# CO-BRANDING: MANAGING FRANCHISE BRAND ASSOCIATIONS

ANN HURWITZ*

## INTRODUCTION

Co-branding is now a familiar term in the current lexicon of franchising and a popular strategy in the expansion efforts of many franchise companies. Consumers are becoming accustomed to ordering their favorite franchised brand of hamburgers, submarine sandwiches, ice cream, or frozen yogurt at the same location in which they purchase gasoline for their automobiles. It is an increasingly common experience to find well-known franchised systems allying with one another to serve tacos and fried chicken or donuts and ice cream under one roof. Announcements of new co-branding alliances appear almost daily in the trade press.

This rush by franchise companies to conclude co-branding alliances can be attributed to the very real benefits that an effective alliance provides. New locations, cost sharing opportunities, increased volumes, and the added market power offered by the combination of two or more strong brands are powerful inducements to enter the co-branding arena. While these alliances potentially offer tremendous benefits to companies and consumers alike, they are not without risk. Co-branded offerings may fail to gain acceptance in the market or co-branding partners may find that they in fact have incompatible systems or goals.

These risks may not be entirely eliminated, but they can be reduced by careful planning that focuses on the selection of co-

* Ms. Hurwitz is a shareholder of Jenkens & Gilchrist, Dallas, Texas. She is a member of the American Bar Association's Forum on Franchising and currently serves as Editor-in-Chief of the Forum's *Franchise Law Journal*. Ms. Hurwitz is also the immediate past Chair of the Franchise and Distribution Law Committee of the Texas State Bar's Intellectual Property Law Section.

branding partners, the development of the co-branded offering, and the creation of a legal structure that is shaped by the attributes of the participants and by their business needs.

## I. CO-BRANDING: WHAT IS IT?

Branding is in essence a marketing concept that has traditionally been identified with product manufacturers. These manufacturers devote significant time, effort, and funds to establish brand identities for their products so that consumers can distinguish such products from those of competing manufacturers. Due to the importance of branding to the marketing dynamic, much has been written about brand development and management.[1]

In managing their brands, manufacturers tend to employ a number of different strategies, including the pairing of different brand names. This may be done for a variety of reasons, such as to introduce a new product under the auspices of a familiar brand name or to inject new life into a sagging product line.[2] Brands may also be paired across company lines in order to create synergies and increase consumer demand. Pairing may be accomplished using a straight licensing arrangement, with one company paying another a license fee to use its name. An ingredient licensing arrangement may also be made with one company paying another to use one of its products as an ingredient in yet another product manufactured by the licensee.[3]

Brand pairing, or co-branding, between companies has not been limited to product manufacturers. Service companies have also used the concept. A prominent example of co-branding may be found in the credit card industry where credit card

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1. *See generally*, Sylvie LaForet & John Saunders, *Managing Brand Portfolios: How the Leaders Do It*, 34 J. OF ADVERTISING RES. 64 (1994).

2. *Id.*

3. A recent example of such an arrangement is the pairing of General Mills' Betty Crocker with Hershey to produce Fudge Brownie Mix. Other examples include Nabisco's Chips Ahoy made with Hershey's chocolate morsels, Ben and Jerry's ice cream made with real Heath bars, and Diet Coke made with NutraSweet.

issuers have partnered with airlines, car manufacturers, and others in an effort to enhance the demand for their card by offering free mileage and other benefits.[4]

Franchise companies have not been immune to the lure of co-branding. A sampling of recent articles shows just how pervasive co-branding has become in franchising.[5] But what is "co-branding," or, more precisely, what does it add to the recent trend of expanding the distribution opportunities of franchise systems in non-traditional ways? To fully appreciate the role of co-branding in franchising, one must view it in the context of this general movement towards non-traditional expansion or alternative distribution.[6]

In its 1987 report on Franchising in the Economy, the U.S. Department of Commerce observed that: "Many franchisors are currently involved in testing a new form of franchising comprised of different products under the same roof—in other words a franchisor would sell products and/or services within the unit of another franchisor . . . ."[7] The Department of Commerce referred to this trend as "combination franchising,"[8] and that term was adopted by some of the early commentators.[9]

Combination franchising, however, is simply one way that franchisors have sought to expand their systems and distribution opportunities. Using a variety of different vehicles, like kiosks, carts, satellites, modules and express units, franchise

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4. For example, the Visa AAdvantage Card and the GM Mastercard.

