compare* WIS. STAT. § 135.02(3) (1985-86) (termination statute defining "dealership" under the Wisconsin Fair Dealership Law and requiring "a community of interest in the business of offering, selling or distributing goods or services") *with* WIS. STAT. § 553.03(4)(a) (1985-86) (Franchise Investment Law, a disclosure statute defining "franchise" as requiring, in addition to a "community of interest" element, that distribution be in accord with "a marketing plan or system prescribed in substantial part by a franchisor"). *See* KIS Corp., 2 Bus. Franchise Guide (CCH) ¶ 8731, at 17,082 to 17,092 (Wis. Comm'r Sec. Dec. 24, 1986) (marketing plan merely suggesting rather than requiring compliance was not "prescribed in substantial part" within the meaning of the Franchise Investment Law and, therefore, did not constitute a franchise).

14. *See, e.g.*, N.C. GEN. STAT. § 66-94 (Supp. 1981) (defining business opportunity as the sale or lease of necessary goods or services to enable buyer to start a business, where seller represents to buyer that he will either: (1) assist buyer in finding locations for the use of the goods; or (2) purchase any or all products made by buyer; or (3) guarantee to buyer that income derived from the opportunity will exceed price paid; or (4) provide a sales or marketing plan).

15. *See, e.g.*, N.C. GEN. STAT. § 75-1.1 (1981 & Supp. 1987); Olivetti Corp. v. Ames Business Sys., Inc., 81 N.C. App. 1, 344 S.E.2d 82 (Ct. App. 1986), *rev'd on other grounds*, 319 N.C. 534, 356 S.E.2d 578 (1987) (extending statute's coverage to distributor/dealer relationship; original intent of the North Carolina unfair trade practices statute was to regulate relationships between persons engaged in business and between persons engaged in business and the consuming public).

16. *See infra* notes 21-25 and accompanying text.

17. *See infra* notes 26-35 and accompanying text.

18. *See infra* notes 36-45 and accompanying text.

19. *See infra* notes 46-68 and accompanying text.

20. *See infra* notes 69-86 and accompanying text.

21. *See, e.g.*, N.J. STAT. ANN. § 56:10-3.a (West Supp. 1987); Ianuzzi v. Exxon Co., 572

implied.[22] When the statute is silent, the courts will generally permit oral agreements to qualify.[23] Moreover, a franchise agreement may be pieced together from a series of separate agreements.[24] For example, a lease of premises plus an agreement to supply products to the lessee may be treated as a franchise, if the lease gives the lessor extensive control over the lessee's business operations.[25]

TRADEMARK OR TRADE NAME

A basic element of the franchise relationship is use of the franchisor's trademark or trade name in the conduct of the franchised business;[26] the ability to use that public image constitutes a principal

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F. Supp. 716, 725 (D.N.J. 1983) (plaintiff had no cognizable claim under New Jersey's Franchise Practice Act because she had not contracted with defendant-franchisor individually in writing). In Texas, while the beer distributors' statute defines an agreement as either written or oral, only those with written contracts can sue for wrongful termination. Ace Sales Co., Inc. v. Cerveceria Modelo S.A., 739 S.W.2d 442 (Tex. Ct. App. 1987).

22. *See, e.g.*, CAL. BUS. & PROF. CODE § 20001 (West 1987); N.Y. GEN. BUS. LAW § 681.3 (McKinney 1984).

23. *See* Car Business, Inc. v. Fleetwood Motor Homes, 23 Ohio Misc. 2d 40, 492 N.E.2d 488 (C.P. Clermont County 1985) (verbal understanding held to satisfy Ohio's statutory requirement that a franchise be a "written agreement, contract, or understanding") (citing OHIO REV. CODE ANN. § 4517.01 (V) (Baldwin 1983)).

24. *See* Atlantic Richfield Co. v. Razumic, 480 Pa. 366, 390 A.2d 736 (1978) (separate agreements between oil company and service station operator, for oil company to provide oil and lease service station, held to be a franchise relationship where lease provisions afforded lessor-oil company extensive control over lessee, including right of inspection and share in the profits).

25. *See id.; see also* Kowatch v. Atlantic Richfield Co., 480 Pa. 388, 390 A.2d 747 (1977) (petroleum supplier's "service station lease," authorizing dealer to operate supplier's station and requiring: 1) display of supplier's trademark; 2) authorization of supplier to inspect station for compliance with supplier's standards; 3) operation of station in manner reflecting favorably on supplier; and 4) periodic check of dealer's financial records, held to be a franchise agreement despite the term "lease" in the agreement). *But see* Franklin Associates v. F-M Oil Co., [1980-1983 Transfer Binder] Bus. Franchise Guide (CCH) ¶ 7876, at 13,323 to 13,324 (Pa. C.P. Dec. 30, 1981) (two separate agreements between petroleum supplier and lessee, one defining terms and conditions of the lease, the other describing terms for the sale and purchase of petroleum products, held not to establish a franchise relationship). R.L.M. Dist. Co. v. W.A. Taylor, Inc., 2 Bus. Franchise Guide (CCH) ¶ 9024, at 18,491 (D. Ariz. Jan. 4, 1988) (agreement required by Arizona Spirituous Liquor Franchises Act could be implied from custom and practice in the industry).

