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## The Sunset of Quality Control in Modern Trademark Licensing

Irene Calboli  
irene.calboli@gmail.com

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# THE SUNSET OF “QUALITY CONTROL” IN MODERN TRADEMARK LICENSING\*

IRENE CALBOLI\*\*

## TABLE OF CONTENTS

Introduction.....	342
I. Trademark Licensing Defined.....	348
II. History of Trademark Licensing and “Quality Control” .....	351
A. The Debate on Licensing and Trademark Protection .....	351
B. The Rule of Licensing With “Quality Control” .....	354
1. The rationale behind “quality control” .....	357
2. Evolution of the standard.....	360
III. Problems in the Application of “Quality Control”.....	364
A. Judicial Inconsistency in Defining “Quality Control” .....	364
1. The dilemma of “adequate” control .....	368
2. Shifting focus on product quality? .....	371
B. Consequences of the Absence of a Clear Definition of “Quality Control” .....	374
IV. The Increasing Unsustainability of “Quality Control” .....	376
A. The Reality of Modern Trademark Licensing .....	377
1. Promotional licensing and (the lack of) “quality control” .....	380
2. Additional practices inconsistent with “quality control” .....	384

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B. Toward a De Facto Abandonment of “Quality Control”?	387
V. The Case for Abandoning “Quality Control”	389
A. The Intrinsic Flaws of “Quality Control”	390
B. The Need for a Better Rule on Modern Trademark Licensing	394
1. It is time to adopt licensing with or without “quality control”	396
2. Protecting consumers and the market under the new rule	400
Conclusion	406

### INTRODUCTION

Imagine that it is Monday morning and you are the managing editor of your school’s law review. As every morning, you are seated in the STARBUCKS coffee shop in front of your school reading the newspaper while sipping your coffee from a STARBUCKS mug. Once you are ready to leave, one of your classmates enters the shop wearing a HARLEY-DAVIDSON T-shirt and a YANKEES hat. You greet her and notice that she carries a backpack and a binder with the logo of your university. Now imagine that you are back in your law review office to work on the final draft of a new issue of the journal. Around noon, you open a bottle of WESTLAW water and call the campus’ PIZZA HUT store with the office’s GE phone to order a grilled vegetable pizza. In the afternoon, you leave the office and write a note to the assistant managing editor on the LEXIS-NEXIS board with instructions to ship the materials to the publisher. Finally, imagine that some of your friends join you for a relaxing evening watching a movie on your new SAMSUNG television. Since last Saturday was your birthday, your friends bring a cake with the logo of your favorite football team to celebrate and a new model of RALPH LAUREN sunglasses as a gift.

These scenarios illustrate some examples of "trademark licensing,"<sup>1</sup> one of the most popular modern business practices, where trademark<sup>2</sup> owners authorize third parties to produce and distribute products under their marks, usually in exchange for royalties. Originally, trademark licensing was used for products that were identical or directly related to those produced by trademark owners to increase market production and save costs, like SAMSUNG televisions or GE phones. In the past decades, however, this practice has also been used with respect to unrelated products to establish brand image in the market, like WESTLAW water or STARBUCKS mugs. Without exaggeration, licensing today interests most products, represents a significant source of revenue for many trademark owners,<sup>3</sup> and continues to grow in importance due to the changes in product manufacturing, the internationalization of trade, and the shift toward a service economy.

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1. The Oxford American Desk Dictionary defines the term "license" as a "permit or permission to own or use something, do something, or carry on a business." OXFORD AMERICAN DESK DICTIONARY 344 (1998). Black's Law Dictionary defines a "license" more narrowly as a "revocable permission to commit some act that would otherwise be unlawful." BLACK'S LAW DICTIONARY 743 (7th ed. 1999). In the trademark context, licensing affords trademark owners the flexibility to grant an exception to what would otherwise be infringing use by the licensee. See 2 JEROME GILSON, TRADEMARK PROTECTION AND PRACTICE § 6.01[2] (1998) ("A trademark license is a contractual arrangement whereby a trademark owner permits another to use his trademark under circumstances where, but for the license, the other would be a trademark infringer."); 3 J. THOMAS MCCARTHY, MCCARTHY ON TRADEMARKS AND UNFAIR COMPETITION § 18:1 (4th ed. 2007) ("[A] 'license' of a mark . . . is a limited permit to another to use the mark . . ."). This Article will use the terms "trademark licensing" and "licensing" interchangeably. So too, "trademark licenses," "licenses," and "licensing agreements" are used interchangeably.

2. A "trademark" is defined as "any word, name, symbol, or device . . . used . . . to identify . . . goods and distinguish them from those manufactured or sold by others" by section 45 of the Trademark (Lanham) Act of 1946, Pub. L. No. 79-489, 60 Stat. 427 (codified as amended at 15 U.S.C. §§ 1051-1141n (2000 & Supp. V 2005)). The Lanham Act defines a "service mark" similarly. See Lanham Act § 45, 15 U.S.C. § 1127. The words "trademark" and "mark" will be used interchangeably in this Article. This Article will also use the words "trademark" and "mark" to refer to any word and symbol protected under the Lanham Act.

3. See, e.g., RICHARD RAYSMAN ET AL., INTELLECTUAL PROPERTY LICENSING: FORMS AND ANALYSIS § 4.08[2] (1999) (explaining the advantages of trademark licensing for the licensor, including increased market presence and brand awareness); JOHN W. SCHLICHER, LICENSING INTELLECTUAL PROPERTY: LEGAL, BUSINESS, AND MARKET DYNAMICS 30-38 (1996) (detailing various legal and economic factors that affect the profitability of trademark licensing); David J. Franklyn, *The Apparent Manufacturer Doctrine, Trademark Licensors and the Third Restatement of Torts*, 49 CASE W. RES. L. REV. 671, 681 (1999) [hereinafter Franklyn, *The Apparent Manufacturer Doctrine*] (recognizing that the explosion of American industry in the early 1900s gave rise to the advantages of trademark licensing); W. J. Keating, *Promotional Trademark Licensing: A Concept Whose Time Has Come*, 89 DICK. L. REV. 363, 363 (1985) (noting that promotional trademark licensing has developed into a "substantial line of commerce").

Considering this preeminent role of licensing, few people would doubt the validity of this practice and the right of trademark owners to license their marks as they see fit. Yet the history of trademark licensing is a controversial one, at least in the United States.<sup>4</sup> Originally prohibited at common law and under the rule of the Trademark Act of 1905 as a violation of the primary function of a mark—to indicate the origin of the marked products<sup>5</sup>—licensing was recognized as a legal practice only with the adoption of the Trademark Act of 1946 (“Lanham Act”).<sup>6</sup> The Lanham Act specifically acknowledges that trademarks can be validly used by “related companies.”<sup>7</sup> Judicial decisions in previous years paved the way for this shift, accepting that trademarks could indicate commercial origin not only as actual product sources, but also in terms of consumers’ expectations by guaranteeing that all products bearing the same mark shared the same quality regardless of the manufacturer.<sup>8</sup> Yet, as a corollary to this principle, courts also required that licensors guarantee a consistent product quality by

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4. For a reconstruction of trademark history, see, for example, FRANK I. SCHECHTER, *THE HISTORICAL FOUNDATION OF THE LAW RELATING TO TRADEMARKS* (1925); see also Sidney A. Diamond, *The Historical Development of Trademarks*, 65 TRADEMARK REP. 265 (1975) (providing a historical overview of the marks used to identify goods from antiquity through the middle ages); Benjamin G. Paster, *Trademarks—Their Early History*, 59 TRADEMARK REP. 551, 552 (1969) (arguing that increasingly complex trade and commerce necessitated the use of trademarks to identify the producer of a product); Edward S. Rogers, *Some Historical Matter Concerning Trade-Marks*, 9 MICH. L. REV. 29, 29 (1910–1911); Gerald Ruston, *On the Origin of Trademarks*, 54 TRADEMARK REP. 127 (1955).

5. “Prior to passage of the Lanham Act many courts took the position that the licensing of a trademark separately from the business in connection with which it had been used worked an abandonment.” *Dawn Donut Co. v. Hart’s Food Stores, Inc.*, 267 F.2d 358, 367 (2d Cir. 1959); see *Hanover Star Milling Co. v. Metcalf*, 240 U.S. 403, 415 (1916), *superseded by statute*, Lanham Act § 22, Pub. L. No. 79–489, 60 Stat. 427, 435 (1946). For an overview of the emergence and acceptance of trademark licensing, see Alfred M. Marks, *Trademark Licensing—Towards a More Flexible Standard*, 78 TRADEMARK REP. 641, 645 (1988); Kevin Parks, “Naked” Is Not a Four-Letter Word: *Debunking the Myth of the “Quality Control Requirement” in Trademark Licensing*, 82 TRADEMARK REP. 531, 532 (1992).

6. 15 U.S.C. §§ 1051–1141n.

7. Lanham Act § 5, 15 U.S.C. § 1055. See 4A RUDOLF CALLMAN, *CALLMAN ON UNFAIR COMPETITION, TRADEMARKS AND MONOPOLIES* § 26:24 (Louis Altman ed., Thomson/West 4th ed. 2006); 3 MCCARTHY, *supra* note 1, §§ 18:49–50.

8. See 3 MCCARTHY, *supra* note 1, § 18:55 (explaining that there is no requirement that the products be of a specific quality, so long as the quality of the products is consistent). See generally Elmer William Hanak, III, *The Quality Assurance Function of Trademarks*, 43 FORDHAM L. REV. 363, 363–64 (1974) (suggesting that, consistent with the traditional function of a mark as indicative of quality, consumers rely on the mark as guaranteeing quality of the product across the board). In contrast, Kevin Parks points to the origin of the “guaranty” function of trademarks attributed to Frank Schechter and argues that this quality guarantee has been overly inflated in subsequent scholarly discussions. Parks, *supra* note 5, at 533.

setting quality control requirements for licensees.<sup>9</sup> Without such control, courts considered licenses "naked" and trademark rights forfeited based on the assumption that without this control, licensors could not guarantee consistent product quality, and this would result in consumer deception.<sup>10</sup> While establishing this principle, however, courts never elaborated on how much control was necessary for licensors to satisfy the requirement and adopted a case-by-case approach on the issue.

Following this judicial doctrine, quality control was introduced into the Lanham Act as part of the definition of "related companies" and has since represented the condition for valid licensing in the United States.<sup>11</sup> Unfortunately, like the judiciary before its adoption, the statute neither provided a definition of "quality" and "control" nor indicated how much control must be used for licensing to be valid. As a result, courts continued to interpret the requirement case by case.<sup>12</sup> Not surprisingly, such an approach has often led to contradictory decisions and uncertainty as to what constitutes a valid license.<sup>13</sup>

Generally, however, the decades that followed the enactment of the Lanham Act were characterized by a growing judicial preference

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9. 1 MCCARTHY, *supra* note 1, § 3:11 ("[I]t is clear that trademark law permits the licensing of a mark under any circumstances where the licensor exercises quality control over goods and services . . .").

10. *See Dawn Donut*, 267 F.2d at 366 ("[T]he Lanham Act places an affirmative duty upon a licensor of a registered trademark to take reasonable measures to detect and prevent misleading uses of his mark by his licensees or suffer cancellation of his federal registration."); *see also* 3 MCCARTHY, *supra* note 1, § 18:42 (suggesting that the trademark owner does not merely have the right to control quality, but rather an obligation to do so).

11. Lanham Act § 45, 15 U.S.C. § 1127.

12. *See Creative Gifts, Inc. v. UFO*, 235 F.3d 540, 548 (10th Cir. 2000); *Exxon Corp. v. Oxxford Clothes*, 109 F.3d 1070, 1075–80 (5th Cir. 1997); *Stanfield v. Osborne Indus.*, 52 F.3d 867, 871–72 (10th Cir. 1995); *Ky. Fried Chicken Corp. v. Diversified Packaging Corp.*, 549 F.2d 368, 387 (5th Cir. 1977); *Dawn Donut*, 267 F.2d at 367; *Halo Mgmt., L.L.C. v. Interland, Inc.*, 308 F. Supp. 2d 1019, 1028–31 (N.D. Cal. 2003); *Westco Group, Inc. v. K.B. & Assocs.*, 128 F. Supp. 2d 1082, 1087–91 (N.D. Ohio 2001); *Stanfield v. Osborne Indus.*, 949 P.2d 602 (Kan. 1997).

13. In addition to adopting inconsistent decisions with respect to licensing, courts have traditionally adopted inconsistent decisions also with respect to trademark assignments. In a previous article, *Trademark Assignment "With Goodwill": A Concept Whose Time Has Gone*, 57 FLA. L. REV. 771 (2005) [hereinafter Calboli, *Assignment "With Goodwill"*], I advocated for the change of the current rule of assignment "with goodwill" and proposed a new standard of assignment "with or without goodwill" because of, *inter alia*, such inconsistency. *See id.* at 788. Due to the similarity of some of the problems surrounding the two rules, some of the criticisms upon which I base my arguments in this paper are similar to those previously expressed in the context of trademark assignment. All arguments expressed in this paper, however, are originally targeted to demonstrate the increasing unsustainability of the current standard for the validity of licensing and to support my proposal for a new standard allowing licensing "with or without control."

toward licensing, and courts rarely declared licenses invalid and trademark rights forfeited. In particular, courts progressively relaxed the interpretation of the control that licensors must exercise over their licensees and held that first “adequate,” then “sufficient,” and then “minimal” control was sufficient to fulfill the statutory requirement. In some instances, courts also declared that evidence of control was unnecessary as long as product quality remained consistent and the public was not deceived. In addition to avoiding the problem of assessing whether the existing control was “sufficient”—a task difficult per se due to the ambiguity of this concept—this approach better adapted to the business world, where licensing with no or minimal control had long been a common practice.<sup>14</sup> As elaborated in this Article, this favorable attitude toward licensing has continued until the present and in recent years the courts have rarely interpreted quality control narrowly.

As expected, trademark owners and attorneys have welcomed this trend as additional evidence supporting their claim against quality control.<sup>15</sup> Throughout the years, they often advocated for the elimination of quality control, arguing that the requirement does not protect consumers and is generally used by competitors as a defense against (often valid) claims of infringement.<sup>16</sup> Trademark scholars,<sup>17</sup> however, have heavily opposed this judicial shift as “evidence that the courts are leaning toward protecting trademarks in gross contrary to the general principles of trademark law.”<sup>18</sup> Still, whether welcoming or opposing this judicial trend, neither party has provided a sufficient explanation for it—are the courts abandoning quality control or are they just interpreting the requirement “broadly”?<sup>19</sup> In addition, neither party has evaluated how the ambiguities that still characterize

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14. See Nathan Isaacs, *Traffic in Trade-Symbols*, 44 HARV. L. REV. 1210, 1210 (1931) (noting that this has happened because of the “ignorance” of the law or by “making the most of the exceptions” recognized by it).

15. See Calboli, *Assignment “With Goodwill,”* *supra* note 13, at 774–75; Parks, *supra* note 5, at 531 (discussing whether there is a need for control in trademark licensing); see also Elizabeth Cutter Bannon, *Revisiting “The Rational Basis of Trademark Protection”: Control of Quality and Dilution—Estranged Bedfellows?*, 24 J. MARSHALL L. REV. 65, 82–84 (1990) [hereinafter Bannon, *Revisiting “The Rational Basis of Trademark Protection”*]; Neil J. Wilkof, *Same Old Tricks or Something New? A View of Trade Mark Licensing and Quality Control*, 18 EUR. INTEL. PROP. REV. 261 (1996), reviewed in 87 TRADEMARK REP. 334 (1997); Michelle S. Friedman, Note, *Naked Trademark Licenses in Business Format Franchising: The Quality Control Requirement and the Role of Local Culture*, 10 J. TECH. L. & POL’Y 353, 363 (2005).

16. See 3 MCCARTHY, *supra* note 1, § 18:38.

17. See, e.g., Mark A. Lemley, *The Modern Lanham Act and the Death of Common Sense*, 108 YALE L.J. 1687, 1688 (1999).

18. Calboli, *Assignment “With Goodwill,”* *supra* note 13, at 775.

19. See *id.* at 774–75.

the definitions of "quality" and "control" are ultimately affecting the application of the requirement in practice. These ambiguities continue to represent the most important obstacle to a consistent enforcement of quality control.<sup>20</sup>

This Article addresses this void in the trademark debate and provides a much needed analysis of licensing, the requirement of "quality control" and the changes that have affected its application since its implementation into trademark law.<sup>21</sup> Part I defines licensing and the various types of licensing agreements that are currently used in the market. Part II reconstructs the history of the acceptance of this practice and the adoption of quality control as the requirement for its validity. Part III considers the difficulties encountered by the judiciary in assessing and defining "control" and "quality," and stresses the consequences of the lack of clear definitions. Part IV highlights the increasing unsustainability of quality control in today's economy and offers evidence that modern trademark practices are already shifting toward licensing de facto without control.

Part V advocates for a more flexible approach to assessing the validity of licensing, which will eliminate the inconsistencies resulting from the erratic application of quality control. Part V argues that the current requirement is failing to serve its purpose and suggests a clear change toward licensing "with or without control," where courts should focus directly on the actual product quality. In particular, the Article suggests that trademark licenses should be declared valid as long as quality remains the same and the public is not deceived. In addition, considering industrial reality, the Article proposes that trademark licenses should be considered valid when product quality is changed due to variations in product standards, marketing

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20. See Parks, *supra* note 5, at 536–39.

21. This Article focuses its analysis of licensing on trademark law and, specifically, the federal trademark statute and relevant judicial decisions. This Article does not elaborate, however, on other aspects of licensing and, in particular, antitrust issues and questions related to vertical restraints with respect to the concept of licensors' control over their licensees. Generally, when a licensor exerts too much control over its licensees, it can have anti-competitive effects that result in antitrust violation. See Stephen P. Ladas, *Trademark Licensing and the Antitrust Law*, 63 TRADEMARK REP. 245, 257–59 (1973). "The question . . . is whether . . . restrictions are justified . . . or whether they are . . . entered into with intent or effect of unduly restricting or preventing competition." *Id.* at 254. For an overview of antitrust aspects of licensing, see Siegel v. Chicken Delight, Inc., 448 F.2d 43 (9th Cir. 1971); Tominaga v. Shepherd, 682 F. Supp. 1489 (C.D. Cal. 1988); Ladas, *supra*; see also Robert E. LeBlanc, *Antitrust Ramifications of Trademark Licensing and Franchising*, 53 TRADEMARK REP. 519 (1963); Comment, *Quality Control and the Antitrust Laws in Trademark Licensing*, 72 YALE L.J. 1171 (1973).



strategies, or other reasons, as long as consumers are made aware and are not deceived because of these changes.

### I. TRADEMARK LICENSING DEFINED

As it is commonly known, the core of trademark rights resides in the ability of trademark owners to exclude unauthorized parties from using similar marks on identical or confusingly similar products.<sup>22</sup> A corollary of this “right to exclude” is the ability of trademark owners to authorize third parties to use their marks on a variety of products under specific conditions.<sup>23</sup> Usually, this authorization is granted by contracts, which are defined as “trademark licensing agreements” or “trademark licenses.”<sup>24</sup> Generally, these contracts can include a variety of clauses or conditions such as exclusiveness, territorial scope, advertising, product quality, and the percentage and frequency of royalties owed to licensors.<sup>25</sup>

As indicated earlier, trademark owners originally used licensing agreements to outsource to third parties—licensees—the production, in whole or in part, of the goods they used to produce under their marks.<sup>26</sup> This practice, called “classical” or “traditional” licensing, continues to be largely used today.<sup>27</sup> This type of licensing happens when companies like General Electric or Samsung, traditionally manufacturers of home appliances, license their marks to one or more producers of the same products who then manufacture and

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22. Since trademark law theoretically does not protect trademarks in gross, the general premise for the protection of trademark rights is that trademarks either are in use or are intended to be in use. See Lanham Act § 1, 15 U.S.C. § 1051 (2000 & Supp. V 2005); see also discussion *infra* Part II.A.

23. See Lanham Act §§ 5, 45, 15 U.S.C. §§ 1055, 1127.

24. For the definitions of “trademark licensing agreement” and “trademark license,” see *supra* note 1.

25. See, e.g., ADAM L. BROOKMAN, TRADEMARK LAW: PROTECTION, ENFORCEMENT, AND LICENSING § 12.02[A] (1999 & Supp. 2006) (providing examples of concepts that are important in the creation of good licenses); NEIL J. WILKOF & DANIEL BURKITT, TRADE MARK LICENSING 221–42 (2005).

26. See, e.g., David J. Franklyn, *Toward a Coherent Theory of Strict Tort Liability for Trademark Licensors*, 72 S. CAL. L. REV. 1, 12 (1998) [hereinafter Franklyn, *Liability for Trademark Licensors*]; Ira Levy et al., *Advanced Trademark Licensing*, 858 PLI/PAT 609, 613–22 (2006); Allison Sell McDade, *Trading in Trademarks—Why the Anti-Assignment In Gross Doctrine Should Be Abolished When Trademarks Are Used as Collateral*, 77 TEX. L. REV. 465, 485–86 (1998); see also *E.I. du Pont de Nemours & Co. v. Celanese Corp. of Am.*, 167 F.2d 484, 487–90 (C.C.P.A. 1948) (setting the early standard for a traditional trademark licensing agreement); *Arthur Murray, Inc. v. Horst*, 110 F. Supp. 678, 679–80 (D. Mass. 1953) (discussing the requirements of a traditional licensing agreement).

27. See GREGORY J. BATTERSBY & CHARLES W. GRIMES, LICENSING DESK BOOK 3 (1999) (providing a general overview of the licensing industry); see also GREGORY J. BATTERSBY & CHARLES W. GRIMES, LICENSING DESK BOOK: 2003 CUMULATIVE SUPPLEMENT 3 (2003) [hereinafter BATTERSBY & GRIMES, 2003 SUPPLEMENT].

distribute home appliances under the GE or SAMSUNG marks. Historically, this type of licensing has been justified on the basis that licensees could manufacture the products more cheaply or effectively due to their specialization, infrastructure, and economies of scale.<sup>28</sup> Today, this practice is also largely used internationally since many companies outsource much of their manufacturing to foreign countries.<sup>29</sup>

Shortly after the enactment of the Lanham Act, a second type of licensing developed and became known as "collateral" licensing.<sup>30</sup> Unlike traditional licensing, this practice usually interests different goods and services even if the products continue to be related, in type, kind, or market sector, to those "in connection with which the public recognition and demand were first created."<sup>31</sup> Collateral licensing happens when companies like General Electric or Samsung, which manufacture—directly or under traditional licensing—home appliances but not home phones, license their marks to one or more phone companies to produce and sell phones under the GE or SAMSUNG marks. Here again, the rationale for collateral licensing has generally been saving on manufacturing costs due to economies of scale. In addition, this practice aims at creating and satisfying consumer demand in areas that are collaterally related to those of the products traditionally manufactured by trademark owners.<sup>32</sup>

Finally, the past decades have witnessed an increasing use of a third type of licensing, commonly known as "promotional trademark licensing" or "trademark merchandising."<sup>33</sup> A subset of collateral licensing, trademark merchandising is generally used for products

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28. See generally Ladas, *supra* note 21, at 252–53 (discussing the economic foundations of trademark licensing).

29. See Jill Sarnoff Riola, *Practical Strategies for Global Licensing*, 7 J. PROPRIETARY RTS. 11, 12–15 (1995) (examining the legal and business issues that commonly affect international licensing); Eva Csiszar Goldman, Comment, *International Trademark Licensing Agreements: A Key to Future Technological Development*, 16 CAL. W. INT'L L.J. 178, 178–80 (1986) (discussing the impact of international licensing on developing nations).