5. For example, Daka International, Inc. has acquired a minority interest in the LaSalsa chain and plans to pair the quick-service taqueria concept with its Fuddruckers gourmet burger concept and Arby's, Inc. has teamed with T. J. Cinnamons. For Arby's, this would enhance its previously announced alliance with ZuZu, Inc., a quick service Mexican chain. Carol Casper, *Jockeying for Position: The Race to Grow a National Chain is Still Wide Open*, 95 NATION'S RESTAURANT NEWS, March 20, 1996, at 118.

6. *See* Charles B. Cannon & Kim A. Goodhard, *Non-Traditional Expansion: The Use and Limitations of Trademark Licenses*, A.B.A. FORUM ON FRANCHISING (1995) (providing an excellent discussion on the background of the co-branding movement in franchising).

7. U.S. DEP'T OF COMMERCE, FRANCHISING IN THE ECONOMY 1985-1987, at 5 (1987).

8. *Id.*

9. *See* Arthur I. Cantor, *Combination Franchising*, INT'L FRANCHISE ASS'N 20TH ANNUAL LEGAL SYMP. (1987); Michael R. Davis & Gary Blumenthal, *Concurrent Franchising*, INT'L FRANCHISE ASS'N 21ST ANNUAL LEGAL SYMP. (1988).

companies have expanded into other franchised systems. They have also expanded into non-franchised chains, such as hospitals, schools, ballparks, hotels, airports, and other non-traditional or "special purpose" venues.[10]

The reasons for this expansion into non-traditional settings have been well documented. These reasons include increased competition for, and the increasing lack of, attractive "traditional" sites, as well as the desire to make a system's products or services more accessible to consumers. Particularly in systems where purchasing decisions are made largely on the basis of convenience and accessibility, significant benefits may be obtained by "going to the consumer," establishing units in non-traditional or "special purpose" venues, and maintaining a presence in as many locations as possible.[11] The ability to share costs and increase volume through many of these non-traditional arrangements can also contribute significantly to bottom-line profitability.[12]

Many of the reasons for engaging in non-traditional expansion also lead companies to consider co-branding arrangements. Similarly, many of the issues presented in the general context of non-traditional expansion are also presented where co-branding is a factor. As with any non-traditional expansion effort, co-branding partners must deal with construction and development, cost sharing, labor, and a host of related issues.[13] It is submitted, however, that the concept of co-branding adds another dimension to the general discussion of non-traditional expansion, focusing as it does on the pairing of two or more distinct "brands." The directed effort to effectively partner with a complementary brand is what distinguishes a discussion of co-

10. *See* Cannon & Goodhard, *supra* note 6.

11. Studies have shown that seventy-five percent (75%) of shoppers decide to purchase Big Macs and Happy Meals five minutes or less before making their purchase. Greg Burns, *French Fries with that Quart of Oil?*, BUS. WK., Nov. 27, 1995, at 86.

12. For further discussion of these and other reasons that franchise companies engage in non-traditional, or alternative, distribution, see Cannon & Goodhard, *supra* note 6; Cantor, *supra* note 9; Davis & Blumenthal, *supra* note 9, H. Bret Lowell & Mark A. Kirsch, *Dual Branding: The New Franchising Phenomenon*, 2 LEADER'S FRANCHISING BUS. & L. ALERT, 2-3 (Nov.-Dec. 1995).

13. *See* Lowell & Kirsch, *supra* note 12 (listing issues that may arise in a co-branding arrangement).

branding arrangements from a general discussion of non-traditional or alternative distribution arrangements. It is also what presents increased opportunities and risks for the participants.

## II. CO-BRANDING: WHY DO IT?

It is not surprising that co-branding appeals to franchise companies. Like traditional product manufacturers, franchisors invest substantial resources in developing their systems, or "brands." Trademarks, servicemarks, trade dress, and signature products and services establish brand identity and are advertised and promoted in a continuous effort to build and maintain system or brand loyalty among consumers. Managing the "brand" in a way that increases market penetration and market share is always a primary concern. Co-branding offers franchised companies a way to achieve those goals.