26. *See* Susser v. Carvel Corp., 206 F. Supp. 636, 640 (S.D.N.Y. 1962) ("the cornerstone of a franchise system must be the trademark or trade name of a product"), *aff'd*, 332 F.2d 505 (2d Cir. 1964); Piercing & Pagoda, Inc. v. Hoffner, 465 Pa. 500, 508, 351 A.2d 207, 211 (1976) ("In its simplest terms, a franchise is a license from the owner of a trademark or trade name permitting another to sell a product or service under the name or mark."); *see also* Collision, *Trademarks—The Cornerstone of a Franchise System*, 24 SW. L.J. 247 (1970); *cf.* Lasday v. County of Allegheny, 55 Pa. Commw. 422, 423 A.2d 789 (Commw. Ct. 1980) (concession agreements providing for operation of newstands and

advantage of the relationship for the franchisee.[27] The statutory definitions reflect this economic reality. For example, under the Missouri statute, a franchise is defined as an agreement granting the right to operate a business substantially associated with a trademark or offering; to distribute products or services using the franchise or its trade name for the purpose of advertising; or to use a trade name or trademark.[28]

More is generally required, however, than simply using a brand name or using promotional brochures as an incident of selling the product. The trade name must be used in such a way as to create the impression that there is such a strong connection that the franchisor in some sense "vouches for" the activities of the franchisee.[29] For exam-

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jewelry/gift shop in county airport held not to create a common-law franchise, where no county trademark or trade name was involved).

27. Franchisees who use the franchisor's trademark receive the benefit of attracting consumers who are familiar with the franchisor's trademark, name, and quality of service, as consumers often utilize trademarks at the time of purchase as a means of reducing the risk of buying poor quality products. Treece, *Trademark Licensing and Vertical Restraints in Franchising Arrangements*, 116 U. PA. L. REV. 435, 438 (1968). The Supreme Court of Pennsylvania has made similiar observations, noting that a franchisee realizes "that much of his trade will be attracted because his station offers the products, services, and promotions of the well-established and well-displayed name [of the franchisor]." *Razumic*, 480 Pa. at 377, 390 A.2d at 742; *see also* Susser v. Carvel Corp., 206 F. Supp. 636, 640 (S.D.N.Y. 1962) ("It is the uniformity of product and control of its quality and distribution which causes the public to turn to franchise stores for the product."), *aff'd*, 332 F.2d 505 (2d Cir. 1964).

28. MO. REV. STAT. § 407.400(1) (1986).

29. *See* Neptune T.V. & Appliance Service, Inc. v. Litton Microwave Cooking Prods. Div., 190 N.J. Super. 153, 160, 462 A.2d 595, 599 (App. Div. 1983):

> [A] hallmark of the franchise relationship is the use of another's trade name in such a manner as to create a reasonable belief on the part of the consuming public that there is a connection between the trade name licensor and licensee by which the licensor vouches, as it were, for the activity of the licensee in respect of the subject of the trade name.

Id. Compare Colt Indus. Inc. v. Fidelco Pump & Compressor Corp., 844 F.2d 117 (3d Cir. 1988) (no trademark license under the New Jersey Franchise statute where the dealer was not permitted to use the trademark in its name but could advertise the trademarked product in accordance with manufacturer's policies to indicate it was a distributor) *and* Business Incentives Co., v. Sony Corp. of America, 397 F. Supp. 63 (S.D.N.Y. 1975) (manufacturer's sales representative agreement, authorizing use of trade name in soliciting sales, held not to create a franchise) *and* Finley & Assocs. v. Borg-Warner, 146 N.J. Super. 210, 219, 369 A.2d 541, 545 (Super. Ct. Law Div. 1976), *aff'd*, 155 N.J. Super. 331, 382 A.2d 933 (Super. Ct. App. Div. 1978) (no franchise created by mere furnishing of advertising material as contemplated by distributorship agreement allowing plaintiff, if it wished, to have its name placed on advertising for its benefit) *with* Martin Investors, Inc. v. Vander Bie, 269 N.W.2d 868, 874 (Minn. 1978) (grant of right to use computer manufacturer's name in marketing of computer sales company's own goods and services held to create a franchise, as Minnesota's statute "requires only that the franchisee be granted the right to use the franchiser's name, not that it be permitted to hold itself out as the franchiser").

ple, this "vouching for" is present when the franchisee is permitted to call himself an "authorized outlet" for the franchisor's product.[30] There is, however, no requirement that the franchisee hold itself out as being the *same* as a franchisor.[31]

Some of the cases are more far-reaching in finding a franchise relationship. For example, a distribution by a wholesaler of advertising material bearing the manufacturer's name has been found sufficient to meet the trade-name requirement of one state's franchise statute.[32] A grant of a territory in which to sell trademark goods may also be considered a sufficient license to use the manufacturer's trademark so as to meet the trade-name element.[33]

Of course, the licensed trade name need not refer to the origin of the products, but may refer to the nature of the business—for example, the name "Walgreen Drug Stores," even though it was held to be a franchised operation, did not imply that most or all of the products were purchased from the franchisor.[34] Rather, the trademark implied conformity with certain standards in pricing, and the franchisee benefited from the national advertising for the chain.[35]

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30. *Neptune,* 190 N.J. Super. at 160, 462 A.2d at 599 (by authorizing licensee to be designated as an authorized service center and to use such designation in its advertising, licensor gave its approval to licensee's business and induced consuming public to expect the standards endorsed by the licensor).

