

DEPARTMENT OF CORPORATIONS

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DEMETRIOS A. BOUTRIS

California Corporations Commissioner
Sacramento, California

IN REPLY REFER TO:

FILE NO: OP 6814 FILCOMMISSIONER'S OPINION 01/1FTHIS LETTER IS NOT AN INTERPRETIVE OPINION
FOR THE REASONS STATED BELOW

September 7, 2001

Mr. Timothy A. Kuncz
Law Offices
Gattis & Kuncz
2729 Fourth Avenue, Suite 3
San Diego, California 92103

Re: Aca Las Tortas

Dear Mr. Kuncz:

The request for an interpretive opinion contained in your letter dated November 21, 2000, as supplemented by your letter dated March 27, 2001, has been considered by the California Corporations Commissioner ("Commissioner"). Your letters raise the question of whether the proposed license agreement to be entered into between Aca Las Tortas International Corporation ("ALT") and Mr. Alex Cienfuegos is a franchise within the definition of Section 31005 of the Corporations Code and, therefore, subject to the provisions of the Franchise Investment Law ("FIL").

In order for an agreement to constitute a "franchise" within the definition of Corporations Code Section 31005(a), all of the following four elements must be met:

1. a right must be granted to the franchisee to engage in the business of offering, selling or distributing goods or services;

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2. the right must be granted to engage in the business under a marketing plan or system prescribed in substantial part by the franchisor;
3. the operation of the franchisee's business must be substantially associated with an advertising or other commercial symbol designating the franchisor or an affiliate of the franchisor, such as a trademark, service mark, trade name or logotype; and
4. the franchisee must be required to pay, directly or indirectly, a fee or charge (known as a "franchise fee") for the right to enter into the business.

You have acknowledged that the proposed agreement may be construed to satisfy the first, third and fourth elements of the definition. Therefore, the focus of your question is whether the second element (marketing plan or system prescribed in substantial part by franchisor) is met by the proposed license agreement. This question is answered in the affirmative. ..

You have represented that ALT, a California corporation, operates a restaurant in Chula Vista, California under the trade name and trademark "Aca Las Tortas" and in connection therewith uses related trade names and trademarks, including the menu items identified on the menu attached as an exhibit to the license agreement, all of which are collectively referred to as the "Mark." Mr. Cienfuegos desires to acquire a license to use the Mark in connection with the operation of a restaurant to be established and operated by him in San Diego County. In addition, Mr. Cienfuegos will be given the right to prepare tortas (Mexican style sandwiches) in accordance with ALT's proprietary recipes, to the extent such proprietary rights exist. You have further represented that ALT currently operates no other restaurants in the United States besides its Chula Vista location and that the principals of ALT, through Mexican affiliates, operate approximately eleven restaurants doing business under the Mark in various locations in Mexico.

As regards the requirement of a marketing plan or system prescribed in substantial part by the franchisor, you have represented that, under the proposed license agreement, Mr. Cienfuegos will be entirely free to operate his business according to his own marketing plan or system and his own policies and procedures; will not be required to purchase products or materials from ALT or from ALT's sources; and will not be supplied with sales aids or props. You further represented that the proposed license agreement imposes no policies regarding the price of goods sold, services rendered, hours of operation or other material incidents of business operation; does not limit or otherwise dictate the menu items which may be offered at the restaurant; imposes no restrictions concerning the appearance of the licensee's business premises, the fixtures and equipment utilized therein, uniforms of employees, housekeeping or decorations; and does not subject the licensee's business to any sort of inspection or examination by the licensor. Based thereon, it is your opinion that the second element of the definition is not met in this case.