Generally speaking, the added value that co-branding offers franchise companies is leverage—that is, the ability of the partners in the co-branding alliance to rely on each other's image, products, services, and locations to increase their own market penetration and market share. Where each system, or brand, in the co-branding arrangement has developed a reputation for quality, the alliance of the systems gives each partner immediate access to the consumer trust, confidence, and acceptance that the other has developed over time.

More particularly, co-branding offers a franchise company the opportunity to expand its offering of products and services without incurring the expense and some of the risks associated with the internal development of new products, services, or outlets. It also provides companies with the opportunity to capture a new customer base or to alter its existing customer profile. For example, a food service franchisor whose system emphasizes dinner may enter into a co-branding alliance with a system that has a heavy breakfast or lunch trade, thereby expanding its customer base. A gas station/convenience store chain may also find that by adding a yogurt or ice cream franchise it draws more women and children as customers. In this respect, the concept of co-branding may be viewed as an extension of the shopping mall, which is an extension of Main Street. Bringing varying merchants together in one place gives them access to consumers who may not otherwise patronize their businesses. While co-branding may not be a necessary predicate to cross-marketing or cross-promotional programs, in which each system advertises the other's products or services in combination with their own, a co-branding alliance clearly provides incentives and opportunities for engaging in those activities.

The impetus for co-branding may also come from external sources. Franchised systems that fail to keep pace with consumer demands and expectations risk experiencing a loss of their customer base and a declining market share. Today's consumers have high expectations and make many purchasing decisions based on a combination of convenience, accessibility and quality. They have also been shown to have strong brand loyalties. In the highly competitive gas station/convenience store market, for example, this trend may well translate into an imperative to ally with a quality, branded food service franchise rather than offering no food service or offering a non-branded food service alternative.

It is also true that in the current business environment different franchised systems may well be owned by a single company or by a commonly controlled group of companies. PepsiCo Inc.'s ownership of the KFC, Pizza Hut, and Taco Bell franchise systems is a prominent example of this trend, but it is by no means the only one. In such situations, management may become convinced that co-branding is an effective strategy to maximize the potential of two or more of these commonly owned systems. Thus, co-branding may come about in the form of a "top-down" directive to ally the systems.[14]

However, for all its perceived and actual benefits, co-branding is not without its risks.[15] Commentators on brand

14. The reasons franchise companies pursue co-branding strategies and the benefits of co-branding are drawn from the author's personal experiences and interviews with various participants in co-branding initiatives. The trade press is also replete with accounts of why companies engage in co-branding and why some co-branding initiatives fail. *See* Steve Dwyer et al., *Branded Fast Food: A Boomlet Becomes a Boom*, 87 NAT'L PETROLEUM NEWS 34 (1995); *McDonalds, Big Oil Don't Tell About Co-Brand Failures*, 32 U.S. OIL WK. 1 (Nov. 13, 1995); Milford Prewitt, *Operators Zoom to Service Stations & Truck Stops*, 28 NATION'S RESTAURANT NEWS 37 (1995); *Survey Underscores Co-Branding Growth, Accelerated Store Upgrade Investments*, 87 NAT'L PETROLEUM NEWS 53 (1995); *Tips for Avoiding Fast Foot Co-Brand Mistakes*, 32 U.S. OIL WK. 1 (Dec. 4, 1995).

15. *See* Dwyer, *supra* note 14; *see also* Burns, *supra* note 11.

management strategies outside the franchise area have suggested that co-branding may result in mixed consumer perceptions, leading to confusion and, eventually, a possible diminution in the value of the participating brands.[16] Some have questioned whether the short term successes of co-branding disguise the potential erosion of each brand's brand equity.[17] Others have asked whether extensive co-branding initiatives might not bring with them a danger of over-saturation.[18]

Apart from such speculative risks, co-branding brings with it other, more concrete, risks, many of which grow out of the very benefits that co-branding offers. As indicated above, one of the benefits of co-branding is the ability of one franchised system (the "tenant") to expand rapidly within locations already established by its franchised or non-franchised co-branding partner (the "host"). However, in order for this opportunity to constitute a true benefit, the tenant system must have the necessary infrastructure in place and be prepared to grow aggressively.

