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Patents, Trademarks, and Copyrights

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PATENTS, TRADEMARKS, AND COPYRIGHTS

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Introduction

The Tenth Circuit this term considered a variety of cases which involved intellectual property. Of particular interest to franchisers and franchisees is the decision in *Redd v. Shell Oil Co.*,[1] in which the Tenth Circuit reversed the decision of the District Court for the District of Utah that Shell's restrictions on the use of its trademark "Shell" for gasoline constituted an illegal tying arrangement under the Sherman Act.[2] *Redd* and *Value House v. Phillips Mercantile Co.*,[3] another trademark case worthy of note, are discussed in greater detail below.

In *CMI Corp. v. Metropolitan Enterprises, Inc.*[4] the Tenth Circuit upheld an opinion of the District Court for the Western District of Oklahoma on the question of patent validity but remanded the case on the issue of patent infringement.[5] Implicit in the decision was a holding that the district court's factual findings comparing the processes of the parties' method patents were clearly erroneous.[6] The district court had given heavy evidentiary weight to the appellant's advertising materials. Descriptions of the process in these materials contradicted those presented at trial; therefore, the district court had held appellant estopped to deny those prior assertions.[7] While the Tenth Circuit agreed that those representations should be considered, it held that the prior

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1 524 F.2d 1054 (10th Cir. 1975), *cert. denied*, 425 U.S. 912 (1976).

2 15 U.S.C. §§ 1-7 (1970).

3 523 F.2d 424 (10th Cir. 1975).

4 534 F.2d 874 (10th Cir. 1976).

5 *Id.* at 878.

6 *See id.* at 883.

7 *Id.* at 876.

statements did not form "a proper basis for an estoppel,"[8] and furthermore that they could not "serve to controvert what is clearly demonstrated to be the actual fact."[9]

Two appeals to the Tenth Circuit were related to copyright and trademark activity but turned on other issues. In *United States v. Blanton*[10] defendants' conviction for criminal infringement of copyrighted sound recordings was upheld after an appeal based primarily on criminal procedure grounds.[11] In *Medco Products Co. v. Commissioner*[12] legal expenses incurred in asserting a trademark were held not to be deductible as ordinary and necessary business expenses, since their origin was capital in nature.[13]

I. *Redd v. Shell Oil Co.*, 524 F.2d 1054 (10th Cir. 1975)

During the past term, an important trademark case arose on appeal from the United States District Court for the District of Utah. The district court had, by summary judgment, dramatically extended the application of per se antitrust tying theories from the field of "rent-a-name" franchises to the field of "distributor" franchises.[14] For only the second time in its history, the United States Trademark Association filed an amicus curiae brief.[15] The Tenth Circuit reversed the summary judgment of the district court and limited antitrust tying violations strictly to the prior precedent involving only "rent-a-name" franchises.[16] The United States Supreme Court denied certiorari.[17]

The facts were simple. Redd had entered into a sales contract with Shell as a jobber, or distributor, of "Shell" gasoline manufactured by Shell. Redd was not restricted in distribution of gasoline from other companies or sources. The sales contract specifi-

[8] *Id.* at 884.
[9] *Id.* at 883.
[10] 531 F.2d 442 (10th Cir.), *cert. denied*, 425 U.S. 935 (1976).
[11] 531 F.2d at 444.
[12] 523 F.2d 137 (10th Cir. 1975).
[13] *Id.* at 139.
[14] *See* 182 U.S.P.Q. 280 (D. Utah 1974).
[15] 65 TRADEMARK REP. 511 (1975).
[16] Redd had relied on Siegel v. Chicken Delight, Inc., 448 F.2d 43 (9th Cir. 1971), for its assertion that a trademark was a separate product for antitrust tying purposes. The *Chicken Delight* situation involved a trademark franchiser whose primary product was its name. In *Redd* the product involved was gasoline which was identified to its source of origin by a trademark. 524 F.2d at 1057.
[17] 425 U.S. 912 (1976).

cally restricted Redd to use of the trademark "Shell" only on gasoline acquired from Shell. Redd, however, purchased gasoline at a significantly lower cost from another supplier and distributed that gasoline as "Shell" gasoline. Upon acquiring knowledge of Redd's substitution activities, Shell demanded that Redd cease this practice. Redd immediately brought an action in federal district court, alleging that Shell's restrictive provision violated per se the antitrust laws based upon *Siegel v. Chicken Delight, Inc.*[18] Shell countersued for trademark infringement.