30. Franklyn, *Liability for Trademark Licensors*, *supra* note 26, at 13.

31. See Marks, *supra* note 5, at 646.

32. See Ladas, *supra* note 21, at 252–53.

33. "Promotional trademark licensing" is defined as "commercial activity" whereby "the consumer is more interested in identification with the trademark owner than in the quality of the goods bearing the trademark." Keating, *supra* note 3, at 363. "Trade-mark merchandising means merchandise that is extensively advertised, and being extensively advertised, must live up to high quality." *Ely Lilly & Co. v. Saunders*, 4 S.E.2d 528, 533 (N.C. 1939), *overruled by Bulova Watch Co. v. Brand Distribs. of N. Wilkesboro, Inc.*, 206 S.E.2d 141 (N.C. 1974). This Article will use the terms "promotional trademark licensing," "promotional licensing," and "trademark merchandising," interchangeably.

that are unrelated to those originally bearing the licensed mark.<sup>34</sup> Examples of trademark merchandising are, *inter alia*, YANKEES hats, WESTLAW water, and binders and backpacks with university logos.<sup>35</sup> Once again, the economic justification of this type of licensing is that third parties can produce the items to which the mark is affixed more cheaply and efficiently than trademark holders. Yet, rather than indicating products' commercial origins, the primary function of merchandising is to increase the attractive function of the marks themselves by providing consumers with a variety of items that, while satisfying common needs, function as brand builders and allow the public to identify with them.<sup>36</sup> As this Article elaborates in Part IV, this type of licensing has become increasingly predominant in most sectors of the market today as an important source of revenues for businesses.<sup>37</sup> Hence, the rise of trademark merchandising has deeply

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34. See, e.g., *Boston Athletic Ass'n v. Sullivan*, 867 F.2d 22, 32–35 (1st Cir. 1989); *Boston Prof'l Hockey Ass'n v. Dallas Cap & Emblem Mfg.*, 510 F.2d 1004, 1011–12 (5th Cir. 1975), *cert. denied*, 423 U.S. 868 (1975); *Nat'l Football League Props., Inc. v. Consumer Enters., Inc.*, 327 N.E.2d 242, 247 (Ill. App. 1975); see also Keating, *supra* note 3, at 363; Marks, *supra* note 5, at 645–48. But see Stacey L. Dogan & Mark A. Lemley, *The Merchandising Right: Fragile Theory or Fait Accompli?*, 54 EMORY L.J. 461, 478–95 (2005) (opposing both the theoretical and practical underpinnings of trademark merchandising); Peter Jaffey, *Merchandising and the Law of Trade Marks*, 3 INTELL. PROP. Q. 240, 240–42 (1998) (criticizing the argument that merchandising is deceptive without established merchandising rights through the trade mark system); Veronica J. Cherniak, Comment, *Ornamental Use of Trademarks: The Judicial Development and Economic Implications of an Exclusive Merchandising Right*, 69 TUL. L. REV. 1311, 1315–16 (1995) (opposing a “merchandising monopoly” for trademark owners).

35. See Franklyn, *Liability for Trademark Licensors*, *supra* note 26, at 14 n.53 (noting that “[p]romotional trademark licensing mushroomed in the 1970s, led by ‘such famous merchandising forerunners as BUSTER BROWN, RAGGEDY ANN, SHIRLEY TEMPLE, BATMAN and ROBIN and MICKEY MOUSE’” (quoting Marks, *supra* note 5, at 646)).

36. See generally Dogan & Lemley, *supra* note 34, at 504 (stressing the problems that are created in a competitive market when the mark itself is considered to be the product); Alex Kozinski, *Trademarks Unplugged*, 68 N.Y.U. L. REV. 960, 961 (1993) (highlighting the “growing tendency to use trademarks not just to identify products but also to enhance or adorn them, even to create new commodities altogether”).

37. See generally Robert C. Denicola, *Institutional Publicity Rights: An Analysis of Merchandising of Famous Trade Symbols*, 62 N.C. L. REV. 603, 604 (1984) (stressing how consumers are willing to pay a higher price for products carrying their favorite logos). As evidence of the growing importance of brands as sources of revenues, *Business Week* has conducted a yearly ranking of the 100 top brands. In 2006, Coca Cola, Microsoft, and IBM placed, respectively, first, second, and third in the ranking. See David Kiley, *Best Global Brands*, BUS. WK., Aug. 7, 2006, at 54, available at <http://bwnt.businessweek.com/brand/2006/index.asp>. Companies are also increasingly aware of the possibility of collecting revenues from strategic marketing and increased brand value. See Intangible Business Brand Valuation: Licensing, <http://www.intangiblebusiness.com/Brand-Services/Marketing-Services/Licensing-78.html> (last visited Sept. 30, 2007) (“Brand licensing generates new revenue streams and other commercial benefits for brands, with little direct cost. It is important, however, to manage the system so licensing strengthens brand value.”).

affected the traditional interpretation of licensing and fundamentally challenged the applicability of quality control.<sup>38</sup>

## II. HISTORY OF TRADEMARK LICENSING AND "QUALITY CONTROL"

A practice scarcely used at the beginning of the twentieth century, trademark licensing is used today in most sectors of the economy and affects all types of products, as the examples above illustrate. Despite its popularity, however, the validity of this practice is still the subject of heated debates among scholars, judges, and practitioners almost eighty years after its acceptance into trademark law.

Part II provides a detailed analysis of these debates while reconstructing the history of the acceptance of licensing and the conditions for its validity. Traditionally, the validity of this practice has been construed upon the requirement that licensors control the quality of the marked products to prevent variation in quality to the detriment of consumers. Yet, until present, neither the courts nor the statute have provided a definition of "quality control" or any guidance as to how to interpret the requirement. As a result, the application of quality control has often proven controversial in practice and courts have applied the requirement inconsistently.

### A. *The Debate on Licensing and Trademark Protection*

The acceptance of licensing and the conditions for its validity have been at the center of the debate on trademark functions and trademark protection since the first usage of this practice in the early twentieth century. Generally, trademark owners advocated for no or minimal restrictions on their ability to license their marks, arguing that licensing could save costs, increase production, and provide additional revenues for their businesses.<sup>39</sup> Despite these arguments, however, trademark law has historically construed the validity of licensing based on the traditional rationale for trademark protection, i.e., by focusing primarily on protecting consumers and market competition.<sup>40</sup> In particular, courts and scholars have usually

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38. See discussion *infra* Part IV.A.1.

39. Parks, *supra* note 5, at 558.

40. Trademarks have been protected over time because they inform individuals about the products to which the marks are affixed, guarantee a predictable quality, and reduce consumer costs of collecting information at the time of purchase. See William M. Landes & Richard A. Posner, *Trademark Law: An Economic Perspective*, 30 J.L. & ECON. 265, 265–66 (1987) ("[T]rademark law . . . can be best explained on the hypothesis that the law is trying to promote economic efficiency."); see also Nicholas Economides, *The Economic Aspects of Trademarks*, 78 TRADEMARK REP. 523, 525–27 (1988); William P. Kratzke, *Normative Economic Analysis of Trademark Law*, 21 MEM. ST. U. L. REV. 199, 202–09 (1991).

advocated against trademark owners' ability to license their marks as "things,"<sup>41</sup> arguing that trademarks cannot be protected per se, but only as conveyors of information about the products they identify and as symbols of business goodwill.<sup>42</sup>

Traditionally, these limits have been justified by considering the social cost of trademarks, particularly the right of trademark owners to exclude third parties from using identical or similar marks to identify identical or similar products for a virtually unlimited period of time.<sup>43</sup> Notably, considering that marks are often common words and symbols, protecting trademarks per se could amount to creating a monopoly on language, a scarce and precious resource in the business world.<sup>44</sup> To prevent such unjustified monopoly, trademark law has historically protected marks only within the limits of protecting consumers against false information and protecting the market against unfair competition.<sup>45</sup>

As a direct result of this approach, trademark law has commonly required that trademark owners control their licensees and the quality of their products as *sine qua non* for the validity of licensing. Without such control, it has been argued, product quality could be affected and consumers could be confused. In addition, allowing licenses without control would facilitate trademark owners' trading in their marks as "things," thus limiting the availability of words and symbols available as marks for competitors to identify similar products.<sup>46</sup>

Despite this traditional position, however, the argument that trademarks can represent the most valuable assets of a business and, accordingly, deserve absolute protection has always been part of the

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41. See, e.g., Lemley, *supra* note 17, at 1687-88.

42. See discussion *infra* Part II.B.1.

43. Calboli, *Assignment "With Goodwill," supra* note 13, at 777. For further explanation of the basis, rationale, and limits for trademark protection, see generally 4 MCCARTHY, *supra* note 1, §§ 24-25.

44. See, e.g., GEORGE J. ALEXANDER, HONESTY AND COMPETITION 25-27 (1967); EDWARD CHAMBERLIN, THE THEORY OF MONOPOLIST COMPETITION 218 (3d ed. 1938); A.G. Papandrew, *The Economic Effect of Trademarks*, 44 CAL. L. REV. 503, 505 (1956).

45. S. REP. NO. 79-1333 (1946) introduces the Lanham Act as follows:

Trade-marks, indeed, are the essence of competition, because they make possible a choice between competing articles by enabling the buyer to distinguish one from the other. Trade-marks encourage the maintenance of quality by securing to the producer the benefit of the good reputation which excellence creates. To protect trade-marks, therefore, is to protect the public from deceit, to foster fair competition, and to secure to the business community the advantages of reputation and good will by preventing their diversion from those who have created them to those who have not.

*Id.* at 4.

46. See discussion *infra* Part II.B.1.

debate on the scope of trademark protection.<sup>47</sup> Originally, common law courts protected trademarks as property and based their jurisdiction on protecting trademark owners from the invasion of their property.<sup>48</sup> Even though this interpretation was abandoned by the courts in the first decades of the twentieth century<sup>49</sup> and the adoption of the Lanham Act in 1946 confirmed trademark protection within the limits of public welfare,<sup>50</sup> the temptation to protect trademarks as property is always present in trademark law, and is often evident in trademark practice.<sup>51</sup>

In recent decades, this property-based approach to trademark protection has been repeatedly revived both by courts and

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47. See Frank I. Schechter, *The Rational Basis of Trademark Protection*, 40 HARV. L. REV. 813, 818 (1927). By importing into the United States an idea originally developed in Germany in the late 1800s, Schechter developed the doctrine of "trademark dilution," which is based upon the premise that trademarks often constitute one of the primary assets of a business. According to Schechter, "[t]he true functions of the trademark are, then, to identify a product as satisfactory and thereby to stimulate further purchases by the consuming public." *Id.*

48. The courts based this protection on natural rights, arguing that trademark owners acquired the property of their marks through their possession and control. For a detailed reconstruction of judicial decisions and the doctrinal discussion on this point, see Edward S. Rogers, *Comments on the Modern Law of Unfair Trade*, 3 ILL. L. REV. 551, 552-54 (1909), which provides a detailed list and analysis of the relevant case law until the early 1900s. See also Daniel M. McClure, *Trademarks and Unfair Competition: A Critical History of Legal Thought*, 69 TRADEMARK REP. 305, 314-16 (1978) (summarizing the problems faced by the courts of equity in protecting trademarks and the recourse to the concept of property). The Supreme Court referred to the right to use a mark as "a property right" in *The Trade-Mark Cases*, 100 U.S. 82, 92 (1879).

49. See, e.g., *McGraw-Hill Pub. Co. v. Am. Aviation Assocs.*, 117 F.2d 293, 297 (D.C. Cir. 1940). In this pre-Lanham Act decision, the court outlines methods for assessing the scope of protection for a trademark that reflect concern for consumer interests:

[T]he law of trade marks is for the market place. Its purpose is to protect the several manufacturers in their respective spheres of public relations and to safeguard the consumer by helping him get what he thinks he wants. The method starts, therefore, with placing oneself in the position of a purchaser. . . . [Another method employed by the plaintiff includes considering] probable confusion by submitting evidence that purports to reveal disorder in the mind of the purchasing public.

*Id.* at 294-95.

50. See S. REP. NO. 79-1333, at 3-6 (1946):

The purpose underlying any trade-mark statute is twofold. One is to protect the public so it may be confident that, in purchasing a product bearing a particular trade-mark, which it favorably knows, it will get the product which it asks for and wants to get. Secondly, where the owner of a trade-mark has spent energy, time, and money in presenting to the public the product, he is protected in his investment from its misappropriation by pirates and cheats. . . . [S]ound public policy requires that trade-marks should receive nationally the greatest protection that can be given them.

*Id.* at 3, 6.

51. See Frank H. Easterbrook, *Intellectual Property is Still Property*, 13 HARV. J.L. & PUB. POL'Y 108, 118 (1990). According to Judge Easterbrook, "we should treat intellectual and physical property identically in the law." *Id.*

legislatures. Courts have often decided trademark cases using property theory,<sup>52</sup> stating that impairing a mark can support trademark protection without likelihood of confusion, particularly in the case of famous marks.<sup>53</sup> In addition, Congress has frequently amended federal trademark law, and all amendments have increased the protection of the value of trademarks per se.<sup>54</sup> As this Article will demonstrate, this trend has influenced the traditional interpretation of trademark licensing and, accordingly, has profoundly undermined the sustainability of the quality control requirement.<sup>55</sup>

### B. *The Rule of Licensing With "Quality Control"*

Sections 5 and 45 of the Lanham Act set forth the current conditions for the validity of trademark licensing. As indicated earlier, licensing was customarily prohibited at common law and under the Trademark Act of 1905 based on the assumption that if licensed, a mark could no longer serve its function as an indicator of origin, and consumers could be confused.<sup>56</sup> Most likely as a result of the changes in manufacturing and distribution that characterized the early twentieth century, the Lanham Act took a different position and legitimized this practice by acknowledging that a mark could be

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52. See, e.g., *K Mart Corp. v. Cartier, Inc.*, 485 U.S. 176, 185–86 (1988) (affirming that trademark protection “like contract law, confers private rights”); *San Francisco Arts & Athletics, Inc. v. U.S. Olympic Comm.*, 483 U.S. 522, 532 (1987) (banning the use of “Olympic” for “Gay Olympic Games” and arguing that an “entity constitutionally may obtain a limited property right in the word” because of its “organization and the expenditure of labor, skill, and money”); *Krebs Chrysler-Plymouth, Inc. v. Valley Motors, Inc.*, 141 F.3d 490, 498 (3d Cir. 1998) (recognizing that “[t]rademarks are property” and belong to an estate in the case of bankruptcy); *Dallas Cowboys Cheerleaders, Inc. v. Pussycat Cinema, Ltd.*, 604 F.2d 200, 206 (2d Cir. 1979) (denying First Amendment defense because of the “property right” nature of the mark at issue).

53. See generally Lemley, *supra* note 17, at 1697–1700 (arguing that the judiciary has increasingly expanded the rationale for trademark protection by considering trademarks “as things owned in their own right, rather than as advertising connected with a particular product”).

54. The most evident example of this trend has been the passing of the Federal Trademark Dilution Act of 1995. Pub. L. No. 104-98, §§ 3(a), 4, 109 Stat. 985, 985–86 (effective Jan. 26, 1996) (codified as amended at 15 U.S.C. §§ 1125, 1127 (2000)). This Act directly protects famous marks against tarnishment and blurring, regardless of any likelihood of confusion. This unnatural extension of trademark protection has been criticized by many scholars. See, e.g., Kenneth L. Port, *The “Unnatural” Expansion of Trademark Rights: Is a Federal Dilution Statute Necessary?*, 85 TRADEMARK REP. 525, 552 (1995). Recently, the Supreme Court also attempted to limit the extent of this Act and stated that, for dilution protection to apply, plaintiffs need to show actual, not just a likelihood of, dilution. See *Moseley v. V Secret Catalogue, Inc.*, 537 U.S. 418, 433 (2003). In response to this case, the Federal Trademark Dilution Act was amended in 2006 to reinstate the standard of likelihood of dilution. Pub. L. No. 109-312 §§ 2, 3(e), 120 Stat. 1730, 1733 (effective Oct. 6, 2006).

55. See discussion *infra* Part IV.

56. See discussion *infra* Part II.B.2.

validly used by "related companies."<sup>57</sup> Still, the statute carefully crafted the conditions for the validity of licensing according to the rationale of trademark law: protecting consumers and fair competition.

Specifically, section 5 of the Lanham Act states that

[w]here a registered mark or a mark sought to be registered is or may be used legitimately by related companies, such use shall inure to the benefit of the registrant or applicant for registration, and such use shall not affect the validity of such mark or of its registration, provided such mark is not used in such manner as to deceive the public.<sup>58</sup>

Section 45 clarifies the extent and limit of "such use" and defines a "related company" as "any person whose use of a mark is controlled by the owner of the mark with respect to the nature and quality of the goods or services on or in connection with which the mark is used."<sup>59</sup>

According to the statute, the control exercised by trademark owners over "the nature and quality" of the licensed products thus represents the *sine qua non* for the validity of trademark licensing. As elaborated below, this requirement was first established at common law when the courts consistently affirmed that licenses without control were invalid because they could lead to consumer deception.<sup>60</sup> Neither sections 5 nor 45, however, expand on the amount of control that is necessary for the validity of licensing or define the meaning of "quality" and "control." As criticized in Part

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57. Lanham Act § 5, 15 U.S.C. § 1055 (2000).

58. *Id.* See RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 33 cmt. b (1995) ("If the trademark owner exercises reasonable control over the nature and quality of the licensee's goods or services, the benefits of the licensee's use accrue to the trademark owner.").

59. 15 U.S.C. § 1127 (2000). Originally, a "related company" was defined as "any person who legitimately controls or is controlled by the registrant or applicant for registration in respect to the nature and quality of the goods or services in connection with which the mark is used." Lanham Act § 45, Pub. L. No. 79-489, 60 Stat. 427, 443 (1946). This definition was amended in 1988 with the adoption of the Trademark Law Revision Act. Pub. L. No. 100-667, 102 Stat. 3935, 3947 (1988). The reason for this change was outlined in the following senate report:

The definition of "related company" is amended to delete the word "legitimately" (the word's presence in Section 5 of the Act avoids any inference that use or control can be illegitimate), and to eliminate the confusion that exists about whether a related company can control the registrant or applicant as to the nature and quality of goods or services. S. REP. NO. 100-515, at 44 (1988), as reprinted in 1988 U.S.C.A.N. 5577, 5606-67.

60. See discussion *infra* Part II.B.2. See generally 3 MCCARTHY, *supra* note 1, § 18:40 (suggesting that the modern view of trademark law and the permissibility of licensing evolved from an emphasis on the source function of trademarks to a focus on consumer reliance on trademarks as guarantors of the continuity of product quality).



III, this lack of statutory guidance has given rise to much inconsistency when assessing the validity of licensing in practice.<sup>61</sup>

Following the approach previously adopted by the courts, the Lanham Act also provides that lack of quality control can lead to the forfeiture of trademark rights if consumers are misled. According to section 14,

[a] petition to cancel a registration of a mark . . . may . . . be filed . . . [a]t any time if the registered mark . . . is being used by, or with the permission of, the registrant so as to misrepresent the source of the goods or services on or in connection with which the mark is used.<sup>62</sup>

In addition to trademark cancellation, invalid licenses can also lead to abandonment of the licensed mark. As indicated by Section 45, “[w]hen any course of conduct of the owner, including acts of omission as well as commission, causes the mark . . . to lose its significance as a mark,”<sup>63</sup> the mark is abandoned regardless of whether the owner intended to abandon the mark.<sup>64</sup> Failure to control their licenses reasonably can also render trademark owners liable for false advertising under the Federal Trade Commission Act<sup>65</sup> when the licensees use the marks as instruments to defraud the public.<sup>66</sup>

Finally, the Lanham Act permits licensing of intent-to-use (“ITU”) trademark applications in addition to marks that are already in use. According to the second sentence of Section 5, which was introduced into the original text of the provision as a result of the Trademark Revision Act of 1988,<sup>67</sup> “[i]f first use of a mark . . . is controlled by the

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61. See discussion *infra* Part III.

62. Lanham Act § 14(3), 15 U.S.C. § 1064(3). See, e.g., *Barcamerica Int'l USA Trust v. Tyfield Imps., Inc.*, 289 F.3d 589, 597–98 (9th Cir. 2002); *Stanfield v. Osborne Indus.*, 52 F.3d 867, 871–72 (10th Cir. 1995).

63. Lanham Act § 45, 15 U.S.C. § 1127; see, e.g., *Oberlin v. Marlin Am. Corp.*, 596 F.2d 1322, 1327 (7th Cir. 1979) (outlining requirement of supervision of trademark licensees by licensor to avoid abandonment of trademark); *Haymaker Sports, Inc. v. Turian*, 581 F.2d 257, 261–62 (C.C.P.A. 1978) (licensing of trademark without control results in abandonment); *Westco Group, Inc. v. K.B. & Assocs.*, 128 F. Supp. 2d 1082, 1086–91 (N.D. Ohio 2001) (asserting abandonment as a defense to breach of license claim).

64. See, e.g., *Barcamerica Int'l*, 289 F.3d at 589 (holding that abandonment of trademarks occurring when an owner fails to exercise adequate quality control over a licensee is purely an involuntary forfeiture of trademark rights).

65. 15 U.S.C. §§ 41–77 (2000 & Supp. V 2005).

66. See discussion *infra* Part V.B.2; see also *Scotch Whiskey Ass'n v. Barton Distilling Co.*, 338 F. Supp. 595, 598 (N.D. Ill. 1971), *aff'd in part, rev'd in part*, 489 F.2d 809, 813 (7th Cir. 1973) (finding violation of Lanham Act § 43(a)); 3 MCCARTHY, *supra* note 1, § 18:48 (citing *Waltham Watch Co. v. FTC*, 318 F.2d 28, 29 (7th Cir. 1963), *cert. denied*, 375 U.S. 944 (1963) (finding Federal Trade Commission Act violation)).

67. See Pub. L. No. 100-667, 102 Stat. 3935, 3938 (1988).

registrant or applicant for registration of the mark with respect to the nature and quality of the goods or services, such first use shall inure to the benefit of the registrant or applicant, as the case may be."<sup>68</sup> Undoubtedly a sign of the increasing favor toward licensing, this provision seems to represent the statutory foundation for promotional licensing.<sup>69</sup> Once again, however, the language of the statute requires that trademark owners control the "nature and quality" of the marked products<sup>70</sup> even though the statute does not specify how much control is necessary for a license to be valid.

1. *The rationale behind "quality control"*

As indicated above, trademark licensing was not accepted as a legitimate practice in trademark law until the adoption of the Lanham Act, and even then, the practice has been strictly confined within the limits of trademark protection. As I have previously noted with respect to other aspects of trademark law, these limits rest on the principles that trademarks are protected only as conveyors of information about the products which they identify and as symbols of commercial goodwill.<sup>71</sup>

It was at common law that courts first formulated the principle that trademarks are protected primarily because of their function of informing the public. This principle replaced the previous majority view—that trademarks were protected as property—and has dominated trademark law ever since.<sup>72</sup> As a fundamental implication

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68. Lanham Act § 5, 15 U.S.C. § 1055 (2000).

69. Intent-to-use ("ITU") applications are most often used for the licensing of promotional products, such as HARLEY-DAVIDSON T-shirts, WESTLAW water, or YANKEES hats, which are usually not directly related to the goods and services manufactured or distributed by the trademark owners. For a discussion of promotional licensing and merchandising, see *infra* Part IV.A.1.

70. According to the Lanham Act, licenses can be declared invalid and ITU applications can be cancelled or declared abandoned as per Sections 14 and 45. See Lanham Act §§ 14, 45, 15 U.S.C. §§ 1064, 1127. *But see* Sands, Taylor & Wood Co. v. Quaker Oats Co., 978 F.2d 947, 958 (7th Cir. 1992) (attempting to license a mark is evidence of intent to use and safeguards against abandonment), *cert. denied*, 507 U.S. 1042 (1993).