Another prominent risk involves the possibility that one of the co-branded systems may come to be viewed negatively by the public and that such negative sentiment may be attributed to the co-branded alliance (e.g., guilt by association). To some degree, this risk may be controlled by entering into co-branding alliances with established, reputable companies. However, even these companies may suffer the misfortunes of fate. For example, who can predict which food product will be shown to be unhealthy in next year's food studies? Moreover, the very prominence of some companies may invite the kinds of actions that give rise to such misfortunes. Everyone who follows the news can cite at least one instance where a well-known company has been made the target of product tampering by persons with real or imagined grievances. Even though a company has little or no control over this type of external activity, its occurrence can have a damaging effect on the company's image. Companies

16. *See* Laura Castenada, *Mixed Companies: Marketers Turn to Co-Brands in Order to Spread the Costs of New Product Development,* DALLAS MORNING NEWS, July 8, 1995, at 15.

17. *Id.*

18. *Id.*

may also be made the subject of adverse publicity that negatively affects their image as a result of internal decisions, even those that may be unrelated to the system's operation. Recent examples are those companies that were targeted for their continued investments in South Africa, before that country's policy of apartheid was abolished. Where the image of one system in a co-branding alliance is damaged, its co-branding partner may be negatively affected as well.

A related risk, and one of particular relevance to franchise companies engaged in co-branding arrangements, relates to the changes that are an inherent aspect of franchise systems. It is an accepted fact that successful franchise systems change in response to competitive forces, as a consequence of an acquisition, or for other reasons. Such changes may well involve a redefinition of the system's image, the introduction of new product or service lines, the identification of a new customer base, the implementation of new financial strategies, and other such matters. While one would not necessarily anticipate these changes to result in a system that is completely different from the one with which the co-branding alliance was initially concluded, the modified system may not be as compatible with the system of its co-branding partner as it formerly was. The dilemma is clear. Franchise systems must have the flexibility to evolve in response to the changing business environment. Yet when two or more franchise systems are linked in a co-branding arrangement, there is a risk that one and not the other will change. The systems may also change in different ways so that the synergies which once existed are no longer present.

Put differently, there is the risk, as with any marriage, that the partners will grow apart or that the relationship will dissolve for other reasons, like a change in corporate strategy. If this happens, it may be difficult to unwind the co-branding arrangement and effectively redirect consumer perceptions. At a minimum, the failure of a co-branding arrangement creates issues of deidentification: how long will the co-branded units continue to operate once the partners have decided to go their separate ways; who is responsible for deidentification; and who pays the associated costs? At worst, the co-branded systems may have become so closely identified in the minds of consumers that it becomes difficult to survive independently after the separation occurs.

## III. Co-Branding: How To Do It.

### A. *Identifying the "Right" Co-Branding Partner.*

The risks associated with co-branding have caused many to question whether companies can have long-term, effective co-branding relationships where there is no common control of the participating brands. One line of thought and, some would argue, the dominant line of thought in franchising today, is that common control of the co-branding participants must exist in order for the alliance to be effective. If true, the result would be that successful co-branding arrangements could only be conducted by those companies with sufficient resources to acquire complementary brands.

However, there is a competing line of thought which holds that common control of participating brands is not necessary as long as the co-branding partners have a common mindset and synergy of purpose. This camp would argue that to be effective, co-branding partners need only have compatible operations and goals, not common control. Whether or not common control is a *necessary* component of an effective co-branding alliance, there are those who maintain that common control in itself is not *sufficient* to overcome deficiencies inherent in any co-branding arrangement where there is no commonality of purpose or compatibility of operations and goals. Common control alone does not automatically confer these attributes, particularly in today's world where systems with different cultures are regularly bought and sold.[19]

If "compatibility" is the necessary ingredient of a successful co-branding relationship, whether with common control or without, how does one identify a "compatible" co-branding partner? While, to date, this has seemed to be more of an art than a science, some general guidelines can be suggested.

19. The author wishes to thank those persons who graciously shared their views on this subject, with special appreciation to Robert Choate, APC, Roth, Choate & Affiliates, Inc., Houston, Texas.