The Tenth Circuit held that Redd was guilty of trademark infringement and that Shell's activities did not constitute a violation of the antitrust laws. This section is based on the trademark infringement holding. A brief discussion of the history of trademark law, in light of the facts of this particular case, ensues, and a summary of the *Chicken Delight* standard and its respective limits also is presented.

A. *Evolution of Trademark "Value"*

The United States Supreme Court in *United Drug Co. v. Theodore Rectanus Co.*[19] recognized the role of trademarks in the United States: "Its 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."[20]

Earlier, the Supreme Court in *Menendez v. Holt*[21] recognized that the trademark owner need not be the manufacturer of the goods on which the trademark is used.

The growth in the United States of the use of trademarks is unsurpassed in commerce. As the United States Supreme Court has recognized:

> The protection of trade-marks is the law's recognition of the psychological function of symbols. If it is true that we live by symbols, it is no less true that we purchase goods by them. A trade-mark is a merchandising short-cut which induces a purchaser to select what he wants, or what he has been led to believe he wants. The

[18] 448 F.2d 43 (9th Cir. 1971).
[19] 248 U.S. 90 (1918).
[20] *Id.* at 97.
[21] 128 U.S. 514, 520 (1888).

> owner of a mark exploits this human propensity by making every effort to impregnate the atmosphere of the market with the drawing power of a congenial symbol. Whatever the means employed, the aim is the same—to convey through the mark, in the minds of potential customers, the desirability of the commodity upon which it appears.[22]

Unfortunately, in early evolution, the common law of trademarks was adjudicated on a state-by-state basis, leading to nonuniformity of protection for trademark owners. Trademark rights were awarded only on a territory of use basis.[23] This Balkanization of trademark common law was substantially eliminated by the passage of the Federal Lanham Act in 1946.[24] Section 45 of that Act incorporated, however, the common law concept of a trademark: "The term trade-mark includes any word, name, symbol, or device, or any combination thereof adopted and used by a manufacturer or merchant to identify his goods and distinguish them from those manufactured or sold by others."[25] With the passage of the Lanham Act, a trademark owner upon using a mark in interstate commerce could for the first time register the mark with the federal government and be accorded nationwide protective rights in his mark—even in those territories not yet entered.

One provision of the Lanham Act provided the impetus for the growth of a new business tool—that of the franchise system. Section 5 of the Lanham Act specifically provides:

> Where 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 its registration, provided such mark is not used in such manner as to deceive the public.[26]

The phenomenal growth of franchise operations in American business has been well documented.[27] A significant portion of these businesses involve trademark licensing franchise systems.[28]

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[22] Mishawaka Mfg. Co. v. Kresge Co., 316 U.S. 203, 205 (1942).

[23] *See* 2 J. McCARTHY, TRADEMARKS AND UNFAIR COMPETITION § 26.1 (1973).

[24] *See id.* § 26.13.

[25] 15 U.S.C. § 1127 (1970).

[26] *Id.* § 1055.

[27] D. THOMPSON, FRANCHISE OPERATION AND ANTITRUST 26-40 (1971).

[28] Pelton, Fisher, & Prestia, *Tying and Trademark Franchising: A Look at the Developing Case Law,* 3 AM. PAT. L.A.J. 254 (1976).

