Goodwill Appropriation as a Distinct Theory of Trademark Liability: A Study on the Misappropriation Rationale in Trademark and Unfair Competition Law

Apostolos Chronopoulos*

I. Introduction ................................................................. 254
II. Trademarks as Part of Unfair Competition Law: A Balancing Exercise ........ 257
III. Trademarks and Product Differentiation: An Economic Analysis .......... 265
    A. Trademarks as Marketing Instruments Incorporating Goodwill .......... 265
    B. Trader Interests in Perspective: Market Power and Brand Extensions .... 266
    C. Welfare Aspects of Dynamic Competition With Differentiated Products .................................................. 269
        1. The Theory of Monopolistic Competition .................................. 269
        2. Product Variety and Social Welfare ........................................ 270
            a. Locational Competition .................................................. 271
            b. Locational Competition in Product Space ............................ 271
            c. Cluster Effects .................................................................. 273
    D. Trademarks and Barriers to Entry ........................................... 273
    E. Advertising: Informative, Persuasive or Simply a Complementary Good? ...................................................... 274
    F. Acquisition and Maintenance of Monopoly Power Through Persuasive Advertising ............................................. 276
    G. Goodwill Protection, Market Niches and Economic Growth .............. 280
IV. Implications for Trademark and Unfair Competition Law ..................... 281
    A. Goodwill Protection and Dynamic Competition With Differentiated Products .................................................................. 281
    B. Limits on Goodwill Protection ..................................................... 282
        1. Limits on the Rent Seeking Activity of the Rights-holder: Goodwill Transferability ................................................. 282
        2. Protecting Locational Competition ............................................. 285

* Research and Teaching Associate, Centre for Commercial Law Studies, Queen Mary, University of London. I wrote this paper during my research stay as a visiting scholar at Stanford Law School. My gratitude goes to Professor A. Mitchell Polinsky who made my research stay possible in the first place. I was very happy to have the opportunity of meeting and discussing my research project with Professor Mark A. Lemley, who has been my sponsor at Stanford, and with Professor Paul Goldstein. Any errors or omissions are mine only.
I. Introduction

Contemporary analysis of trademark rights rests on the premise that consumer confusion constitutes the primary, if not the sole, rational basis for awarding legal protection. Dilution theory has gradually come to be considered an almost undesired exception to the general rule of confusion-based liability and has been continuously shrinking in scope of application. Trademarks are viewed mainly as an offspring of the law against passing-off. Property rights in trademarks are acceptable to the extent that they vindicate interests of consumers in making informed decisions. Rights-holder interests recognized by trademark law should, accordingly, be merely a reflex of protecting consumers from various types of confusion. Authorities of exclusion with respect to a trademark going beyond the scope necessary to implement the policy of promoting the accuracy of information transmission in the marketplace are thought to be anticompetitive because they supposedly restrict the
freedom of competition without bringing forward any redeeming procompetitive virtue.

This paper conveys the argument that trademark rights may be extended in scope so as to protect the competitive interests of the rights-holder independent from a finding of consumer confusion and at the same time promote the effectiveness of competition to the benefit of consumers. Various trader interests have been put forward as justifications of rational theories of trademark protection, most of them leaning towards the idea that the rights-holder has an interest in the economic exploitation of the advertising message incorporated into his trademark. The antecedent analysis examines the legitimacy of protecting trader interests in the internalization of advertising value through exclusive rights in trademarks.

Pivotal to our syllogism is the idea that trader interests are not simply a concomitant of the policy combating different sorts of consumer confusion (Part II). The principle that trader interests are independent and protectable in their own merit has been prevalent at the time of the inception of trademarks as property rights at the courts of equity. Passing-off principles were sufficient to protect traders from fraudulent trade diversion or damage to reputation. Property rights in trademarks were necessary for protecting trader interests in the exclusive use of a source-designator as a prerequisite for their ability to build up commercial goodwill. Determining trademark scope should be viewed as a balancing exercise accommodating the diverse interests of trademark proprietors, their competitors, and the consuming public. Consumer confusion cannot be the sole reference point of the analysis, because the economic interests involved in trademark disputes do not exclusively revolve around concerns related to market transparency. Shifting to an analysis of trademark scope that takes into account the effectiveness of competition would reveal further competitive and consumer interests equally worthy of protection through trademark law.

Trademark owners have an economic incentive to internalize the advertising value generated by their product differentiation strategies. Therein lies their ability to exercise some significant control over the price in regard to a certain group of consumers having a preference for products encompassing their advertising message. The inquiry into the legitimacy of such business interests in competition relies on the economics of product differentiation (Part III). A differentiated supply side entails losses in static efficiency due to unexhausted economies of scale but simultaneously promotes consumer welfare by increasing available product variety. Whereas competition policy should carefully strike a balance between these two proxies of a system of effective competition, the competitive interest of the rights-holder in the internalization of advertising value deserves consideration in view of the consumer preference for products artificially differentiated by persuasive advertising. Economic analysis implies that protecting the intangible value of goodwill in its broad conception, including elements of advertising directed at consumer patronage, from appropriation would facilitate dynamic competition with differentiated products. At the same time, economic analysis calls for crafting new limitations to
trademark rights (Part IV). Thus, goodwill protection should not be conceptualized as an absolute copyright-like property right in advertising value. Instead, trademark law should define those market segments where the rights-holder has a legitimate interest in the economic exploitation of his goodwill taking into account his needs for business expansion strategies and the effectiveness of competition with differentiated products. Because goodwill protection is also a means of providing to smaller undertakings or new entrants an economic foothold to thrive in the marketplace, limitations should be available for protecting the ability of competitors to locate themselves in a profitable niche of the product space by launching their own differentiation strategies. Limitations should further consider the interests of competitors in language sharing and the adoption of suggestive trademarks. Exceptions to the general rule of goodwill protection would have to apply in markets for generic pharmaceuticals and tobacco products.

Misappropriation theories of trademark protection have been invoked in the past by courts within the framework of the unfair competition cause of action (Part V). Junior users have been enjoined for causing consumer confusion or inflicting dilutive harm to trademarks. Legal opinions in the vast majority of the cases have blatantly confirmed the fulfillment of both requirements for liability when confronted with uses of senior trademarks in connection with non-competing goods without much inquiry and emphasized instead the defendant’s efforts to appropriate business values of the rights-holder. In essence, the cases were decided on the basis of this particular misappropriation theory. These ideas were transferred into trademark law (Part VI). Some opinions created an additional type of actionable confusion in order to combat free-riding of advertising value on the grounds of Section 43(a) of the Lanham Act. Identical or similar uses have been held to capitalize on the goodwill of another by borrowing some of the likeness of senior trademarks to promote their own sales (subliminal confusion doctrine). Dilution was also thought for some time to constitute a doctrine meant to prevent the misappropriation of business values. Case law has light-handedly delivered findings of dilution, while being primarily concerned with junior users’ predatory intent to take an unfair advantage of the goodwill attached to a senior trademark.

The theory of goodwill misappropriation deteriorated gradually due to the lack of a convincing justification for the free-riding rationale. Equally influential to this development was the phenomenon of intellectual property expansion, which called for caution towards the expansion of trademark scope in particular. Both the federal legislature and case law reacted by preempting the free-riding rationale and conditioning extended trademark protection on dilutive harm caused to a narrow circle of famous marks (Part VII). This paper argues that this approach is counterproductive because it does not adequately take into account the actual ways in which trademarks affect competition. Current trademark law does not sufficiently consider traders’ interests in implementing their branding strategies or consumer welfare that might arise from dynamic competition with differentiated products.
II. Trademarks as Part of Unfair Competition Law: A Balancing Exercise

The roots of trademark protection in the Anglo-American legal systems lie in the tort of deceit. Using the product identifying sign of another in order to promote one’s own sales amounted to a fraud against the consumers, who were misled as to the origin of the goods purchased. The action based on deceit could not remedy the loss of trade suffered by the trademark owner because in its initial inception the right to sue accrued solely to the receiver of the misrepresentation. To surmount this legal deficit the tort of deceit was extended by rendering consumer deception actionable for those traders who had suffered economic loss as a result of the wrongful act. The modification of the tort of deceit created a new legal action, which was directed at protecting the interests of both traders and consumers while simultaneously serving the public interest in an “ethical” business competition (“tort of passing-off” or “tort of unfair competition”). Damages were awarded to the


3 Singer Mfg. Co. v. Wilson, [1876] 2 Ch.D. 434, 453–54 (Eng.); James Love Hopkins, The Law of Trademarks, Tradenames and Unfair Competition § 181 at 411 (1924); see also Lever v. Goodwin, [1887] 36 Ch.D. 1, 2–3, 7 (Eng.) (“The law on this head is plain. It is founded on fraud. The simplest case is where the seller misrepresents to the buyer that the goods which are being offered for sale are the goods not of the person who made them, but of some other manufacturer. That is a simple case between the buyer and the seller. Then there comes the case, which is a simple one also, and one that does, I am sorry to say, occur, where the manufacturer, by subtle devices, which are to accompany the goods on their sale in the market, gets them up in such a form as to be calculated to deceive the ultimate buyer into the belief that the goods which he is putting on the market are the goods of some other maker. Here, generally speaking, a double fraud, is committed. First there is the fraud which is perpetrated, where it is successful, on the ultimate buyer; and secondly, there is a fraud perpetrated or committed upon the other manufacturer, who loses his trade.”) (emphasis added).