Borrowing a page from the co-branding experiences of other industries, one may begin by asking three basic questions.[20] First, does the prospective co-branding partner offer added name brand equity; that is, do consumers recognize and value the brand? Some branding experts would also hasten to add that even if the new brand offers added value and prestige in the form of consumer recognition and acceptance, it should do so without overshadowing a company's own brand.[21]

Second, does the prospective co-branding arrangement offer additional marketing benefits? These benefits may be in the form of increased advertising dollars, cross-marketing, and/or cross-promotional opportunities.

Third, does the prospective co-branding partner have a strong and complementary customer base? This may be evaluated in a number of different ways. Every successful franchise system knows the demographics its units must have in order to succeed and be profitable. A straightforward evaluation of a prospective co-branding partner would ask whether that partner requires compatible demographics. It is important to realize, however, that other factors may influence the analysis. For example, a prospective host system may offer locations in a geographic area that the tenant has been unwilling to exploit because the demographics of the area will not support the costs of developing its traditional unit. However, the possibility of developing lower cost non-traditional units at established host locations within the geographic area may well serve to justify the partnership, notwithstanding general demographic concerns.

Similarly, both prospective participants in the co-branding arrangement presumably know their target customer. Where the target customers are different, should the relationships proceed? There is no simple answer to such a question and experiences differ. It may well be that the co-branding arrangement serves to broaden or alter the traditional customer base of the host so as to benefit both host and tenant by increasing the volume of traffic, or by changing customer profiles in a way

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20. *See Exxon Goes With START*, 11 FIN. SERVICES REP., July 6, 1994, at 5.

21. *Co-Branding Partnerships Expand Share in Market Segments, Experts Say*, 50 PR NEWS 20 (1994).

that favorably alters the mix of products sold. However, it may also be that the participants discover the host's typical customer is not the tenant's typical customer and that the presence of the tenant fails to independently attract its own customer base. Because these and other issues cannot be satisfactorily answered in theory, but may only be proved in practice, companies contemplating a co-branding partnership are well advised to conduct a thorough test of the co-branded offering, as discussed in more detail below.

Apart from the three considerations described above, it is submitted that there are at least three others that are very relevant to the identification of a compatible co-branding partner. In brief, there must also be operational, financial and legal compatibility.

It seems axiomatic that in order for a co-branding relationship to succeed, the participants must be operationally compatible or must be able to achieve compatibility. Operational issues may include how the two brands are physically presented together, whether one partner has more stringent quality, service, or cleanliness standards than the other, who has managerial responsibility for the tenant's operations, and what products and services of the tenant will be offered.

It is also essential that both the host and the tenant achieve the financial returns necessary for economic success. While the precise measure of success may vary, a co-branding arrangement that does not afford each participant an adequate rate of return is doomed to failure.

Finally, there must be no overriding legal impediment to the proposed alliance. If, for example, the operation of a tenant's units within the host's locations is determined to negatively impact or encroach on the tenant's existing franchisees, the relationship may have to be rejected where there is no ability to contain the negative impact. One approach to containment that may or may not prove feasible is to exclude from the arrangement those host locations that are within an unacceptable proximity to an existing tenant franchisee. This and other approaches may not be acceptable to the host, however.

*B. Testing Your Partner and the Offering.*

While guidelines like those described above are useful starting points, most co-branding participants rightfully believe that the only way many of these factors can be adequately explored, and other relevant considerations identified, is through the conduct of a test. It is the test phase that allows the co-branding participants to shape and refine the co-branded offering, to identify and attempt to resolve problematic operational issues, and to measure the potential for success in terms of financial returns and consumer acceptance. A successful test can also provide the data used to "sell" the co-branding concept to the participants' franchisees.[22] Thus, the test phase often proves to be a critical step in the identification of a compatible co-branding partner. Given the potential consequences of a failure after the co-branding arrangement has been launched, a test can significantly limit future exposure by helping to determine at an early stage which co-branded offerings are not likely to succeed.