Such operations provide predictable quality for consumers, security and guidance for franchisees, and may well provide for lower failure rates than is common in nonfranchised businesses.[29] Yet attempts by franchisers to control various aspects of franchisee activity have been criticized as being anticompetitive.[30]

B. *Antitrust Tying Restrictions on Franchise Trademark Use*

In *Siegel v. Chicken Delight, Inc.*[31] the Ninth Circuit held that the trademark owner (franchiser) had violated the antitrust laws by requiring its franchisees to purchase certain supplies only from the franchiser. The franchiser made no use of the mark and merely licensed other people to use it. Such use of a trademark has been termed a "rent-a-name" use.[32] In this case the franchise operated as "Chicken Delight" and was required to buy mixes, paper plates, napkins, cooking utensils, and the like from the franchiser at significantly higher prices than such commodities were priced from other sources. The Ninth Circuit stated:

> The burgeoning business of franchising has made trade-mark licensing a widespread commercial practice and has resulted in the development of a new rationale for trade-marks as representations of product quality. This is particularly true in the case of a franchise system set up not to distribute the trade-marked goods of the franchisor, but, as here, to conduct a certain business under a common trade-mark or trade name. Under such a type of franchise, the trademark simply reflects the goodwill and quality standards of the enterprise which it identifies. As long as the system of operation of the franchisees lives up to those quality standards and remains as represented by the mark so that the public is not misled, neither the protection afforded the trade-mark by law nor the value of the trademark to the licensee depends upon the source of the components.[33]

The purpose of this article is not to challenge the soundness of the *Chicken Delight* case; however, its logic is specious. The Ninth Circuit concluded: "Just as the patent or copyright forecloses competitors from offering the distinctive product on the market, so the registered trade-mark presents a legal barrier

[29] D. THOMPSON, *supra* note 27, at 33-34.
[30] *Id.* at 55-123.
[31] 448 F.2d 43 (9th Cir. 1971).
[32] McCarthy, *Trademark Franchising and Antitrust: The Trouble with Tie-ins*, 58 CALIF. L. REV. 1085, 1086 (1970).
[33] 448 F.2d at 48-49 (footnotes omitted).

against competition."[34] Yet a trademark differs markedly from a patent or a copyright. Patents and copyrights are constitutionally protected monopolies—no other person or company can manufacture a patented or copyrighted article without infringement thereof.[35] Patents and copyrights present true barriers to competition. However, a trademark presents no such barrier and would, rather, seem to enhance competition. The use of a trademark does not prevent others from offering the same product but merely prevents others from using a confusingly similar trademark to offer their products. The value to the public, and hence the enhancement of competition, is the public's ability to identify between the *same* competing products.

The soundness of the *Chicken Delight* holding notwithstanding, the facts of the *Shell* case simply did not fall within the teachings of *Chicken Delight.* In fact, *Chicken Delight* specifically limited itself to the case of a franchise system "set up not to distribute the trademarked goods."[36] Chicken Delight, Inc. neither raised nor sold chickens but merely franchised a method of doing business, which it tied to purchases of common items such as paper products. The *Chicken Delight* decision specifically limited its findings of a tie-in to those situations "where the tied product is not itself the product represented by the mark."[37]

J. Thomas McCarthy, a recognized expert in the law of trademarks, has distinguished between "rent-a-name" and "distributing" franchises as follows: "In those franchises where the franchisor manufactures nothing itself, but really is in the business of selling a franchise package consisting primarily of the trademark license, it appears correct to characterize the trademark as a tying item and designated items as tied-in."[38] Professor McCarthy defines "distributing franchises" as having as their "primary purpose . . . to provide the franchisor with a system for marketing his wares, either at the wholesale or retail level."[39]

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[34] *Id.* at 50.

[35] *Contra,* Susser v. Carvel Corp., 332 F.2d 505, 513 (1964) (Lumbard, C.J., dissenting in part). Judge Lumbard felt the economic power generated by a trademark was indistinguishable from that generated by a copyright or patent. His analysis is commented on in Pelton, Fisher, & Prestia, *supra* note 28, at 262.