4 Christopher Wadlow, The Law of Passing-Off: Unfair Competition by Misrepresentation 21–23, 37 (4th ed. 2011) (making the point that this might indeed be the conceptual development of passing-off, although the process of molding this tort could not with certainty be said to have been seamless, given that the information derived by the case reports is inadequate or sometimes even deficient). It seems that there is still much space for research on the historical foundations of trademark law.


6 See 1 Harry D. Nims, Unfair Competition and Trademarks 36–40 (4th ed. 1947) (discussing the threefold purpose of the unfair competition cause of action in its original form to protect hones-
claimant proving actual damage and fraudulent intent on behalf of the junior trademark user through an action at law.\(^7\) Equity could then intervene to provide injunctive relief when the action at law was established.\(^8\)

In the landmark case of *Millington v. Fox*,\(^9\) an English Chancery Court deviated from the established legal practice of protecting signifiers of commercial origin on the grounds of passing-off principles and recognized a right of property in trademarks.\(^10\) Plaintiffs had been using the marks “CROWLEY,” “CROWLEY MILLINGTON” and the letters “I.H.” to identify their steel bars. The defendant marked his own steel products with the same indicia honestly believing that they were technical terms referring to the specific type of the metal here in question. An action at law could not be established because the defendant did not act fraudulently in using the marks of the plaintiff.\(^11\) By awarding an injunction, the court of equity did not actually exercise its auxiliary jurisdiction to supplement the common law principle. Moreover, Lord Cottenham was convinced that the plaintiffs had a right to the exclusive use of their marks, which could only be sufficiently protected if they were awarded a perpetual injunction.\(^12\) In fact, the court seems to have exercised its exclusive jurisdiction to enforce a property right not recognized by the common law.

*Millington* is often contrasted\(^13\) with *Blanchard v. Hill*,\(^14\) a case that is famous for expressing disregard to monopolies in view of the newly established era of trade freedom. This case has simultaneously been considered a strong authority for the notion that trademark protection should rest solely on fraud and for the proposition
that the recognition of proprietary interests other than avoiding consumer confusion would result in an unlawful monopoly.\textsuperscript{15} In \textit{Blanchard}, an injunction was sought against the use of the Great Mogul stamp on playing cards sold by the defendant. The plaintiff asserted that he had appropriated the stamp by virtue of an old royal charter and that, in any event, he suffered damage from the defendant using the same mark, as he was losing trade. Lord Hardwicke denied the injunction on the grounds of the invalidity of the charter that had developed to an illegal monopoly at the time the case was tried.\textsuperscript{16} In passing, he noted that there had been no authority supporting the view of equity having the jurisdiction to protect the right of a trader to the exclusive use of a mark.\textsuperscript{17} He went on to express that it “would be of mischievous consequence” to recognize such right.\textsuperscript{18} \textit{Blanchard v. Hill} was clearly a “monopolies case” though, which was decided on the illegality of the charter without a clear intention to make good law in regard to trademark protection. The Lord Chancellor was concerned with the enforcement of the plaintiffs’ title to a mark that would have practically given effect to an illegal monopoly. After rejecting the property claim based on the charter, he was confronted with an alternative claim of the plaintiff, who was insisting so as to accomplish his anticompetitive end. As his primary concern was to implement the public policy against monopolies and since there was no precedential authority supporting the proprietary nature of trademark rights, he was at ease to reject the claim relying upon precedent that confined trademark protection to fraudulent junior uses.\textsuperscript{19} The opinion expresses some skepticism about the possibility that the courts of equity might recognize a protectable interest in the exclusive use of a mark but it cannot be understood as linking the concept of the proprietary mark to an anticompetitive monopoly. \textit{Blanchard v. Hill} is conclusively a case nullifying an illegal monopoly on playing cards seeking to promote the freedom of trade. Therein lies its primary significance as precedent.\textsuperscript{20} \textit{Millington} does not refer to this case, most probably because there was no clear analogy to it.

The new type of legal exclusivity created in \textit{Millington} is supposed to have arisen as a result of a deduction from the property concept in an era where legal formalism was the prevalent method of ascertaining the law.\textsuperscript{21} In particular, property rights were established in items that were usurped and used for one’s own purpose. The usurpation of a sign and its use for identifying goods as stemming from a single commercial source accordingly gave rise to a right of property. Formalist legal thinking would invoke the property concept to adjudicate disputes without inquiring into the broader effects of legal protection, e.g. on competition or on the

\begin{thebibliography}{9}
\bibitem{15} Glynn S. Lunney, Jr., \textit{Trademark Monopolies}, 48 EMORY L.J. 367 (1999).
\bibitem{17} \textit{Id.} at 694.
\bibitem{18} \textit{Id.}
\bibitem{19} \textit{Id.}
\bibitem{20} \textit{Id.}
\bibitem{21} \textit{Id.}
\end{thebibliography}
need for balancing the interests of the parties involved.\textsuperscript{22} Because property was then an absolutist concept, the legal exclusivity was unqualified.\textsuperscript{23} This meant practically that the trademark owner had authority to prohibit the use of his mark even when it was used on unrelated goods and in the absence of any likelihood of confusion. In addition, traders would be able to usurp and eventually monopolize the use of words belonging to the common vocabulary, such as descriptive terms or geographical names.

In U.S. trademark law, the problem of overbroad trademark rights was initially tackled by maintaining the system of protection based on property for the narrow circle of coined marks (technical trademarks). Protection of other types of marks was deferred to the unfair competition cause of action (passing-off), which still relied on the subjective element of fraud.\textsuperscript{24} The new state of legal affairs in regard to trademarks was soon deemed to be unsatisfactory as well, mainly because it was understood that traders might have legitimate interests in asserting trademark rights even in descriptive terms or trade dress. A more balanced approach was introduced in order to take some fair account of the interests colliding in the context of trademark disputes. Legal theory reserved the use of a sign as a trademark for the rights-holder, while exempting from liability uses of the mark, such as its referential use, which competitors and other members of the public had a legitimate interest in making. The qualification of the property right purged the stigma of monopoly that had been surrounding trademarks.\textsuperscript{25}

The vast significance of \textit{Millington} has been that it summoned the courts to scrutinize the interests of the trademark holder in the exclusive use of a trademark. Lord Westbury took up the gauntlet some years later with a series of judgments including the important case of \textit{Hall v. Barrows}.\textsuperscript{26} He affirmed that the ground of equitable jurisdiction rested upon property but at the same time he urged that the scope of the trademark owner’s exclusive legal position should be narrowed in twofold manner.\textsuperscript{27} First, trademarks were supposed to be treated like property only “as applied to a particular manufacture or vendible commodity.”\textsuperscript{28} Second, trespass upon property can only take place if the junior use of the defendant has caused or is

\textsuperscript{22} \textit{Id.} The language used by Lord Cottenham in \textit{Millington} gives the impression that the courts had actually invoked the property concept in a formalistic manner. \textit{Millington v. Fox}, (1838) 40 Eng. Rep. 956 (Ch.) 961 (stating that “having previously come to the conclusion that there was sufficient in the case to shew that the plaintiffs had a title to the marks in question; and they undoubtedly had a right to the assistance of a Court of Equity to enforce that title.”). As we shall see, when the courts of equity recognized a property right in a trademark, they were essentially making unfair competition law.


\textsuperscript{26} \textit{Hall v. Barrows}, (1863) 46 Eng. Rep. 873 (Ch.).

\textsuperscript{27} \textit{Id.} at 876–77.

\textsuperscript{28} \textit{Id.} at 877.
likely to cause confusion as to source. For otherwise, there is no injury inflicted upon the plaintiff. The ruling spotted the legitimate interests of the trademark owner in classic passing-off concerns about possible harm to business reputation and, most of all, loss of trade. Thus, in Hall v. Barrows, the exercise of equitable jurisdiction was actually thought to be resting on property but could only be sustained in the case of fraud. Fraud was a necessary element of the claim in order for the plaintiff to maintain that he had sustained damage. Even if the defendant had not been in fact using the senior mark fraudulently, because he was not aware of its existence for example, the courts of equity would justify their intervention on the basis of fraud. The argument was that if the defendant carried on with his confusing junior use after the proceedings had been initiated, fraud would have been committed. The analysis of Lord Westbury has certainly been fundamental for the development of confusion-based theories of trademark liability.