31. *See Martin,* 269 N.W.2d at 874 (rejecting computer manufacturer's claim that the manufacturer must have contractually permitted computer sales company to hold itself out as the manufacturer in order for a franchise to be created, as franchise was held to exist when the sales company was granted the right to use the manufacturer's name).

32. *See* RJM Sales & Mktg., Inc. v. Banfi Prods. Corp., 546 F. Supp. 1368, 1373 (D. Minn. 1982) (a franchisee need only be granted right to use franchisor's name to be considered a franchise); *Martin,* 269 N.W.2d at 874 (franchisee needs only permission to use franchisor's name and does not have to hold itself out as a franchise).

33. *See* Lobdell v. Sugar 'N Spice, Inc., 33 Wash. App. 881, 658 P.2d 1267, 1272-73 (Ct. App. 1983) (grant to use manufacturer's name is implicit in the grant of territory).

34. Kealey Pharmacy & Home Care Servs., Inc. v. Walgreen Co., 761 F.2d 345 (7th Cir. 1985). In *Kealey,* independent pharmacies sued Walgreen for damages resulting from Walgreen's termination of dealerships, without cause, in violation of the Wisconsin Fair Dealership Law, WIS. STAT. §§ 135.01-135.07 (1985-86). *Id.* at 347. The Court of Appeals for the Seventh Circuit affirmed the award of damages below over objections that the statute did not apply, holding that the pharmacies' "shared . . . interest in the promotion of [Walgreen's] name and reputation for service, integrity and value," established a "dealership" within the meaning of the statute. *Id.* at 349.

35. *Id.* at 349. As the court stated at length,

> [the pharmacies] shared [Walgreen's] interest in the promotion of its name and reputation and made substantial financial investments in their stores and fixtures, in their Walgreen signs and Walgreen inventory. They displayed the Walgreen trademark prominently outside their stores and on the labels of their prescription drug containers. In addition, they spent their own money for advertising, sold directly from their Walgreen inventory to customers, extended credit and assumed all risks of late payment or nonpayment. *They depended on*

MARKETING PLAN

The third element of the statutory definition of franchise is that the franchisee's activities take place pursuant to a marketing plan "prescribed by the franchisor."[36]

Obviously, whether such a plan exists may be a hotly contested factual issue. The difference, for example, between an exclusive distribution arrangement and a franchise under a marketing plan may not be easy to discern.[37] The presence of sales assistants, sales quotas,

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their affiliation with Walgreen for their image, thus advising the public that their drugstores furnished the quality service and low prices associated with Walgreen.

Id. (emphasis added).

36. *See, e.g.*, CAL. BUS. & PROF. CODE § 20001(a) (West 1987) ("A franchisee is granted the right to engage in the business of offering, selling or distributing goods or services under a marketing plan or system prescribed in substantial part by a franchisor. . . ."); CAL. CORP. CODE § 31005(a) (West Supp. 1988) (same language employed in California's "Franchise Investment Law"); CONN. GEN. STAT. § 42-133e(b) (1987) (same language); ILL. ANN. STAT. ch. 121 ½, para. 703(1)(a) (Smith-Hurd Supp. 1987) (same language); IND. CODE ANN. § 23-2-2.5-1(a)(1) (Burns 1984 & Supp. 1987) (same language); MD. ANN. CODE art. 56, § 345(d)(1) (1983) (same language); N.Y. GEN. BUS. LAW § 681.3 (McKinney 1984) (same language).

Another statutory indication of the existence of a marketing plan prescribed by a franchisor is whether the franchisor and the franchisee share a financial interest in marketing goods or services, termed a "community of interest." *See, e.g.*, N.J. STAT. ANN. § 56:10-3.a (West Supp. 1987). The New Jersey statute defines a franchise as

> a written arrangement for a definite or indefinite period, in which a person grants to another person a license to use a trade name, trademark, service mark, or related characteristics, and in which there is *a community of interest in the marketing of goods or services at wholesale or retail, by lease, agreement, or otherwise.*

Id. (emphasis added); *see also* WIS. STAT. § 135.02(1) (1985-86) (" 'Community of interest' means a continuing financial interest between the grantor and grantee in either the operation of the dealership business or the marketing of such goods or services."); *id.* § 135.02(3) (" 'Dealership' means a contract . . . by which a person is granted the right to sell or distribute goods or services . . . in which there is a community of interest. . . ."). For a further discussion of the "community of interest" component, see *infra* notes 47-57 and accompanying text.