[36] 448 F.2d at 48.

[37] *Id.* at 52.

[38] McCarthy, *supra* note 32, at 1109.

[39] *Id.* at 1089.

With regard to these types of distributing franchises, he states: "The franchisee who is primarily a conduit through which products made by the franchisor flow to consumers is in a somewhat different position. He can legitimately be required to deal exclusively in his franchisor's line of products."[40] Perhaps on a prophetic note concerning the *Redd* case, McCarthy continues: "Similarly, a gasoline refiner might properly require its own brand of gas to be pumped from leased pumps and tanks bearing its trademark, but cannot require a dealer to sell only a designated brand of tires, batteries, and accessories without violating the prohibition against tying."[41]

If the Tenth Circuit had upheld the district court's summary judgment that Shell's acts constituted a per se tying relationship, then the entire evolution of trademark law would have been ignored. The amicus curiae brief of the United States Trademark Association stated:

> [T]he decision below will have an adverse impact on those systems of distribution in which manufacturers sell products bearing their trademarks through independent distributors. Many products are thus distributed to retailers or to the public. Shell, for example, distributes its gasoline and other petroleum products to its dealers through jobbers such as Redd.
>
> If Shell could be required to furnish its jobbers with standards and specifications so that they can sell non-Shell gasoline under the SHELL trademark, then other manufacturers would be obligated to do likewise with the distributors of their branded merchandise. As a result a distributor of branded merchandise, such as appliances, automobiles, etc., would be free to sell under the brand name or trademark products which were neither made nor selected by the trademark owner. The trademark would then no longer identify source but only quality, and any product which the user believes to meet the quality could be sold thereunder. The resultant system would be the functional equivalent of having no trademarks at all.[42]

Confusion and lack of business certainty result from a situation in which distributors or even retailers sell, for example, "Ford" cars not manufactured by Ford or "IBM" typewriters not made by IBM. Fixing responsibility for repairs would be chaotic.

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[40] *Id.* at 1118.

[41] *Id.* at 1109 (footnote omitted).

[42] 65 TRADEMARK REP. 511, 523 (1975) (footnote omitted). *Contra, A Review of Recent Tenth Circuit Decisions*, 1976 UTAH L. REV. 227, 239-41.

C. *The Tenth Circuit Holding In* Redd *Is Eminently Correct*

The Tenth Circuit opinion in *Redd* carefully distinguished between Redd's position as a jobber ("not doing business as Shell Oil Company")[43] and that of a franchisee. Emphasizing that trademark use in this case was permissive, the court concluded that in such circumstances the trademark could not be held to be a separate product for purposes of antitrust law.[44] The court singled out the following facts: (1) The gasoline was sold as a trademarked product; (2) no one else in the market sold the Shell trademark; and (3) Shell did not sell the trademark separately.[45] For the court to extend the rule of the Chicken Delight situation to such a "typical sale of a trademark product"[46] would have been unwarranted.

D. *Conclusion*

Had the Tenth Circuit upheld the district court, then the Tenth Circuit would have condoned and approved Redd's acts of unfair competition. Redd had sought to palm off cheaper gasoline as gasoline coming from Shell; yet Redd was not paying Shell for the privilege of using the "Shell" mark as is the situation in the "rent-a-name" franchises. Redd was simply attempting to force Shell, at virtually no profit to Shell, to maintain quality control standards over any gasoline sold by Redd.

In truth, Redd had chosen to use an identical trademark, "Shell," on an identical product, gasoline, in direct competition with Shell. This is per se trademark infringement—per se unfair competition. It flies in the face of our common law heritage and the whole philosophy of the Lanham Act.

II. *Value House v. Phillips Mercantile Co.*, 523 F.2d 424 (10th Cir. 1975)

In *Value House* the Tenth Circuit restated the relationship between trademarks registered under the Lanham Act[47] and al-

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[43] 524 F.2d at 1056.