In making the determination whether there is a prescribed marketing plan or system, it is necessary to keep in mind the objective of the FIL to deal with a multiplicity of business arrangements created by the franchisor and presented to the public as a unit or marketing concept, and for all of which the franchisor ostensibly assumes responsibility by causing these arrangements to be operated with the appearance of some centralized management and uniform standards regarding the quality and price of the goods sold, services rendered, and other material incidents of the operation. The marketing plan or system prescribed by the franchisor is one of the important means by which the appearance of centralized management and uniform standards is achieved. Furthermore, significance attaches to provisions imposing a duty of observing the licensor's directions or obtaining the licensor's approval with respect to the selection of locations, the use of trade names, advertising, signs, sales pitches, and sources of supply, or concerning the appearance of the licensee's business premises and the fixtures and equipment utilized therein, uniform of employees, hours of operation, housekeeping, and similar decorations. (See Commissioner's Release No. 3-F (Revised), dated June 22, 1994, pages 3 and 4.)

In our opinion, several requirements and restrictions set forth in the proposed license agreement and representations contained in your letters, when taken together, are sufficient to create an appearance of uniformity of operation and appearance and centralized management and control so as to amount to a marketing plan or system prescribed in substantial part by ALT. As examples, the proposed licensing agreement of ALT:

- (1) requires Mr. Cienfuegos' restaurant to be operated under the name and logo of the licensor, i.e., "Aca Las Tortas";
- (2) requires the use of "trade dress" by licensee, i.e., the distinctive color scheme (bright red and white) which is used by the licensor in the operation of its restaurant;
- (3) requires the use of certain specified menu, menu items, and prices;
- (4) prohibits licensee from changing the location of the restaurant without the licensor's prior consent;
- (5) prohibits licensee from using, directly or indirectly, the Mark at or in connection with any other location, or in connection with any other business without the prior written consent of the licensor;
- (6) grants exclusive or protected territory to licensee;
- (7) prohibits the Mark, which includes menu, logo, etc., from being changed or partially used without the licensor's prior consent;

- (8) prohibits the use of the Mark in conjunction with any other name or logo without the licensor's prior consent;
- (9) grants licensor the right to require prior approval on any and all use of the Mark by the licensee and any and all advertising, publicity and promotional material concerning any use of the Mark;
- (10) grants licensor the right to request, prior to production, sale or distribution of any products under the Mark or any advertising or promotional material for use in any media, the furnishing by licensee of a complete set of artwork, sketches, photographs, and prototype samples; and
- (11) requires food products to be of such style, appearance and quality as to be similar to those food products marketed by licensor.

We do not concur in your opinion that, in many respects, the proposed license agreement is similar to that which was the subject of Commissioner's Opinion No. 93/1F, which was determined not to provide for a "marketing plan or system." The facts are distinguishable. Unlike this case, Commissioner's Opinion No. 93/1F involved an arrangement where: (1) the licensee would not operate his restaurant under the same name and logo of the licensor, i.e., the licensee would merely be allowed to utilize the licensor's trade name and logo solely as a featured product which would be part of an inventory or menu item of other food products to be offered by licensee's restaurants, (2) there were no trade dress or color scheme requirements, and (3) there were no restrictions or limitations that required the prior approval of licensor such as with respect to change of location, use of trade name and logo, advertising, or promotion.

In our opinion, this case is more analogous to Commissioner's Opinion No. 72/45F, wherein it was determined that the subject license agreement constituted a franchise. There were several primary factors present in Commissioner's Opinion No. 72/45F, as in the present case, that were determinative in concluding the presence of a marketing plan or system prescribed in substantial part by the franchisor. These analogous factors included the following: (1) the licensee would be operating its business under the licensor's service mark name, (2) the prior written consent of licensor was required to provide any other service, (3) the prior written consent of licensor was required to carry out licensed services at any other location, and (4) the prior written approval of the licensor was required for the use of signs, advertising, and other material bearing the service mark.

Accordingly, it is our opinion that the proposed license agreement constitutes a franchise as that term is defined under Corporations Code Section 31005 and is therefore subject to the provisions of the FIL.

Inasmuch as interpretive opinions are issued for the principal purpose of providing a procedure by which members of the public can protect themselves against liability for acts

done or omitted in good faith in reliance upon the administrative determination made in the opinion, and since there can be no such reliance where the Commissioner asserts jurisdiction with respect to a particular situation or determines that a legal requirement is applicable, advice to that effect, as contained in this letter, does not constitute an interpretive opinion.