37. *See* Quirk v. Atlanta Stove Works, Inc., 537 F. Supp. 907 (E.D. Wis. 1982). In *Quirk*, plaintiff sought injunctive relief and damages against Atlanta for allegedly violating the Wisconsin Fair Dealership Law. *Id.* at 908. The court held that Atlanta's termination of Quirk's exclusive sales contract was not actionable under the statute, because the relationship between a manufacturer and its exclusive sales representative did not constitute a dealership—i.e., a franchise. *Id.* at 910-11. Plaintiff's sole function was to solicit customers for the manufacturer. *Id.* at 910. Quirk made no investment in inventory, other than samples, nor was he required to assume any risks of late payment or non-payment. *Id.* at 910-11. He was paid monthly, taxes were withheld, and Atlanta contributed to state unemployment insurance. *Id.* at 911. Based on the foregoing, the court held that Quirk was essentially an employee, not a franchisee. *Id; see also* George R. Darche Assocs., Inc. v. Beatrice Foods Co., 676 F. Supp. 429 (D.N.J. 1981), *aff'd*, 676 F.2d 685 (3d Cir. 1982). In this case, Darche brought an action for wrongful termination

mandatory sales training, etc., may convert what otherwise would be a distribution arrangement into a franchise relationship.[38] Under California law, indicia of a marketing plan could include mandatory training sessions, exclusive territories, required purchase of new products, required trade dress, or suggestions for marketing techniques in company publications.[39]

There may also be close questions as to whether a plan is "prescribed."[40] This issue arose recently in connection with an opinion of

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of a franchise agreement. *Id.* at 430. The court held that Darche was a sales representative for, and not a franchise of, the manufacturer. *Id.* at 435. Its sole function was to solicit orders; it could not make an "offer" that would in any way bind the manufacturer. *Id.* at 434. Additionally, Darche paid no franchise fee and was not required to maintain a place of business. *Id. But see* Kealey 761 F.2d 345 (independent pharmacies were considered "dealers" because they shared supplier's interest, made investments, displayed supplier's trademark, and sold directly from supplier's inventory to customers).

38. *See* Master Abrasives Corp. v. Williams, 469 N.E.2d 1196 (Ind. Ct. App. 1984) (sale and distribution agreement held to be a franchise, because element of "marketing plan or system," though not expressly mentioned in the agreement, was satisfied by the agreement's division of the state into marketing areas, the establishment of sales quotas, the approval rights over personnel in grantor/Master, and the mandatory training by Master of Williams' personnel); *see also* IND. CODE ANN. § 23-2-2.5-1(a) (Burns 1984 & Supp. 1987).

39. *See, e.g.*, Boat & Motor Mart v. Sea Ray Boats, Inc., 825 F.2d 1285, 1289 (9th Cir. 1987) ("Boat" recognized as franchisee under a marketing plan, where it was one of several outlets selling "Sea Ray" products, which outlets operated under central management and uniform price and quality standards, and where it was obliged under a dealer agreement "to advertise intensively, to conduct a variety of promotions and to carry Sea Ray's array of accessory sales devices"); People v. Kline, 110 Cal. App. 3d 587, 594, 168 Cal. Rptr. 185, 188 (Ct. App. 1980) (in conviction for unlawfully offering and selling unregistered franchise, court found existence of franchise by virtue of implied marketing plan, which was evidenced by purchaser's agreement to sell defendant's products pursuant to a scheme whereby defendant assisted in advertising, supplied food, planned the menu, and required identifiable kiosks to sell his products).

40. *See Boat & Motor Mart*, 825 F.2d at 1289 (finding plan, whereby outlet actively promoted, displayed, and advertised "Sea Ray" products; maintained "Sea Ray" sales quotas; serviced the products according to "Sea Ray" specifications; and was obliged to purchase promotional videos from "Sea Ray," to be "prescribed in substantial part" by "Sea Ray"); Grand Light & Supply Co. v. Honeywell, Inc., 771 F.2d 672, 678 (2d Cir. 1985) (possible indicia of franchisor control, and consequently of what the franchisor prescribes, include bookkeeping audits, inspection of the premises, "control of lighting, employee uniforms, prices, trading stamps, and hiring, [the] establish[ment] of sales quotas[,] management training and financial support"); Meadow Fresh Farms, Inc. v. Sandstrom, 333 N.W.2d 780, 784-85 (N.D. 1983) (" 'marketing plan or system prescribed in substantial part' by Meadow Fresh" was indicated by: (1) a structure for distributor compensation and bonuses; (2) centralized bookkeeping and record keeping; (3) a prescribed system for becoming distributors and district, regional and zone directors; (4) the franchisor's approval rights over all promotional material; (5) prohibitions on distributor repackaging of product; (6) "opportunity meetings"; (7) franchisor-suggested retail prices; and (8) a "comprehensive advertising and promotional program" by the franchisor).

the Wisconsin Commissioner of Securities, which held that "prescribed" may be less than "required" but must be more than merely "suggested."[41] The Commissioner stated the test as whether, as a practical matter, the franchisee's autonomy is restricted; that would occur, for example, if there are franchisor-imposed consequences of not following the plan.[42] At the same time, the Commissioner held invalid regulations which stated that mere suggestion was sufficient to establish prescription.[43] In other states, however, it may be sufficient if the marketing plan is suggested by the franchisor, as provided by the Illinois statute.[44] In California, it is sufficient to create a franchise if the franchisor provides marketing materials to the franchisee, irrespective of whether it requires or even tells the franchisee to use them.[45]