The delving into the nature of the legally protectable interests of the trademark owner continued. The competitive interest, legitimizing the recognition of a right of exclusion in regard to a specific commercial source identifier, was finally perceived as the certainty for every economic operator that he will be in a position to trade on the basis of the reputational merits acquired by his performance in the market. Every trader has the right not only to acquire but also to exploit goodwill. To this effect, the possession of an exclusive sign is indispensable, as the mark could only stand for its proprietor’s goodwill if it is exclusively associated with him. The source identifier establishes a communication channel between its proprietor and the consuming public. Hence, it forms a platform upon which reputation is con-

---

29 Id. ("Imposition on the public is indeed necessary for the Plaintiff’s title, but in this way only, that it is the test of the invasion by the Defendant of the Plaintiff’s Right of property; for there is no injury if the mark used by the Defendant is not such as is mistaken, or is likely to be mistaken, by the public for the mark of the Plaintiff; but the true ground of this Court’s jurisdiction is property, and the necessity of interfering to protect it by reason of the inadequacy of the legal remedy.").

30 On this reception of Millington by the courts, see Bently, supra note 1, at 14–15; see also Edelsten v. Vick, (1853) 11 Hare 78, 84, 68 Eng. Rep. 1194 at 1197 (V.C.). ("I agree with the argument on the part of the Defendants there must be an intention to deceive the public, or this Court will not interfere.").

31 See, e.g., Singer Mach. Mfrs. v. Wilson, (1877) 3 App. Cas. 376 (H.L.) at 400 (appeal taken from Eng.) ("This is not an action to recover damages for a wrong already committed, but an application for an injunction to prevent the continuance of a wrong which has been committed, and is threatened to be repeated; and I think that if it were proved that the course pursued would really produce the effect of passing-off the defendant’s goods as and for the plaintiffs’, the injunction should be granted (whatever might be the case as to the account), whether the defendant heretofore meant it to produce that effect or not. For if he persevered, as he threatens to do, in this course, after learning that it does produce this effect, he would (unless in very exceptional cases) do a wrong injurious to the plaintiffs, and should be prevented from doing that wrong.").

32 The House of Lords affirmed Lord Westbury’s analysis of trademarks as property in Leather Cloth Co. v. Am. Leather Cloth Co., (1865) 11 HLC 523, 533–34 (ruling that trademarks constitute property that could be sold and transferred along with the underlying business, but only a use calculated to deceive purchasers trespasses upon that kind of property). For a more detailed analysis see Bently, supra note 1.

33 SCHechter, supra note 1, at 157.
stantly being forged. The courts of equity were determined to protect this economic interest as soon as they recognized that the nature of the right in a trademark is proprietary. In doing so, they were essentially creating unfair competition law. Because the creation of the property right was intended to protect business interests in competition, trademarks were conceptualized, from the moment of their inception, as nothing more than a part of unfair competition law.

Some courts, troubled by the social and marketplace consequences instigated by an eventual grant of trademark protection based on an absolutist concept of property, considered the proprietary right of the trademark holder to extend to the goodwill incorporated into a sign but not to the trademark itself. Proprietary rights in one’s own goodwill have been justified with arguments flowing out of the natural rights theory. Goodwill protection has also been justified as providing incentives and rewards for commercial/Advertising inventiveness or for the creation of famous marks because goodwill attached to a trademark constitutes an economic good that

34 ANDREW GRIFFITHS, AN ECONOMIC PERSPECTIVE ON TRADE MARK LAW 121 (2011).
35 Int’l News Serv. v. Associated Press, 248 U.S. 215, 234–35 (1918) (“We need spend no time, however, upon the general question of property in news matter at common law, or the application of the copyright act, because it seems to us the case must turn upon the question of unfair competition in business. . . . In order to sustain the jurisdiction of equity over the controversy, we need not affirm any general and absolute property in the news as such. The rule that a court of equity concerns itself only in the protection of property rights treats any civil right of a pecuniary nature as a property right; and the right to acquire property by honest labor or the conduct of a lawful business is as much entitled to protection as the right to guard property already acquired. It is this right that furnishes the basis of the jurisdiction in the ordinary case of unfair competition.”); Fisher v. Star Co., 132 N.E. 133, 137 (N.Y. 1921) (“Any civil right not unlawful in itself nor against public policy, that has acquired a pecuniary value, becomes a property right that is entitled to protection as such. The courts have frequently exercised this right. They have never refused to do so when the facts show that the failure to exercise equitable jurisdiction would permit unfair competition in trade or in any matter pertaining to a property right.”). Therefore, the introduction of the property concept in trademark law should not be simply attributed to a technicality, namely that the courts of equity invented this theory so as to combat commercial fraud, because equity jurisdiction could supposedly only intervene in order to protect a property right. But see Robert G. Bone, Hunting Goodwill: A History of the Concept of Goodwill in Trademark Law, 86 B.U.L. REV. 547, 561–62 (2006). It is a fact, though, that equity had intervened to prevent fraudulent practices not actionable at law even in the absence of a property right. See WADLOW, supra note 4, at 22–23.
36 See, i.e., Prestonettes, Inc. v. Coty, 264 U.S. 359, 368 (1924) (“Then what new rights does the trade-mark confer? It does not confer a right to prohibit the use of the word or words. It is not a copyright. . . . A trade-mark only gives the right to prohibit the use of it so far as to protect the owner’s good will against the sale of another’s product as his.”); Coca-Cola Bottling Co. v. Coca-Cola Co., 269 F. 796, 806 (1920) (“Trade-marks and the good will of a business are inseparable. In fact, a trade-mark is merely one of the visible mediums by which the good will is identified, bought, and sold, and known to the public.”).
has been created through the labor of the rights-holder. Constructing the interest position of the trademark owner as being correlative to the intangible value of goodwill has been a very fruitful analytical instrument for exploring trader interests that might be worthy of protection. Non-competing uses, for instance, have been held to be impermissible because they are harmful to the interests of the trademark holder in numerous respects. They make the reputation of the trademark holder dependent on the business practices of junior users, which would defy the legitimate interest to autonomously define the content of goodwill.

In addition, they may obstruct the trademark holder from expanding his trade on another field of economic activity under the same mark. The adoption of a senior mark for unrelated goods or services would often be motivated by a predatory intent of a third party to capitalize on the goodwill of the trademark proprietor, so as to promote his own sales. Apparently, the opinions of Justice Hand greatly contributed to the legal exploration of the interest position of the rights-holder.

Legal history shows that the development of a property theory of trademarks corresponded to the willingness of the courts of equity to accommodate the legitimate interests of the trademark holder and integrate them into the value system of trademark protection along with those of the competitors and the public in an “hon-

---


40 Yale Elec. Corp. v. Robertson, 26 F.2d 972, 974 (1928).


44 The opinions of Justice Hand seem to be driven by an effort to take into account all interests that could possibly be involved in trademark disputes. He could see that the interests of the trademark holder might not necessarily be concomitant with the public interest in avoiding confusion as to source. At the same time, he was concerned about the limits of the trademark monopoly. See L. E. Waterman Co. v. Gordon, 72 F.2d 272, 273 (2d Cir. 1934). In my view, the relevant opinions of Justice Hand should be read as authorities for this broad proposition. At this point, we cannot get any deeper into the controversies about the meaning and the value of Justice Hand’s opinions. For a different view on this issue, see Robert G. Bone, *Taking the Confusion Out of “Likelihood of Confusion”: Toward a More Sensible Approach to Trademark Infringement*, 106 Nw. U. L. REV. 1307 (2012) and Kenneth L. Port, *Learned Hand’s Trademark Jurisprudence: Legal Positivism and the Myth of the Prophet*, 27 PAC. L.J. 221, 243–52 (1996).
est” and “fair” business competition. The conceptualization of trademarks as property called eventually for a nuanced balance of all interests involved in the context of trademark protection. Contemporary trademark doctrine lost sight of the duty to balance the diverse interests colliding with each other incidentally to trademark disputes when it ascribed to trademarks a purely informational role in the marketplace as a commercial source designator. Most likely, as pointed out by Mark McKenna, the misconception arose from a transplantation of Chicago School notions on economic efficiency being the sole concern of the antitrust laws to trademark doctrine. Seen under the prism of information economics, trademarks are solely dedicated to prevent market failures resulting from informational asymmetries in the marketplace. Thus, trademarks promote economic efficiency by economizing consumer search costs and by saving the markets from collapse caused by an adverse selection problem. Implied therein is the idea that the protectable interests of the trademark owner simply reflect the public interest in avoiding consumer confusion. Consequently, the interest position of the rights-holder as an economic operator who seeks to commercially exploit his trademark as a property right was neglected.

The revelation of the true nature of trademark rights as mechanisms balancing diverse trader, consumer and public interests is an important step towards the future development of trademark law because it calls for the reconsideration and probably the recalibration of the respective interest positions. Exploring trader interests as a part of the legislative program of trademark laws would also be a very helpful analytical tool for studying the relationship between trademarks and competition because it would provide an insight of how trademarks are actually being utilized for

---

45 Mark P. McKenna, *The Normative Foundations of Trademark Law*, 82 Notre Dame L. Rev. 1839, 1850–73 (2007); see also Ameritech, Inc. v. Am. Info. Techs. Corp., 811 F.2d 960, 964 (1987) (“Although trademark protection may have had its start in common law as an action in fraud, over the past one hundred fifty years it has come to focus also on protecting property interests in trademarks themselves. . . . Thus, trademark law now pursues two related goals—the prevention of deception and consumer confusion, and, more fundamentally, the protection of property interests in trademarks.”). After enumerating the various types of trademark infringement resting on consumer confusion, the court referred to dilution as a theory which, “[r]ather than focusing on consumer confusion, . . . seeks to protect the senior user’s interests in the trademark.” *Ameritech, Inc.*, 811 F.2d at 965. It should be noted, however, that the protection of such proprietary interests has to be justified by reference to the effectiveness of competition.