Dated: September 7, 2001
Sacramento, California

DEMETRIOS A. BOUTRIS
California Corporations Commissioner

By: _____
TIMOTHY L. Le BAS
Assistant Commissioner
Office of Law and Legislation
(916) 322-3553

TL:kc

OP 6814/FIL

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RICHARD E. GATTIS
TIMOTHY A. KUNCZ

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November 21, 2000

DEPT OF CORPORATIONS
OFFICE OF POLICY

William Kenefick, Acting Commissioner
c/o OFFICE OF POLICY
DEPARTMENT OF CORPORATIONS
980 9th Street, Suite 500
Sacramento, CA 95814-2725

Re: Aca Las Tortas;
Request For Interpretive Opinion Pursuant to
Corporations Code Section 31510

Dear Commissioner:

The purpose of this letter is to request an interpretive opinion pursuant to Corporations Code Section 31510 of the Franchise Investment Law (the "FIL") on behalf of our client Aca Las Tortas International Corporation, a California corporation ("ALT"), regarding a license agreement which ALT proposes to enter into with Alex Cienfuegos, an individual. A copy of the license agreement setting forth all of the terms and conditions of the proposed grant of license by ALT to Mr. Cienfuegos is enclosed herewith. Specifically, this letter requests an opinion as to whether the relationship contemplated by the license agreement between ALT and Mr. Cienfuegos constitutes a "franchise" within the definition of Section 31005 of the Corporations Code, and therefore subject to the provisions of the FIL.

As is reflected in the license agreement, ALT operates a restaurant in Chula Vista, California under the tradename and trademark "Aca Las Tortas" and in connection therewith uses related tradenames and trademarks, including the menu items identified on the menu attached as Exhibit "A" to the license agreement, all of which are collectively referred to as the "Mark". Mr. Cienfuegos desires to acquire a license to use the Mark in connection with the operation of a restaurant to be established and operated by him in San Diego County. In addition, Mr. Cienfuegos will be given the right to prepare tortas (Mexican style sandwiches) in accordance with ALT's proprietary recipes, to the extent such proprietary rights exist. ALT currently operates no other restaurants in the United States besides its Chula Vista location. The principals of ALT, through Mexican affiliates, however, operate approximately eleven restaurants doing business under the Mark in various locations in Mexico.

William Kenefick, Acting Commissioner
c/o OFFICE OF POLICY
DEPARTMENT OF CORPORATIONS
November 21, 2000
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The proposed license agreement authorizes Mr. Cienfuegos to utilize the Mark for a five-year term, with a five-year option to renew, in exchange for an initial royalty payment of \$10,000 and monthly royalty payments in the amount of \$350 through the term of the agreement. Under the proposed license agreement, Mr. Cienfuegos will be entirely free to operate his business according to his own marketing plan or system, and will not be required to purchase products or materials from ALT or from ALT's sources.

As noted in the Guidelines for Determining Whether an Agreement Constitutes a "Franchise" (Release 3-F, revised June 22, 1996) (the "Guidelines") the following four elements are deemed essential in order for an agreement to constitute a "franchise" within the definition of Section 31005(a) of the FIL:

1. A right must be granted to the franchisee to engage in the business of offering, selling or distributing goods or services;
2. The right must be granted to engage in the business under a marketing plan or system prescribed in substantial part by the franchisor;
3. The operation of the franchisee's business must be substantially associated with an advertising or other commercial symbol designating the franchisor or an affiliate of the franchisor, such as a trademark, service mark, tradename or logo type; and
4. The franchisee must be required to pay, directly or indirectly, a fee or charge, known as a "franchise fee" for the right to enter into the business.

It is understood that each of the four elements identified above must be present in order for a franchise to exist (See The Meaning of "Franchise" Under the California Franchise Investment Law: A Definition in Search of a Concept, 30 McGeorge L.Rev. 1163, 1185-1186, (Summer 1999)).