[44] *Id.* at 1057.

[45] *Id.*

[46] *Id.*

[47] 15 U.S.C. §§ 1052-1127 (1970).

leged infringing marks which were in use prior to that registration.[48]

Plaintiff began using the name "The Value House" in Maine in 1961 and was granted federal registration for that tradename in October of 1969. Without knowledge of the plaintiff's use of the name, defendant adopted on or about May 1, 1968, the name "Value House" in connection with its retail business in New Mexico and registered the mark under the New Mexico Trademark Act[49] on August 5, 1968.[50]

Plaintiff began to expand outside of Maine in 1969 and now has business locations in Maine and six other eastern states.[51] After discovering defendant's use of a nearly identical name in a similar business, plaintiff brought suit in federal district court for trademark infringement, claiming under the Lanham Act a right to exclusive use of the name throughout the United States. The court dismissed plaintiff's complaint and granted defendant's counterclaim by issuing an injunction restraining plaintiff from using the name in New Mexico, western Texas, and southern Colorado.[52] The Tenth Circuit upheld both the ruling on infringement and the injunctive relief.[53]

The court of appeals rejected each of the plaintiff's arguments after holding there was no error in the findings of fact of the trial court.[54] The Tenth Circuit held that, although plaintiff had used the tradename first, the defendant did not have knowledge of that prior use.[55] Thus, since defendant's use preceded plaintiff's registration, the constructive notice provision in section 22 of the Lanham Act could not apply.[56]

The court also concluded that, although the Lanham Act provides for registration with constructive notice and affords nationwide protection, the remedies section of the statute limits a

[48] For a discussion of this limited area defense, see 2 J. McCarthy, *supra* note 23, § 26.18 (1973).

[49] N.M. Stat. Ann. § 49-4-6 to -12 (1953).

[50] 523 F.2d at 427.

[51] *Id.*

[52] *Id.* at 426.

[53] *Id.* at 430-32.

[54] *Id.* at 426-27.

[55] *Id.* at 428.

[56] *Id.* at 429 (applying 15 U.S.C. § 1072 (1970)).

defendant's liability to instances in which the defendant's use is intended to cause confusion or mistake or to deceive.[57] Since there had been no finding of actual confusion or even of any customers in common, the Tenth Circuit held plaintiff had no basis for a remedy.[58] Defendant had also innocently adopted the use of the mark prior to plaintiff's registration and was, therefore, entitled to a prior use defense.[59]

The court rejected the plaintiff's common law infringement claim on the grounds that the parties had established rights to their widely separated markets.[60] In addition the preservation of defendant's geographical market against any future expansion by plaintiff was upheld.[61] Thus, under *Value House*, the owner of a registered trademark may be permanently prevented from using the name in the geographic area of an innocent user.[62]

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[57] Lanham Act § 32, 15 U.S.C. § 1114(1) (1970).

[58] 523 F.2d at 429.

[59] *Id.* at 430. 15 U.S.C. § 1115(b)(5) requires that such use must precede *registration*. The court, therefore, also rejected the plaintiff's argument that the date of filing should be the determining date. 523 F.2d at 430. 15 U.S.C. § 1052(d) provides that concurrent registration may be granted only if prior use occurs before the *filing* date. Plaintiff argued that the disparity between the operative dates in the two sections would produce the anomalous result of an innocent user being able to preserve concurrent use though not eligible for concurrent registration. The court limited its analysis to the plain meaning of the statute. The two sections, however, are reconcilable. The key date for analysis of defenses is the date of registration, which cuts off the prior use defense. But in a concurrent use proceeding neither party yet owns a registration. Some prior date would, therefore, logically be required.

[60] 523 F.2d at 430-31.

[61] *Id.* at 432.

[62] *Id.* Only after an abandonment by defendant or "other changed circumstances" might the decree be reexamined. *Id.*