46 Cf. Ramirez-Montes, supra note 1, at 135–65.

47 Cf. supra note 45, at 1845–49.


competitive purposes in the marketplace.\textsuperscript{51} Herewith, a more accurate picture of the actual competitive interests involved can be gained. Adjacently, trader interests have to be balanced with the interests of both competitors and the consuming public. Striking a new balance cannot occur in a vacuum but it does, however, necessitate a reference point. Because trademarks are part of a broader complex of norms that seek to establish effective competition, namely a competitive process yielding socially desirable outcomes, the effect of the protection of each interest position on the effectiveness of competition becomes decisive as soon as a decision about the scope of trademark rights has to be reached.\textsuperscript{52} Protecting interests of the trademark owner beyond source identification is not meritorious in itself,\textsuperscript{53} but only inasmuch as it serves the effectiveness of competition and thereby promotes consumer welfare beyond the optimization of market transparency.\textsuperscript{54} Such a balancing exercise would modernize the principle that trademarks form a constituent part of unfair competition laws.

III. Trademarks and Product Differentiation: An Economic Analysis

A. Trademarks as Marketing Instruments Incorporating Goodwill

Trademarks constitute communicative instruments (signs) conveying information about the commercial source of the goods or services marketed thereunder. Apart from this elementary informational function, which initially prompted the recognition of exclusive legal rights in product-identifying signs, trademarks also contain the information representing the marketing message of the right-holder.\textsuperscript{55} Trademark owners generate this type of information through advertising measures strategically unfolded so as to improve the likeness (goodwill) of their products. Branding activity assigns to commodities attributes absent in the generic version of those goods, such as luxurious flair, vivaciousness or youthfulness. Differentiation

\textsuperscript{51} See, e.g., Jerre B. Swann & Theodore H. Davis, Jr., Dilation, an Idea Whose Time Has Gone: Brand Equity as Protectable Property, the New/Old Paradigm, 1 J. INTELL. PROP. L. 219 (1994) (making the case for property interests in brand equity); Roger H. Marks, Trademark Protection Under the “Natural Area of Business Expansion” Doctrine, 53 NOTRE DAME L. REV. 869 (1978); McCarthy, supra note 1, § 24:17, at 24–48 (elaborating on the rights-holder’s interest in the exclusive use of his mark in adjacent markets).

\textsuperscript{52} Chronopoulos, supra note 39.

\textsuperscript{53} See Dev S. Gangjee, Property in Brands: The Commodification of Conversation, in CONCEPTS OF PROPERTY IN INTELLECTUAL PROPERTY LAW 29 (Helena Howe & Jonathan Griffiths eds., 2013) (arguing that natural law justifications of goodwill protection would also stumble upon the fact that the trademark holder is not the sole creator of a brand because consumers take part in the shaping of brands by providing feedback through the market mechanism).

\textsuperscript{54} Cf. Wendy J. Gordon, On Owning Information: Intellectual Property and the Restitutionary Impulse, 78 VA. L. REV. 149 (1992) (emphasizing that restitutionary considerations in intellectual property and unfair competition law should only be acceptable when such legal protection serves the public interest overall).

generates goodwill, which can be broadly defined as an intangible asset embracing all features contributing to customer patronage and triggering repeated sales.56

The emerging legal task involves the evaluation of the possible market consequences of constructing exclusivity rights in such intangible subject matter, in view of the legitimate competitive interests of the rights-holder, the competitors and the consuming public in an effective competitive process. Trademarks’ capacity to symbolically codify information appertaining to the goodwill of the rights-holder links them to the economic phenomenon of product differentiation.57

B. Trader Interests in Perspective: Market Power and Brand Extensions

Differentiation strategies create positions of economic power. Within the boundaries of a specific market niche comprised of consumers who have a preference for a specific brand, a firm may exercise monopolistic pricing, limited only by the possibility of a consumer switching to a substitutable product if the price for his ideal preference becomes too high.58 Price competition is consequently mellowed and the firm obtains a certain degree of market power that enhances profitability. The commercial success of the brand would motivate the firm to expand to other markets, where its advertising message would be marketable and capable of generating sales. Brand extensions would accordingly be successful, provided the goodwill attached to the trademark is transferable to other markets even if these are distant markets for unrelated goods or services. Some marketing studies suggest that feature similarity between the core brand and the product extension class is essential for a successful brand extension. Accordingly, similarity rests on the respective products being substitutes, complements or involving such common manufacturing methods and expertise that the consumer would be convinced of the trademark holder’s competence as a producer of the extension good.59 Probably the most useful approach for analyzing the competitive interests of the trademark holder is to ask whether the attribute associations of the core brand fit into the extension product (brand consistency).60

56 EDWARD S. ROGERS, GOODWILL, TRADE-MARKS AND UNFAIR TRADING 13 (1914).
57 See generally S. Chesterfield Oppenheim, The Public Interest in Legal Protection of Industrial and Intellectual Property, 40 TRADEMARK REP. 613, 624 (1950) (explaining the link between trademarks, product differentiation, and market power).
58 Cf. Mishawaka Rubber & Woolen Mfg. Co. v. S. S. Kresge Co., 316 U.S. 203, 208 (1942) (“The creation of a market through an established symbol implies that people float on a psychological current engendered by the various advertising devices which give a trade-mark its potency. It is that which the Trade-mark Act of 1905 protects.”); the extent to which the various products or services may be prone to differentiation through persuasive advertising may not be the same. Consumer experience goods would, in principle, be more prone to subjective differentiation than pure search goods, for instance. Marketing measures may create brand image for almost any product or service though. See generally, DOUGLAS F. GREER, INDUSTRIAL ORGANIZATION & PUBLIC POLICY 62-66 (1980).
60 Kevin Lane Keller & David A. Aaker, The Effects of Sequential Introduction of Brand Extensions, 29 J. MARKETING RES. 35, 36 (1992); C. Whan Park, Sandra Milberg & Robert Lawson, Evalua-
Exploitation takes place in these cases through the use of the mark incorporating the economic value of goodwill in connection with products or services of the market the trademark holder wishes to enter. For instance, the mark “BIC”, presumably connoting in branding terms durable and disposable goods used in everyday life with some retro aura, was initially used in connection with pens and has been thereafter transferring the goodwill of its owner to lighters, magnets and shaving razors. Another example would be the trademark “CAMEL” originally used in connection with cigarettes. Through advertising measures and the marketing of a certain quality the trademark holder has created a brand image, which refers to the qualities characterizing the consumer of “CAMEL” products. Consumer associations related to a core brand are marketable as part of other product bundles.

Expansion to other industry sectors by means of extending brand equity would usually be a part of a wider strategy for the internal growth of the firm. The rights-holder has also an economic interest in licensing a trademark. Third parties may free-ride upon the business values embodied in a senior trademark by adopting a similar mark for a product category to which the goodwill of the rights-holder is transferrable. Apart from transferring goodwill to other markets, brand extensions may leverage quality assurances associated with the trademark or signaled through advertising measures in the market of the core brand, so as to remedy informational asymmetries. Spreading the advertising costs over multiple products brings forward efficiencies related to economies of scope. Last but not least, the rights-
holder is always concerned with the recoupment of investments he has committed to building up the reputation of his trademark.

Brand extensions also occur when owners of famous or widely known brands have an economic interest in the use of their trademarks even on unrelated goods or services. This is likely to occur when the trademark holder spots the existence of monopoly profits in less concentrated markets. Even if the relevant goodwill is not transferable to the new market, the rights-holder will enjoy some competitive advantage over the incumbent firms due to the high degree of recognition of his mark, at least as far as competition for the initial interest of the consumers is concerned. When extending the brand to product categories that do not amount to a “good fit” for his existing goodwill, the rights-holder runs the risk of diluting his own trademark by dissolving the association of his source signifier with a certain type of product. Nevertheless, the trademark holder may still decide to expand a brand if the potential loss to be sustained by this “dilution” would be overcompensated by prospective monopolistic profits in the new market. Of course, the success of the business strategy depends also on the competition from owners of other strong brands who decide to enter the same market through the same business strategy.