The circumstances of each situation will contribute to the terms of the test agreement. As other commentators have noted, it is important to establish at the outset such things as the length of the test period; whether company-owned or franchised units will be involved in the conduct of the test; and the scope of the test, both in geographical terms and the number of locations tested. It is also desirable for the test agreement to establish what constitutes a successful test, and to provide a blueprint for unwinding the alliance if the criteria for success are not met.[23] It is, of course, possible for the agreement to establish criteria for success that are subjective and to give any participant the right not to proceed in its discretion. But even though the test agreement itself may not set objective criteria for success, management of the respective participants should

22. *See* Ann Hurwitz, Richard Asbill, & Jerry Lovejoy, *Reshaping the System: Cooperative Strategies for Overcoming Business and Legal Obstacles to Change in the Mature Franchise System*, A.B.A. FORUM ON FRANCHISING (1995).

23. *See* Lowell & Kirsch, *supra* note 12.

formulate an objective definition of success internally to use as a tool in determining whether the proposed arrangement should go forward.

### *C. Structuring the Co-Branding Arrangement.*

In structuring a co-branding arrangement, one must potentially address issues present in any non-traditional expansion effort. Even in situations where brand leveraging is not a factor, expansion into non-traditional settings can present such issues as: What is the best way to physically integrate the franchised unit into the non-traditional setting? Given that many non-traditional settings serve a discrete and often captive market, what is the unit's appropriate contribution to the system's overall advertising effort? Does the location of the franchised unit within the non-traditional setting negatively impact sales of surrounding franchisees or violate territorial protections granted to them? Is the host the best person to manage the unit, or should it be operated by a franchisee who is not affiliated with the host ? If the unit is operated by the host, should the host be granted a franchise or is it possible to structure the arrangement as the grant of a trademark license?[24]

The addition of a co-branding element can serve to exacerbate these and other general non-traditional expansion issues. Moreover, co-branding brings with it its own set of issues. These include image, trademark control, and brand preeminence issues. Which partner's brand takes the primary position on signage? Will the participants offer dual branded products and if so, who will control those products? Questions of exclusivity also arise. For example, should the tenant give the host the exclusive right to co-brand with the tenant system, and should the tenant seek a covenant from the host that it will not engage in co-branding arrangements with other systems in the tenant's industry?

Still other issues are raised if both branded systems are franchised. In that circumstance, the participants must reconcile the operation of the host and tenant franchise agreements

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24. *See* Cannon & Goodhard, *supra* note 6.

or must evaluate whether there is a viable alternative to a direct grant of the tenant's franchise to the members of the host system.[25]

The issues that arise and the ways in which those issues are addressed depend on the facts involved in a particular transaction. Although not an exclusive listing, some important factors that may influence the way in which particular issues are resolved include: whether the host and tenant are both franchised, or whether only the tenant is franchised; whether the host and tenant are in the same or different industries; how the level of experience required to operate the tenant's system compares with the level of experience required to operate the host's system; the geographic coverage of the participating systems; and whether the system includes company-owned units as well as franchised units. These factors will also help shape the ultimate structure of the co-branding arrangement. There are at least three basic structures that may be employed in a co-branding arrangement, which are described below. However, the appropriateness of a particular structure will depend on the relevant facts.

### 1. The Grant of Franchises by the Tenant to Members of the Host System

There are numerous variations on this theme. For example, a tenant franchisor may reserve the right to grant franchises directly to the host for its company-owned units and, if the host system is franchised, to franchisees of the host for franchised units. The tenant franchisor may also make the host a subfranchisor, area representative, or franchise broker of the tenant. A subfranchisor "stands in the shoes" of the franchisor and is given the rights to grant franchises to third parties on its own initiative, as well as to perform the obligations under the franchise agreement that would otherwise be performed by the franchisor. In a subfranchise arrangement, the franchise agreement is between the franchisee and the subfranchisor, although in some cases the franchisor may also be made a party. As a

25. *See* Lowell & Kirsch, *supra* note 12 (listing categories of issues that may arise in a co-branding arrangement).

subfranchisor, the host could grant tenant franchises directly to the host's franchisees and could perform training, inspections, and other obligations that would normally be performed by the tenant franchisor.

A franchise broker solicits prospective franchisees for a franchisor, but the franchisor grants the franchise and enters directly into the agreement with the franchisee. An area representative also solicits prospective franchisees, who enter into direct agreements with the franchisor. By agreement with the franchisor, the area representative also performs certain services for the franchisees following the sale, services that would otherwise be performed by the franchisor. As the tenant franchisor's area representative or franchise broker, the host could solicit its own franchisees on behalf of the tenant franchisor. If qualified as an area representative, the host could also service those franchisees after the sale.