71. See Calboli, *Assignment "With Goodwill," supra* note 13, at 781–84 (elaborating on these principles to discuss the rationale of the rule on trademark assignment); see also United Drug Co. v. Theodore Rectanus Co., 248 U.S. 90, 97 (1918). Here, the Supreme Court stated that a trademark's "function is simply to designate the goods as the product of a particular trader and to protect his good will against the sale of another's product as his; and it is not the subject of property except in connection with an existing business." *Id.* For a discussion of the limits of trademark protection, see generally 4 MCCARTHY, *supra* note 1, §§ 23:1–124.

72. See generally McClure, *supra* note 48, at 325–26. "The property justification of protection was replaced by arguments in favor of protecting business good will or values resulting from use. Protecting the public from confusion and deception

of this principle, courts required that trademarks guarantee the "continuity"—in terms of quality and characteristics<sup>73</sup>—of marked products. On the contrary, trademarks could provide inaccurate information to the public, thus losing significance as distinctive signs.<sup>74</sup> This judicial approach, however, was not absolute as courts often clarified that such "continuity" did not necessarily entail the sale of identical products.<sup>75</sup> Instead, courts generally reasoned that "substantial similarity" was sufficient to guarantee such "continuity"<sup>76</sup> and protect the public against deception.<sup>77</sup>

Yet, most likely to compensate for this shift away from protecting trademarks as property, courts also developed the principle that trademarks constituted symbols of commercial "goodwill" and that, while trademarks could not enjoy direct protection, their goodwill could be protected *per se*.<sup>78</sup> As noted earlier, this principle was based upon the consideration that protecting marks as property would create a monopoly on language and symbols to the benefit of trademark owners but to the detriment of the rest of society.<sup>79</sup> In

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became a more prominent rationale than protecting property." *Id.* at 329 (footnote omitted).

73. See, e.g., *Dawn Donut Co. v. Hart's Food Stores, Inc.*, 267 F.2d 358, 360 (2d Cir. 1959); *Land O'Lakes Creameries, Inc. v. Oconomowoc Canning Co.*, 221 F. Supp. 576, 581-82 (E.D. Wis. 1963), *aff'd*, 330 F.2d 667 (7th Cir. 1964).

74. See 1 MCCARTHY, *supra* note 1, § 3:2 ("Without the identification function performed by trademarks, buyers would have no way of returning to buy products that they have used and liked."); see also *Hanak*, *supra* note 8, at 364 ("[A] consumer wishes to match a trademark with what he likes and dislikes. If the origin of a product is of concern to a consumer, it is only because the manufacturer's products have come to be associated with a certain level of quality.").

75. This would prove unrealistic, particularly when changes in the features or characteristics of a product are required by law or for marketing reasons. See *Franklyn, Liability for Trademark Licensors*, *supra* note 26, at 15-16.

76. *Id.* *Franklyn* examines what he terms the "diverse quality" problem and the attendant challenges of enforcing requirements of quality control when "quality" remains variously defined from a standard of high, medium, or low quality or the mere requirement of consistent quality. *Id.*

77. *Calboli, Assignment "With Goodwill," supra* note 13, at 782-83.

78. Under the rule of the 1905 Act, Justice Holmes stated, "[a] trademark only gives the right to prohibit the use of it so far as to protect the owner's good will." *Prestonettes, Inc. v. Coty*, 264 U.S. 359, 368 (1924). See *E.I. du Pont de Nemours Powder Co. v. Masland*, 244 U.S. 100, 102 (1917); 1 MCCARTHY, *supra* note 1, § 2:15 ("Good will of a business and its symbol, a trademark, are inseparable. Early in the development of trademark law, the courts recognized that a trademark is 'property' only in the sense that it is a symbol of good will . . .").

79. See *Avery & Sons v. Meikle & Co.*, 4 KY. L. RPTR. 759, 767 (1883).

The alphabet, English vocabulary and Arabic numerals are to man in conveying his thoughts, feelings and the truth, what air, light and water are to him in the enjoyment of his physical being. Neither can be taken from him. They are the common property of mankind, in which all have an equal share and character of interest. From these fountains whosoever will may drink, but an exclusive right to do so can not be acquired by any.

*Id.*; see also *Calboli, Assignment "With Goodwill," supra* note 13, at 782-83.

contrast, protecting solely their goodwill would protect fair competition and prevent unscrupulous free riding, without impairing societal use of common words and phrases.

As a result of these principles, particularly the position that trademarks had to guarantee consistent product quality, the majority of courts took the position that trademarks could not be licensed freely but rather only under the control of their owners.<sup>80</sup> Such control, the courts argued, provided a greater guarantee to the public that product quality would be the same, or substantially the same. In contrast, lack of control on the part of trademark owners, i.e., naked licenses, could create a breach in product continuity that could lead, in turn, to consumer confusion or deception if the public continued to purchase the marked products while relying on previous quality.<sup>81</sup> Hence, to require that trademark owners control the "nature and quality" of the licensed products as the standard for the validity of licensing seemed to be the only effective way to avoid the risk of defrauding the public.<sup>82</sup>

Generally, from an economic standpoint, the quality control requirement has also been justified based on the assumption that changes in product quality resulting from uncontrolled licenses could create market failures.<sup>83</sup> Even if consumers may sometimes benefit from changes in quality, that is, when the quality of the products is higher than expected, it has traditionally been affirmed that these changes can result in increased consumer search costs, thus frustrating the most important function of the mark—to decrease consumer search costs by providing accurate information about the origin and quality of the marked products.<sup>84</sup> Additionally,

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80. *E.g.*, *E.I. du Pont de Nemours & Co. v. Celanese Corp. of Am.*, 167 F.2d 484, 489 (C.C.P.A. 1948). "[A] license agreement, not merely a naked license to use, where the licensor expressly reserves his right to continue the use of the mark and which license agreement provides that the agreement may be terminated by the licensor, is not an abandonment of its registered mark." *Id.* at 487.

81. *See* F. Vern Lahart, *Control—The Sine Qua Non of a Valid Trademark License*, 50 TRADEMARK REP. 103, 107–09 (1960). An assurance of continuity of product quality is necessary in licensing arrangements to preserve the trademark function of conveying information to consumers and preventing confusion. *See, e.g.*, *PepsiCo, Inc. v. Grapette Co.*, 416 F.2d 285, 288 (8th Cir. 1969) ("Inherent in the rules involving the assignment of a trademark is the recognition of protection against consumer deception.")

82. *See* *Dawn Donut Co. v. Hart's Food Stores, Inc.*, 267 F.2d 358, 367 (2d Cir. 1959) ("Clearly the only effective way to protect the public where a trademark is used by licensees is to place on the licensor the affirmative duty of policing in a reasonable manner the activities of his licensees.")

83. *E.g.*, James M. Treece, *Trademark Licensing and Vertical Restraints in Franchising Arrangements*, 116 U. PA. L. REV. 435, 453–54 (1968).

84. WILLIAM M. LANDES & RICHARD A. POSNER, *THE ECONOMIC STRUCTURE OF INTELLECTUAL PROPERTY LAW*, 166–68 (2003).

these changes can thwart consumer expectation about the marked products, regardless of their actual quality.<sup>85</sup>

Scholars have also pointed out that without the quality control requirement, unscrupulous licensors or licensees could change product quality and take advantage of unwary consumers.<sup>86</sup> Licensors could be tempted, for example, to maximize revenues by asking licensees to decrease product quality when facing difficulties in the market, bankruptcy, or awareness that their marks have no future.<sup>87</sup> Similarly, licensees could decide to change product quality when they face financial problems or because of other reasons. Although licensees should also be interested in keeping a consistent product quality, lest they risk losing customers, their lack of direct ownership of the mark could make them less interested in the long-term success of the products.<sup>88</sup> Accordingly, they could be more inclined to increase short-term profits by decreasing product quality, to the detriment of consumers, who could face unexpected drops in product quality and likely be deceived when relying on the licensed mark for their purchases.

## 2. *Evolution of the standard*

As mentioned above, trademarks were originally viewed as serving a single function: to identify the origin of the goods to which they were affixed in terms of physical "source."<sup>89</sup> Under this interpretation, any use of a mark on a product that did not come directly from its owner was seen as potentially confusing for consumers.<sup>90</sup> Accordingly, considering that licensing necessarily implied the outsourcing of product manufacturing to third parties, the majority of the courts

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85. *Id.* at 184–85.

86. *Dawn Donut*, 267 F.2d at 367. "The public is hardly in a position to uncover deceptive uses of a trademark before they occur and will be at best slow to detect them after they happen." *Id.*

87. See *Treese*, *supra* note 83, at 453–54 ("A licensee . . . is somewhat more likely than a mark owner to vary product quality, giving rise to a requirement that a mark owner who chooses to license the use of his mark must eliminate this additional increment of risk to the consumer by supervising his licensee.").

88. LANDES & POSNER, *supra* note 84, at 184–85.

89. See discussion *supra* Part II.A.

90. See *Am. Broad. Co. v. Wahl Co.*, 121 F.2d 412, 413 (2d Cir. 1941), *superseded by statute*, Lanham Act § 5, Pub. L. No. 79-489, 60 Stat. 427, 429 (1946), *as recognized in Dawn Donut*, 267 F.2d at 366–67; *Everett O. Fisk & Co. v. Fisk Teachers' Agency, Inc.*, 3 F.2d 7, 8–9 (8th Cir. 1924), *superseded by statute*, Lanham Act § 5; *Bulte v. Igleheart Bros.*, 137 F. 492, 501–02 (7th Cir. 1905); *Broeg v. Duchaine*, 67 N.E.2d 466, 468 (Mass. 1946); see also Ralph S. Brown, Jr., *Advertising and the Public Interest: Legal Protection of Trade Symbols*, 108 YALE L.J. 1619, 1638 ("If, by using A's mark, B confuses buyers who mean to buy from A and rely on the mark to denote A's goods, A is injured and can claim protection against the diversion of trade caused by B's appropriation.").

initially saw this practice as "philosophically impossible"<sup>91</sup> and thus prohibited it.<sup>92</sup>

This position officially continued until the adoption of the Lanham Act in 1946. Yet a few courts decided to accept a broader interpretation of the "source theory" and started to indirectly allow licensing prior to the enactment of the statute.<sup>93</sup> The Supreme Court itself paved the way for this gradual acceptance of licensing when, in 1879, in *Kidd v. Johnson*,<sup>94</sup> the Court ruled that the owner of a trademark, who entered into a partnership and used a trademark for the benefit of the partnership, did not need to transfer ownership of the mark to the partnership.<sup>95</sup> Although indirectly, the result of this transaction was essentially a license and the Court allowed it to stand.<sup>96</sup> A few decades later, in the 1916 decision *Hanover Star Milling Co. v. Metcalf*,<sup>97</sup> the Court went further and held that a trademark was not abandoned and could continue to serve its function as a mark although it had been licensed.<sup>98</sup> Building upon these decisions, several lower courts thus started to permit limited forms of licensing in different factual situations.<sup>99</sup>

By the end of the 1920s, this trend was irreversible. Licensing had become an important part of the economy due to growing demand in the market and surge in production, and courts were increasingly

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91. See 3 MCCARTHY, *supra* note 1, § 18:39; see also Comment, *supra* note 21, at 1174.

92. *E.g.*, *MacMahan Pharm. Co. v. Denver Chem. Mfg. Co.*, 113 F. 468, 471-72 (8th Cir. 1901). "A trademark cannot be . . . licensed, except as incidental to a transfer of the business or property in connection with which it has been used." *Id.* at 474-75.

93. See *Hicks v. Anchor Packing Co.*, 16 F.2d 723, 725 (3d Cir. 1926) (noting that in Section 7(c) of the 1918 Trading with the Enemy Act, Pub. L. No. 65-233, 40 Stat. 1020 (codified as amended at 50 U.S.C. app. § 7(c) (2000)), Congress authorized seizure of enemy trademarks and their license to U.S. companies; the grant of such a license did not create ownership of the mark in the licensee); *Keebler Weyl Baking Co. v. J. S. Ivins' Son, Inc.*, 7 F. Supp. 211, 214 (E.D. Pa. 1934) (describing a subsidiary licensing other subsidiaries of United Biscuit Co.); *Nelson v. J. H. Winchell & Co.*, 89 N.E. 180, 183-84 (Mass. 1909) (upholding the concept of a licensed right to use as distinct from the right to use flowing from ownership); 3 MCCARTHY, *supra* note 1, § 18:39 (citing *Martha Washington Creamery Buttered Flour Co. v. Martien*, 44 F. 473, 474-75 (E.D. Pa. 1890) (finding that when a trademark license is terminated, continued use by the former licensee is an infringement of the rights of the owner of the mark)).

94. 100 U.S. 617 (1879).

95. *Id.* at 619.

96. *Id.* at 620.

97. 240 U.S. 403 (1916), *superseded by statute*, Lanham Act § 22, Pub. L. No. 79-489, 60 Stat. 427, 435 (1946).

98. See *id.* at 418-19 (setting forth that "trademark rights, like others that rest in user, may be lost by abandonment").

99. 3 MCCARTHY, *supra* note 1, § 18:39.

inclined to uphold this practice.<sup>100</sup> As a result, courts and scholars started to search for a legitimate way to justify licensing under trademark law theory while still focusing on protecting consumers.<sup>101</sup> The solution to this quest was provided by a new interpretation of trademark protection that brought about the acceptance of a second trademark function in addition to that of indication of source: the so-called “quality assurance” theory.<sup>102</sup>

The seeds of this new trademark function had already been put into place by the Supreme Court in 1883 in *Manhattan Medical Co. v. Wood*,<sup>103</sup> when Justice Field wrote that a mark “is both a sign of the quality of the article and an assurance to the public that it is the genuine product of his [the owner’s] manufacture.”<sup>104</sup> Starting in the 1920s, courts and scholars elaborated on this principle and argued that in modern society trademarks not only signified commercial source but also represented symbols of product quality.<sup>105</sup> In other words, trademarks were symbols of “uniformity or quality in the products to which they [were] attached,”<sup>106</sup> on which consumers relied to guarantee that all products with the same mark shared the same quality. To reconcile this “quality assurance” function with the traditional “source theory,” courts and scholars expanded the interpretation of the latter and argued that, rather than necessarily indicating “actual” product source, trademarks represented product source “at large,” that is, the source “controlling” the products regardless of the actual manufacturer.<sup>107</sup>

Under this new theory, licensing could thus be accepted since the licensed marks continued to identify the “controlling source” of the products. As a necessary corollary of this theory, however, the judiciary started to require that trademark owners control their

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100. Parks, *supra* note 5, at 533.

101. *Id.*

102. See 1 MCCARTHY, *supra* note 1, § 3:10 (recognizing a new concept that “a trademark did not necessarily have to indicate only manufacturer or merchant source, but could also serve to indicate a level of consistent quality”); see also Isaacs, *supra* note 14, at 1215–16; Treece, *supra* note 83, at 445.

103. 108 U.S. 218 (1883).

104. *Id.* at 222–23.

105. Much of the credit for developing the trademark “quality assurance” theory goes to Frank Schechter, who identified the primary function of a mark as a “guaranty that the goods purchased under the trade-mark will have the same meritorious qualities as those previously noted.” SCHECHTER, *supra* note 4, at 150.

106. Hanak, *supra* note 8, at 363.

107. In the early 1930s, trademarks were seen as fulfilling two different but interrelated functions—indicating the source of the products in terms of “single controlling source” and guaranteeing to the public that all products bearing the same mark shared the same quality. 3 MCCARTHY, *supra* note 1, § 18:40.

licensees to guarantee consistent product quality.<sup>108</sup> If, by contrast, trademark owners failed to exercise such control, courts adopted the position that the license was invalid because the mark could not guarantee against changes in product quality,<sup>109</sup> and this, in turn, could lead to consumer confusion.<sup>110</sup> Yet, while they stressed the importance of control, courts never elaborated on how much control was adequate for licensing to be valid. Instead, arguing that it was not possible to define control in the abstract,<sup>111</sup> they left to individual judges the task of deciphering control case by case.<sup>112</sup>

The judiciary continued to follow the same line of reasoning after the adoption of the Lanham Act.<sup>113</sup> Once again, the courts stressed that "the only effective way to protect the public where a trademark is used by licensees is to place on the licensor the affirmative duty of policing in a reasonable manner the activities of his licensees."<sup>114</sup> Otherwise, the concern was that "the public [would] be deprived of its most effective protection against misleading uses of a

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108. See, e.g., Comment, *Trademark Licensing: The Problem of Adequate Control*, 17 DUKE L.J. 875, 882 (1968); see also *Mascaro v. Snelling & Snelling, Inc.*, 243 A.2d 1, 9 (Md. 1968), cert. denied, 393 U.S. 981 (1968). In a series of cases preceding the Lanham Act, courts set forth the principle that licensing of a trademark apart from the business to which it had been attached would result in an abandonment. See *Am. Broad. Co. v. Wahl Co.*, 121 F.2d 412, 413 (2d Cir. 1941) ("A trade-mark is intended to identify the goods of the owner and to safeguard his good will. The designation if employed by a person other than one whose business it serves to identify would be misleading."), superseded by statute, Lanham Act § 5, Pub. L. No. 79-489, 60 Stat. 427, 429 (1946), as recognized in *Dawn Donut Co. v. Hart's Food Stores, Inc.*, 267 F.2d 358, 366-67 (2d Cir. 1959).

109. E.g., *Atlas Beverage Co. v. Minneapolis Brewing Co.*, 113 F.2d 672, 677-78 (8th Cir. 1940); *Dietz v. Horton Mfg. Co.*, 170 F. 865, 870-71 (6th Cir. 1909).

110. See, e.g., *Bulte v. Igleheart Bros.*, 137 F. 492, 499 (7th Cir. 1905) ("[A] trademark or trade-name . . . gives assurance to a purchaser that the article upon which is stamped the trade-mark or trade-name is the genuine production of the manufacturer to whom the trade-name or trade-mark points by association as the maker of the article.").

111. Elizabeth C. Bannon, *The Growing Risk of Self-Dilution*, 82 TRADEMARK REP. 570, 575-79 (1992) [hereinafter Bannon, *The Growing Risk of Self-Dilution*].

112. E.g., *Barcamerica Int'l USA Trust v. Tyfield Imps., Inc.*, 289 F.3d 589, 596-97 (9th Cir. 2002).

113. Lanham Act §§ 5, 45, 15 U.S.C. §§ 1055, 1127 (2000); see, e.g., *Thomas Pride Mills, Inc. v. Monsanto Co.*, 155 U.S.P.Q. (BNA) 205, 208 (N.D. Ga. 1967) ("The primary functions of a trademark are to indicate a single source of origin of the articles to which it refers and to offer assurance to ultimate consumers that articles so labeled will conform to quality standards established and, when licensed to others, controlled by the trademark proprietor.").

114. *Dawn Donut*, 267 F.2d at 367; see *Ky. Fried Chicken Corp. v. Diversified Packaging Corp.*, 549 F.2d 368, 387 (5th Cir. 1977) ("If a trademark owner allows licensees to depart from its quality standards, the public will be misled, and the trademark will cease to have utility as an informational device."); see also *Haymaker Sports, Inc. v. Turian*, 581 F.2d 257, 261 (C.C.P.A. 1978) ("The purpose of such a requirement is to protect the public from being misled.").



trademark,"<sup>115</sup> and "the risk that [it] [would] be unwittingly deceived [would] be increased."<sup>116</sup> Even after the enactment of the Lanham Act, however, courts did not elaborate on how to interpret "control" or how much control had to be exercised by trademark owners. Instead, this task was left, again, with individual judges as a fact-intense issue. Not surprisingly, the result has been judicial inconsistency.

### III. PROBLEMS IN THE APPLICATION OF "QUALITY CONTROL"

Central to the interpretation of the quality control requirement are the definitions of "control" and "quality," and in particular what represents "adequate control" and "consistent quality." As highlighted above, traditionally it has proven difficult to provide clear definitions of these terms in the abstract. This in turn has brought the judiciary to define control and quality on a case-by-case basis. Not surprisingly, such an approach has led to uncertainty as to how to interpret the requirement and ultimately to judicial inconsistencies.

Part III explores these inconsistencies, focusing on the difficulty encountered by the courts in defining quality control. Because of this difficulty, courts have adopted an increasingly open-ended interpretation of "control" and often focused more on product quality—i.e., whether product quality remained the same—than on the control exercised by trademark owners. Still, this approach has profoundly eroded the practical impact of quality control while still leaving many doubts as to what constitutes valid licensing.

#### A. *Judicial Inconsistency in Defining "Quality Control"*

With the exception of minor linguistic clarifications, Sections 5 and 45 of the Lanham Act have remained formally unchanged since the enactment of the statute.<sup>117</sup> The interpretation of quality control, however, has changed considerably in the past century, primarily due to the growing role of licensing in the economy and the rise of different types of licensing, such as merchandising.<sup>118</sup> The changes in interpreting the requirement have directly followed the variations in the judicial interpretation of the concepts of "control of related companies" and "product quality." Still, these concepts are per se

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115. *Dawn Donut*, 267 F.2d. at 367.

116. *See id.* (explaining that "this is precisely what the Act is in part designed to prevent").

117. *See supra* note 59 and accompanying text (discussing the change in definition of the term "related company" in the Lanham Act).

118. *See* discussion *infra* Part IV.A.1.

ambiguous and, as indicated above, neither the courts nor the statute provide any guidance for their interpretation.<sup>119</sup> As a result, courts have historically defined them in a variety of ways, often reaching contradictory interpretations.<sup>120</sup>

In particular, prior to the enactment of the Lanham Act, courts affirmed that licensing was valid as long as "such agreements [were] not merely naked license agreements"<sup>121</sup> and the mark remained "associated with the same product or business with which it ha[d] become associated in the public mind."<sup>122</sup> Thus, the critical inquiry for the validity of licensing under this premise was whether licensors maintained control over product quality and, specifically, whether licensees' products "conform[ed] to any fixed standard."<sup>123</sup> Courts also held that once trademark owners had used and established a mark "as a guaranty of the quality of [their] merchandise," they could not validly license it "to those who may sell an inferior product."<sup>124</sup> Licensors were held responsible for strictly enforcing quality control, and courts consistently found licenses without control invalid and trademark rights forfeited.<sup>125</sup>

Courts continued to require trademark owners' control after the enactment of the Lanham Act. Almost invariably, judicial decisions in the 1940s and early 1950s included the customary language that licenses without control were void.<sup>126</sup> Yet, during the same years, several courts started to show an increasing willingness to uphold licensing by adopting a broader interpretation of quality control. Specifically, courts stated that "strict" control was not necessary and

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119. See discussion *supra* Part II.B.

120. See Comment, *supra* note 108, at 894 ("[A]n examination of case law since the Lanham Act reveals judicial approval of a wide spectrum of licensing agreements, ranging from those involving detailed control provisions to those in which licensee inspection is made at the licensee's option.")

121. See *E.I. du Pont de Nemours & Co. v. Celanese Corp. of Am.*, 167 F.2d 484, 489 (C.C.P.A. 1948) (citing *Menendez v. Holt*, 128 U.S. 514, 524 (1888)). See generally *Bacardi Corp. of Am. v. Domenech*, 311 U.S. 150 (1940); *Saalfeld Pub. Co. v. G. & C. Merriam Co.*, 238 F. 1 (6th Cir. 1917); *Mathy v. Republic Metalware Co.*, 35 App. D.C. 151 (D.C. Cir. 1910); *Shaver v. Heller & Merz Co.*, 108 F. 821 (8th Cir. 1901).

122. *E. F. Prichard Co. v. Consumers Brewing Co.*, 136 F.2d 512, 519 (6th Cir. 1943).

123. *Broeg v. Duchaine*, 67 N.E.2d 466, 468 (Mass. 1946) (stating that the license at issue was not valid because it was not subject to any requirement that the licensee's products conform to fixed standards).