The economic arguments directly set forth provide a clear explanation for the business rationality of dilution claims against non-competing uses, even those taking place in connection with totally unrelated products. Dilution protection scrutinizes non-competing uses for their potential to blur the distinctiveness of a famous trademark or to tarnish its semantic content. Apparently, the dilution rationale is not an apt means to analyze the competitive dimensions of disputes where the plaintiff is seeking relief on a non-confusion-based theory of trademark liability because it fails to squarely consider the interests at stake in the context of such disputes. The harm prescribed by the dilution theory does not find strong empirical confirma-

---

65 Lynne M. Pepall & Daniel J. Richards, The Simple Economics of Brand Stretching, 75 J. Bus. 535 (2002). On the other hand, if the targeted market is characterized by a dynamic competition with differentiated products, the mark’s high degree of distinctiveness may serve as a vehicle for enabling the penetration of the market even though the goodwill at issue would not be transferrable to the relevant goods or services.

66 Cf. William M. Landes & Richard A. Posner, The Economic Structure of Intellectual Property Law 208 (2003) (arguing that legal protection against non-competing uses of prestigious marks is not likely to confer a significant competitive advantage upon the rights-holder because the number of prestigious marks is so vast that the brand extensions of the rights-holder could not be profitable since competition from other, equally prestigious, extended brands would drive prices down to the marginal cost of production).

tion and is definitely difficult to prove. A much more sensible approach for developing effective trademark systems would therefore be to analyze the rightsholder’s actual competitive interests, in light of their effect on competition, and to bring them into a balance with those of the competitors and the consuming public.

C. Welfare Aspects of Dynamic Competition With Differentiated Products

Because marketing science is principally directed at highlighting the most effective business strategy for the brand owner, it cannot serve as the lodestar for determining the optimal scope of trademark rights in competition. A better understanding of the effects of goodwill protection on competition, and more generally on consumer welfare, could be provided by an economic analysis.

1. The Theory of Monopolistic Competition

In order to assess the welfare effects of product differentiation, economic theory has constructed a model that assumes conditions of perfect competition, except that each seller offers a differentiated version of the marketed commodity. The existence of differentiated goods creates consumer preferences and confers upon each seller the possibility to exploit relatively inelastic demands by pricing above marginal cost. Further, consumer preferences are symmetrical in the sense that there is no product accumulating more buyers than the other. Consumer preferences are in other words symmetrically spread over the various existing products. At the beginning of economic interaction the number of sellers is low enough to allow supra-competitive profits. The absence of barriers to entry invites new sellers to compete with incumbents up to the point that economic profits amount to zero.

---


Due to the assumption of symmetric consumer preferences, each new entrant subtracts market share from all incumbents proportionally. The market structure in equilibrium is characterized by the existence of a large number of sellers offering differentiated products. Because each seller is only able to serve a small proportion of the market, namely the sum of consumers having a preference for his product, no one has a market share that allows exhaustion of economies of scale (“excess capacity theorem”).

From the perspective of productive efficiency, market performance leads to welfare loss, because the same amount of (commoditized) goods could have been produced by fewer producers fully exploiting their economies of scale. The possibility of taking advantage of the efficiencies associated with mass production in many industry sectors would also improve the efficiency of an economy. However, Edward Hastings Chamberlin, who was the first to assess the welfare implications of differentiation as a market imperfection, noticed that some sacrifices in productive efficiency could be justified by the fact that the demand side is better off with product variety because it makes the satisfaction of diverse consumer needs possible.

2. Product Variety and Social Welfare

It was not until the late 1970’s that the parameter of product variety was formally introduced into the economic model of monopolistic competition as a determinant of consumer welfare. The core assumption underlying these works is that consumers’ total utility increases with each new product entering the market, as their preference for variety is insatiable. The price increase accompanying the existence of unexhausted economies of scale is considered as a price premium that consumers have to pay in order to enjoy product diversity. Accordingly, the task for economic policy remains to balance the benefits of productive efficiency against the gains in consumer welfare arising from supply-side diversity. The calculus is aimed at formulating an economic decision on how many brands a given market produce and in what quantity. Neo-Chamberlinian economic models of monopolistic competition conclude that the market mechanism would not alone lead to


76 Carlton & Perloff, supra note 71, at 215–19.
the socially optimal amount of product variety.\(^{78}\) If the fixed costs in a specific production sector tend to be low, excessive entry would minimize gains associated with economies of scale. Respectively, the amount of marketed brands would be suboptimal where the fixed costs of entry are very high.\(^{79}\)

a. Locational Competition

While the theory of monopolistic competition illuminates the effect of product diversity on consumer welfare, it cannot explain the particularities of competition with differentiated products, because it assumes that all brands offered in a certain marketplace are equally substitutable for each other. In imperfectly competitive markets, consumers do not view the various competing brands as interchangeable. Each one rather aspires to an ideal product depicting the attributes that the consumer desires most. Only those products that are highly substitutable for the consumer’s first-choice good may come into play as reasonable buying alternatives. Competition is thus intensified within smaller market segments comprised of highly substitutable products. Strategic interaction in monopolistically competitive markets was first studied in regard to products differentiated by their transport cost, such as gas stations located in different parts of a city.\(^{80}\) Of course, consumers would prefer the vendor closest to their individual location, so as to avoid high transport costs. Firms would accordingly spread around in the city, choosing locations that would render them exclusive sellers for a group of consumers residing, for example, within some neighboring blocks, in an effort to avoid price competition (principle of maximum product differentiation).\(^{81}\) In return, consumers get the benefit of being able to optimize their transport costs by having more gas stations available to choose from.\(^{82}\)

b. Locational Competition in Product Space

Products are also differentiated in many respects other than the cost of their transport. Fruit-yogurt products, for instance, may vary according to their sweetness, mouth-sensation, packaging form, calories contained, fat percentage or brand image. Within such a multidimensional spectrum, sellers try to form unique product bundles by altering these individual parameters. The objective of this differentiation strategy is, as already explained, to match consumer taste so as to capture a group of buyers who have a strong preference for a specific product bundle and whose demand is therefore inelastic to some extent (market niche). Firms therefore

\(^{78}\) *Id.*

\(^{79}\) *Id.*


\(^{82}\) Samuelson & Nordhaus, *supra* note 70, at 175–76.
possess a limited possibility to avoid price competition, which depends on the degree of demand elasticity.

The application of locational theory to the analysis of competition with differentiated products was facilitated by the “characteristics approach” to consumer behavior. Consumer utility is correspondingly not simply a function of the number of available consumption units. The consumer is rather consciously seeking to satisfy a preference for specific product characteristics, regardless of the number of products needed for the satisfaction of the desired product attributes. Because consumer preferences are directed not at the product units but at specific product characteristics and their particular combinations, sellers try to locate their products into a fictitious product space by marketing a unique bundle of consumable characteristics, just like the operators of gas stations try to spot the profit maximizing location for their outlet.

A good exemplification of competition with different products refers to a single-product industry supplying ice cream, which faces competition only from an outside good, cake. Ice cream is being differentiated according to its taste, with each seller offering only one variety, while the outside good remains commoditized. Both products may be in competition, but for those consumers who have a preference for ice cream, it is only the various tastes of it that count as reasonable buying alternatives. The product characteristics space consisting of different flavors of ice cream is modeled as a circle, whose perimeter is uniformly occupied by consumers. Each point of the circumference represents the ideal flavor of the consumer located there. Sellers are motivated to locate themselves as far as possible from each other so as to exercise some control over the price in respect to those consumers that are located near to their point of location in the product space. The expectation of monopolistic profit induces the sellers to supply highly diversified flavors so as to ensure that competition on the price is avoided. When barriers to entry and fixed costs are high the number of firms competing would be so low that the segments of the circumference these firms serve would not intersect (monopolistic regions). This would allow them to compete monopolistically, subjected only to the laws governing the elasticity of demand. A great proportion of the product space would be vacant from suppliers offering a corresponding taste of ice cream (suboptimal variety). If no considerable barriers to entry are present, the number of com-

86 Carlton & Perloff, supra note 71, at 223.
87 Circular models of locational competition are founded upon the work of Steven C. Salop, Monopolistic Competition with Outside Goods, 10 Bell J. Econ. 141, 156 (1979).
88 Carlton & Perloff, supra note 71, at 223.
89 Id. at 225.
90 Id. at 225–26.
petitors would be high, resulting in the intersection of the circumference segments allocated to them and giving rise to intensive price competition between the neighboring sellers (competitive regions).91

Spatial economic models confirm the principle of maximum differentiation, namely that the supply side is prone to differentiate in the expectation of becoming a local monopolist. Product differentiation promotes consumer welfare through the satisfaction of diverse consumer needs. Monopolistic competition imposes a price premium in return for product variety.

c. Cluster Effects

The assumption of symmetric preferences would rarely be consistent with market reality. Some locations would be under-populated or even lack consumers entirely as the preferences of the latter may concentrate on certain bundles of product characteristics. Sellers would still tend to differentiate, but they would not be evenly distributed across the product space. There would also be some clustering of suppliers—and consequently intense price competition among them—around locations attracting a large proportion of consumers’ preferences.92

D. Trademarks and Barriers to Entry

Trademarks are often seen suspiciously as barriers to entry. The existence of strong brands makes it necessary for new entrants to incur their own expenditure on advertising so as to be able to penetrate the market. These cost disadvantages faced by newcomers have an impedimental effect on new market entry.93 In this broad sense, incumbent trademarks qualify as barriers to new competition.94 Viewing trademarks and advertising as barriers to entry allows us to take into account their effect on the market in a specific case so as to decide whether certain conduct harms competition.95 A functional approach should be followed when assessing the potential market foreclosure effect of trademarks.96 Entry barriers unleashed by branding activity may decrease the number of trademarks used in an industry towards the optimum when the cost of entry is low.97 In markets characterized by large barriers to entry, such as high fixed costs, the additional impediment to new entry flowing out of incumbent trademarks would tend to keep the number of brands available to con-

91 Id. at 227–28.
92 Lancaster, supra note 69, at 198.
97 Id. at 536.
sumers at a suboptimal level. Thus, there is no room for an across-the-board condemnation of trademarks for being anticompetitive entry barriers. Trademarks’ effect on competition has to be appreciated in relation to specific market conditions.