We acknowledge that the terms of the proposed license agreement may be construed to satisfy the first element (right to engage in business); the third element (substantial association with franchisor's commercial symbol); and the fourth element (payment of fees) of the franchise definition. It is our position however, that the second element (marketing plan or system) is not met by the proposed license agreement, and that hence, the contemplated relationship does not constitute a franchise.

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As reflected therein, the proposed license agreement prescribes no marketing plan or system and the licensee is left entirely free to operate the restaurant according to his own policies and procedures. More particularly, the license agreement imposes no policies regarding the price of goods sold, services rendered, hours of operation or other material incidents of business operation. The only substantive controls (beyond restrictions on the use of the Mark) deal with general quality standards as to any products sold under the Mark.

The license agreement makes no attempt to establish uniformity of prices or other marketing terms. Moreover, the license agreement does not limit or otherwise dictate the menu items which may offered at the restaurant to be established by the licensee. No restrictions are imposed by the license agreement concerning the appearance of the licensee's business premises, the fixtures and equipment utilized therein, uniforms of employees, hours of operation, housekeeping or decorations. Hence, it would appear that no "marketing plan or system" within the meaning of the FIL is prescribed in the proposed license agreement based on the Guidelines' analysis of this requisite element.

It would further appear that no marketing plan may be prescribed by implication in that ALT will not be supplying Mr. Cienfuegos with sales aids or props, on conducting any training materials or courses. (See, Comm. Op. No. 71/61F.)

In many material respects, the proposed license agreement is similar to that which was the subject of Commissioner's Opinion 93/1F, which was determined not to provide for "a marketing plan or system." For the reasons noted herein and in Commissioner's Opinion 93/1F, it is respectfully submitted that the proposed license agreement does not include a "marketing plan or system prescribed in substantial part" by ALT as required (a) (1) by Corporations Code Section 31005(a) (1) and thus should not constitute a franchise within the meaning of Section 31005.

Should you require any additional information in order to issue the interpretive opinion, please do not hesitate to contact me.

Very truly yours,

Timothy A. Kujacz

TAK:kes
Enclosure
cc: Mr. Alphonsa Rocha
Z\23RKL

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RICHARD E. GATTIS
TIMOTHY A. KUNCZ

March 27, 2001

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**DEPT OF CORPORATIONS
OFFICE OF POLICY**

Re: Aca Las Tortas
Request for Interpretive Opinion
Your File No. OP 6814FIL

Dear Mr. Partida:

Below please find the information requested in your letter of March 12, 2001 regarding our request for an interpretive opinion. Please note that the paragraph numbers correspond to those set forth in your March 12, 2001 letter.

1. The name of the restaurant to be established by Mr. Cienfuegos will be "Aca Las Tortas."
2. The licensee will not be required to sell only (or all of) the menu items listed on the menu attached as Exhibit "A" to the proposed license agreement. Neither will licensor impose any price restrictions on licensee's menu items. Licensee will be free to sell such other items and products he wishes without the prior consent or approval of licensor. Similarly, licensee will be free to change any of his menu items or prices without licensor's prior consent or approval.
3. It is anticipated that licensor will provide initial training to licensee and/or the licensee's employees with respect to the cooking and preparation of those menu products which have been developed by licensor. Such training, however, is not a requirement under the proposed license agreement and will be provided on a reasonable basis only to the extent licensee requests such assistance.
4. The licensee's business (including the premises, books and records, etc.) will not be subject to any sort of inspection or examination by the licensor.
5. The determination of the restaurant site will be left entirely to the discretion of the licensee.

Gerardo Partida
March 27, 2001
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6. The term "trade dress" is intended solely to refer to the distinctive color scheme (bright red and white) which is used by the licensor in the operation of its restaurant.

Please contact me if you require any additional information in order to issue the interpretive opinion.

Very truly yours, /

Timothy A. Kunz

TAK/as
cc: Alphonso Rocha