COMMUNITY OF INTEREST

The requirement that there be a community of interest between the franchisor and franchisee focuses on the basic dichotomy of the franchise relationship—while the franchisor and franchisee do not share profits and while the franchisor cannot dictate to the franchisee as it can to its own agent, each is dependent upon the other for its economic well-being.[46] Some statutes define the required community interest as a continuing financial interest between the franchisor and the franchisee in the operation of the franchise business.[47] This goes beyond a simple voluntary purchaser-seller relationship. The community of interest may be created by an agreement to purchase brand-name goods for a definite term since the parties share contractual interest in future sales during the term.[48] The community may also be

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41. *In re* KIS Corp., 2 Bus. Franchise Guide (CCH) ¶ 8731, at 17,083 (Wis. Comm'r Sec. Dec. 24, 1986). The Commissioner stated:

> (1) A marketing plan can be deemed "prescribed" under the [Wisconsin Franchise Investment Law] by a showing of something less than "compulsory compliance" or mandatorily "required" conduct. . . . (2) Written or oral "representations" by an offeror or sellor of a business arrangement that do no more than "suggest" or make available a marketing plan to a purchaser . . . may not provide the basis for establishing a "prescribed" marketing plan under the meaning of that term in [the statute].

Id.

42. *Id.* at 17,084.

43. *Id.* at 17,088.

44. *See* ILL. ANN. STAT. ch. 121 ½, para. 703(19) (Smith-Hurd Supp. 1987).

45. *See* CAL. BUS. & PROF. CODE § 20001(a) (West Supp. 1987).

46. *See* Neptune T.V. & Appliance Serv., Inc. v. Litton Microwave Cooking Prods. Div., 190 N.J. Super. 153, 163, 462 A.2d 595, 600-01 (Super. Ct. App. Div. 1983); Lobdell v. Sugar 'N Spice, Inc., 33 Wash. App. 881, 892, 658 P.2d 1267, 1273-74 (Ct. App. 1983).

47. *E.g.*, HAW. REV. STAT. § 482E-2 (1985); WASH. REV. CODE ANN. § 19.100.010(2) (Supp. 1988); WIS. STAT. § 135.02(1) (1985-86).

48. *Lobdell*, 33 Wash. App. at 893, 658 P.2d at 1274.

created by contractual obligation by the franchisee to maintain inventory, promote company products, and submit regular reports of sales.[49]

There have been several approaches to determining whether the requisite community of interest exists. The question has arisen in the context of a distributor who is not financially dependent upon a particular supplier (because he distributes the products of a number of manufacturers) but who nevertheless claims a community of interest. In *Grand Light & Supply Co., Inc. v. Honeywell, Inc.*,[50] for example, the Second Circuit looked to the purpose of Connecticut's statute, namely to prevent ruination of a distributor because of a franchisor's unilateral termination of the relationship, and applied a "financial disaster" test to hold that the statute did not cover the multi-product distributor.[51] The court was concerned that, absent such a limitation, the statute could apply to any manufacturer that wished to offer promotional guidance to distributors.[52] Some state statutes specifically address the multi-product distributor. For example, Delaware includes in its definition of franchise a requirement that the franchisee not sell products bearing the name of more than three manufacturers.[53] In New Jersey, at least twenty percent of the franchisee's gross sales must derive from the franchised product.[54]

Other courts have, however, resisted any bright-line test of "community of interest." In *Ziegler Co., Inc. v. Rexnord, Inc.*,[55] the manufacturer's products constituted only one to eight percent of the distributor's sales during the period the distribution agreement was in effect,

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49. *Id.*

50. 771 F.2d 672 (2d Cir. 1985).

51. *Id.* at 677. The court stated "that the purpose of the statute was to prevent a franchisor from taking unfair advantage of the relative economic weakness of the franchisee." *Id.* The weakness becomes apparent when "the franchisee is completely dependent on the public's confidence in the franchised product for most or all of his business"; therefore, an "abrupt severance of the franchise tie, without good cause and without sufficient notice could spell ruination." *Id.* The court, however, found that the loss of business would constitute "a scant three percent" of Grand Light's business. *Id.* As such, termination was not catastrophic. *Id.; see* Kusel Equip. Co. v. Eclipse Packaging Equip. Ltd., 647 F. Supp. 80, 81 (E.D. Wis. 1986) ("a dealer who sells products of from 75-100 manufacturers cannot use the Wisconsin Fair Dealership Law to sue a grantor whose products account for less than 2% of sales"); *see also* American T.V. & Appliance, Inc. v. Nakamichi U.S.A. Corp., [1983-1985 Transfer Binder] Bus. Franchise Guide (CCH) ¶ 8029, at 13,813 (Wis. Cir. Ct. July 11, 1983) (franchise statute was designed "to protect the Wisconsin franchisee who sunk his savings into a business to market the grantor's product . . . not to protect multi-product retail outlets that carry hundreds of product lines from one product choosing to discontinue making its product available to that outlet for sale").

52. *Grand Light*, 771 F.2d at 677.

53. *See* DEL. CODE ANN. tit. 6, § 2551(1)(b) (1975).

54. *See* N.J. STAT. ANN. § 56:10-4(3) (West Supp. 1987).

