Cannabis Franchising

Opportunities and Legal Perils

Franchising Is at the Forefront of the Cannabis Sector

Why? Because cannabis is big business. And its growth shows no signs of slowing. So far, 33 states and the District of Columbia have enacted some form of marijuana legalization, and 12 of those jurisdictions have adopted laws allowing for adult use.

- adult use sales **$7.0 billion**
- medical cannabis patients **2.4 million**
- medical sales **$5.9 billion**
- projected hemp (CBD) market **$1.4 billion**

Why Would a Cannabis Business Want to Franchise?

The No. 1 reason to consider the franchise model is to maximize return on a good idea. In an industry that is brand loyal, name recognition and goodwill have lasting and portable value. Consumers and B2B purchasers grow comfortable with the brands they know and trust.

By franchising, your cannabis business can:

- **EXPAND** its footprint more rapidly
- **HARNESS** other people's capital
- **LEVERAGE** your market knowledge
- **ECONOMIZE** on advertising

Franchisors also enjoy limited liability and benefit from local owners who know the region.

Franchising, Like Cannabis, Is a Regulated Industry

Cannabis businesses are accustomed to operating in a sector that is highly regulated. But opting to pursue the franchise model will add new hurdles to clear.

The federal government and at least 15 states regulate the offer and sale of franchises.

These regulations may include:

- Applying consumer protection laws to the franchisor-franchisee relationship ("Little-FTC Acts")
- Requiring the registration of a franchise offering with state agencies
- Mandating the filing of franchise marketing/advertising materials
- Enacting franchisee relationship laws providing special protections for franchisees

Penalties for non-compliance are strict.

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Avoiding the 'Accidental Franchise' Trap

Businesses may avoid the term "franchising" by calling their structure something else – a license, direct selling, joint venture, sales agency, distribution or partnership. But this approach is risky because state and federal regulators look at structure and execution, not terminology.

Cannabis businesses that pursue brand expansion through other models, such as licensing, should be mindful of the accidental or inadvertent franchise trap. Some jurisdictions make it particularly difficult to avoid being deemed a "franchise."

"If it quacks like a duck … it's a duck."

At the end of the day, if a business meets the definition of a franchise, then it will be considered a franchise under state law and federal regulation. Simply put, the definition of a franchise hinges on three components. If all three exist, then the business structure is likely to be deemed a franchise.

FEE STRUCTURE	Requires payment of a minimal fee to the franchisor.
TRADEMARK	Licenses the franchisee to distribute goods or services under, or operate using, the franchisor's trademark or commercial symbol.
CONTROL	Provides a marketing plan or renders significant assistance to the franchisee in operating its business or the franchisee's method of operation.

Although there's no quick and easy fix, a business that wishes not to operate as a franchise may consider eliminating one or more of the key elements in the three-prong test outlined above. Guidance from an experienced franchise professional is essential.

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