124. *Id.*

125. *E.g., id.* at 468–69; *Detroit Creamery Co. v. Velvet Brand Ice Cream Co.*, 153 N.W. 664, 666 (Mich. 1915).

126. See *Huber Baking Co. v. Stroehmann Bros.*, 252 F.2d 945, 952–53 (2d Cir. 1958); *Arthur Murray, Inc. v. Horst*, 110 F. Supp. 678, 679 (D. Mass. 1953) ("[T]he trade-mark license is valid if 'control' by the licensor over the licensee exists.")

started to assess the validity of licensing based on “whether the plaintiff sufficiently policed and inspected its licensees’ operations.”<sup>127</sup> They thus required licensors to exercise only “adequate” control.<sup>128</sup> Still, because of the case-by-case approach adopted in evaluating agreements, the definition of what constituted “adequate” control varied considerably, making it particularly challenging to predict whether an agreement would be declared valid.<sup>129</sup>

In addition to this uncertainty as to the required amount of control, the decades following the adoption of the Lanham Act also revealed conflicting decisions regarding the formality of including quality control in licensing agreements. Under the traditional approach, quality control provisions had to be part of the language of the agreement for licensing to be valid. Yet, while many courts continued to require this language to uphold the licenses at issue,<sup>130</sup> others decided to use a more flexible approach in this respect. In particular, starting in the 1960s, a significant part of the judiciary adopted the position that “actual” rather than contractual control was sufficient to establish the validity of the licenses under their scrutiny.<sup>131</sup> Courts could not agree, however, on a definition of “actual” control and again defined it case by case, thus adding more uncertainty to this area of the law.<sup>132</sup>

Still, most likely because of the increasing role of licensing in the economy, the majority of the courts continued to show a friendly attitude toward this practice in subsequent decades and only rarely did the judiciary interpret quality control conservatively.<sup>133</sup> Most courts showed their “willingness . . . to leave no stone unturned in finding evidence of sufficient quality control”<sup>134</sup> and declared

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127. *Dawn Donut Co. v. Hart’s Food Stores, Inc.*, 267 F.2d 358, 367 (2d Cir. 1959).

128. *E.g., id.* at 369; *Joseph Bancroft & Sons Co. v. Shelley Knitting Mills, Inc.*, 212 F. Supp. 715, 740 (E.D. Pa. 1962); *Alligator Co. v. Robert Bruce, Inc.*, 176 F. Supp. 377, 378–79 (E.D. Pa. 1959).

129. *E.g., Parks, supra* note 5, at 557–61.

130. *See, e.g., Societe Comptoir De L’Industrie Cotonniere Etablissements Bousac v. Alexander’s Dep’t. Stores, Inc.*, 299 F.2d 33, 35 (2d Cir. 1962); *Arthur Murray*, 110 F. Supp. at 679–80 (finding the licensing agreement valid because it contained a provision to control defendant’s methods of operation).

131. *See infra* Part III.A.1.

132. *See Embedded Moments, Inc. v. Int’l Silver Co.*, 648 F. Supp. 187, 194 (E.D.N.Y. 1986) (holding that actual control is sufficient to prove adequate regulation of a license and that contractual control is unnecessary); *see also Bishops Bay Founders Group, Inc. v. Bishops Bay Apts.*, 301 F. Supp. 2d 901, 909 (W.D. Wis. 2003) (“[A]n oral license may be sufficient if actual control is exercised by the licensor.” (quoting 2 MCCARTHY, *supra* note 1, § 18:59)).

133. For an example of a conservative interpretation by the Trademark Trial and Appeal Board, *see Heaton Enterprises of Nevada, Inc. v. Lang*, 7 U.S.P.Q.2d (BNA) 1842, 1847 (T.T.A.B. 1988).

134. *Bannon, The Growing Risk of Self-Dilution, supra* note 111, at 579.

licensing valid as long as trademark owners exercised some control over their licensees.<sup>135</sup> Considering that findings of insufficient control could lead to forfeiture of the mark by involuntary abandonment, courts consistently affirmed that claimants of naked licenses "face[d] a stringent standard [of proof]."<sup>136</sup> In addition, in some instances courts seemed willing to declare licensing valid, either without focusing on licensor control or in the absence of control, as long as product quality remained consistent.<sup>137</sup>

For the most part, this favorable judicial approach toward licensing has continued in recent years, and only occasionally has the lack of adequate control brought the judiciary to declare licenses void.<sup>138</sup> Generally, courts have continued to recite that lack of control will lead to naked licensing, yet they have found most licenses valid<sup>139</sup> and accepted almost any evidence of control to uphold licensing.<sup>140</sup> Courts have also repeated that minimal control can satisfy the quality control requirement and that evidence of actual control is sufficient to prove a license valid regardless of the contractual language.<sup>141</sup> Lastly, some courts have continued to uphold licensing "regardless of control" as long as quality remains the same and the public is not deceived.<sup>142</sup> Yet because of courts' case-by-case approach and the possibility that the agreement at issue will be assessed conservatively, trademark owners, licensees, and the market are left with many doubts as to what constitutes valid licensing.

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135. *E.g.*, *Ky. Fried Chicken Corp. v. Diversified Packaging Corp.*, 549 F.2d 368, 387–88 (5th Cir. 1977).

136. *Taco Cabana Int'l, Inc. v. Two Pesos, Inc.*, 932 F.2d 1113, 1121 (5th Cir. 1991) (citing *Am. Foods, Inc. v. Golden Flake, Inc.*, 312 F.2d 619, 624–25 (5th Cir. 1963)), *aff'd*, 505 U.S. 763 (1992).

137. *See id.*; *see also* *Hurricane Fence Co. v. A-1 Hurricane Fence Co.*, 468 F. Supp. 975, 987–89 (S.D. Ala. 1979).

138. *E.g.*, *Ritchie v. Williams*, 395 F.3d 283, 290 (6th Cir. 2005); *Barcamerica Int'l USA Trust v. Tyfield Imps., Inc.*, 289 F.3d 589, 595–98 (9th Cir. 2002); *Halo Mgmt., L.L.C. v. Interland, Inc.*, 308 F. Supp. 2d 1019, 1029–31 (N.D. Cal. 2004); *Stanfield v. Osborne Indus.*, 839 F. Supp. 1499, 1504–07 (D. Kan. 1993), *aff'd*, 52 F.3d 867 (10th Cir. 1995). *But see* *Westco Group, Inc. v. K. B. & Assocs.*, 128 F. Supp. 2d 1082, 1090–91 (N.D. Ohio 2001).

139. *See generally* D. Peter Harvey, *IP Maintenance: Protecting Intellectual Property Assets Through Registration, Proper Use and Contractual Provisions*, 709 PLI/PAT 33, 56–57 (2002) (noting that, because abandonment constitutes forfeiture of trademark, courts hesitate to make such a finding).

140. *E.g.*, Karen Marie Kitterman, *Quality Control in Trademark Licensing*, 821 PLI/PAT 509, 515 (2005).

141. *E.g.*, *Oberlin v. Marlin Am. Corp.*, 596 F.2d 1322, 1326–27 (7th Cir. 1979); *Heaton Distrib. Co. v. Union Tank Car Co.*, 387 F.2d 477, 482–85 (8th Cir. 1967); *Syntex Labs., Inc. v. Norwich Pharmacal Co.*, 315 F. Supp. 45, 56 (S.D.N.Y. 1970), *aff'd*, 437 F.2d 566 (2d Cir. 1971).

142. *See, e.g.*, *Embedded Moments, Inc. v. Int'l Silver Co.*, 648 F. Supp. 187, 194 (E.D.N.Y. 1986) ("It is not necessary, however, for the licenses themselves to contain a written provision for control; actual control by the licensor is sufficient.").

### 1. *The dilemma of “adequate” control*

Soon after the adoption of the Lanham Act in 1946, courts started drifting away from the position that, for licensing to be valid, trademark owners had to enforce strict quality control.<sup>143</sup> Instead, several courts adopted a broader interpretation and upheld licensing agreements as long as trademark owners could prove that the control they exercised was “adequate” to guarantee such quality.<sup>144</sup> Courts never elaborated, however, a specific test to assess whether the control used by licensors was in fact “adequate.” Rather, they adopted a case-by-case analysis and assessed control based on how licensors guaranteed product quality<sup>145</sup> and whether the agreements included quality control provisions. Hence, since decisions were based upon the facts of individual cases, courts often reached different positions on what constituted “adequate” control.<sup>146</sup>

Still, despite these differences, the majority of the courts adopted an increasingly favorable approach toward licensing starting in the 1950s.<sup>147</sup> Notably, they declared most agreements valid and invariably affirmed that claimants of naked licensing faced a stringent burden of proof.<sup>148</sup> In their attempt to uphold most licenses, courts also continued to relax the interpretation of quality control, and specifically what constituted “adequate” control. Accordingly, several courts affirmed that “adequate” could be interpreted as “reasonable”<sup>149</sup> and that findings of “reasonable” control could

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143. See discussion *supra* Part III.A.

144. *E.g.*, *Susser v. Carvel Corp.*, 206 F. Supp. 636, 641 (S.D.N.Y. 1962), *aff'd*, 332 F.2d 505 (2d Cir. 1964); *Morse-Starrett Prods. Co. v. Steccone*, 86 F. Supp. 796, 805 (N.D. Cal. 1949).

145. Traditional methods of controlling quality have included approval requirements, regular testing procedures, requirements to buy certain supplies from certain sources, and sending samples. See *Arner v. Sharper Image Corp.*, 39 U.S.P.Q.2d (BNA) 1282, 1286–89 (C.D. Cal. 1995) (finding that licensing agreements contained provisions that showed a reasonable inference of quality control even though such control provisions were not explicitly spelled out); *Embedded Moments*, 648 F. Supp. at 194–95 (holding that quality control was sufficient when samples were sent to the licensor and the licensee consulted with the licensor about manufacture); see also Karin Segall, *Trademark Licensing: The Quality Control Requirement*; *International Trademark Licensing Provision*; *Click Licenses*, 775 PLI/PAT 353, 357–58 (2004) (explaining that the amount of control required, such as policing, approval, or inspection depends on the type of good and potential variability in quality).

146. Segall, *supra* note 145, at 357–58.

147. *E.g.*, *Susser*, 206 F. Supp. at 641; *Morse-Starrett*, 86 F. Supp. at 805.

148. *Doebler's Pa. Hybrids, Inc. v. Doebler*, 442 F.3d 812, 823–25 (3d Cir. 2005); *Creative Gifts, Inc. v. UFO*, 235 F.3d 540, 548 (10th Cir. 2000); *U.S. Jaycees v. Phila. Jaycees*, 639 F.2d 134, 139 (3d Cir. 1981).

149. See generally *Siegel v. Chicken Delight, Inc.*, 448 F.2d 43, 48–49 (9th Cir. 1971) (finding that as long as the licensor exercises reasonable control over the product's quality, as opposed to maintaining control over specific component articles used in operation and production, a license can be valid).

dismiss claims of naked licensing.<sup>150</sup> Here again, definitions of "reasonable" control varied case by case, but courts usually found that trademark owners had used "reasonable" control. Then, part of the judiciary lowered this threshold even further and interpreted "adequate" as merely "sufficient."<sup>151</sup> Again, what constituted "sufficient" control was decided case by case, yet courts accepted almost any evidence and even declared that a close working relationship between licensors and licensees could prove "sufficient" control<sup>152</sup> or that such control could be exercised by third parties,<sup>153</sup> including licensees.<sup>154</sup>

As part of this favorable trend, the judiciary also developed the position that "actual" rather than contractual control could support valid licensing.<sup>155</sup> This tendency to look outside the contractual provisions to find indicia of control was first affirmed in 1959 in *Dawn Donut Co. v. Hart's Food Stores, Inc.*,<sup>156</sup> where the court held that the language of the contract was not directly relevant to the validity of the license as long as the licensor exercised actual control.<sup>157</sup> However, the court clarified that in the absence of actual control, abandonment could still be found even if the agreement contained quality control provisions.<sup>158</sup> Since then, this principle has commonly been affirmed by the judiciary and, building upon it, some courts have declared that, if actual control is present, an oral agreement can also constitute valid licensing.<sup>159</sup>

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150. *TMT N. Am., Inc. v. Magic Touch GmbH*, 124 F.3d 876, 885–86 (7th Cir. 1997).

151. *E.g., Susser*, 206 F. Supp. at 641.

152. *See Segall, supra* note 145, at 360 (affirming that another instance in which sufficient control may be achieved is a phase-out agreement that provides for quality control). For an example where the court stated that phase-out agreements were not per se abandonment, see *Exxon Corp. v. Oxxford Clothes, Inc.*, 109 F.3d 1070, 1080 (5th Cir. 1997).

153. *See, e.g., Westco Group, Inc. v. K. B. & Assocs.*, 128 F. Supp. 2d 1082, 1091 (N.D. Ohio 2001) (finding that the licensor exerted enough control over the licensee by monitoring operations through industry sources and sales representatives).

154. *See, e.g., Syntex Labs., Inc. v. Norwich Pharmacal Co.*, 315 F. Supp. 45, 56 (S.D.N.Y. 1970) (finding that the agreement at issue was valid based on the relationship between the licensor and licensee and the fact that the licensee complied with FDA regulations), *aff'd*, 437 F.2d 566 (2d Cir. 1971).

155. *E.g., Embedded Moments, Inc. v. Int'l Silver Co.*, 648 F. Supp. 187, 194 (E.D.N.Y. 1986); *Nat'l Lampoon, Inc. v. Am. Broad. Cos.*, 376 F. Supp. 733, 737 (S.D.N.Y. 1974), *aff'd per curiam*, 497 F.2d 1343 (2d Cir. 1974).

156. 267 F.2d 358, 368 (2d Cir. 1959).

157. *Id. But see Robinson Co. v. Plastics Research & Dev. Corp.*, 264 F. Supp. 852, 864 (W.D. Ark. 1967) (holding that "it is the *right* to control rather than the actual exercise of control which determines whether or not a license is valid").

158. *Dawn Donut*, 267 F.2d at 368.

159. *Transgo, Inc. v. Ajac Transmission Parts Corp.*, 768 F.2d 1001, 1017–18 (9th Cir. 1985).

Courts continued to lower the bar for what constituted “adequate” control in the following decades. In particular, the judiciary stated that “adequate” control was a very low standard and that even “minimal” control was sufficient for a license to be valid.<sup>160</sup> This approach was first elaborated in 1972 in *Kentucky Fried Chicken Corp. v. Diversified Packaging Corp.*,<sup>161</sup> where the court found that the fact that KFC failed to promptly discover that its licensees had purchased food containers from unapproved sellers did not indicate lack of control per se, since this requirement was included in the licensing agreement.<sup>162</sup> Following this decision, several courts continued to use findings of “minimal” control to uphold licensing agreements.<sup>163</sup> They also affirmed the decision in *Dawn Donut* and repeated that evidence of “actual” control was sufficient for valid licensing regardless of the language of the actual agreement.<sup>164</sup>

As highlighted earlier, this favorable attitude toward licensing has continued until today. Present any sign of control, courts have generally proven reluctant to declare licenses invalid,<sup>165</sup> and only occasionally have claims of inadequate control resulted in findings of naked licensing.<sup>166</sup> Moreover, a minority of the courts have also disagreed with *Dawn Donut* in recent years and stated that contractual language providing for quality control constitutes sufficient evidence of control even in the absence of actual control.<sup>167</sup> This position was

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160. *Bureau Nat'l Interprofessionnel Du Cognac v. Int'l Better Drinks Corp.*, 6 U.S.P.Q.2d (BNA) 1610, 1617–18 (T.T.A.B. 1988); *Penta Hotels Ltd. v. Penta Tours*, 9 U.S.P.Q.2d (BNA) 1081, 1108–09 (D. Conn. 1988); *Nestle Co. v. Nash-Finch Co.*, 4 U.S.P.Q.2d (BNA) 1085, 1089 (T.T.A.B. 1987); *Embedded Moments*, 648 F. Supp. 187 at 194.

161. 549 F.2d 368, 387 (5th Cir. 1977) (“Retention of a trademark requires only minimal quality control, for in this context we do not sit to assess the quality of products sold on the open market.”).

162. *Id.* at 386–88.

163. *See, e.g., Hurricane Fence Co. v. A-1 Hurricane Fence Co.*, 468 F. Supp. 975, 989 (S.D. Ala. 1979) (“The plaintiffs have numerous licensed dealers throughout the country and to impose upon the mark owner the duty of monitoring every sale of every dealer to regulate its use of the mark would be unconscionable. . . . The fencing business is unique and only minimal quality controls ought to be required.”).

164. *E.g., Nat'l Lampoon, Inc. v. Am. Broad. Cos.*, 376 F. Supp. 733, 737 (S.D.N.Y. 1974), *aff'd per curiam*, 497 F.2d 1343 (2d Cir. 1974).

165. *Lemley, supra* note 17, at 1710–11. According to the *Restatement (Third) of Unfair Competition*, the ultimate test should be “whether the control exercised by the licensor is sufficient under the circumstances to satisfy the public’s expectation of quality assurance arising from the presence of the trademark on the licensee’s goods or services.” § 33 cmt. c (1995).

166. *See Ritchie v. Williams*, 395 F.3d 283, 290 (6th Cir. 2005); *Barcamerica Int'l USA Trust v. Tyfield Imps., Inc.*, 289 F.3d 589, 598 (9th Cir. 2002); *Halo Mgmt., L.L.C. v. Interland, Inc.*, 308 F. Supp. 2d 1019, 1028–31 (N.D. Cal. 2004).

167. *See 3 MCCARTHY, supra* note 1, § 18:56 (citing *Pike v. Ruby Foo's Den, Inc.*, 232 F.2d 683, 685–86 (D.C. Cir. 1956)); *see also Ideal Toy Corp. v. Cameo Exclusive Prods., Inc.*, 170 U.S.P.Q. (BNA) 596, 598 (T.T.A.B. 1971) (finding proper “control”

highlighted most recently in 2003 in *Glow Industries, Inc. v. Lopez*,<sup>168</sup> where the court declared that "[t]he language of the agreement demonstrate[d] that [defendant] maintained control over the quality of the . . . products . . . and the burden thus shift[ed] to [plaintiff] to demonstrate that [defendant] did not exercise that control."<sup>169</sup> This approach represents a clear step toward licensing de facto without control and as such has been criticized by supporters of quality control.<sup>170</sup> Still, not all courts have subscribed to this trend, and inadequate quality control, or lack thereof, continues to be a "risky business" for trademark owners.<sup>171</sup>

## 2. *Shifting focus on product quality?*

Because of the ambiguities surrounding the concept of "control" and, in particular, of what represents "adequate" control, the past decades have also witnessed a shift in focus directly onto product quality, rather than on control, to assess the validity of trademark licensing. Rather than focusing on the control that licensors had supposedly exercised over their licensees, several courts started to look at whether the quality of the products was consistent—that is, whether all products bearing the same mark in fact shared the same quality so the public would not be deceived. If so, courts *assumed* that licensors had exercised "sufficient" quality control.

This approach was first established in 1964 in *Land O'Lakes Creameries, Inc. v. Oconomowoc Canning Co.*<sup>172</sup> In this case, the petitioner claimed that the defendant engaged in naked licensing and accordingly that its mark ought to be cancelled.<sup>173</sup> However, the court held that even if Oconomowoc Canning had not exercised affirmative control on its licensee, the agreement was still valid because the company had justifiably relied on its licensee to control quality since the licensee had maintained consistent product quality

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where licensor had a "right" to control, even though there was no evidence of actual control); *Robinson Co. v. Plastics Research & Dev. Corp.*, 264 F. Supp. 852, 864 (W.D. Ark. 1967); *Arthur Murray, Inc. v. Horst*, 110 F. Supp. 678, 680 (D. Mass. 1953); *Wolfies Rest., Inc. v. Lincoln Rest. Corp.*, 143 U.S.P.Q. (BNA) 310, 310-11 (N.Y. Sup. Ct. 1964).

168. 273 F. Supp. 2d 1095 (C.D. Cal. 2003).

169. *Id.* at 1111.

170. Such an approach has been criticized as a breach in rationale of the quality control requirement. Bannon, *The Growing Risk of Self-Dilution*, *supra* note 111, at 579.

171. See 3 MCCARTHY, *supra* note 1, § 18:10 (discussing the rule against trademark assignment in gross).

172. 330 F.2d 667 (7th Cir. 1964).

173. *Id.* at 668.



for more than forty years of their licensing relationship.<sup>174</sup> Still, from a theoretical standpoint, the court continued to affirm that licensors have an affirmative duty to police their licensees, but that this was not necessary in the case at issue because of the circumstances.<sup>175</sup>

In subsequent years, several courts followed this decision and held that evidence of control was not strictly necessary to uphold trademark licenses as long as product quality was consistent.<sup>176</sup> Two circuit court decisions from 1985 proved particularly interesting in this respect: *Transgo, Inc. v. Ajac Transmission Parts Corp.*<sup>177</sup> and *Taco Cabana International, Inc. v. Two Pesos, Inc.*<sup>178</sup> In *Transgo*, the court upheld the license at issue because the licensor and licensee worked closely together for ten years, and even though the licensor did not inspect the final products, quality was deemed to have been adequately controlled by the licensee.<sup>179</sup> Similarly, in *Taco Cabana* the court upheld the agreement at issue based on the close working relationship between the licensors and licensees.<sup>180</sup> In this case, two brothers jointly operated a restaurant. When one later opened a similar restaurant under a licensing agreement, the court found the license valid, despite the lack of a quality control provision, on the assumption that, after working together for eight years, the brothers could reasonably rely on each other to maintain consistent product quality.<sup>181</sup>

Still, like the court in *Land O'Lakes*,<sup>182</sup> the courts in *Transgo*<sup>183</sup> and *Taco Cabana*<sup>184</sup> did not dismiss the theoretical need for control as a condition for valid licensing. Instead, they focused on product quality and whether the public was deceived to assess and eventually uphold the agreements at issue. In particular, in *Taco Cabana*, the court stated that "[t]he purpose of the quality-control requirement is to prevent the public deception that would ensue from variant quality

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174. *See id.* "The controversy here must be viewed in light of the innocence of each party in adopting the same trade-mark, the length of time the parties have used the mark, and the noncompetitive nature of their products." *Id.* at 671. Theoretically, the court did not dismiss the need for quality control, but the result of this license was a de facto upholding of a naked license.

175. *Id.* at 670-71.

176. *E.g.*, *Haymaker Sports, Inc. v. Turian*, 581 F.2d 257, 262 (C.C.P.A. 1978); *Embedded Moments, Inc. v. Int'l Silver Co.*, 648 F. Supp. 187, 194 (E.D.N.Y. 1986).

177. 768 F.2d 1001 (9th Cir. 1985).

178. 932 F.2d 1113 (5th Cir. 1991), *aff'd*, 505 U.S. 763 (1992).

179. *Transgo*, 768 F.2d at 1017-18.

180. *Taco Cabana*, 932 F.2d at 1113, 1121.

181. *Id.* at 1121-22.

182. 330 F.2d 667 (7th Cir. 1964).

183. 768 F.2d at 1017.

184. 932 F.2d at 1121.

standards"<sup>185</sup> and "[w]here the particular circumstances of the licensing arrangement persuade us that the public will not be deceived, we need not elevate form over substance and require the same policing rigor appropriate to more formal licensing."<sup>186</sup> In addition, the court specified that, where it "may justifiably rely on each parties' . . . standards and procedures to ensure consistent quality, and *no actual decline in quality standards is demonstrated*, [it] would depart from the purpose of the law to find an abandonment simply for want of all the inspection and control formalities."<sup>187</sup>

This tendency to uphold licensing "regardless of actual control" where product quality remains consistent has grown in recent years.<sup>188</sup> In particular, an increasing number of courts have adopted the approach, first affirmed in *Kentucky Fried Chicken*,<sup>189</sup> that "the consuming public must be the judge of whether the quality control efforts have been ineffectual,"<sup>190</sup> thus shifting the analysis of the validity of licensing from quality control to consistent product quality. Still, no court has openly defied the theoretical validity of quality control or rejected the requirement so far.<sup>191</sup> Instead, the judiciary has adopted a compromise in the form of a broad definition of control—that control can be implied as long as product quality is consistent and the public is not misled—to "skip" the analysis of quality control and either uphold agreements or declare them void.