55. 139 Wis. 2d 593, 407 N.W.2d 873 (1987).

but a grant of summary judgment in favor of the manufacturer was reversed.[56] The Wisconsin Supreme Court decided that the two guideposts for community of interest are " 'continuing financial interest' and 'interdependence.' "[57] Determining whether such community exists requires analysis of a number of factors, some of which are (i) how long the parties have dealt with each other; (ii) the extent and nature of the contractual obligations; (iii) the percentage of time or revenue the dealer devotes to the supplier's products or services; (iv) the extent and nature of the territory granted to the dealer; (v) the extent and nature of the dealer's uses of the supplier's trademarks or logos; (vi) the dealer's financial investment in inventory, facilities and good will of the alleged franchise and the personnel devoted to the alleged dealership; (vii) the dealer's expenditures on advertising or promotional expenditures; and (viii) the extent and nature of any supplementary services provided by the alleged dealer to consumers of the alleged supplier's products or services.[58] Thus, the court held that the dealer might be able to demonstrate a community of interest by showing large capital investments made in reliance on the relationship, etc., even if the product did not account for a large percentage of its sales.

The result of this flexible approach will be to make it more difficult to dispose of termination cases, and to strengthen the dealer's hand in seeking a preliminary injunction against termination.[59]

Other courts focus on whether the alleged franchisor exercises control over the operations of the dealer by, for example, imposing sales quotas or whether the relationship was a cooperative relationship between two parties of equal bargaining power.[60] Local service or repair centers that perform warranty repairs for a manufacturer have been found to lack a community of interest with the manufacturer.[61] Insofar as the authorized repair center is doing warranty work which is reimbursed by the manufacturer, it has no business of its own and no com-

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56. Ziegler Co. v. Rexnord, Inc., 2 Bus. Franchise Guide (CCH) ¶ 8632, at 16,608 (Wis. Ct. App. July 15, 1986), *rev'd*, 139 Wis. 2d 593, 407 N.W.2d 873 (1987).

57. 139 Wis. 2d at 605, 407 N.W.2d at 879.

58. *Id.* at 606, 407 N.W.2d at 879-80.

59. *See* Dederich Corp. v. Eurozyme S.N.C., 839 F.2d 373 (7th Cir. 1988) (denial of preliminary injunction reversed and remanded for further fact finding under the *Ziegler* standards).

60. *See* Colt Indus., Inc. v. Fidelco Pump & Compressor Corp., 44 F.2d 117, 124 (3d Cir. 1988) (no franchise where dealer failed to establish that "it was subject to the whim, direction and control of a more powerful entity whose withdrawal from the relationship would shock a court's sense of equity").

61. *See* Neptune T.V. & Appliance Serv., Inc. v. Litton Microwave Cooking Prods. Div., 190 N.J. Super. 153, 462 A.2d 595 (Super. Ct. App. Div. 1983) (holding that, although the manufacturer had licensed a service center to use the manufacturer's name, the service contract between the parties did not involve the community of interest required by New Jersey's Franchise Practices Act).

munity of interest in the manufacturer's business; rather, it is acting as an agent for the manufacturer. Insofar as the repair center does non-warranty work, the franchisor has no interest in the repair center's business; the franchisor's only concern is having adequate repairs done on its product.[62] Some courts have dealt with this factual situation by noting the lack of any separate franchise fee.[63]

Another judicial gloss which has been used to prevent an overly broad application of the franchise statute has appeared in the context of manufacturers' representatives who solicit sales but do not set prices, make sales, or carry inventory.[64] Such representatives have been held not to be franchisees if they have not made a substantial investment in the business which would be "decimated" by termination.[65] The nature of the investment, however, may be significant. If the investment is in specialized resources (such as store decor) which would lose its value on termination, application of a franchise statute to limit the franchisor's exercise of power is appropriate. On the other hand, the legislative purpose would not be forwarded by applying the statute where the investment is deposited with the supplier and is readily returnable upon termination, since such an investment does not place the dealer in its supplier's power.[66] In determining whether there was an investment to be decimated, the courts have held that inventory can constitute the required investment, as can payments to a third party to acquire the business.[67] On the other hand, good will—running losses at the start-up of the business—would not constitute an investment, only an ordinary business expense.[68]

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62. *See id.; see also* Kania v. Airborne Freight Corp., 99 Wis. 2d 746, 300 N.W.2d 631 (1981) (where a local delivery agent was retained by a nationwide freight forwarder, the court held that the cartage contract between the freight forwarder and local cartage service did not fulfill the requisite community of interest to invoke Wisconsin's franchise protection legislation).

63. Communications Maintenance, Inc. v. Motorola, Inc., 761 F.2d 1202, 1206 (7th Cir. 1985) (service station's agreement to subcontract for installation of Motorola radios according to Motorola specifications and at a price lower than the Motorola contract price held not to involve any franchise fee under the State Franchise Act).

64. *See* Foerster, Inc. v. Atlas Metal Parts Co., 105 Wis. 2d 17, 19-20, 313 N.W.2d 60, 63 (1981) (holding that manufacturer's representative who did not maintain inventory of the manufacturer's products, or pay a fee for the right to represent them, was not a "dealer" for purposes of the Fair Dealership Law).