If the host has or intends to have company-owned units, it could be made an area developer of the tenant. An area developer is granted the right to establish a certain number of outlets, generally in a designated geographic area, over a specified period of time. The area developer undertakes the development obligation itself, with no right to grant franchises to third parties. Each outlet established by the area developer is typically subject to a separate franchise agreement.

### 2. The Grant of Trademark Licenses by the Tenant to Members of the Host System

Although listed separately as an alternative structure, this may also be properly considered a variation of the structure described in paragraph one above. One advantage of such a structure is that it may minimize or eliminate many of the regulatory concerns involved when a franchise is granted. However, care must be exercised to ensure that what is created is a true trademark license and not a disguised franchise. Federal and state laws typically define a "franchise" as including three elements: the payment of a fee, the right to use the franchisor's marks, and significant control or assistance by the franchisor over the franchisee's business.[26] A true trademark license does

26. FTC Franchise Trade Regulation Rule, 16 C.F.R. §§ 436-436.6 (1979). For a

not contemplate the significant level of assistance or control that characterizes a franchise. The tenant must be comfortable from a business standpoint that the elimination of the assistance and controls required to "convert" the franchise to a true trademark license will not jeopardize operation of the unit.[27]

### 3. The Direct Grant of a Franchise by the Tenant Franchisor to a Non-Host Franchisee, Coupled with the Lease or Sublease of Space Within the Host's Location to that Franchisee

This structure may be appropriate, and even necessary, where the operation of the tenant's unit requires a level of expertise not easily achieved by the host, or where the host has made a business judgment not to become directly involved with the operation of the tenant's business. This may occur frequently where the host and tenant systems have different focuses (e.g., a host system directed to product merchandising and a tenant system directed to food service).

As has been noted in the literature, each of these alternatives and their variations have certain consequences, including assigning responsibility for compliance with federal and state franchise laws.[28] Such laws generally require pre-sale disclosure (on the federal and state level) and pre-sale registration (on the state level only). In considering whether one of the structures described above is an appropriate structure for a particular co-branding arrangement, one is well-advised to focus on the requirements of the businesses involved and the capabilities of the respective participants. For example, where the tenant and host are in different industries, it may be inappropriate to make the host a subfranchisor or area representative of the tenant, since the host is not likely to have the degree of experience needed to effectively discharge the responsibilities of those positions.

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discussion of definitional considerations under state franchise laws (some of which follow a scheme that requires a "community of interest") see Kim A. Lambert & Charles G. Miller, *The Definition of a Franchise: A Survey of Existing State Legislative and Judicial Guidance*, 9 FRANCHISE LAW J., 3 (1989).

27. Cannon & Goodhard, *supra* note 6 (discussing this alternative).

28. Cantor, *supra* note 9; Lowell & Kirsch, *supra* note 12.

A franchise company may employ one or more of these or other alternative structures in its co-branding program, depending on facts and circumstances like those listed above. Yet another important fact that contributes to how co-branding issues are resolved and to how relationships are structured is the relative bargaining positions of the prospective co-branding partners. In the early days of co-branding, strong partners—whether host or tenant—used the strength of their brands to gain significant concessions from their weaker partners. However, that trend may be changing, as both host and tenant systems are coming to appreciate that winning concessions from one's co-branding partner does little to ensure the ultimate success of the alliance. Both hosts and tenants are increasingly discovering that they must each make concessions if they are to design an effective co-branded offering that is accepted by consumers. It is only with consumer acceptance of the co-branded offering that the success of the participants in that offering is assured.

## CONCLUSION

Co-branding has added an exciting and potentially rewarding dimension to the non-traditional expansion efforts of franchise companies. However, co-branding initiatives are not without risk. To minimize those risks, careful consideration must be given to the selection of a compatible co-branding partner, and attention devoted to designing and structuring a co-branded offering that is perceived as viable by consumers. Co-branding initiatives that ignore these basic principles risk failure and diminishment of the participants' brand equity.