Yet, despite its clear advantage over the traditional approach—avoiding the daunting task of defining control while focusing on the reality of the agreements—this trend has continued to be based on a case-by-case analysis rather than on a clear change in the traditional standard. In addition, as with "adequate control," courts have never defined what constitutes "consistent quality." Accordingly, in the absence of any statutory guideline on the matter,<sup>192</sup> judicial positions

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185. *Id.*

186. *Id.*

187. *Id.* (emphasis added).

188. *See, e.g., Embedded Moments, Inc. v. Int'l Silver Co.*, 648 F. Supp. 187, 194 (E.D.N.Y. 1986) ("It is not necessary, however, for the licenses themselves to contain a written provision for control; actual control by the licensor is sufficient.").

189. 549 F.2d 368 (5th Cir. 1977).

190. *Id.* at 387.

191. *Bach v. Forever Living Prods. U.S., Inc.*, 473 F. Supp. 2d 1110 (W.D. Wash. 2007). "The general rule is that a trademark owner who 'fails to exercise adequate quality control over [a] licensee' of a trademark creates a 'naked license' and thereby abandons the trademark." *Id.* at 1120 (citation omitted). *See Dep't. of Parks & Recreation v. Bazaar Del Mundo, Inc.*, 448 F.3d 1118, 1131 (9th Cir. 2006) ("[W]ell-established trademark law imposes a duty upon the licensor to retain sufficient control over the mark to prevent public deception.").

192. *See generally* Franklyn, *The Apparent Manufacturer Doctrine*, *supra* note 3, at 686 (highlighting that "[n]either 'quality' nor 'control' is defined in the Lanham Act;

in this respect are also likely to vary, thus creating further inconsistency.<sup>193</sup> Finally, this trend away from the enforcement of quality control has not been universally accepted and some courts have continued to assess agreements conservatively, thus leaving licensors, licensees, and competitors uncertain as to how to structure a valid license.<sup>194</sup>

*B. Consequences of the Absence of a Clear Definition of "Quality Control"*

As stressed earlier, the uncertainty surrounding the definition of quality control created much ambiguity in its judicial application. In particular, courts often interpreted the requirement as they saw fit and stretched the concept of "control"—a concept per se open ended—to include any type of control, from "strict" to "adequate," to "sufficient," and eventually to "minimal" control. Courts also used criteria such as consistent product quality or a close working relationship between the licensors and licensees to affirm that control could be "implied." Yet, while the judiciary generally favored licensing and found traces of control in most agreements, courts have never followed a totally consistent path on the issue and have continued to randomly adopt a more conservative approach in recent years.<sup>195</sup>

As a result, much ambiguity continues to exist today as to what constitutes a valid license and how much control trademark owners should exercise to avoid the involuntary forfeiture of their marks. Accordingly, licensors are commonly advised to use caution and include explicit quality control provisions in their contracts in addition to exercising actual control over their licensees to avoid findings of naked licensing.<sup>196</sup> Still, the degree of control that licensors ought to adopt remains uncertain in practice and often varies according to the circumstances of the individual cases and the

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they are common law creatures whose evolution is incomplete and inconsistent") (citation omitted).

193. See *Nitro Leisure Prods., L.L.C. v. Acushnet Co.*, 341 F.3d 1356, 1370 (Fed. Cir. 2003) (stating that consistent quality means the product is of "the same character and source . . . as other goods previously purchased bearing the mark" (quoting 1 MCCARTHY, *supra* note 1, § 3:10)); *Taco Cabana Int'l, Inc. v. Two Pesos, Inc.*, 932 F.2d 1113, 1121 (5th Cir. 1991) (indicating that consistent quality means "no actual decline in quality standards"), *aff'd*, 505 U.S. 763 (1992); *Gorenstein Enters., Inc. v. Quality Care-USA, Inc.*, 874 F.2d 431, 435 (7th Cir. 1989) (stating that consistent quality means the product "really is the same good or service").

194. *E.g.*, *Parks*, *supra* note 5, at 531.

195. See discussion *supra* Part III.A.1–2.

196. *E.g.*, Ann E. Doll, *Trademark Licensing: Quality Control*, 12 J. CONTEMP. LEGAL ISSUES 203 (2001).

view of the individual court.<sup>197</sup> For example, while some courts may be appeased by the consistent quality of licensed products, others may require evidence of actual, and even strict, control to avoid a finding of naked licensing.<sup>198</sup> Furthermore, since part of the judiciary has indicated that third parties or even licensees can effectively monitor quality control, licensors face confusion as to who should monitor quality control—that is, whether they must exercise control directly—for licensing to be valid.<sup>199</sup>

Besides creating many problems for trademark owners and licensees with respect to the drafting and enforcing of their licenses, the ambiguity surrounding the interpretation of quality control has also allowed unfair competitors to present claims of invalid licensing as a defense against accusations of trademark infringement, arguing that trademark owners forfeit their rights as a result of insufficient quality control.<sup>200</sup> Not surprisingly, this trend has increased the number of unnecessary and frivolous lawsuits to the detriment of the judicial system and the market overall.<sup>201</sup> Here again, to avoid counterclaims of naked licensing in response to infringement claims, trademark owners are usually advised to be cautious and enforce quality control beyond what would normally be sufficient. Yet, while this approach undoubtedly serves the purpose of proving the validity of the agreement at issue, it also comes with increased costs for trademark owners which, in many instances, are eventually transferred to the final prices of products, and thus directly affect consumers and the market.<sup>202</sup>

Most likely in order to prevent this cost shifting and as a result of the growing importance of licensing, the judiciary has drifted away

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197. See *id.* at 205 ("How much control must the licensor exercise to assure consumers and to protect against mark abandonment? The courts do not provide specific answers . . ."); see also *Dep't. of Parks & Recreation v. Bazaar Del Mundo, Inc.*, 448 F.3d 1118, 1131 (9th Cir. 2006) (requiring "sufficient control"); *Doebler's Pa. Hybrids, Inc. v. Doebler*, 442 F.3d 812, 823 (3d Cir. 2006) (requiring that licensors use "adequate control"); *Bishops Bay Founders Group, Inc. v. Bishops Bay Apts.*, 301 F. Supp. 2d 901, 909 (W.D. Wis. 2003) (requiring "actual control").

198. *E.g.*, *Ritchie v. Williams*, 395 F.3d 283, 290 (6th Cir. 2005); *Barcamerica Int'l USA Trust v. Tyfield Imps., Inc.*, 289 F.3d 589, 596 (9th Cir. 2002); *Halo Mgmt., L.L.C. v. Interland, Inc.*, 308 F. Supp. 2d 1019, 1028–30 (N.D. Cal. 2003); *Stanfield v. Osborne Indus.*, 839 F. Supp. 1499, 1504–05 (D. Kan. 1993).

199. See Richard M. Steuer, *Exclusive Dealing in Distribution*, 69 CORNELL L. REV. 101, 132 (1983) ("Federal law requires a trademark owner that licenses its trademark to exercise control over the quality of the trademarked goods produced and distributed by its licensees.").

200. See discussion *infra* Part V.B.2.

201. See Parks, *supra* note 5, at 531. See also William R. Woodward, *Some Observations on Legitimate Control of the Nature and Quality of the Goods*, 49 TRADEMARK REP. 609 (1959) (criticizing the quality control requirement).

202. See discussion *infra* Part V.B.

from the strict interpretation of quality control to a more flexible approach since the adoption of the Lanham Act.<sup>203</sup> Specifically, as detailed in the previous paragraphs, the majority of the courts have increasingly adopted a sort of rule of reason and a broad interpretation of “control” to assess licenses based on their possible effects on consumers and the market.<sup>204</sup> As a result, courts have accepted that “sufficient” or even “minimal” control could satisfy the quality control requirement, and a growing number of judges have decided to focus on the substance and the result of the agreements, that is, the consistency of product quality, rather than on actual control.<sup>205</sup>

Despite this growing trend, the traditional view that lack of control will result in naked licensing has nonetheless continued to be included in the language of most judicial decisions, proving courts generally reluctant to abandon quality control as the theoretical standard for valid licensing.<sup>206</sup> Still, instead of assisting the courts in preventing fraudulent licensing and protecting consumers and the market from such fraud, this adherence to the traditional theoretical framework of licensing has increased the existing confusion by leaving room for courts to interpret quality control as they see fit based on the circumstances of the individual case. Ultimately, this lack of a clear direction as to what constitutes a valid license continues to permit attacks among competitors, often regardless of consumer confusion, thus undermining the original goal of the requirement—protecting product quality and the purchasing public.<sup>207</sup>

#### IV. THE INCREASING UNSUSTAINABILITY OF “QUALITY CONTROL”

In the last hundred years, trademark licensing has become a vastly more important and lucrative tool for businesses. As elaborated in Part I, modern licensing has also extended to nontraditional agreements such as collateral and promotional licensing, whose primary functions differ considerably from that of classical licensing,

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203. See discussion *supra* Part III.A.1–2.

204. See *Doebler’s Pa. Hybrids, Inc. v. Doebler*, 442 F.3d 812, 824–25 (3d Cir. 2006) (requiring “reasonable” control).

205. See 3 MCCARTHY, *supra* note 1, § 18:58 (“[S]ome courts are reluctant to interfere with reasonable quality control arrangements agreed to by the parties and will often accept even minimal control . . .”).

206. See *supra* Part II.A.

207. See *University of Pittsburgh v. Champion Products, Inc.*, 686 F.2d 1040, 1047 (3d Cir. 1982), and *Ryan v. Volpone Stamp Co.*, 107 F. Supp. 2d 369, 380 (S.D.N.Y. 2000), for examples of cases where the court found no consumer confusion and upheld the agreements at issue.

i.e., enhancing and exploiting the value of a mark per se. Still, trademark law continues to subject all types of licensing to the same validity requirement that was used in the early twentieth century for classical licensing—quality control.

Part IV considers the changes that have affected modern trademark licensing and the increasing unsustainability of quality control. This Part also highlights how modern trademark practices are increasingly shifting toward licensing de facto without control. This shift is particularly apparent when one considers practices such as promotional licensing, trademark assignment and license-back, and the doctrine of licensee estoppel. Considering that most foreign countries do not require quality control for valid licensing, this shift can also be attributed to the proliferation of international licensing and the growing importance of international trade.

#### A. *The Reality of Modern Trademark Licensing*

As indicated in Part I, the origin of trademark licensing can be traced back to the desire of trademark owners to increase the production of their existing products or to manufacture affiliated goods.<sup>208</sup> Rather than increasing production or directly starting new manufacturing, however, trademark owners often found it more convenient to delegate this task to third parties, who specialized in the same field, through licensing agreements. In addition to avoiding the costs and the risks of manufacturing, these agreements seemed more economical since licensees manufactured products more cheaply due to economies of scale and trademark owners still enjoyed a share of profits due to royalties.<sup>209</sup> On their part, such arrangements also suited licensees, who often seek them directly to take advantage of the goodwill established by the licensed mark and thus avoid the risks connected to selling products independently under a new and unknown name.<sup>210</sup>

In its essence, the above rationale has continued to characterize trademark licensing until present, and both licensors and licensees continue to enter agreements to save costs and increase their profits by exploiting the goodwill established by the licensed marks.<sup>211</sup> Since

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208. See discussion *supra* Part I.

209. *E.g.*, SCHLICHER, *supra* note 3, at 27.

210. *Id.*

211. See Parks, *supra* note 5, at 533–35 (discussing the various theories that have justified trademark licensing over the years and suggesting the introduction of a new theory, different from “quality assurance”); see also Friedman, *supra* note 15, at 357 (discussing quality assurance theory as a justification for trademark licensing (citing Schechter, *supra* note 47, at 823)).

its early days, however, trademark licensing has profoundly evolved. In particular, from an occasional business technique, licensing has become a fundamental pillar of the economy due to the changes in manufacturing, the rise of the consumer society, and the globalization of trade.<sup>212</sup> Because of these changes, licensing has also developed into several types of agreements whose objectives are often different in scope from those of classical licensing.<sup>213</sup>

Notably, modern trademark licensing has expanded beyond the production of the same or similar products to encompass a growing number of collateral and promotional products whose primary intent is that of enhancing, and exploiting, the image of the brand embodied by a mark.<sup>214</sup> As critics have often pointed out, this increasing focus on trademarks as stand-alone business assets is additional evidence of the modern shift toward “proPERTIZING” trademark rights.<sup>215</sup> Still, well aware of the importance of trademarks as a source of revenues for businesses, particularly in an economy that is increasingly moving toward a service economy, both the courts and legislators have proven willing to support this shift as long as the public is not confused or misled and competition in the market continues to be fair.<sup>216</sup>

Similarly, recent decades have also witnessed the growth of a practice closely related to licensing—franchising.<sup>217</sup> Primarily used in the service and retail areas, franchising usually involves the licensing of famous marks along with the licensors’ technology and methods of operation. Here again, however, the primary reason for this practice, both on the part of the franchisor and franchisee, is almost always the desire to exploit the fame and established goodwill of the licensed

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212. *E.g.*, BATTERSBY & GRIMES, 2003 SUPPLEMENT, *supra* note 27, at 3.

213. The Lanham Act does not differentiate between types of licensing and applies quality control as a requirement for the validity of all agreements. Lanham Act § 5, 15 U.S.C. § 1055 (2000).

214. *See* discussion *infra* Part IV.A.1.

215. *E.g.*, Lemley, *supra* note 17, at 1687–88; *see also* Dogan & Lemley, *supra* note 34, at 479–80.

216. For an analysis of the case law on promotional licensing, *see* discussion *infra* Part IV.A.1. Legislators showed their favor toward this practice when, in 1988, section 5 of the Lanham Act was amended to include the licensing of intent-to-use trademark applications. “If first use of a mark by a person is controlled by the registrant or applicant for registration of the mark with respect to the nature and quality of the goods or services, such first use shall inure to the benefit of the registrant or applicant, as the case may be.” Lanham Act § 5, 15 U.S.C. § 1055. *See* 3 MCCARTHY, *supra* note 1, §§ 18:48, 18:60; *see also* discussion *supra* Part II.B.

217. *E.g.*, Marlene B. Hanson & W. Casey Walls, *Protecting Trademark Good Will: The Case for a Federal Standard of Misappropriation*, 81 TRADEMARK REP. 480, 484 (1991); Thomas M. Pitegoff, *Franchise Relationship Laws: A Minefield For Franchisors*, 45 BUS. LAW. 289, 290–92 (1989); *see also* *Susser v. Carvel Corp.*, 206 F. Supp. 636, 640 (S.D.N.Y. 1962), *aff’d*, 332 F.2d 505 (2d Cir. 1964).

mark to attract a higher number of consumers.<sup>218</sup> In some instances, franchising has reached such success that it constitutes the only activity carried out by the owners of the licensed mark.<sup>219</sup> Not surprisingly, considering its growing importance in the economy, courts have also endorsed this practice and have upheld franchising as long as the agreements at issue do not damage the public or competition.<sup>220</sup>

The increasing internationalization of trade and the need for businesses to expand their markets abroad have also deeply affected the interpretation of modern licensing. In particular, as a result of the rising number of foreign countries involved in licensing programs, calls for the adoption of a common standard for the validity of licensing worldwide have been mounting in recent years as part of the general trend toward harmonizing intellectual property laws worldwide.<sup>221</sup> These calls have interested primarily the United States, which retains quality control opposite to most other jurisdictions that do not provide for any similar requirement.<sup>222</sup> While the United States has so far formally resisted these calls, the growing international pressure for a change, along with the criticism of United States businesses, have certainly contributed to the recent shift toward licensing with minimal control, thus approaching national trademark law de facto to that of other countries.

Finally, trademark owners and other parties in the market have increasingly used licensing as a strategic tool to reaffirm trademark

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218. Friedman, *supra* note 15, at 355–58.

219. *E.g.*, McDonald's Corporation, FAQ's, <http://www.mcdonalds.com/corp/franchise/faqs2.html> (last visited Sept. 29, 2007).

220. *See Susser*, 206 F. Supp. at 647 (upholding an ice cream franchise agreement); *Smith v. Waite*, 424 S.W.2d 691, 693 (Tex. Civ. App. 1968) (upholding a franchise agreement).

221. The most relevant international agreement on trademark licensing is the Agreement on Trade-Related Aspects of Intellectual Property Rights. *See* Agreement on Trade-Related Aspects of Intellectual Property Rights, Including Trade in Counterfeit Goods, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex IC, Legal Instruments—Results of the Uruguay Round, 33 I.L.M. 81 (1994) [hereinafter TRIPS]; *see also* 5 MCCARTHY, *supra* note 1, § 29:36; WORLD INTELLECTUAL PROP. ORG., WIPO INTELLECTUAL PROPERTY HANDBOOK: POLICY, LAW AND USE 345 (2d ed. 2004), available at <http://www.wipo.int/export/sites/www/about-ip/en/iprm/pdf/ch5.pdf>. Yet, despite the increased harmonization of laws, conditions for the validity of licensing continued to be left to the discretion of member countries. According to article 21 of TRIPS, “[m]embers may determine conditions on the licensing and assignment of trademarks, it being understood that the compulsory licensing of trademarks shall not be permitted.” TRIPS, *supra*, art. 21.

222. For a reconstruction of various countries' approaches on trademark licensing, *see* 2 STEPHEN P. LADAS, PATENTS, TRADEMARKS, AND RELATED RIGHTS: NATIONAL AND INTERNATIONAL PROTECTION §§ 715–720 (1975); *see also* MARY M. SQUYRES, 1–2 TRADEMARK PRACTICE THROUGHOUT THE WORLD §§ 6–17 (2007).



rights, settle trademark disputes, or enter agreements whose purpose is, in essence, market control or division of market shares.<sup>223</sup> As noted earlier, this use of licensing to trade in trademarks as things per se has always been common in the marketplace,<sup>224</sup> but recent decades have seen an unusual increase in this trend.<sup>225</sup> Also in this respect, however, courts have generally tolerated these practices as long as the agreements included the formal provisions of quality control and the public was not negatively affected.<sup>226</sup> Not surprisingly, this attitude has further eroded the real applicability of quality control and brought the judiciary a step closer to granting property rights in trademarks.<sup>227</sup>

1. *Promotional licensing and (the lack of) "quality control"*

As indicated above, the growing tendency toward recognizing, and exploiting, the intrinsic value of trademarks per se has deeply affected the traditional interpretation of licensing and quality control. In particular, over the past decades, this trend has led to the rise of a new type of licensing—promotional licensing or trademark merchandising—whose purpose is not that of classical licensing, that is, to augment the quantity of the products originally produced by trademark owners, but that of building and enhancing brand image and consumer affiliation by licensing a mark for unrelated goods or services.<sup>228</sup> Not surprisingly, because of its very nature, this type of licensing has profoundly challenged the enforcement of quality control.<sup>229</sup>

Historically, the recognition of trademark merchandising dates back to a landmark decision by the Fifth Circuit in 1975: *Boston Professional Hockey Association v. Dallas Cap & Emblem Manufacturing*.<sup>230</sup> In that case, Boston Hockey refused Dallas Cap permission to duplicate its logo on clothing based on a prior exclusive licensing

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223. See discussion *infra* Part IV.A.2.

224. Isaacs, *supra* note 14, at 1210.

225. See generally Lisa H. Johnston, *Drifting Toward Trademark Rights in Gross*, 85 TRADEMARK REP. 19, 22–36 (1995) (discussing the increasing drift of trademarks toward rights in gross).

226. For an analysis of the case law on strategic uses of trademarks, see discussion *infra* Part IV.A.2.

227. *E.g.*, Lemley, *supra* note 17, at 1687–88.

228. See discussion *supra* Part I.

229. Promotional trademark licensing changed the role of trademarks with respect to consumer information. Their function changed from one of creating “consumer reliance on the mark” to one of “engender[ing] consumer identification with the mark.” Franklyn, *Liability for Trademark Licensors*, *supra* note 26, at 13 (citing Keating, *supra* note 3, at 372).

230. 510 F.2d 1004 (5th Cir. 1975), *cert. denied*, 423 U.S. 868 (1975).

agreement, but Dallas Cap manufactured and sold clothing bearing the "B" mark regardless.<sup>231</sup> By reversing the lower court's decision,<sup>232</sup> the Fifth Circuit determined that Dallas Cap had infringed upon Boston Hockey's mark and found likelihood of confusion<sup>233</sup> in "the fact that the defendant duplicated the protected trademarks and sold them to the public knowing that the public would identify them as being the teams' trademarks."<sup>234</sup> Hence, the court departed from the traditional interpretation of the Lanham Act and found that confusion existed because consumers associated the logos—the "triggering mechanism for the sale"<sup>235</sup>—with the team even in the absence of confusion as to the source of the products.<sup>236</sup>

As expected, this decision was criticized as a step further toward establishing property rights in trademarks.<sup>237</sup> Still, the court's position reflected the growing importance of promotional licensing, which had already become a source of major revenues for trademark holders at that time, primarily for sport teams and colleges.<sup>238</sup> This favorable trend continued during the following years and, even if many courts proved reluctant to directly affirm *Boston Hockey* and

231. *Id.* at 1009.

232. *Boston Prof'l Hockey Ass'n v. Dallas Cap & Emblem Mfg.*, 360 F. Supp. 459 (N.D. Tex. 1973), *rev'd*, 510 F.2d 1004 (5th Cir. 1975). The district court found no infringement, stating that consumers did not necessarily expect affiliation between the apparel bearing the logos and the hockey team. *Id.* at 463. "The test is not whether the products in question are duplications of their marks, but whether the defendant's use of [them] would mislead the public as to the source of the goods." *Id.* at 462–63. The court issued, however, a limited injunction requiring that Dallas Cap disclaim any association with the teams since some consumers could assume that the products were officially licensed by the National Hockey League. *Id.* at 465.

233. *Boston Hockey*, 510 F.2d at 1012. The Fifth Circuit based its decision on three arguments: (1) the commercial value of the logos was created by plaintiffs' efforts; (2) defendant sought a license and, if obtained, would have enforced it against infringers; and (3) selling reproductions of trademarks per se on emblems is an accepted use for sport teams. *Id.* at 1011. The court acknowledged, however, that its decision "may slightly tilt the trademark laws from the purpose of protecting the public to the protection of the business interests of plaintiffs." *Id.*

234. *Id.* at 1012.

235. *Id.* The Fifth Circuit stated: "The argument that confusion must be as to the source of the manufacture of the emblem itself is unpersuasive, where the trademark, originated by the team, is *the triggering mechanism* for the sale of the emblem." *Id.* (emphasis added). See *Nat'l Football League Props., Inc. v. Consumer Enters., Inc.*, 327 N.E.2d 242, 246 (Ill. App. 1975) (finding infringement because "the buying public has come to associate the trademark with the sponsorship of the NFL or of the particular member team involved").

236. *Boston Hockey*, 510 F.2d at 1012.

237. See *Dogan & Lemley*, *supra* note 34, at 471–72 ("[T]he mark in these cases is rarely serving the traditional function of a trademark. Rather than indicating something to the consumer about the source . . . of a product, the mark *is* the product . . ."); see also *id.* at 473–76 (discussing the role of *Boston Hockey* and trademark licensing in establishing a property right in trademarks).

