

Franchise Trademarks 101 – Part 1: Does a Franchisee's Trademark Use Accrue to the Franchisor?

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Trademarks represents a unique form of intellectual property. A trademark is a word, phrase, design, colour, sound, fragrance, texture, or other identifying/symbol that conveys to the user or consumer an assurance as to the source of origin of the product or service with which the trademark is used. According, the rights arise and only continue by reason of the trademark owner's *use* of the trademark.

The exclusive right to use and enforce a trademark is lost if the trademark is not used, if it becomes generic through uncontrolled use (i.e., it becomes an industry or consumer term of art for the goods or services associated with it), or if it does not continue to identify the claimed trademark owner as the source of origin of the associated goods and services.

In any trademark infringement or enforcement matter, there are only three groups of defences:

1. Firstly, that the defendant did not engage in the activity alleged - the defendant did not use the trademark as alleged;
2. Secondly, that if the defendant did use the trademark, he or she did so with the express or implied consent of the trademark owner; and
3. Thirdly, the nuclear option – namely, if the first two defences are not available, that the trademark owner's rights are invalid principally because the trademark does not serve to identify the correct name of the entity that is the source of origin of the goods and services in question.

The use requirement to obtain and maintain trademark rights presents a challenge in aggregated business models such as dealerships and franchises. Under those business models, trademark rights are tied to a brand or franchised system in which the goods and services are in fact offered by a franchisee and not the franchisor claiming to be the trademark owner. Moreover, it could even be a scenario where a separate back-office entity is established by the franchisor to hold trademark rights for preferential tax treatment or to insulate intellectual property from trade creditors and consumer claims. In these circumstances, does the consumer believe that his or her favourite fast-food meal or bath products comes from the store around the corner, or from the franchisor or that foreign royalty trust established by the franchisor?

In Canada, Section 50(1) of the *Trademarks Act* (Act) offers some help to trademark owners, including franchisors. This section provides that if an entity, such as a franchisor, authorizes another, such as a franchisee, to use a trademark and the franchisor has, under license, direct or indirect control of the

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character and quality of the goods and services associated with the trademark, then the use, advertisement, or display of the trademark by the franchisee is deemed always to have had the same effect as the use, advertisement or display of the trademark by the franchisor. In other words, in these circumstances, the franchisee's use of the trademark accrues to and is deemed to be the franchisor's use of the trademark, thus underpinning the franchisor's rights in the trademark. Further assistance can be found in Section 50(2) of the Act, which provides that to the extent that public notice is given of the fact that the use of a trademark is a licensed use and of the identity of the owner, it is presumed that the use is licensed by the owner of the trademark and that the character or quality of the goods or services are offered under the control of the trademark owner. This shifts the onus to the infringer/challenger to disprove the *prima facie* notice assumption that the franchisor does exercise the requisite degree of control.

Although Section 50 of the Act provides significant assistance to franchisors, it is *not* a complete resource and solution to the problem of protecting franchisor rights. There are nuances to the interpretation of the legislation that have arisen out of the case law that must be addressed in any examination of a franchisor's trademarks.

The jurisprudence arising from the Act continues to evolve, but generally speaking, the license between the franchisor and the franchisee does not have to be in writing and oral licenses may be acceptable. However, a written license is more valuable than an oral understanding for evidentiary purposes and for clearly setting out the scope and parameters of the license. The case law is also clear that the exercise of control over the character or quality of the goods or services must not only be *de jure* control (a legal right to control) but must also be *de facto* control (control that is exercised in fact and can be evidenced as such). There must be an evidentiary basis to establish that the franchisor does in fact, and not just in theory or on paper, exercise control over the character and quality of the goods and services associated with the trademark. Simply having interconnected corporate boards of directors between franchisor and franchisee may not be sufficient to establish the required level of control by the franchisor. Moreover, recent case law establishes and underscores that the control must be exercised over the character and quality of the goods and services associated with the trademark and not just the advertising content or packaging associated with those goods and services. Arguably, the public notice of the franchisor/franchisee relationship should be evaluated from the perspective of the consumer and not the franchisor or the franchisee. Accordingly, the question arises as to how to establish that public notice. Can the trademark ownership notice be placed in the fine print online or in instructions or on packaging, or be put inside a product package not brought to the attention of the consumer until after the product is purchased or the service performed? Or is it a safer route to give notices as part of point-of-sale information?

In Part 2, we will look at some approaches to best practices in compliance with the provisions of Section 50 of the Act to protect the franchisor's valuable family of trademarks and the goodwill they represent.