65. *See id.;* Bush v. Nat'l School Studios, Inc., 131 Wis. 2d 435, 389 N.W.2d 49 (Ct. App. 1986) (Wisconsin Fair Dealership Law was meant to protect only those small businessmen who make a substantial financial investment in inventory), *aff'd,* 139 Wis. 2d 635, 407 N.W.2d 883 (1987).

66. Moore v. Tandy Corp., 819 F.2d 820 (7th Cir. 1987).

67. *See Bush,* 131 Wis. 2d at 440, 441, 389 N.W.2d at 52.

68. Agee Agric. Equip. Sales v. Trail King Indus., 2 Bus. Franchise Guide (CCH) ¶ 8721, at 17,032 (D.S.D. Oct. 27, 1986) (early losses associated with the purchase of promotional items treated as ordinary business expenses), *aff'd mem.,* 822 F.2d 1094 (8th

FRANCHISE FEE

Many statutes require payment of a franchise fee, and in some states there is a requisite minimum amount.[69] A few states do not require any franchise fee.[70] Generally, a franchise fee includes any payment the franchisee is required to make to the franchisor with certain exceptions. The common intent of these exceptions is to exclude ordinary business expenses from what are otherwise categorized as franchise fees.[71]

The first generally-recognized exception is the making of payments to the franchisor to purchase goods at bona fide wholesale prices.[72] This exception includes only purchases of goods, and thus may not exempt required payments for services rendered by the franchisor, such as data processing services.[73] Moreover, sales of equipment (for example, stoves or refrigerators), intended to be used by the franchisee in his business, are not exempted.[74] Such equipment is not usually sold at wholesale, but rather to the ultimate user, the franchisee; nor is the equipment held for resale.[75]

Another exception involves the making of minimum initial inventory purchases. These purchases generally are not treated as involving

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Cir. 1987).

69. *E.g.*, CAL. BUS. & PROF. CODE § 20007(d) (West 1987); DEL. CODE ANN. tit. 6, § 2551(3) (Supp. 1986); ILL. ANN. STAT. ch. 121½, para. 703(1)(c) (Smith-Hurd Supp. 1987).

70. *E.g.*, ARK. STAT. ANN. § 70-808(a) (1979); WASH. REV. CODE ANN. § 19.100.010(4) (Supp. 1988); WIS. STAT. ANN. § 135.02(3) (West 1987).

71. *Compare* Wine Distribs., Inc. v. Canandaigua Wine Co., [1980-1983 Transfer Binder] Bus. Franchise Guide (CCH) ¶ 7882, at 13,332 (D. Minn. Sept. 27, 1982) (thirty-five-cent-per-case merchandising charge to facilitate sale of the product was not a franchise fee) *and* Siedare Assocs. v. Amperex Sales Corp., [1980-1983 Transfer Binder] Bus. Franchise Guide (CCH) ¶ 7732, at 12,861 (D. Minn. July 20, 1981) (sales representative's expenses for sending employees to sales meetings and mailing promotional material did not constitute a franchise fee) *with* Kojanchich v. Bridges, 93 Ill. App. 3d 550, 417 N.E.2d 694 (App. Ct. 1981) (payment to franchisor as settlement for inducing franchisor's employee to change jobs considered a franchise fee).

72. *See* MINN. STAT. ANN. § 80C.01(9)(a) (1987); N.Y. GEN. BUS. LAW § 681.7(a) (McKinney 1984).

73. *See* Martin Investors, Inc. v. Vander Bie, 269 N.W.2d 868 (Minn. 1978) (payment of fees for computer services purchased constituted a franchise fee).

74. *See, e.g.*, IND. CODE ANN. § 23-2-2.5-1(i) (Burns 1984 & Supp. 1987); Department of Corporations, State of California, Guidelines for Determining Whether an Agreement Constitutes a Franchise Under the California Franchise Investment Act, Release No. 3-F (1974) (interpreting CAL. CORP. CODE § 31011 (West 1987)). *But see* HAW. REV. STAT. § 482E-2(5) (1985); MD. ANN. CODE art. 56, § 345(j)(7) (1983).

75. *See In re* KIS Corp., 2 Bus. Franchise Guide (CCH) ¶ 8731, at 17,095 (Wis. Comm'r Sec. Dec. 24, 1986) (the statutory terms "wholesale" and "goods" imply an intent to resell).

payment of a franchise fee,[76] but if the prices charged exceed bona fide wholesale prices, a franchise fee may be held to apply.[77] Further, the franchise fee may be found if the required purchases exceed the reasonably expected requirements of the business, even if sold at bona fide wholesale prices.[78] Other charges paid to the franchisor ostensibly as expenses may be found to be concealed franchise fees.[79] Tying agreements[80] may also create a franchise fee to the extent that the unwanted purchases of the tied product can constitute a fee.[81]

Payments to third persons are generally not considered franchise fees, because they are treated as ordinary business expenses which do not benefit the franchisor.[82] The same result follows even if the payments are required by the franchise contract, and even if they are col-

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76. *See* A.R. Dervaes, Co. v. Houdaille Indus., Inc., [1980-1983 Transfer Binder] Bus. Franchise Guide (CCH) ¶ 7803, at 13,069-70 (Del. Ch. Sept. 29, 1981) (declining to find a franchise despite purchase of minimum inventory requirement worth $90,000, based on nonpayment of $100 consideration as required by statute).