238. On the role of promotional licensing providing revenues for non-profit and for-profit institutions, see Keating, *supra* note 3, at 370–71.

enforce trademark rights based simply on consumer association,<sup>239</sup> the majority of the judiciary has adopted a sympathetic attitude toward merchandising. In particular, courts developed the doctrine of confusion “as to the sponsorship,” according to which infringement can be found when consumers mistakenly believe that the trademark owners sponsored the products bearing identical or confusingly similar marks.<sup>240</sup> Since consumer perception has increasingly become that trademark owners authorize promotional products, this doctrine has undoubtedly facilitated the protection of promotional licensing.<sup>241</sup>

Besides broadening the scope of the likelihood of confusion, the spread of promotional licensing gave rise to several criticisms of the quality control requirement as the standard for the validity of trademark licensing.<sup>242</sup> Specifically, it was argued that in promotional licensing, “the consumer is merely interested in attaining a symbol to display loyalty, affection or sympathy to a person, institution or cause and the quality-control function has no substantial value.”<sup>243</sup> Thus, considering that most often trademark holders lack expertise in the

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239. See, e.g., *United States v. Giles*, 213 F.3d 1247, 1250 (10th Cir. 2000) (stating that the Fifth Circuit in *Boston Hockey* relied “upon a novel and overly broad conception of the rights that a trademark entails”); *Int’l Order of Job’s Daughters v. Lindeburg & Co.*, 633 F.2d 912, 919 (9th Cir. 1980) (defining *Boston Hockey* as “an extraordinary extension of the protection . . . afforded trademark owners”).

240. See, e.g., *Univ. of Pittsburgh v. Champion Prods., Inc.*, 686 F.2d 1040, 1047 (3d Cir. 1982); *Nat’l Football League Props., Inc. v. Wichita Falls Sportswear, Inc.*, 532 F. Supp. 651, 659 (W.D. Wash. 1982) (“Likelihood of confusion in a sponsorship context focuses on the product bearing the allegedly infringing marks and asks whether the public believes the product bearing the marks originates with or is somehow endorsed or authorized by the plaintiff.”). The Fifth Circuit itself also adopted this standard and narrowed its holding in *Boston Hockey*. See Supreme Assembly, *Order of Rainbow for Girls v. J.H. Ray Jewelry Co.*, 676 F.2d 1079, 1082 (5th Cir. 1982); *Ky. Fried Chicken Corp. v. Diversified Packaging Corp.*, 549 F.2d 368, 388 (5th Cir. 1977) (“Trademark infringement occurs only when the use sought to be enjoined is likely to confuse purchasers with respect to such things as the product’s source, its endorsement by the plaintiff, or its connection with the plaintiff.”).

241. See Keating, *supra* note 3, at 372 (“A recent survey indicated that 45.3 percent of the respondents believed that companies making jerseys corresponding to National Football League jerseys were required to obtain authorization from the NFL.” (citing *Wichita Falls Sportswear*, 532 F. Supp. at 658–59)). More recently, for example, in 2004, “[t]he University of North Carolina at Chapel Hill’s net licensing royalties . . . totaled \$3.7 million.” News Release, Univ. of N.C., Chapel Hill, Trademark Licensing Revenue Totals \$3.7 Million for Fiscal 2004; UNC is Nation’s Top Performer (Sept. 22, 2004), available at <http://www.unc.edu/news/archives/sep04/license092204.html>. See Pallavi Gogoi, *Wal-Mart’s Luxury Problem*, BUS. WK. ONLINE, June 13, 2006, [http://www.businessweek.com/investor/content/jun2006/pi20060613\\_187965.htm](http://www.businessweek.com/investor/content/jun2006/pi20060613_187965.htm) (discussing the effect of counterfeit goods on consumer perception of trademarks and brands).

242. See, e.g., Marks, *supra* note 5, at 653 (quoting Keating, *supra* note 3, at 378–79).

243. Keating, *supra* note 3, at 378.

promotional goods industry, to require them "to inaugurate an imaginary quality-control program to satisfy legal requirements" would "elevate form over substance"<sup>244</sup> to the detriment of licensors and licensees. Additionally, critics stressed that retaining quality control in trademark merchandising would not benefit consumers, who often do not expect "a preordained quality level" for promotional products,<sup>245</sup> but instead infringers, who could challenge infringement claims based on the inadequacy of quality control.<sup>246</sup>

Still, despite these criticisms, the traditional standard for the validity of licensing has continued to hold, thus obliging licensors to implement quality control with respect to promotional licenses lest they face claims of naked licensing.<sup>247</sup> Yet, as anticipated, this duty has often proved a formality rather than an actual exercise of control.<sup>248</sup> Notably, even if most agreements included standard quality control provisions, licensors have usually relied on their licensees, and their knowledge of the promotional products, to ensure the quality of the marked goods.<sup>249</sup> This has not translated, however, into a lack of interest for product quality and its consistency on the part of licensors.<sup>250</sup> On the contrary, because promotional products aim precisely at building brand image, product quality has always been of utmost importance for trademark owners, who just choose to delegate the details of the production process, and thus the technicalities of quality control, to licensees.<sup>251</sup>

Naturally, this trend greatly contributed to the general drifting away from a strict enforcement of quality control. Well aware of these issues, the judiciary tried to fit promotional licensing under the current requirement by broadening the interpretation of "adequate control" and affirming that quality control could be effectively

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244. *Id.*

245. Johnston, *supra* note 225, at 35 ("The argument for abolishing the quality control requirement focuses on the fact that in promotional merchandising the consumer does not expect a preordained quality level . . .").

246. Keating, *supra* note 3, at 378; *see* Johnston, *supra* note 225, at 35–36 n.79 (citing Keating, *supra*).

247. Lanham Act § 5, 15 U.S.C. § 1055 (2000).

248. *E.g.*, Johnston, *supra* note 225, at 35–36.

249. *See* discussion *supra* Part III.A.2.

250. The lack of litigation in this respect seems to signify that consumers have been generally satisfied with the quality of promotional products. *See generally* David Kiley, *Best Global Brands: How the BusinessWeek/Interbrand Top 100 Companies Are Using Their Brands to Fuel Expansion*, BUS. WK., Aug. 7, 2006, at 54 (discussing the ability of the nation's top brands to provide consistent customer satisfaction).

251. As elaborated in Part V, trademarks have a self-enforcing feature, and the market will not forgive, in the long term, brand owners who sacrifice quality for short-term gains. *See* discussion *infra* Part V.A; *see also* LANDES & POSNER, *supra* note 84, at 168.

exercised by third parties, including licensees.<sup>252</sup> Yet, while accepting that control at large could also satisfy the legal requirement, courts have turned to the reality of the agreement at issue, and to the consistency of the product quality, to determine its validity.<sup>253</sup>

## 2. *Additional practices inconsistent with "quality control"*

Besides the rise of promotional licensing, additional trademark practices have contributed to the discontinuity between modern trademark licensing and the quality control requirement. In particular, the past two decades have witnessed the expansion of the practice of assignment and license-back, where a trademark owner assigns her mark to an assignee, who in turn grants back to the assignor a license to continue using the mark.<sup>254</sup> Most often, this type of agreement is used by trademark holders as a useful means to settle claims of trademark infringement<sup>255</sup> or to secure priority over a mark in order to assert claims of opposition or trademark infringement.<sup>256</sup> During the past decades, trademark holders have also increasingly adopted this type of agreement to use their marks as collaterals for loans.<sup>257</sup>

The rationale behind this practice, however, profoundly deviates from the traditional view of trademark law.<sup>258</sup> Specifically, the primary purpose for the assignees/licensors is to acquire the control of the assigned mark and avoid claims of trademark abandonment, or laches and acquiescence on the part of future infringers, rather than

252. See discussion *supra* Part III.A.1–2.

253. See discussion *supra* Part III.A.2.

254. Calboli, *Assignment "With Goodwill," supra* note 13, at 795.

255. See 3 MCCARTHY, *supra* note 1, § 18:9 (“[I]n settlement of pending litigation, plaintiff may obtain an assignment of rights in the mark and license back [to] the defendant. If there was evidence of customer confusion, this arrangement would bring commercial reality into congruence with customer perception that plaintiff was controlling defendant’s use.”).

256. See Calboli, *Assignment "With Goodwill," supra* note 13, at 795 (citing *Glow Indus. v. Lopez*, 273 F. Supp. 2d 1095, 1097, 1104 (C.D. Cal. 2003)).

257. The *Restatement (Third) of Unfair Competition* recites:

An assignee may license the assignor to use the trademark after an assignment. If the assignment satisfies the requirements stated in this Section and the subsequent license back to the assignor satisfies the requirements stated in § 33, the priority arising from the assignor’s original use of the trademark is maintained.

§ 34 cmt. c (1995).

258. See discussion *supra* Part II.A. This practice strongly resembles a coexistence agreement between the parties. A coexistence agreement creates “concurrent use rights” in a particular mark. See *Times Mirror Magazines, Inc. v. Field & Stream Licenses Co.*, 103 F. Supp. 2d 711, 713 (S.D.N.Y. 2000), *aff’d*, 294 F.3d 383 (2d Cir. 2002); see also *Indus. Indem. Co. v. Apple Computer, Inc.*, 79 Cal. App. 4th 817, 823, 842 (1999) (further defining coexistence agreements).

entering "substantially similar" businesses.<sup>259</sup> On their part, assignors/licensees enter these transactions primarily to avoid a finding of trademark infringement and to continue using the mark at issue for the same products as prior to the signing of the agreement, rather than producing or distributing under a licensing program. Likewise, when a mark is used as collateral for a loan, the purpose of the agreement for the assignee/licensor/lender is just to acquire nominal control over the mark and, for the assignor/licensee/borrower to continue disposing of it as previously.<sup>260</sup>

As expected, the judiciary has confirmed the validity of this procedure<sup>261</sup> as a "well-settled commercial practice,"<sup>262</sup> further supporting the contention that the judiciary is moving away from quality control. Theoretically, courts have continued to affirm that these transactions are valid only as long as they do not disrupt the continuity of the marked products and provided that assignees/licensors maintain control over their quality.<sup>263</sup> Yet, these limits have proved sterile and formalistic,<sup>264</sup> and the courts have generally relied on the language of the agreement regardless of the effective control exercised by licensors.<sup>265</sup> In other words, by using

259. Calboli, *Assignment "With Goodwill," supra* note 13, at 795.

260. *E.g.*, *Visa, U.S.A., Inc. v. Birmingham Trust Nat'l Bank*, 696 F.2d 1371, 1374 (Fed. Cir. 1982).

261. J. Thomas McCarthy provides an overview of judicial decisions on the issue. *See* 3 MCCARTHY, *supra* note 1, § 18:9 n.4 (citing *Brewski Beer Co. v. Brewski Bros.*, 47 U.S.P.Q.2d (BNA) 1281, 1288-89 (T.T.A.B. 1998)); *Sands, Taylor & Wood v. Quaker Oats Co.*, 18 U.S.P.Q.2d (BNA) 1457, 1467-68 (N.D. Ill. 1990), *aff'd in part and rev'd in part*, 978 F.2d 947 (7th Cir. 1992); *Raufast S.A. v. Kicker's Pizzazz, Ltd.*, 208 U.S.P.Q. (BNA) 699, 702 (E.D.N.Y. 1980); *Syntex Labs., Inc. v. Norwich Pharmaceutical Co.*, 315 F. Supp. 45, 55-56 (S.D.N.Y. 1970), *aff'd*, 437 F.2d 566 (2d Cir. 1971).

262. *See E. & J. Gallo Winery v. Gallo Cattle Co.*, 967 F.2d 1280, 1290 (9th Cir. 1992) (quoting *Visa*, 696 F.2d at 1377). This practice has "the beneficial effect of bringing "commercial reality into congruence with customer perception." *Id.* (citation omitted).

263. *See, e.g.*, *Haymaker Sports, Inc. v. Turian*, 581 F.2d 257, 261 (C.C.P.A. 1978) ("A licensor may license his mark if the licensing agreement provides for adequate control by the licensor over the quality of goods or services produced under the mark by a licensee."); *see Visa*, 696 F.2d at 1377.

264. *See Visa*, 696 F.2d at 1377 ("Contrary to the view of the Board, *it is not determinative* that there was 'no evidence showing to what extent Visa has actually exercised real and effective control over the nature and quality of the services performed by Alpha Beta under the licensed mark.'") (emphasis added).

265. *Glow Indus. v. Lopez*, 273 F. Supp. 2d 1095, 1114-15 (C.D. Cal. 2003).

The language of the agreement demonstrates that [defendant] maintained control over the quality of the . . . products distributed by [the assignor] pursuant to the license-back, and the burden thus shifts to [plaintiff] to demonstrate that [defendant] did not exercise that control. [The assignor]'s lack of recollection [of such control] is not sufficient to meet that burden, and *it must be assumed* . . . that [defendant] maintained control over the quality of the products [the assignor] distributed under the mark.

assignments and licenses-back, trademark owners and other market players bypass the legal requirement for trademark assignment and licensing under the implicit consent of the courts and exchange marks as “things” in the market place as they seem convenient.

Finally, as additional evidence of the growing trend against findings of naked licensing, part of the judiciary has developed the so-called doctrine of “licensee estoppel,”<sup>266</sup> according to which trademark licensees are estopped from challenging the validity of the licensed marks, inter alia, for lack of quality control.<sup>267</sup> In particular, to safeguard licensors and licensing agreements, courts have held that a licensee is estopped from challenging the validity of the licensed mark for the whole duration of the agreement and, should he bring a claim against the mark afterwards, the claim should be limited to facts that arose after the expiration of the contract.<sup>268</sup>

The rationale of this doctrine, according to the courts, is based on equitable principles<sup>269</sup> and is aimed at balancing the interest of the public in challenging invalid marks against that of trademark owners in “predictable contractual relationships.”<sup>270</sup> Yet, in practice, several courts have held that licensee estoppel foreclosed licensees from challenging the licensed mark on the ground that licensors failed to exercise adequate control over the licensing agreements.<sup>271</sup> In addition, even if part of the judiciary has not agreed with this position,<sup>272</sup> courts have consistently affirmed that licensees “should

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*Id.* at 1111 (emphasis added).

266. James M. Treece, *Licensee Estoppel in Patent and Trademark Cases*, 53 IOWA L. REV. 525, 525 (1967).

267. For a general overview of this practice and various situations where licensees may be estopped from bringing claims against licensors, see 3 MCCARTHY, *supra* note 1, § 18:63.

268. See generally *Profl Golfers Ass’n v. Bankers Life & Cas. Co.*, 514 F.2d 665, 671 (5th Cir. 1975) (dismissing claim of abandonment because of uncontrolled licensing during the license because estoppel barred the defense).

269. RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 33 cmt. d (1995) (“[A] court remains free to consider the particular circumstances of the case, including the nature of the licensee’s claim and the terms of the license.”); see *Idaho Potato Comm’n v. M & M Produce Farm & Sales*, 335 F.3d 130, 134–39 (2d Cir. 2003).

270. 3 MCCARTHY, *supra* note 1, § 18:63.

271. See *Creative Gifts, Inc. v. UFO*, 235 F.3d 540, 548 (10th Cir. 2000); *Profl Golfers*, 514 F.2d at 671; *Alpha Tau Omega Fraternity, Inc. v. Pure Country, Inc.*, No. IP 01-1054-C-B/F, 2004 WL 3391781, at \*10 (S.D. Ind. Oct. 26, 2004); *STX, Inc. v. Bauer USA, Inc.*, 43 U.S.P.Q.2d (BNA) 1492, 1500–01 (N.D. Cal. 1997); *Estate of Biro v. Bic Corp.*, 18 U.S.P.Q.2d (BNA) 1382, 1386 (T.T.A.B. 1991); see also RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 33 cmt. d, reporters’ note (1995) (“The case for estoppel is weaker when the licensee asserts a lack of control by the licensor over other users.”).

272. See, e.g., *Sheila’s Shine Prods., Inc. v. Sheila Shine, Inc.*, 486 F.2d 114, 123–24 (5th Cir. 1973); *Miller v. Glenn Miller Prods.*, 318 F. Supp. 2d 923, 945–46 (C.D. Cal. 2004), *aff’d*, 454 F.3d 975 (9th Cir. 2006); *Westco Group, Inc. v. K. B. & Assocs.*, 128 F. Supp. 2d 1082, 1088–90 (N.D. Ohio 2001).

not be permitted to rely upon [their] own conduct of selling non-complying and inferior goods . . . as a basis for challenging the adequacy of quality control exercised by the trade mark owner."<sup>273</sup> Similarly, courts have agreed that the licensees who resisted complying with quality standards are not permitted to challenge the validity of marks at issue, arguing that such non-compliance constitutes inadequate control.<sup>274</sup>

In summary, even if the courts have emphasized that licensee estoppel aims at safeguarding "predictable contractual relationships," this doctrine has increasingly permitted the judiciary to relax the application of quality control to the point of excluding licensees from bringing claims of naked license. Admittedly, most often licensees may not have a direct interest in bringing such claims since they also have a specific interest in the validity of the licensed mark.<sup>275</sup> Still, in some instances, they may also have valid reasons for such challenges.<sup>276</sup> As a result, this doctrine confirms the growing inclination of the courts to treat marks as property, and as such, to apply equitable principles to them, including overlooking lack of quality control and upholding the licensing contractual relationship as long as it does not bring harm to the public.

#### B. *Toward a De Facto Abandonment of "Quality Control"?*

In light of the above, it seems clear that modern trademark licensing is drifting away from, and in some instances has already de facto abandoned, the requirement of quality control as traditionally intended by the courts and the Lanham Act in 1946.<sup>277</sup> As indicated in Part II, this trend has directly followed the general shift toward the "proPERTIZATION" of trademark protection and the resulting willingness of courts and legislators to protect trademarks as things per se on the basis of the impairment of the marks, regardless of consumer confusion.<sup>278</sup>

Notably, and well aware of the growing importance of licensing both as a business technique and source of revenues, courts have repeatedly proven reluctant in adopting a conservative approach to trademark licensing and requiring a strict application of quality

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273. See 3 MCCARTHY, *supra* note 1, § 18:63 (citing *Leatherwood Scopes Int'l v. Leatherwood*, 63 U.S.P.Q.2d (BNA) 1699 (T.T.A.B. 2002); *Westco Group*, 128 F. Supp. 2d 1082)).

274. *Id.*

275. See discussion *supra* Part II.B.1.

276. 3 MCCARTHY, *supra* note 1, § 18:63.

277. Parks, *supra* note 5, at 545; Lemley, *supra* note 17, at 1714.

278. See discussion *supra* Part II.A.



control.<sup>279</sup> Likewise, the judiciary has generally favored, or at least tolerated, practices such as merchandising and assignment and license-back, whose primary objectives are to exploit the value, and control the use, of trademarks *per se*.<sup>280</sup> In addition, the judiciary itself has applied equitable principles to trademark licensing and developed the doctrine of licensee estoppel to protect licensors and licensing contracts regardless of the lack of quality control.<sup>281</sup>

Still, despite this shift toward protecting trademark rights in gross, the judiciary has never officially repealed or formally criticized the current standard for the validity of licensing.<sup>282</sup> Instead, courts have adopted a pragmatic position that reaches a compromise between the need to foster business endeavors and the traditional rationale of trademark law—protecting consumers and the market.<sup>283</sup> A growing number of courts have increasingly focused on the final quality of products when assessing the validity of licensing and have “assumed” that control was exercised where quality remained consistent and the public was not deceived, even if licensors did not strictly monitor their licensees.<sup>284</sup>

Undoubtedly, this approach has allowed the judiciary to provide licensors and licensees with a more flexible standard without the need to challenge the current requirement.<sup>285</sup> Despite this obvious advantage, however, the shift toward licensing *de facto* with minimal or no control has eroded, slowly but steadily, the scope of quality

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279. See discussion *supra* Part III.A.1–2.

280. See Keating, *supra* note 3, at 372; see also Franklyn, *Liability for Trademark Licensees*, *supra* note 26, at 14 (“In promotional licensing, the trademark functions primarily as an advertising tool, not as an indicator of the physical source of the goods or that the goods are of the same quality as all other goods bearing the same mark.”).

281. See *Creative Gifts, Inc. v. UFO*, 235 F.3d 540, 548 (10th Cir. 2000) (“The licensee is estopped from claiming any rights against the licensor which are inconsistent with the terms of the license. . . . He is estopped from contesting the validity of the mark . . . or challenging the license agreement. . . .” (quoting 3 CALLMAN, *supra* note 7, § 19:48)); see also discussion *supra* Part IV.A.2.

282. See, e.g., *Barcamerica Int’l USA Trust v. Tyfield Imps., Inc.*, 289 F.3d 589, 595–96 (9th Cir. 2002) (“It is well-established that ‘[a] trademark owner may grant a license and remain protected provided quality control of the goods and services sold under the trademark by the licensee is maintained.’” (quoting *Moore Bus. Forms, Inc. v. Ryu*, 960 F.2d 486, 489 (5th Cir. 1992))); see also Kitterman, *supra* note 140, at 516 (“Though many merely pay lip service to the quality control obligation . . . the requirement that some degree of quality control actually be exercised remains effective.”).

283. See discussion *supra* Part III.A.1–2.

284. See, e.g., *Taco Cabana Int’l, Inc. v. Two Pesos, Inc.*, 932 F.2d 1113, 1121 (5th Cir. 1991), *aff’d*, 505 U.S. 763 (1992); *Transgo, Inc. v. Ajac Transmission Parts Corp.*, 768 F.2d 1001, 1017 (9th Cir. 1985); *Land O’Lakes Creameries, Inc. v. Oconomowoc Canning Co.*, 330 F.2d 667, 670–71 (7th Cir. 1964).

285. See discussion *supra* Part III.A.2.

control, which has increasingly been reduced to a sterile requirement.<sup>286</sup> Still, since quality control continues to be the formal standard for the validity of licensing, a minority of the courts have continued to require actual proof of control to uphold licensing agreements, thus creating further uncertainty as to what constitutes a valid license.<sup>287</sup> As elaborated in Part V, this uncertainty is no longer sustainable and the time has come to provide a consistent standard for the validity of licensing that will bridge the gap between the current de facto situation, the desire of licensors and licensees to exploit their marks, and the need to protect consumers and the market against unscrupulous licensing.<sup>288</sup>

#### V. THE CASE FOR ABANDONING "QUALITY CONTROL"

As described in Parts II, III, and IV, the general trend seems to favor a flexible standard for the validity of licensing. Since the implementation of the Lanham Act, courts have adopted an increasingly broad interpretation of quality control and accepted almost any evidence to declare licensing valid. Additionally, they have required a very high burden of proof to declare the forfeiture of trademark rights and have also upheld licensing de facto without control. This trend, however, has not established a clear path of acceptance for licensing without control, and the outcomes of judicial decisions are still proving inconsistent.<sup>289</sup>

This Part stresses the failures of the current requirement and advocates for a change allowing licensing "with or without control" as long as the public is not deceived.<sup>290</sup> This Part argues that this change

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286. See *Taco Cabana*, 932 F.2d at 1121 (requiring only "adequate control" for trademark licensing); *Ky. Fried Chicken Corp. v. Diversified Packaging Corp.*, 549 F.2d 368, 387 (5th Cir. 1977) ("Retention of a trademark requires only minimal quality control . . ."); see also *Parks*, *supra* note 5, at 538 (claiming the quality control requirement is outdated and useless).

287. *Ritchie v. Williams*, 395 F.3d 283, 290 (6th Cir. 2005); *Barcamerica Int'l*, 289 F.3d at 596–97; *Halo Mgmt., L.L.C. v. Interland, Inc.*, 308 F. Supp. 2d 1019, 1028–31 (N.D. Cal. 2003).

288. See generally *Parks*, *supra* note 5, at 538–41 (discussing the problems created for trademark owners and courts when quality control is defined inconsistently).

