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## **Goldstein Legal's Guide to Franchising vs Licensing**

Franchising and licensing are excellent options for business owners looking at expansion, because they provide an alternative to organic growth, which often entails less risk. But there is often a lack of clarity as to how the two models differ and business owners sometimes head in the direction of one, without fully understanding the merits of the other. However, there really is no great mystery involved and to prove it, we will run through the pros and cons of each to help you understand which might suit your business best.

### **Terminology**

First up, let's look at terminology. In the majority of cases the term '**franchising**' refers to business format franchising. The **franchisor**, being a business with a strong brand and a well-established and profitable business model, looks to replicate that model by **franchising** it to other people – the **franchisees**.

In a **licence agreement**, on the other hand, the **licensor** grants a **licensee** the right to use the licensor's brand name and/or other intellectual property rights (such as copyrights).

As with a franchise, the licensee's business benefits from the brand and intellectual property of the licensor, and the licensee pays fees to the licensor accordingly.

The important difference is that a licence arrangement tends not to involve the replication of an existing business format. In many cases, the intention is the opposite, with the licensor licensing their brand to a third party who will be able to exploit it in a consumer sector where the licensor has no presence or expertise.

### **Is there a rule as to which model works best with certain business-types?**

Sadly, it is not quite as simple as that! It is, of course, **franchising** that brought the likes of MacDonalds, Starbucks, Mail Boxes Etc., Hard Rock Café and hundreds of other brands their international reach and huge success.

Indeed, the advantages of franchising are well-known: new start-up franchises have a much lower failure rate than other start-up businesses. Moreover, franchise arrangements extend the use and reputation of the brand to a wider geographic area and a bigger audience, to the benefit of both the franchisor and the franchisees.



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Does this mean that franchising produces a win-win for everyone? Sometimes, yes. But not always. Franchising is not the perfect solution for every business, and it isn't easy. As a potential franchisor, you soon realise that there are more franchise opportunities on offer than there are potential franchisees wanting to take them on. Your franchise offer must be as, or even more, attractive, than those of your competitors.

Furthermore, a franchise concept is unlikely to thrive unless you first have a business model with a proven track-record of profitability. In getting your franchise offering off the ground, you are likely to have invested time, effort and money in everything from a company operations manual to a franchise prospectus and detailed marketing strategy.

It is no surprise therefore that successful franchisors will often have spent upwards of £30,000 to launch a franchise business model, and sometimes more.

As for **licensing**, the perfume industry is a good illustration of where this particular model has thrived. The majority of all the big name fragrances are made and sold by just two or three perfume houses. Calvin Klein, Cerruti, Vera Wang and Chloe, for example, are all manufactured and distributed by Coty under licence from the brand owners.

**Licensing** also works well where the licensor has developed some specific technology, know-how, brand images or design which are attractive to licensees who wish to incorporate it into their existing businesses. Take software and database technology, for example, which are invariably exploited through licensing.

On the other hand, coaching and training concepts have been shown to work well either as franchised businesses or licences. Action Coach and Pitmans Training are examples of successful franchised operations. But there are also a number of businesses that have developed coaching and personal development tools that are exploited through licences to training establishments who incorporate those tools into their own business structures, such as Neuro-Linguistic Programming (NLP).



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### **Pros & Cons**

To clarify, let's highlight the pros and considerations that apply to each business model.

### **Franchising: pros**

- A franchisor will receive an immediate income from their franchisees, for the use of their brand and business model
- A franchisee has the opportunity to buy into an already proven and profitable business concept
- Both franchisor and franchisee benefit from franchise arrangements which extend the use and reputation of the brand to a wider geographic area and audience

### **Franchising: considerations**

- A franchise is unlikely to thrive unless you already have a business model with a proven track-record of profitability
- A franchisor will often have spent upwards of £30,000 prior to launching their business model. This sum will include the following items:
  - **Business analysis** (to include a franchise model and pro-forma financials)
  - **Pilot** franchise operation
  - An attractive and compelling **franchise prospectus**
  - **Marketing strategy**, both for franchisee recruitment and brand awareness
  - **Franchise Agreement** which is tailor-made for your particular business and which protects your rights as a franchisor

### **Pros: licensing**

- A licence can be easier to manage than a franchise
- The licensee has more freedom to run their business their own way
- As a general rule, a licence arrangement is cheaper and easier to set up than a franchise concept, and less demanding in terms of ongoing management time

### **Considerations: licensing**

- A licence agreement has to focus very carefully on quality assurance and compliance with the licensor's standards



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- Products or services sold under licence should enhance and complement the reputation of the licensor, and the licence agreement must allow the licensor to “pull the plug” whenever quality or compliance are compromised
- Before granting any licence, the business owner will need to demonstrate how they will monitor quality in practical terms

Both franchising and licensing can set your business on the road to success, but it is essential to choose the right direction. Hopefully this short guide will help clarify the model best suited to your business and ambitions, and once you have made that important decision the sky should be your limit!

Goldstein Legal has extensive experience and expertise both in franchising and licensing. If you'd like a **free consultation** to find out more about both business models, get in touch on **01753 865165**, or email us at **[info@goldsteinlegal.co.uk](mailto:info@goldsteinlegal.co.uk)**.