77. *See* OT Indus., Inc. v. OT-tehdas Oy Santasalo-Sohlberg Ab, 346 N.W.2d 162, 166 (Minn. Ct. App. 1984) (recognizing that a minimum volume sales requirement could be a disguised franchise fee if the sales were at prices exceeding bona fide wholesale prices).

78. *See* American Parts Sys., Inc. v. T&T Automotive, Inc., 358 N.W.2d 674 (Minn. Ct. App. 1984) (holding that required purchase of a minimum amount of goods, if unrelated to the business' reasonable needs, constitutes a franchise fee); *OT Indus.*, 346 N.W.2d at 166 (recognizing that a minimum volume requirement, even at wholesale prices, may be a franchise fee, if the franchisee is required to purchase amounts or items it otherwise would not purchase); *cf.* Cambee's Furniture, Inc. v. Doughboy Recreational Inc., 825 F.2d 167, 171 (8th Cir. 1987) (South Dakota Act, which declares that an agreement to purchase goods at bona fide wholesale prices "shall not be considered the payment of a franchise fee," makes the quantity purchased irrelevant).

79. *See* Craig D. Corp. v. Atlantic-Richfield Co., 45 Wash. App. 563, 567, 726 P.2d 66, 69 (Ct. App. 1986) (holding percentage leases of convenience stores run in connection with gas stations to constitute franchise fees); Lobdell v. Sugar 'N Spice, 33 Wash. App. 881, 891, 658 P.2d 1267, 1273 (Ct. App. 1983) (finding hidden franchise fee in payments made by franchisee to find retail locations and to advertise the franchisor's products); Luzim v. Philips, 2 Bus. Franchise Guide (CCH) ¶ 9020, at 18,474 (E.D.N.Y. Dec. 10, 1987) (required payment of three percent of the bona fide wholesale price of the goods sold to the dealer into an advertising fund could constitute a franchise fee).

80. A "tying arrangement" is formed "when a person agrees to sell one product, the 'tying product,' only on the condition that the vendee also purchase another product, the 'tied product.'" BLACK'S LAW DICTIONARY 1361-62 (5th ed. 1979).

81. *See* Blanton v. Mobil Oil Corp., 721 F.2d 1207 (9th Cir. 1983) (required purchase of overpriced motor oil and automotive accessories tied to service station lease and supplying of gasoline may constitute a franchise fee), *cert. denied*, 471 U.S. 1007 (1985).

82. *See* Premier Wine & Spirits v. E. & J. Gallo Winery, 644 F. Supp. 1431, 1439 (E.D. Cal. 1986) (payment not a franchise fee unless made to putative franchisor); RJM Sales & Mktg., Inc. v. Banfi Prods. Corp., 546 F. Supp. 1368, 1373 (D. Minn. 1982) (payments to outside firm for advertising are not franchise fees but ordinary business expenses); *OT Indus.*, 346 N.W.2d at 167 (payments for advertising made to suppliers and not franchisor do not constitute franchise fees).

lected by the franchisor for the benefit of the third party.[83] Similarly, payments to third parties to purchase the franchise do not constitute fees.[84] However, there may be an "indirect" franchise fee if payments to third parties are required by the franchise contract, and the third party is either affiliated with the franchisor or pays any consideration to the franchisor.[85] Other forms of indirect consideration passing to the franchisor might also qualify as a franchise fee.[86]

CONCLUSION

Because of the extensive protection offered by many state franchise statutes, a strong incentive exists for a potential plaintiff to try to fit itself within its protective scheme. To do so may require imaginative use of the key concepts, such as finding a "marketing plan" in a collection of separate suggestions and documents, or a "franchise fee" in various types of payments. The result, however, may be to provide a small businessman more protection than the antitrust laws had traditionally provided, and certainly far more protection than is available today under those laws.

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83. *See Premier Wine*, 644 F. Supp. at 1438-39 (hiring and paying personnel required to handle distributor's product line does not qualify as a franchise fee).

84. See Schultz v. Onan Corp., 737 F.2d 339, 345 (1984) (payments to previous franchisee to buy the business not a franchise fee); Laurence J. Gordon, Inc. v. Brandt, Inc., 554 F. Supp. 1144 (W.D. Wash. 1983) (payment to former franchisee for business and no-compete covenant did not constitute a franchise fee).

85. *See* ILL. REG. 104, 105 (promulgated under ILL. ANN. STAT. ch. 121½, para. 703(14) (Smith-Hurd 1974)), *quoted in* Kojanchich v. Bridges, 93 Ill. App. 3d 550, 555, 417 N.E.2d 694, 698 (1981); ILL. ADMIN. CODE tit. 14, § 200.105 (1985).

86. *See* Communication Maintenance, Inc. v. Motorola, Inc., 761 F.2d 1202, 1206 (7th Cir. 1985) (indirect franchise fee may consist of consideration in the form of a discount on services rendered).