E. Advertising: Informative, Persuasive or Simply a Complementary Good?

The juxtaposition between the informative and the persuasive elements of advertising has traditionally been the starting point of economic analysis. Ideally, informative advertising reports to the consumer all objective characteristics of a product, such as its weight, functionality, taste or selling terms including the price or the relevant paying scheme. Hereby, firms can build up good reputations. Informative advertising is procompetitive because it remedies potential information asymmetries between sellers and buyers. It therefore protects the market from adverse selection as well as moral hazard problems and price dispersion. Persuasive advertising is, in contrast, more like a game to capture consumers’ demand for differentiated products. Instead of nakedly presenting their commercial offer, firms try to persuade and induce the consumer into a transaction through image advertising or by praising the marketed product in the superlative.

Competition on consumer persuasion has been thought to be defiant of allocative efficiency. Due to the alteration of consumer preferences, valuable resources are spent on products that do not cover the “actual” needs of the consuming public. Resources spent on persuasion are wasted because great expenditure is made for generating information of low quality, as the advertisements stem from the traders themselves and are therefore biased. Persuasion in competition has also been disregarded from an ethical point of view. Image advertising allegedly interferes

---

98 Id.
99 CARLTON & PERLOFF, supra note 71, at 476–77; SHY, supra note 85, at 283.
100 CARLTON & PERLOFF, supra note 71, at 481–83.
102 JOAN ROBINSON, THE ECONOMICS OF IMPERFECT COMPETITION 90 (1964) (“Lastly, the customer will be influenced by advertisement, which plays upon his with studied skill, and makes him prefer the goods of one producer to those of another because they are brought to his notice in a more pleasing or forceful manner.”).
103 Dorothea Braithwaite, The Economic Effects of Advertisement, 38 ECON. J. 16, 26 (1928) (touching upon many issues that are still pervasive in economic theory and considering the possibility that the creation of reputations may positively affect consumer welfare but generally rejecting the idea of advertising being a signal of good quality).
104 Nicholas Kaldor, The Economic Aspects of Advertising, 18 REV. ECON. STUD. 1 (1950-1951) (arguing that advertising promotes market concentration due to the ability of larger firms to finance costly advertisements and making the point that such oligopolistic structures are more likely to yield efficient outcomes associated with economies of scale). It should be noted that even informative advertising measures might constitute a wasteful way of using resources. S.A. Ozga, Imperfect Markets Through Lack of Knowledge, 74 Q.J. ECON. 29, 40 (1960) (noting that informative advertising might lead to diminishing returns “due to the fact that as more and more of the potential buyers become informed of what is advertised, more and more of the advertising effort is wasted, because a greater and greater proportion of people who see the advertisements are already familiar with their content”).
with the buying decisions of the consumer to the extent that it can change preferences and eventually corrupt him by turning him into a “brand personality.”

Further, competition on consumer persuasion is also thought to incentivize firms to squander their creative effort on advertising rather than focusing on maintaining and improving actual product quality. Persuasive advertising is also seen suspiciously as a factor that ameliorates competition on the price.

None of the allegations mentioned above make a valid case for legally condemning persuasive advertising or for obliterating goodwill protection from misappropriation by virtue of trademark and unfair competition law. Moreover, a demand for differentiated products does exist and consumers inevitably will wish to consume information generated by persuasive advertising. This is because the advertising message of the trademark owner is complementary to some basic product. Thus, persuasive advertising does not necessarily provide traders with incentives to neglect the quality of the “actual product.” Protecting the marketing message as goodwill attached to a trademark would not adversely affect competition on product quality.

Exactly because the marketing message of the trademark holder is a complementary good demanded by consumers, it could not be axiomatically taken for granted that persuasive advertising forcefully shapes consumer preferences. Differentiation creates preferences, but the consumer is better off in a market offering a variety of choices. Even if some consumers are prone to be easily carried away by flashy advertising, there are enough countervailing powers able to neutralize the potential harmful effects of persuasive advertising. As long as competitors do not commit any commercial wrong such as trade disparagement, they are free to be critical of the irrationality surrounding the beliefs associated with the brand of the trademark holder. If, additionally, the right of the public to criticize and parody brands remains in tact, the consumers would have enough social stimuli to become

105 John Kenneth Galbraith, The Affluent Society 127–129 (1998); Brown, supra note 93, at 1169; Lunney, supra note 15, at 427–28. For a particularly negative view of persuasive advertising as manipulative method see Vance Packard, The Hidden Persuaders (2007). There might indeed be some cases in which the consumer may be particularly vulnerable to persuasive advertising. See generally Greer, supra note 58, at 75–80. But this should call for legal intervention against particular advertising measures rather than lead to a denial to protect the advertising value through trademark law.

106 See Katya Assaf, Brand Fetishism, 43 CONN. L. REV. 83 (2010) (providing a thorough analysis of the arguments presented above and an illustration of their potential impact on trademark doctrine if considered normative); Brown, supra note 93, at 1168 (expressing concerns about the possible social consequences of advertising); Elizabeth Mensch & Alan Freeman, Efficiency and Image: Advertising as an Antitrust Issue, 1990 DUKE L.J. 321 (1990).


critical of brands themselves. Given that the law seeks to reserve for individuals a broad discretionary authority to freely decide themselves on ethical matters, an argument for enforcing ethic by restricting persuasive advertising becomes at least very arguable.\(^{110}\) Whereas the discussion on the effect of advertising on consumer welfare will probably continue for the foreseeable future, no valid economic argument for the abolition of persuasive advertising can be made because the eradication of its allegedly pernicious effects would simultaneously diminish its significant pro-competitive virtues to signal quality\(^ {111} \) and to satisfy consumer demand for branded products.\(^ {112} \) Consequently, the distinction between informative and persuasive aspects of advertising should not be normatively significant for trademark law.\(^ {113} \)

F. Acquisition and Maintenance of Monopoly Power Through Persuasive Advertising

As persuasive advertising enhances brand loyalty, it enables not only the acquisition but also the maintenance of market power. Trademarks facilitate the emergence of this monopolistic element in competition. Only through its codification in a trade symbol can the advertising message of a firm be turned into a consumable and tradable good. Due to the monopolistic nature of trademarks, commentators have often expressed concerns about their anticompetitive potential.\(^ {114} \) The view of trademarks as monopolies found its way to the FTC, which attacked a famous trademark on antitrust grounds in a rather extreme case.\(^ {115} \) Borden was accused of having monopolized the market for processed lemon juice by engaging in

\(^{110} \) See J. Thomas McCarthy, Compulsory Licensing of a Trademark: Remedy or Penalty?, 67 TRADEMARK REP. 197, 243–53 (1977) [hereinafter McCarthy, Compulsory Licensing] (“Undeniably advertising may sometimes be used to create irrational brand preferences and mislead consumers as to the actual differences between products, but it is very difficult to discover at what point advertising ceases to be an aspect of healthy competition. . . . It is not the Commission’s function to decide which lawful elements of the ‘product’ offered the consumer should be considered useful and which should be considered the symptoms of industrial ‘sickness.’ It is the consumer who must make that election through the exercise of his purchasing power.”) (citing the opinion of Justice Harlan in Fed. Trade Comm’n v. Procter & Gamble Co., 368 U.S. 568, 603–04 (1967). See also J. Thomas McCarthy, Trademarks, Antitrust and the Federal Trade Commission, 13 J. MARSHALL L. REV. 151, 157 (1979) (“The fallacy of this approach [namely that brand loyalty constitutes irrational consumer behavior] seems self-evident to me because it is based on an essentially undemocratic thesis: the consumer should not want what he or she wants.”).

\(^{111} \) On the important limitations of the signaling theory of advertising see PEPALL, RICHARDS & NORMAN, supra note 85, at 395–99.

\(^{112} \) CARLTON & PERLOFF, supra note 71, at 489; PAUL KRUGMAN & ROBIN WELLS, ECONOMICS 400–01 (2005).

\(^{113} \) Very often, it would be difficult to distinguish between informative and persuasive business practices. Advertising that provides instructions for the stylistic use of a product would qualify as informative in the eyes of a “branding personality.” CARLTON & PERLOFF, supra note 71, at 489.