289. See discussion *supra* Part III.B.

290. *Calboli*, *Assignment "With Goodwill," supra* note 13, at 828–41. As I have indicated above, see *supra* note 13, the arguments in favor of a legislative change toward a regime of trademark assignment "with or without goodwill" and those in favor of licensing "with or without control" are partially similar, in particular with respect to the failures and the ambiguities surrounding the respective requirements. As a result, the reader may encounter some similarities between the main text of this section and the corresponding footnotes, and the text and footnotes in *Calboli*, *Assignment "With Goodwill," supra* note 13, at 828–41. As indicated earlier, however, all the arguments and reference used in this section are originally targeted toward supporting my claim in favor of licensing "with or without control."

will restore consistency between the standard for the validity of licensing and its subsequent interpretation and enforcement. Despite common criticism, this change will not adversely affect consumers, for the courts have alternative and better tools to protect the purchasing public. Additionally, it will prevent superfluous legal actions initiated by competitors whose ultimate goal is not to safeguard consumers, but to control the course of trade.<sup>291</sup>

#### A. *The Intrinsic Flaws of "Quality Control"*

As repeatedly noted, the adoption of the quality control requirement has traditionally rested on the belief that requiring trademark owners to exercise such control increases the chances of continuity in product quality.<sup>292</sup> As this Article has highlighted, however, the reality of trademark practice has called into question this assumption, and courts have interpreted and enforced the quality control standard inconsistently at best.<sup>293</sup> As a result, the original goal of the requirement—protecting consumers and competition—has often not been achieved, whereas trademark owners and licensees continue to wonder what constitutes valid licensing under the current standard.<sup>294</sup> Once again, the lack of a consistent and clear definition of what represents "quality control" primarily accounts for such uncertainty.<sup>295</sup> Not surprisingly, this uncertainty has brought increasing criticism, calling for the abandonment of the current requirement.<sup>296</sup>

The reasons for much of this uncertainty can be uncovered by revisiting the rationale of the requirement and, in particular, by highlighting its obvious flaws. Notably, despite the general intention behind it, the adoption of quality control has never included a direct prohibition that licensees do not modify product quality. Instead, the letter of the law has only required that licensors "control" licensees with respect to the "nature and quality" of the marked products so as

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291. See Friedman, *supra* note 15, at 373; see also Noel Gillespie, *Licensing and the "Related Companies" Doctrine*, 12 J. CONTEMP. LEGAL ISSUES 209, 210–11 (2001); Parks, *supra* note 5, at 538–41.

292. See 1 MCCARTHY, *supra* note 1, § 3:10 ("[A] trademark . . . could also serve to indicate a level of consistent quality.").

293. See *supra* Part III.A–B.

294. See Parks, *supra* note 5, at 536–37; see also Bannon, *Revisiting "The Rational Basis of Trademark Protection," supra* note 15, at 65.

295. See discussion *supra* Part III.A–B.

296. See Parks, *supra* note 5, at 557 ("[T]he quality control requirement should be abandoned as a rule of law. The failure of the strict quality theory of marks means that, in reality, there is no reasoned basis on which to distinguish licensed from non-licensed trademarks, and to impose vague, ad hoc quality requirements on licensed goods only."); see also Keating, *supra* note 3, at 378–79.

to not "deceive the public."<sup>297</sup> In other words, trademark owners have been legally obligated only to monitor their licensees who, in turn, have been obligated only to refrain from using the mark misleadingly.<sup>298</sup> As a result, quality control has never truly guaranteed, but merely facilitated, continuity in product quality, in the hope that, because of trademark owners' control, licensees would not change product quality or face claims of invalid licensing.<sup>299</sup>

In addition, the current requirement imposes the duty to maintain consistent product quality only to trademark owners that are licensors and not to all trademark owners. In other words, trademark law has never questioned the ability of non-licensor trademark owners to change the quality of their products<sup>300</sup> provided that the public is not deceived,<sup>301</sup> yet the law has historically restricted the ability of trademark licensors to effect such changes. Not surprisingly, licensors and practitioners have lamented this differential treatment, for which no sound legal reasoning has been offered and which cannot "be justified in the name of the public interest"<sup>302</sup> since the public "has no collective 'right' to prevent licensors from making the same subjective business decisions concerning the quality of marked

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297. See Lanham Act § 5, 15 U.S.C. § 1055 (2000); see also Bannon, *Revisiting "The Rational Basis of Trademark Protection,"* *supra* note 15, at 77 ("The consumer understands the mark to function as a proclamation of the producer's commitment that all goods bearing the identical mark will be consistent in 'nature, quality, and characteristics.'" (citation omitted)).

298. Generally, trademark owners and licensees are the primary beneficiaries of consistent product quality. Landes and Posner provide an accurate analysis of this aspect of trademark. Specifically, they stress that "trademarks have a self-enforcing feature" and that "[t]hey are valuable only insofar as they denote consistent quality, and so[,] only a firm able to maintain consistent quality has an incentive to expend the resources necessary to develop a strong trademark." LANDES & POSNER, *supra* note 84, at 168.

299. See discussion *supra* Part II.B; see also Calboli, *Assignment "With Goodwill,"* *supra* note 13, at 829–30 (elaborating a similar argument against the rule on trademark assignment).

300. As indicated in Calboli, *Assignment "With Goodwill,"* *supra* note 13, at 830 n.317, the "New Coke" case clearly exemplified this point. In that case, Coca-Cola, Inc. decided to discontinue its traditional cola and produce, instead, the "New Coke." Yet, the market reacted very negatively to such change, and accordingly the company decided to reinstate the traditional cola under the name "Coca-Cola Classic." See Michael Bastedo & Angela Davis, *God, What a Blunder: The New Coke Story*, COLA FOUNTAIN, Dec. 17, 1993, <http://web.archive.org/web/20060515214006/http://members.lycos.co.uk/thomassheils/newcoke.htm>; see also Parks, *supra* note 5, at 545–47 (discussing the faults of the quality assurance theory).

301. Deceptive trademarks are subject to cancellation according to section 14(c). Lanham Act § 14(c), 15 U.S.C. § 1064(3). Section 2(a) of the Lanham Act also expressly prohibits the registration of trademarks that are "deceptive." 15 U.S.C. § 1052(a). *E.g.*, *In re Budge Mfg. Co.*, 857 F.2d 773, 776 (Fed. Cir. 1988); *Bureau Nat'l Interprofessionnel Du Cognac v. Int'l Better Drinks Corp.*, 6 U.S.P.Q.2d (BNA) 1610, 1616 (T.T.A.B. 1988).

302. Parks, *supra* note 5, at 537.

goods as are made by non-licensors."<sup>303</sup> Furthermore, the current requirement does not consider that, at times, quality variations may be required, or suitable, to respond to changes in product standards and market demands.<sup>304</sup> Accordingly, to prevent licensors and licensees from changing product quality could possibly affect their very existence in the marketplace.<sup>305</sup> As a result, to deny licensors and licensees this flexibility may eventually undermine their abilities to compete in the marketplace.

The increasing use of promotional licensing among many sectors of the market has brought additional criticisms to quality control.<sup>306</sup> As repeatedly noted, this type of licensing usually involves the use of a mark on unrelated products<sup>307</sup> whose quality can rarely be monitored effectively by trademark owners because of their lack of direct expertise in the field. Instead, trademark owners delegate such control to their licensees and simply ensure that all products bearing their marks share the same quality once in the market.<sup>308</sup> Accordingly, if "[i]n promotional trademark licensing, failure of the licensor to maintain quality-control of the product . . . does not constitute . . . misrepresentation,"<sup>309</sup> it is thus increasingly difficult to sustain the idea that the same requirement should be applied to traditional trademark licensing. Similarly, the increasing use of trademark strategies such as assignments and licenses-back, and the development of judicial doctrines such as licensee estoppel have also called into question the validity of quality control and the extent to which it satisfies the current needs of the marketplace.<sup>310</sup>

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303. *Id.*

304. Car emission standards, environmental requirements, food and drug requirements, and labeling requirements are examples where businesses/trademark owners are obliged to change the quality of their products. *See generally id.* at 545-46 (discussing some of these mandatory requirements).

305. *See Calboli, Assignment "With Goodwill," supra* note 13, at 833-36 (making a similar argument against the rule of assignment "with goodwill").

306. *See* discussion *supra* Part IV.A.1.

307. Keating, *supra* note 3, at 365-69.

308. *See Marks, supra* note 5, at 650-53.

So long as the public obtains what it expects, there is no harm to the trademark, whether or not quality controls are exercised by the licensor. Only if the licensee changes the quality of the goods, for better or for worse, are expectations upset and only then could the trademark be denigrated or diminished. In such case, the licensor has an obligation to act and to reassert quality control standards over the marketing and distribution of the goods, if possible.

*Id.* at 654.

309. *See id.* at 653; *see also id.* (noting that "in this type of marketing the consumer does not expect a preordained quality level").

310. *See* discussion *supra* Part IV.A.2.

To respond to these problems, courts have opted for a realistic approach, defined quality control broadly,<sup>311</sup> and accepted a vast range of evidence to prove that control had, in fact, been exercised. Courts have also increasingly focused their analysis on whether the public has been deceived as the result of variations in product quality. Lastly, they have refrained from voiding licensing agreements with the exception of cases where consumer deception was beyond any doubt.<sup>312</sup>

As indicated earlier, the main reason courts have been hesitant to declare trademark licenses invalid is their fear that trademark infringers will exploit this argument to support a defense that their accusers have "unclean hands."<sup>313</sup> In other words, rather than protecting consumers damaged by differences in the quality of the marked products, quality control most often protects infringers who use the requirement as a counterclaim to divert the court's attention from the infringement itself.<sup>314</sup> Indeed, most courts agree that consumers do not have standing under the Lanham Act.<sup>315</sup> Similarly, nobody, not even the USPTO, has the duty to monitor whether or not trademark owners comply with the requirement of quality control, and licensors are not obliged to present evidence of such control to anyone.<sup>316</sup> Certainly, this lack of supervision and the fact that the enforcement of quality control is left to the discretion of

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311. See discussion *supra* Part III.A.1–2.

312. See discussion *supra* Part III.A.1–2.

313. The "unclean hands" defense is often asserted affirmatively as a counterclaim for cancellation of the plaintiff's trademark registration pursuant to sections 14 and 37 of the Lanham Act. See 15 U.S.C. § 1064 (2000) (regarding the power of a private party to apply for cancellation of a registration); *id.* § 1119 (regarding the power of the court to cancel registration); see also 6 MCCARTHY, *supra* note 1, § 31:44–58 (discussing extensive case law on this aspect).

314. See, e.g., *Everett O. Fisk & Co. v. Fisk Teachers' Agency, Inc.*, 3 F.2d 7, 9 (8th Cir. 1924), *superseded by statute*, Lanham Act § 5, Pub. L. No. 489, 60 Stat. 427, 429 (1946); *In re Celanese Corp. of Am.*, 136 U.S.P.Q. (BNA) 86, 87–88 (T.T.A.B. 1962).

315. Although the trademark statute extends the right to bring a civil action to "any person," Lanham Act § 43, 15 U.S.C. § 1125(a)(1), courts have usually denied that the general public has standing under the Lanham Act. See, e.g., *Seven-Up Co. v. Coca-Cola Co.*, 86 F.3d 1379, 1383–87 (5th Cir. 1996); *Serbin v. Ziebart Int'l Corp.*, 11 F.3d 1163, 1170 (3d Cir. 1993); *Dovenmuehle v. Gildorn Mortgage Midwest Corp.*, 871 F.2d 697, 699–701 (7th Cir. 1989); *Colligan v. Activities Club of N.Y., Ltd.*, 442 F.2d 686, 691–94 (2d Cir. 1971); see also 5 MCCARTHY, *supra* note 1, § 27:39 (discussing consumer and non-commercial standing to sue).

316. See Jennifer Rudis Deschamp, *Has the Law of Products Liability Spoiled the True Purpose of Trademark Licensing? Analyzing the Responsibility of a Trademark Licensor for Defective Products Bearing Its Mark*, 25 ST. LOUIS U. PUB. L. REV. 247, 271 (2006) ("[T]rademark licensors have an existing obligation to monitor the licensees and exercise control over the quality of the goods produced bearing their trademarks.").

competitors (and defendants) have contributed to the uncertainty surrounding the requirement.<sup>317</sup>

Finally, courts' reluctance to embrace the quality control standard stems from the serious implication of voiding a trademark license. If a trademark owner has allowed another party to invalidly use its mark, the mark may be declared abandoned or cancelled, and the trademark owner will have forfeited its right to use the mark. Thus, "a finding of abandonment through insufficient control means that multiple sources can sell products . . . of varying quality under the mark, enhancing the risks of consumer deception and confusion."<sup>318</sup> Paradoxically, this would harm rather than help consumers, for without the guarantee that a mark stands for a certain product of a certain quality, consumers will have to invest more time and money into deciding which products to buy. In other words, if a mark is cancelled and returned to the public domain where multiple parties may freely use it, consumers will have a very difficult time identifying the product they originally sought from the many products that now bear the same mark, and they will thus face a greater chance of deception than if the licensing agreement had been upheld as valid.<sup>319</sup>

### B. *The Need for a Better Rule on Modern Trademark Licensing*

In the light of the above, it seems undisputable that the current standard for the validity of trademark licensing has been reduced, in practice, to a formalistic and confusing requirement, which is also out of touch with the needs of modern manufacturing and distribution.<sup>320</sup> As this Article has demonstrated, the judiciary is just as responsible for this situation. Courts have in fact interpreted quality control erratically and inconsistently, and, in some instances, have declared agreements valid even without control as long as the public is not

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317. See Parks, *supra* note 5, at 561 ("[T]he 'public protection' afforded by trademark laws is indirect, flowing from successful infringement suits which remove infringing marks from the market place, thereby eliminating public confusion as to the true source of marked goods."); see also Calboli, *Assignment "With Goodwill," supra* note 13, at 831-32 (elaborating a similar argument against the rule of assignment "with goodwill").

318. Gillespie, *supra* note 291, at 211; Hanak, *supra* note 8, at 367.

319. See Rudolph J. Kuss, Comment, *The Naked Licensing Doctrine Exposed: How Courts Interpret the Lanham Act to Require Licensors to Police Their Licensees & Why this Requirement Conflicts with Modern Licensing Realities & the Goals of Trademark Law*, 9 MARQ. INTELL. PROP. L. REV. 361, 384-86 (2005). But see Johnston, *supra* note 225, at 26-27; Noah D. Genel, Note, *Keep It Real: A Call for a Broader Quality Control Requirement in Trademark Law*, 8 FORDHAM INTELL. PROP. MEDIA & ENT. L.J. 269, 291 (1997).

320. Parks, *supra* note 5, at 531.

confused.<sup>321</sup> Recent trademark practices such as promotional licensing, assignments and licenses-back, and the doctrine of licensee estoppel have also proven incompatible with the traditional interpretation of quality control.<sup>322</sup>

As elaborated earlier, this judicial indulgence toward licensing can best be explained by considering the growing importance and use of this practice in the economy during the past century.<sup>323</sup> Generally, besides adopting a broad interpretation and accepting a vast range of evidence to prove the existence of control, courts have also established very high burdens of proof for claimants before declaring trademark rights forfeited due to naked licensing.<sup>324</sup> Only in a minority of cases has the judiciary reverted to a conservative approach and declared licensing without control invalid. Still, trademark owners and licensees continue to be left with many doubts as to the conditions upon which they can license their marks or use them, and predicting judicial responses represents a risky, and potentially costly, business.<sup>325</sup>

This situation must be addressed. Today's economy heavily relies on the use of licensing in most sectors of the market, both for the production and distribution of goods and services, and such uncertainty clearly jeopardizes the ability of trademark owners and licensees to compete in the marketplace. Thus, "[i]f it is true that ambiguities [have always] characterize[d] trademark law because of its social, emotional, and irrational basis,"<sup>326</sup> the legal system cannot impose upon trademark owners and licensees the burden to rely on "an unpredictable [judicial] rule of reason"<sup>327</sup> to decide how to structure valid licensing agreements. Accordingly, this Article advocates for a change in the current rule in favor of a new, and

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321. See discussion *supra* Part III.A.2.

322. See discussion *supra* Part IV.A.1-2.

323. See, e.g., Steven P. Mandell et al., *Drafting Software and Trademark Licenses for Litigation*, 845 PLI/PAT 795, 822 (2005) ("Trademark licensing is big business. The trademark licensing business has grown into nearly a \$100 billion industry in the U.S. alone."); Marks, *supra* note 5, at 645-48.

324. E.g., Oberlin v. Marlin Am. Corp., 596 F.2d 1322, 1326-27 (7th Cir. 1979); Heaton Distrib. Co. v. Union Tank Car Co., 387 F.2d 477, 485 (8th Cir. 1967); Embedded Moments, Inc. v. Int'l Silver Co., 648 F. Supp. 187, 194 (E.D.N.Y. 1986); Syntex Labs., Inc. v. Norwich Pharmacal Co., 315 F. Supp. 45, 56 (S.D.N.Y. 1970), *aff'd*, 437 F.2d 566 (2d Cir. 1971); Susser v. Carvel Corp., 206 F. Supp. 636, 641-43 (S.D.N.Y. 1962), *aff'd*, 332 F.2d 505 (2d Cir. 1964); Morse-Starrett Prods. Co. v. Steccone, 86 F. Supp. 796, 805 (N.D. Cal. 1949).

325. See 3 MCCARTHY, *supra* note 1, § 18:10 (discussing the rule against assignment in gross); see also Calboli, *Assignment "With Goodwill," supra* note 13, at 832-33 (stressing the same problem with respect to the judicial application of the rule on assignment).

326. Calboli, *Assignment "With Goodwill," supra* note 13, at 833.

327. *Id.*



better, standard, which will resolve most of the current controversy and provide more flexibility for competitors, while still protecting the public against confusion and deception.

1. *It is time to adopt licensing with or without "quality control"*

Considering the current situation, a change toward a regime of more flexible licensing, and particularly of licensing "with or without quality control," seems to represent the only viable solution to resolve the intrinsic flaws of the present standard.<sup>328</sup> Accordingly, following the position de facto adopted by part of the judiciary, this Article suggests that licenses should be considered automatically valid regardless of trademark owners' actual control when product quality stays the same or when, if variations in quality have occurred, licensors and licensees have taken all necessary measures to inform consumers to prevent deception.<sup>329</sup> In particular, considering that quality control has traditionally found its statutory basis in the definition of "related company" as per Section 45, this Article advocates for an amendment to the language of Section 45 by erasing any reference to the "control" that trademark owners should supposedly exercise.<sup>330</sup> Instead, a "related company" should be defined as "any person whose use of a mark is authorized by the owner of the mark provided that such mark is not used to deceive the public with respect to the nature and quality of the goods or services on or in connection with which the mark is used."<sup>331</sup>

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328. Parks, *supra* note 5, at 558.

Elimination of the quality control requirement will result in the consistent treatment of licensing and non-licensing trademark owners. Licensors will no longer be forced to attempt adherence to indefinite standards of "quality" and "control," at the risk of a judicial holding (however rare) that a licensed mark has been "abandoned" through uncontrolled licensing. Rather, like their non-licensing counterparts, licensors will be free to market goods and services at quality levels consistent with their own business judgment.

*Id.*

329. See, e.g., *Miller v. Glenn Miller Prods.*, 454 F.3d 975, 992 (9th Cir. 2006) ("A license agreement need not contain an express quality control provision because trademark law, rather than the contract itself, confers on the licensor the right and obligation to exercise quality control."). But note that most cases do not designate a license as "automatically" valid, but rather describe conditions in which an agreement may be determined to be automatically invalid.

330. Currently, section 45 defines "related company" as "any person whose use of a mark is controlled by the owner of the mark with respect to the nature and quality of the goods or services on or in connection with which the mark is used." Lanham Act § 45, 15 U.S.C. § 1127 (2000); see also discussion *supra* Part II.B.

331. See Parks, *supra* note 5, at 568 (advocating for a similar change to the definition of "related company" in section 45 so that the term "would be construed to include any entity which has been granted a license by the trademark owner, regardless of the license terms").

Despite the criticisms expressed by some scholars and part of the judiciary against "free" licensing,<sup>332</sup> the suggested amendment will provide a better standard for the validity of licensing, while still fostering consumer protection. First, this amendment will bring the statute in line with the majority of judicial decisions and business reality. More importantly, however, it will eliminate the major flaw in the current rule—the impossibility to define quality control consistently. Instead, the proposed amendment will focus the validity of licensing directly on whether the public has been deceived, thus providing a much clearer guideline for trademark owners compared to the erratic judicial interpretation of quality control.<sup>333</sup>

This new approach would also close a loophole often used by trademark infringers to escape liability. As stressed earlier, defendants in trademark infringement suits often use the quality control standard to argue that plaintiffs invalidly licensed their mark and thus have "unclean hands" and have forfeited their claim of trademark infringement.<sup>334</sup> Under the new standard proposed by this Article, defendants would still be entitled to question the validity of the license at issue, but the validity would not rest on the amount of control exercised by the licensor. On the contrary, the validity of the license would depend on whether the public would be deceived when purchasing the marked product sold by the licensee.<sup>335</sup> As a result, the public and the market will benefit from this change since trademark owners will focus on actual quality and consumer deception rather than on control, while litigants will likely refrain from bringing frivolous suits, thus saving costs and time to the legal system as a whole.<sup>336</sup>

The proposed change in the definition of Section 45 will also bring uniformity between the statutory definition of "related company" and the language of Section 5 of the Lanham Act. As indicated earlier,

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332. See Lemley, *supra* note 17, at 1710–11; see also *In re Roman Cleanser Co.*, 802 F.2d 207, 208–09 (6th Cir. 1986); *Money Store v. Harriscorp Fin., Inc.*, 689 F.2d 666, 676–77 (7th Cir. 1982).

333. See discussion *supra* Part III; see also Calboli, *Assignment "With Goodwill," supra* note 13, at 834 (propping up a new rule of assignment "with or without" goodwill).

334. See discussion *supra* Part III.A.

335. To elaborate on the scenarios in the Introduction, courts will thus invalidate the license at issue and possibly declare the forfeiture of trademark rights if two identically looking HARLEY-DAVIDSON T-shirts or YANKEES hats, which are sold in the same premises on the same shelf, prove to be of different quality. Likewise, courts will invalidate the license if the GE phone or SAMSUNG television proves to be of different quality than the item in the show room or advertised in the newspaper.

336. Parks, *supra* note 5, at 558; Friedman, *supra* note 15, at 364 (generalizing some of the practical problems that courts and consumers face when trying to grasp the meaning of the current quality control standard).

Section 5 does not mention or require direct control on the part of licensors over their licenses.<sup>337</sup> The provision simply requires that the mark not be “used in such a manner as to deceive the public.”<sup>338</sup> Considering that several courts have already adopted a similar position in practice and either found evidence of control when control was minimal or nonexistent, or directly stated that actual control was not necessary, a change toward licensing with or without control will have the beneficial effect of bringing the language of the provision in line with reality.<sup>339</sup>

Furthermore, a change in the current requirement will restore consistency between the requirement for the validity of licensing and modern trademark practices such as promotional licensing and, *inter alia*, assignments and licenses-back. As elaborated in Part IV, even amidst the skepticism of some courts and scholars,<sup>340</sup> the economic relevance of promotional licensing is only destined to grow,<sup>341</sup> and a clearer standard for the validity of this practice is much needed both for consumers and trademark owners. Similarly, despite the argument that trademark rights do not exist in gross, trademarks are increasingly treated, and exchanged, as things in and of themselves, as demonstrated daily by modern trademark practices.<sup>342</sup> Accordingly, to adopt a more flexible standard for the validity of licensing that still focuses primarily on consumer deception will benefit the market while providing clearer guidance for licensors and licensees. Equally importantly, this new standard will also bring national trademark law closer to the approach followed by the

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337. See discussion *supra* Part III.A.

338. Lanham Act § 5, 15 U.S.C. § 1055 (2000); see Keating, *supra* note 3, at 378 (stating that the Lanham Act merely prohibits the use of a trademark to misrepresent goods, and does not expressly require quality control).