\(^{114} \) See, e.g., W van Caenegem, Striking a Balance Between Protecting Commercial Reputation and Promoting Competition, 77 AUSTL. L.J. 598, 606, 613 (2003) (arguing that the discussion of the possibly overbroad protection of intellectual property rights should extend to commercial goodwill and reputation as well); Sigmund Timberg, Trade-Marks, Monopoly, and the Restraint of Competition, 14 L. & CONTEMP. PROBS. 323, 324–28 (1949) (considering trademarks as “direct restraints of trade” because of their capacity to confer market power upon the rights-holder).

intense advertising and promotion of its brand “ReaLemon” and subsequently raising insurmountable barriers for new competition. Despite the fact that the competing brands were chemically identical, Borden’s product commanded a significant price premium ensuing from the very strong brand loyalty brought about by the preceding extensive advertising measures. With a market share between 75% and 90% the brand owner was able to dominate the market. By virtue of its scale economies, the defendant could effectively drive its new competitors out of the market by undercutting them in price or by providing retailers with incentives to restrict the sales of competing brands.\(^\text{116}\) The business activities of Borden were held to be of exclusionary nature in the initial decision, as they were designed to exclude competition and did not correspond to an effort of competing on the merits of superior efficiency.\(^\text{117}\) Hence, defendant’s maintenance of monopoly power was unlawful.\(^\text{118}\)

On the issue of remedy, following a finding that the underlying trademark was the core of Borden’s position of monopoly, the administrative law judge (ALJ) concluded that the restoration of a competitive market structure called for Borden to compulsorily license its trademark to competing undertakings.\(^\text{119}\) The Commission affirmed the decision of the ALJ to the extent that it rules the pricing behavior of the monopolist as a violation of Section 5 of the FTC Act.\(^\text{120}\) In addition, the final opinion did not consider an encroachment upon the rights of the trademark holder necessary for the reinvigoration of competition in the relevant market. Such remedy should only be available in exceptional circumstances.\(^\text{121}\) In this case, it would be sufficient to regulate the pricing behavior of the monopolist.\(^\text{122}\) The FTC seems to have discarded the theory of trademarks as embodying a pernicious monopoly right at its own inception.\(^\text{123}\) Even though brand loyalty was extraordinarily strong in the case of Borden, it was not the trademark itself but the exclusionary behavior of the rights-holder that led to the monopolization of the market.\(^\text{124}\) Monopoly profits attributed to product differentiation would normally attract new entrants in the mar-

\(^{116}\) Id. at 770–73.

\(^{117}\) Id. at 772–73.

\(^{118}\) The 6th Circuit affirmed the holding that the business practices of Borden violated both Section 2 of the Sherman Act and Section 5 of the Federal Trade Commission Act. Borden, Inc. v. Fed. Trade Comm’n, 674 F.2d 498, 512–16 (6th Cir. 1982).


\(^{120}\) In re Borden, 92 F.T.C. at 802–05, 875.

\(^{121}\) Id. at 832–34.

\(^{122}\) Id. at 806–09, 832–36.


\(^{124}\) While trademarks may indeed contribute to the establishment and maintenance of positions of economic power, many markets remain highly concentrated mainly for other reasons. Market conditions may favor oligopolies, for instance. Market concentration may also emerge due to the cumulative effect of exclusive distribution agreements. Large market shares may also be attributable to significant advantages enjoyed by the brand owner that are related to economies of scale.
As long as there are profitable market niches within the product space available, new competitors will be able to penetrate the market and challenge the position of economic power possessed by incumbent firms. Trademarks confer monopoly power but they are not anticompetitive monopolistic positions per se. The perception of trademarks as dangerous monopolies could be credited to the outdated idea of perfect competition being the ideal paradigm for the purposes of sound competition policy.126

In his separate opinion on the issue of remedy, Chairman Pertschuk expressed the opinion that a pricing order was not sufficient for restoring competition in the relevant market.127 Because he regarded the “ReaLemon” mark as the “core” of Borden’s alleged monopoly, he considered that a remedy directed at reducing the market power linked with the specific trademark would be more appropriate.128 Commissioner Pitkofsky thought also that a trademark remedy should be available under the circumstances presented before him.129 The remedy of compulsory licensing is in many respects problematic because, at least temporarily, it would spread some confusion as to source or affiliation in the marketplace.130 While it would facilitate the process of a successful trademark becoming generic and thereby destroy an operational indicator of source in the market,131 it would not resolve the alleged antitrust problem of trademarks being the source of significant monopoly power, because the resourceful rights-holder would usually be in a position to quickly introduce a new strong trademark.132 Compulsory licensing would thus extort trademark policy without any procompetitive benefit.133 It would also create false positives by discouraging brand differentiation.134 For all these reasons, remedies requiring the rights-holder to refrain from using his trademark for some period in order to dispel dominant market positions achieved by unlawful monopoliza-

---


126 Jules Backman, The Role of Trademarks in Our Competitive Economy, 58 TRADEMARK REP. 219 (1968); see also Yale Brozen, New FTC Policy from Obsolete Economic Doctrine, 41 ANTITRUST L.J. 477 (1972).

127 In re Borden, 92 F.T.C. at 809–13.

128 Id.

129 Id. at 831.


131 McCarthy, Compulsory Licensing, supra note 110, at 231–32 (noting that compulsory trademark licensing amounts to illegitimate trademark confiscation and to an improper means of opposing to “irrational advertising”).


133 Id. at 542–51.

134 Sara V. Dobb, Compulsory Trademark Licensure as a Remedy for Monopolization, 26 CATH. U. L. REV. 589, 601–05 (1977); Holmes, supra note 130, at 138 (suggesting that compulsory trademark licensing should only be ordered as ultimum refugium).
tion should be avoided. Assuming the theoretical existence of a scenario where a single brand would come to foreclose an antitrust market because the advertising costs of successful entry would be unbearable for newcomers, a trademark remedy would be deemed appropriate. The FTC could then issue an order allowing third parties to appropriate goodwill through the adoption of similar marks in order to facilitate the emergence of new competition under conditions of high advertising costs of entry and promote competition on the price. Such remedy would be more likely to be proportional to the alleged antitrust harm.

Trademarks may confer monopoly power but they are not monopolies in the antitrust sense. Another indication for the same proposition is that the courts have not yet come to sustain a misuse defense, as they have done in the past when adjudicating claims of patent infringement. It is hardly conceivable that a trademark can itself be the prime and fundamental instrument for causing antitrust injury. Trademark rights would be incidental to antitrust violations flowing out of licensing agreements imposing anticompetitive exclusive dealings, horizontal market divisions, vertical restraints or tie-in arrangements. In ReaLemon the alleged antitrust injury was not actually attributed to the trademark itself but to Borden’s unilateral exclusionary conduct. The market power bestowed upon the rights-holder as a result of the goodwill incorporated into the trademark is not in itself a monopolistic element that threatens competition. It therefore makes no sense to disapprove of the protection of goodwill in its broad sense, including the advertising message attached to a trademark, as an anticompetitive position of economic power.


137 McCARTHY, supra note 1, § 31:91, 31-195 to 31-196 (recognizing the theoretical possibility of a successful misuse defense against trademark infringement suits); William E. Ridgway, Revitalizing the Doctrine of Trademark Misuse, 21 BERKELEY TECH. L.J. 1547 (2006) (proposing the suppression of critique and parody on trademark as possible rationales for the theory of trademark misuse); see, e.g., Helene Curtis Indus., Inc. v. Church & Dwight Co., Inc., 560 F.2d 1325, 1336–37 (7th Cir. 1977); Estee Lauder, Inc. v. Fragrance Counter, Inc., 189 F.R.D. 269, 273 (S.D.N.Y. 1999).


139 Id.

140 McCARTHY, supra note 1, § 31:108-38. See also Kurt Borchardt, Are Trademarks an Antitrust Problem?, 31 GEO. L.J. 245, 261 (1943); Bartholomew Diggins, Trade-Marks and Restraint of Trade, 34 TRADEMARK REP. 71, 72 (1944).
G. Goodwill Protection, Market Niches and Economic Growth

Ecological niches are comprised of the sum of conditions and resources necessary for an organism, taking into account its tolerances and requirements, in order to practice its way of life. Niches refer also to the circumstances under which organisms are more likely to survive and persist. Shifted onto the domain of economics, the niche concept has come to connote the state of a firm having insulated itself from competitive pressure to such an extent that it enjoys some security from price undercutting by rival competitors. Market niches may emerge as a result of barriers to entry or barriers to mobility, the latter impeding other incumbent firms from gaining a foothold in a specific segment of a given market. Product differentiation is a very effective means of fortifying a market niche. As already pointed out, the protection of differentiation strategies through trademark law has a positive impact on product diversity. The occupation of a profitable economic niche augments profitability and in that way provides a financial basis for expansion and possibly R&D. Market niches become therefore beneficial for long-term economic growth and development. Assuming an absence of barriers to entry, the equilibrium of the Chamberlinian model entails a large number of sellers selling slightly differentiated products. Due to the vast traffic in the product space, the monopolistic positions around the circumference of Salop’s circle are too narrow to promote economic growth. When assessing the optimal number of brands, given that marginal brands create losses in static efficiency, it is not only product variety but also the aspect of growth that has to be taken into consideration.