339. See Parks, *supra* note 5, at 531 (“[T]he quality control requirement should be abandoned as a legal fiction that lacks a sound theoretical foundation, has no practical benefits, and is inconsistent with the realities of the modern market place.”).

340. See generally Dogan & Lemley, *supra* note 34, at 466 (criticizing the theoretical justification of trademark merchandising).

341. Marks, *supra* note 5, at 646–47.

Over the last few years, the volume of merchandising activity has grown by several hundred percent as a few specific examples will show. In 1978, Walt Disney Productions reported \$21.3 million in licensing royalties based on \$427 million in retail sales of licensed products. In 1983, Yves Saint Laurent S.A. showed a gross income of \$27 million, of which \$17 million was derived from licensing.

*Id.* (footnote omitted).

342. See *id.* at 652 (discussing the development and growth of promotional trademark licensing).

majority of other countries, thus eliminating many inconsistencies to the advantage of international trade.<sup>343</sup>

Lastly, the suggested amendment will directly benefit consumers by enhancing the ability of trademark owners to compete in the marketplace. Under the new rule, licensors and licensees will be allowed to alter the quality of the marked products to satisfy not just legal requirements but also market demand and consumer needs,<sup>344</sup> as long as they apply these changes to the whole production,<sup>345</sup> or the public could otherwise be deceived.<sup>346</sup> Trademark owners will also enjoy more flexibility in monitoring their licensees and, more importantly, will not fear unfounded claims of naked licensing in response to their legitimate claims of infringement. This could save costs in administering licenses and licensing portfolios and, in turn, these savings could translate into cheaper prices for marked products to the benefit of consumers.<sup>347</sup>

The proposed amendment will also benefit consumers by preventing cases where licensors and licensees decide to discontinue production due to the fact that their mark has been cancelled because of lack of quality control, regardless of whether or not the public was deceived. In these occurrences, consumers and competition are greatly affected since the number of products available in the market is reduced, even in the absence of consumer confusion. Yet, to allow licensing "with or without" control will limit these occurrences to truly unscrupulous agreements to the benefit of consumers, who will not otherwise see their product choices reduced.<sup>348</sup> The same applies when, considering that trademark cancellation allows other interested parties to use the mark, licensors

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343. See 2 LADAS, *supra* note 222, §§ 715–720; see also discussion *supra* Part IV.A.

344. See Marks, *supra* note 5, at 651 ("Trademark theory should provide for consumer protection, but it should also be flexible enough to permit satisfactory adaptation to new situations." (quoting William M. Borchard & Richard M. Osman, *Trademark Sublicensing and Quality Control*, 70 TRADEMARK REP. 99, 114 (1980))); see also Hanak, *supra* note 8, at 367.

345. Differences in quality standards required by state laws would represent the only exception to this rule. Friedman, *supra* note 15, at 373.

346. Interestingly, courts have denied consumer confusion in cases where such confusion was, instead, very clear. See, e.g., *Jordan v. Nissan N. Am., Inc.*, 853 A.2d 40, 44 (Vt. 2004) (dismissing a consumer fraud claim because of the fact that the public was not aware that parts of Nissan Quests were produced by Ford Motor Company); *Szajna v. Gen. Motors Corp.*, 503 N.E.2d 760, 771 (Ill. 1986) (denying that the mark "Pontiac Ventura" was per se a guarantee of the quality of the car components).

347. See Calboli, *Assignment "With Goodwill," supra* note 13, at 834 (considering similar arguments to support assignment "with or without goodwill").

348. For a discussion on the economic aspects of trademark protection, particularly with respect to the distinctive function of trademarks, see discussion, *supra* Part II.A.

and licensees have to incur extra costs to rename their products and market them under the new name. Not surprisingly, these extra costs impact the ability of trademark owners and licensees to compete in the market and ultimately work to the detriment of consumers, who eventually will carry parts of these costs.<sup>349</sup> To amend the current requirement as suggested will thus prevent these additional costs in most circumstances by limiting trademark cancellation to agreements that are truly misleading and unfair for the market.

## 2. *Protecting consumers and the market under the new rule*

Despite the many benefits listed above, any shift toward licensing “with or without control” must still guarantee that the public will receive accurate information about the quality of the marked products. In other words, even under the suggested amendment, licensors and licensees should not be able to use “free” licensing to deceive or confuse purchasers, because the primary function of trademark law is to protect consumers and the market.<sup>350</sup> As stressed earlier, consumers are not “legally entitled to receive goods and services of the same quality,”<sup>351</sup> yet licensors and licensees cannot betray their trust on certain marks by providing, misleadingly and without notice, products qualitatively different from those previously identified by them.<sup>352</sup>

A shift toward licensing with or without control, however, will not affect the protection that is currently available to consumers and the market, should licensors and licensees decide to use a mark to defraud the public trust. In particular, from a general standpoint, an amendment to the current language of the Lanham Act will leave unaffected the current provisions against consumer fraud; that is, licensors and licensees will be as liable to consumers for the quality of their products as they are today under the current standard. Accordingly, the public and the market will continue to rely upon the remedies granted by consumer protection and product liability laws

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349. See Marks, *supra* note 5, at 648–49, on the costs of licensing. Marks considers, in particular, the costs incurred by companies that are less sophisticated in policing and controlling a popular trademark in licensing contexts. *Id.*

350. See Calboli, *Assignment “With Goodwill,” supra* note 13, at 836 (stressing that a regime of assignment in gross will not necessarily detriment competition).

351. *Id.* at 836.

352. On the contrary, trademark owners should be held liable for consumer fraud and face the civil and criminal consequences provided by the law. For some of the relevant provisions, see, for example, Magnuson-Moss Warranty—Federal Trade Commission Improvement Act, 15 U.S.C. §§ 2301–2312 (2000), and Consumer Product Safety Act, 15 U.S.C. §§ 2051–2085 (2000 & Supp. IV 2004). See also RESTATEMENT (SECOND) OF TORTS § 402B (1965) (amended 1998 by RESTATEMENT (THIRD) OF TORTS: PROD. LIAB. § 9).

against any misleading use of a mark.<sup>353</sup> Likewise, even if more enforcement could be desirable in these areas of the law in practice,<sup>354</sup> those engaged in abusive licensing will continue to be held liable for commercial fraud, and pay the consequences provided by civil and criminal laws.<sup>355</sup>

The proposed change will also leave untouched the role currently played by the Federal Trade Commission ("FTC") under Section 14(5) of the Lanham Act<sup>356</sup> in protecting consumers against the misleading use of trademarks.<sup>357</sup> Specifically, according to the provision, "the Federal Trade Commission may apply to cancel . . . any mark"<sup>358</sup> on the grounds that, inter alia, a mark has become generic, has been registered fraudulently, or misrepresents the source of the marked products.<sup>359</sup> Even if the FTC has rarely enforced this rule,<sup>360</sup> a transition towards a system of "free" licensing will not affect its ability to act and cancel trademark registration should any of the conditions listed in the law arise in practice.<sup>361</sup>

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353. See, e.g., 15 U.S.C. §§ 2301–2312 (regulating product warranties for the public and outlining the role of the Federal Trade Commission); *id.* § 2051 (relating congressional findings and statements of purpose designed to protect and assist the public against risks "associated with consumer products"); see also Franklyn, *The Apparent Manufacturer Doctrine*, *supra* note 3, at 675 (arguing that trademark licensors should be subjected to liability under the apparent manufacturer doctrine when a licensor induces consumers to believe that the licensor controlled the standards for manufacturing the product).

354. Franklyn, *The Apparent Manufacturer Doctrine*, *supra* note 3, at 721.

355. See, e.g., 15 U.S.C. § 2069 (providing civil penalties for the violation of 15 U.S.C. § 2068); *id.* § 2070 (providing for criminal penalties for the violation of 15 U.S.C. § 2068); see also Calboli, *Assignment "With Goodwill," supra* note 13, at 841 (noting that the same provisions will continue to operate in a regime of assignment "with or without goodwill").

356. 15 U.S.C. § 1064(5) (2000); see Calboli, *Assignment "With Goodwill," supra* note 13, at 841 n.360 (highlighting the role of the FTC with respect to the misleading use of trademarks in the context of trademark assignment).

357. See *Jacob Siegel Co. v. FTC*, 327 U.S. 608, 611–12 (1946) (reaffirming the power of the FTC in these areas). "The Commission has wide discretion in its choice of a remedy deemed adequate to cope with the unlawful practices in this area of trade and commerce." *Id.* at 611.

358. Lanham Act § 14(5), 15 U.S.C. § 1064(5).

359. Lanham Act § 14(3), 15 U.S.C. § 1064(3). The FCT can also cancel a certification mark, at any time, when the mark is in use without the owner's control or if the mark's use may mislead the public. Lanham Act § 14(5), 15 U.S.C. § 1064(5).

360. See Hanak, *supra* note 8, at 373 (stressing that "the Commission rarely has used the authority granted" while pointing out one "notable" exception found in *Bart Schwartz International Textiles, Ltd. v. Federal Trade Commission*, 289 F.2d 665 (C.C.P.A. 1961)).

361. *Bart Schwartz*, 289 F.2d 665 (C.C.P.A. 1961), represents the most noticeable example where the FTC used its authority to restore fair market competition and consumer protection under the Lanham Act. "The obligation which the Lanham Act imposes on an applicant is that he will not make *knowingly* inaccurate or *knowingly* misleading statements in the verified declaration forming a part of the

In addition, the role of supervision of the FTC is not limited to the wording of the Lanham Act. Notably, under Section 5 of the Federal Trade Commission Act ("FTCA"),<sup>362</sup> the FTC is granted the authority to prevent, in general, acts of unfair competition. This capacity also extends to all instances where a mark is used to deceive or confuse the public.<sup>363</sup> In this respect, the FTC has often enforced its power, warning trademark owners not to use their marks misleadingly and prohibiting "the use of trademarks that inherently are deceptive."<sup>364</sup> Here again, the proposed standard will not affect the status quo, and the FTC will continue to operate in the same capacity to protect consumers and competition in the marketplace.<sup>365</sup>

Furthermore, from a strict trademark law standpoint, occurrences involving abusive licenses—whether under a regime of "free" licensing or "with quality control"—will continue to fall within the provision of Sections 14 and 45 of the Lanham Act, and courts can continue to use these rules to declare unfair licensing invalid and cancel the corresponding marks.<sup>366</sup> Even more importantly, the

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application for registration." *Id.* at 669. See *FTC v. Wolf*, No. 94-8119, 1996 U.S. Dist. LEXIS 1760, at \*14 (S.D. Fla. Jan. 30, 1996).

362. 15 U.S.C. §§ 41-58 (2000 & Supp. V 2005).

363. According to Section 5(a)(1) of the FTCA, "[u]nfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful." 15 U.S.C. § 45(a)(1). Section 5(n) defines "unfair" practices as practices that "cause . . . or [are] likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or to competition." *Id.* § 45(n).

364. Hanak, *supra* note 8, at 373. Interesting examples in this respect are *R. Neumann & Co. v. Overseas Shipments, Inc.*, 326 F.2d 786, 788 (C.C.P.A. 1964), where the court denied registration for potentially misleading mark, and *Gaffrig Performance Indus. v. Livorsi Marine, Inc.*, No. 99 C 7822, 2003 U.S. Dist. LEXIS 23018, at \*58 (N.D. Ill. Dec. 19, 2003), where the court canceled a misleading trademark registration. "It is well settled by the decisions of this court and other courts of competent jurisdiction that no trademark rights can be acquired in a trademark that is deceptive or deceptively misdescriptive." *Neumann*, 326 F.2d at 788.

365. In addition, the suggested amendment will not increase the cost of FTC's supervision over misleading uses of trademarks since it does not add any new power to the FTC. Simply, it demands that the FTC will continue to control the correct functioning of the market as it has done, or should have done, until present. See Calboli, *Assignment "With Goodwill," supra* note 13, at 841 (stating that a rule of assignment "with or without goodwill" will not affect the FTC's ability to regulate the market); see also Arthur Best, *Controlling False Advertising: A Comparative Study of Public Regulation, Industry Self-Policing, and Private Litigation*, 20 GA. L. REV. 1, 20-25 (1985); Thomas L. Ruffner, *The Failed GE/Honeywell Merger: The Return of Portfolio-Effects Theory?*, 52 DEPAUL L. REV. 1285, 1299 (2003) (briefly outlining the FTC's role in the marketplace).

366. See Calboli, *Assignment "With Goodwill," supra* note 13, at 837 (making a similar argument against the rule of assignment "with goodwill"); cf. *Dawn Donut Co. v. Hart's Food Stores, Inc.*, 267 F.2d 358, 367 (2d Cir. 1959) ("If the licensor is not compelled to take some reasonable steps to prevent misuses of his trademark in the hands of others the public will be deprived of its most effective protection against

proposed amendment will leave untouched the provision of Section 43(a) of the Lanham Act under which competitors can bring civil suits, at any time, if a mark has been registered fraudulently or is used to mislead the public as to the origin of the marked products.<sup>367</sup> Accordingly, competitors will continue to be able to call upon this rule to bring actions against abusive licensors and licensees<sup>368</sup> and courts will retain the ability to cancel, or declare abandoned, the marks at issue also under a standard of licensing "with or without control."<sup>369</sup>

Simply put, under the proposed standard, courts will focus directly on the result of licensing—whether consumers are confused or misled—rather than on the conduct of licensors—whether they exercised quality control—to assess the validity of the agreements at

misleading uses of a trademark. . . . Clearly the only effective way to protect the public where a trademark is used by licensees is to place on the licensor the affirmative duty of policing in a reasonable manner the activities of his licensees.").

367. See Lanham Act § 43(a), 15 U.S.C. § 1125(a) (2000):

(a) Civil action

(1) Any person who, on or in connection with any goods or services, or any container for goods, uses in commerce any word, term, name, symbol, or device, or any combination thereof, or any false designation of origin, false or misleading description of fact, or false or misleading representation of fact, which—

(A) is likely to cause confusion, or to cause mistake, or to deceive as to the affiliation, connection, or association of such person with another person, or as to the origin, sponsorship, or approval of his or her goods, services, or commercial activities by another person, or  
(B) in commercial advertising or promotion, misrepresents the nature, characteristics, qualities, or geographic origin of his or her or another person's goods, services, or commercial activities, shall be liable in a civil action by any person who believes that he or she is or is likely to be damaged by such act.

*Id.*; see also Calboli, *Assignment "With Goodwill," supra* note 13, at 837–38 (noticing that the provision will continue to operate under a regime of assignment "with or without goodwill").

368. See *supra* note 315. As indicated by 5 MCCARTHY, *supra* note 1, § 27:39, "[a]t one point in Congress, a House version of the bill which eventually led to the Trademark Law Revision Act and the rewriting of § 43(a) contained language expressly giving consumers the right to sue for a violation of § 43(a)." *Id.* (citing H.R. REP. NO. 100-1028, at 13–15 (1988)). However, "the provision was deleted in a House-Senate Conference Committee." *Id.* McCarthy also points out that "Representative Kastenmeier inserted a statement in the record to the effect that he believed that consumers have standing under the case law and that the deleted consumer standing proposal would only have 'clarified that law.'" *Id.* (citing 134 CONG. REC. H10419 (daily ed. Oct. 19, 1988) (statement of Rep. Kastenmeier)). In support of consumer standing under the Lanham Act, see Tawnya Wojciechowski, *Letting Consumers Stand on Their Own: An Argument for Congressional Action Regarding Consumer Standing for False Advertising Under Lanham Act Section 43(a)*, 24 SW. U. L. REV. 213 (1994).

369. Unfortunately, courts have never held that inconsistent product quality amounts to a violation of Section 43(a) of the Lanham Act under the theory that inconsistent product quality misrepresents the marked good or services. Parks, *supra* note 5, at 552–53.



issue. Courts will then assess variation in product quality as part of a general assessment of the validity of the contracts under scrutiny and, to this end, will use the provision of Sections 14 or 45, or Section 43(a), to establish whether any existing difference is likely to deceive the purchasing public. Since, however, trademark licensing often extends to unrelated products, courts should consider quality variations primarily among the same kind of products—that is, RALPH LAUREN sunglasses versus RALPH LAUREN sunglasses, and not other RALPH LAUREN products. Specifically, courts should evaluate whether any existing difference in quality is likely to deceive the public by using factors similar to those that are traditionally used to establish trademark infringement.<sup>370</sup> Ultimately, courts should invalidate any agreement where even a minor part of the public is likely to be deceived by a different product quality. Courts should allow agreements to stand when confusion and deception cannot be found.<sup>371</sup>

Generally, when assessing the consistency of product quality, courts should also consider whether any variation in such quality is required by law<sup>372</sup> and should presume licenses valid as long as all new products

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370. For a general overview of the factors taken into account by the courts while assessing trademark infringement, see GRAEME B. DINWOODIE & MARK J. JANIS, *TRADEMARKS AND UNFAIR COMPETITION: LAW AND POLICY* 469–71 (2004). In particular, although no list of factors is per se exclusive, factors listed by the Second Circuit in *Polaroid Corp. v. Polaroid Electronics Corp.*, 287 F.2d 492 (2d Cir. 1961), are often cited as the most complete:

[T]he prior owner's chance of success is a function of many variables: the strength of his mark, the degree of similarity between the two marks, the proximity of the products, the likelihood that the prior owner will bridge the gap, actual confusion, and the reciprocal of defendant's good faith in adopting its own mark, the quality of defendant's product, and the sophistication of the buyers.

*Id.* at 495.

371. Accordingly, as long as all HARLEY-DAVIDSON T-shirts or YANKEES hats that are sold in the same premises and on the same shelf, i.e., as the same items to the public, are of identical quality, courts should allow the license at issue to stand regardless of whether the trademark owners exercised any control. The same is applicable to all other scenarios in the Introduction: as long as the quality of the same marked products is identical, i.e., consumers cannot be deceived, courts should not declare licenses invalid because of lack of quality control.

372. Product quality is not only affected by licensor and licensee control, but also by laws, regulations, and consumer demand. For example, many restaurants, including franchising chains such as MCDONALD's, have recently changed well-known recipes in order to eliminate trans fats from their menus, in response to a demand for healthier products. See Jeannine DeFoe, *Food Makers Get on a Health Kick: PepsiCo, Kraft, and others are making strides in reducing trans fats and producing healthier foods to meet consumer demand*, BUS. WK. ONLINE, Dec. 14, 2006, [http://www.businessweek.com/print/investor/content/dec2006/pi20061214\\_187559.htm](http://www.businessweek.com/print/investor/content/dec2006/pi20061214_187559.htm); see also 21 C.F.R. § 101.45 (2007) (detailing strict labeling requirements for foods containing trans fats). To return to the examples offered in the Introduction, GE phones and SAMSUNG TVs also change over time as technology progresses and new product

follow the new quality guidelines.<sup>373</sup> However, if quality variation applies only to part of the marked products without a specific reason, such as changes in state laws or geographical differences,<sup>374</sup> courts should presume the licenses invalid because the public could be deceived.<sup>375</sup>

Finally, courts should look at the efforts that licensors and licensees have undertaken to notify the public of any variation in product quality.<sup>376</sup> In particular, courts should not invalidate agreements when the packaging of the products or the premises where they are sold contain disclaimers or labels that exhaustively indicate the quality variation so that the average consumer will unlikely be mistaken about the actual quality of the products at issue.<sup>377</sup> Traditionally, courts have looked at disclaimers with diffidence, yet even if part of the public will not be aware of the commercial advertising the new quality of GE phones, or pay attention to the labels and signs on the seller's premises indicating the changes in the quality of SAMSUNG televisions or RALPH LAUREN sunglasses, these actions can serve as evidence that licensors and licensees

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lines reach the market. Consumers demand new technology, and as new products are introduced into the market, quality changes. For example, GE's website offers an innovation timeline that lists three to four "innovations" per year, including the releases of new technology (phones and otherwise) into the market. General Electric, Explore the Innovation Timeline, <http://www.ge.com/innovation/timeline/index.html> (last visited Sept. 30, 2007).

373. See *supra* note 371.

374. See, e.g., Friedman, *supra* note 15, at 375 (considering the quality control requirement in the context of permissible variable uses of similar trademarks in diverse geographical areas).

375. See *supra* note 367; see also Calboli, *Assignment "With Goodwill," supra* note 13, at 838–39 (elaborating a similar test for a proposed rule of assignment "with or without goodwill").

376. "Courts have uniformly held that an adequate explanation negates the possibility of deception and hence the loss of trademark rights." Hanak, *supra* note 8, at 374. Specifically, the author uses the case of *Hy-Cross Hatchery, Inc. v. Osborne*, 303 F.2d 947 (C.C.P.A. 1962), as an example where the court "held that a change in the breed of chickens did not constitute grounds for cancellation of the trademark when 'the type of chick appears to have been otherwise indicated by the trademark.'" Hanak, *supra* note 8, at 374 (citation omitted). Hanak also discusses the decision in *Menendez v. Faber, Coe & Gregg, Inc.*, 345 F. Supp. 527 (S.D.N.Y. 1972), where "enforceable rights in a trademark formerly applied to cigars made exclusively in Cuba of Cuban tobacco were not forfeited when the mark was applied to cigars made in Florida of non-Cuban tobacco since the fact was stated on the cigar boxes." Hanak, *supra* note 8, at 374.

377. See *Carter v. Joseph Bancroft & Sons Co.*, 360 F. Supp. 1103, 1106–08 (E.D. Pa. 1973); Franklyn, *The Apparent Manufacturer Doctrine, supra* note 3, at 707; see also Lynn M. LoPucki, *Toward a Trademark-Based Liability System*, 49 UCLA L. REV. 1099, 1119–21 (2002) (discussing the use of disclaimers by trademark owners with respect to the use of trademarks by licensees).

adopted adequate means to inform, and did not intend to mislead, consumers.<sup>378</sup>

Notices to the public will not help consumers when licensors or licensees intend to act in bad faith and still take advantage of consumer reliance on a certain mark.<sup>379</sup> These instances, however, represent clear examples of consumer fraud and accordingly, as mentioned earlier, should be punished as such by using the tools that are already available to the courts.

#### CONCLUSION

As consumers, we will likely not care whether HARLEY-DAVIDSON, the YANKEES, or WESTLAW control the manufacturers of their promotional products, as long as the quality of these products is the same or we are made aware of any changes. Likewise, we will likely not care whether PIZZA HUT, GE, or SAMSUNG control their licensees as long as the products we buy are identical to those advertised and shown in the store before our purchases. Yet should one of these marks ever be cancelled or declared abandoned because its owner has not sufficiently controlled its licensees, we would undoubtedly be confused if a third party with no connection to the original business started to use the mark.

As this Article has illustrated, a trademark licensor's failure to control its licensees does not necessarily trigger consumer deception. Instead, such deception is generally triggered by the (unfair) actions of licensors and licensees. Although indirectly, courts have confirmed this view by increasingly upholding licensing with minimal or no control as long as consumers are not deceived. Still, the official standard continues to hold trademark owners liable for the lack of quality control, thus leaving the door open to judicial inconsistency as to what represents valid licensing. The suggested amendment in favor of licensing "with or without control" will resolve this inconsistency and finally reconcile the conditions for the validity of licensing with the market necessity of a flexible standard on this issue. Even if many will criticize it, this amendment will not have negative consequences on consumers, and the judiciary has many alternative ways to enforce and prevent deceptive and confusing licensing. In

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378. See Hanak, *supra* note 8, at 374 (stating that clearly explaining any changes in the product to the public may preclude a finding of deception); see also Calboli, *Assignment "With Goodwill," supra* note 13, at 837 (underlying the role of disclaimers in support of assignment "with or without goodwill").

379. See Hanak, *supra* note 8, at 374–75 (describing a case in which a token change in labeling was not adequate to overcome a finding of deception).

addition, it is likely to improve competition in the marketplace, and accordingly should be welcomed by all parties.

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