The economic concept of niche indicates that the market power conferred by a trademark is a monopolistic element in competition, which gives smaller undertakings an opportunity to survive while competing with established rivals and growing internally. Protecting an economic niche would be in many instances essential for maintaining an effective competition process. In view of their scale economies and their right to control their own shelves, large retailers are able to undercut individual sellers by marketing look-alike products bearing similar marks, colors and trade dress. As far as trade dress is concerned, this point is usually overlooked. Contrary to the suggestions of the US Supreme Court in Wal-Mart Stores, Inc. v. Samara Brothers, Inc., the imposition of a secondary meaning requirement would not promote effective competition in such a market context.

143 See R.E. Caves & M.E. Porter, From Entry Barriers to Mobility Barriers: Conjectural Decisions and Contrived Deterrence to New Competition, 91 Q.J. Econ. 241, 249 (1977) (explaining the notion of barriers to mobility).
144 Tisdell & Seidl, supra note 142, at 127.
145 Id. at 129.
Goodwill protection would in all these cases enhance product variety and keep larger undertakings under constant competitive pressure to better match consumer preferences. Clearly, the market power inherent in a trademark should not only evoke alertness about the existence of monopolistic tendencies in competition but also awareness of the fact that broad goodwill protection might yield substantial procompetitive benefits.

IV. Implications for Trademark and Unfair Competition Law

A. Goodwill Protection and Dynamic Competition With Differentiated Products

The preceding analysis has shown that the procompetitive benefits of protecting the advertising value attached to trademarks outweigh the expansion of monopolistic elements in competition arising from the enhancement of the legal entitlement’s exclusionary effect. Broad goodwill protection will stimulate dynamic competition with differentiated products. Consumer welfare increases as firms become incentivized to effectively match consumer taste. Awarding protection for economic niches based on product differentiation through trademark and unfair competition law can be a means for facilitating economic growth. Even though our knowledge of the welfare effects of advertising is not perfect, the existent clues militate, as we already saw, in favor of adopting a trademark protection paradigm based on the notion that the rights-holder has a legitimate proprietary interest in the intangible economic value of goodwill. Moreover, goodwill protection through trademark law would promote more dynamic forms of competition, such as product line rivalry, which secure further incentives for product differentiation and maintenance of good quality. At the same time, we should be cautious about possible anticompetitive effects of goodwill protection in specific cases and continuously strive to draw relevant limits.

This approach aligns the legal regulation to the actual effect of trademark protection on competition. It substantiates the principle of complementarity between intellectual property rights and competition law in the field of trademarks. A system of protection constructed upon confusion-based theories of liability and exceptional dilution protection under stringent requirements disregards not only the way trademarks affect competition but also the actual interests of rights-holders, their competitors and consumers. Notably, the expansion of the trademark exclusivity so

148 Luís M.B. Cabral, Optimal Brand Umbrella Size (N.Y. Univ. Stern Sch. of Bus., Working Paper No. EC-01-06, 2001) (suggesting that umbrella marketing reduces seller moral hazard and increases incentives to maintain good product quality because consumer punishment in the opposite case would be especially harsh. Even if a broad brand portfolio may allow the trademark holder some failure to market good product quality, consumers will still harshly punish repeated delivery of bad quality). See also Fredrik Andersson, Pooling Reputations, 20 Int’l J. Indus. Org. 715, 723–24 (2002).
149 See generally APOSTOLOS CHRONOPOULOS, DAS MARKENRECHT ALS TEIL DER WETTBEWERBSORDNUNG (2013).
as to embrace the economic value of goodwill is not meant to simply favor the rights-holder. The prohibition of goodwill appropriation cannot also be justified through a theory of unfairness derived from principles of unjust enrichment. The justification relates to the necessity of shaping trademark rights in a manner that promotes the effectiveness of competition.

B. Limits on Goodwill Protection

1. Limits on the Rent Seeking Activity of the Rights-holder: Goodwill Transferability

The finding that the effectiveness of competition relies significantly on the protection of goodwill against free-riding raises the duty of defining the limits of the exclusionary effect of trademark rights. If the goodwill attached to a trademark were to be fully internalized for the benefit of the rights-holder, this may seem at first sight to suggest that the scope of trademark rights should expand so as to prohibit the junior use of the respective sign for all imaginable product categories, even in connection with the most unrelated goods. The mark would then in effect become the absolute property of the rights-holder. Such a broad scope of the trademark right would for many reasons unduly restrict competition. Most obviously, the prohibition to use the sign in product categories where it does not fulfill any function of source identification, either because the rights-holder is not active in the specific market segment or because the third party use would not create any confusion as to the commercial source due to the lack of proximity between the relevant goods, would amount to a monopolization without any redeeming procompetitive virtue in regard to market transparency. Furthermore, it would be an unnecessary burden on competition if third parties did not attempt to free-ride on the rights-

---

150 Cf. Swann & Davis, supra note 51, at 257 (arguing that positive brand associations should give rise to a property right and that overtoning the rights-holder’s “property interest” in the exclusive use of a source identifier has suppressed the rights-holder’s “property interest” in brand equity”). See also Joel H. Steckel, Robert Klein & Shelley Schussheim, Dilution Through the Looking Glass: A Marketing Look at the Trademark Dilution Revision Act of 2005, 96 TRADEMARK REP. 616 (2006); Jerre B. Swann, An Intuitive Approach to Dilution, 89 TRADEMARK REP. 907 (1999).


holder’s goodwill or they had a legitimate reason to use an identical or similar mark in the specific market segment.

The consideration of avoiding these overbroad exclusionary effects led to the abandonment of the concept of trademarks as absolute and limitless property rights in favor of a more functional approach, which sought to demarcate the scope of exclusivity by anchoring trademark law to the policy of combating consumer confusion as to the commercial source of products. As already indicated this approach does not do justice neither to the rights-holder’s interest in exploiting his goodwill in distant markets nor to the effectiveness of competition in terms of product variety. The problem of defining the market segments that could be affected by the prohibitive authority of the trademark owner while simultaneously bearing no relation to the goods or services, for which a trademark has been registered or with respect to which a trademark has been acquired at common law, has always been one of the most strenuous problems of trademark theory.

The development of workable criteria for determining the market segments where the rights-holder should be able to commercially exploit his goodwill should rest upon the consideration that the trademark exclusivity is a mechanism for securing incentives to create goodwill and allow undertakings to expand their trade. Competition drives undertakings to differentiate so as to secure their own market niche and exercise market power. To secure these incentives to differentiate stimulated by the prospect of monopolistic profits, trademark law must allow the rights-holder to prevent third parties from usurping goodwill by adopting identical or similar marks.

Trademark rights should accordingly develop their exclusionary effect in all market segments whose integration in the legal exclusivity is necessary for maintaining incentives to differentiate. When the goodwill attached to a trademark plays a role in generating demand for a specific product category, then the rights-holder should be able to exploit such goodwill in that specific market segment. Goodwill transferability, as defined above, determines the scope of trademark protection.\(^{153}\)

The criterion of goodwill transferability is not congruent with the so-called “natural expansion of business” doctrine, which has also been deployed in order to determine the authority of the rights-holder to prevent third parties from using a trademark on non-competing goods.\(^{154}\) Specifically, the relevant test inquires whether the products or services, for which a third party uses the senior mark, are a natural outgrowth of the rights-holder’s line of products.\(^{155}\) A straightforward example is the case of goods or services bearing the same descriptive properties. For the rest, courts relying upon this theory to enjoin junior uses in non-competing goods have required the plaintiff to show that there is a reasonable likelihood of ex-

\(^{153}\) This could be the answer to the concerns of Justice Hand, who emphasized the need to draw limits on the authority of the rights-holder to prevent non-competing uses of his mark. L. E. Waterman Co. v. Gordon, 72 F.2d 272, 273 (2d Cir. 1934).

\(^{154}\) See generally Marks, supra note 51, at 869; McCarthy, supra note 1, § 24:17.

\(^{155}\) L. E. Waterman Co., 72 F.2d at 273.
pansion into a new market.\textsuperscript{156} Evidence of the rights-holder’s intent to extend the use of his trademark to a new field of activity would ensure the requirement is met.\textsuperscript{157} Absence of such intent would be inferred when the rights-holder has been using a trademark in commerce for a very long time without attempting to penetrate the market at issue.\textsuperscript{158} The doctrine protects “expansion interests” of the trademark proprietor and not product diversification in general.\textsuperscript{159} Even a widely diversified business could only enjoin non-competing uses as long as the marketing of the extension product would not require the trademark holder to substantially alter his manufacturing operations or distributional practices.\textsuperscript{160} Another interpretation has been to make the expansion interests of the trademark holder dependent on consumer confusion. Junior uses may therefore be enjoined only when consumers are likely to believe that the trademark owner has already “bridged the gap” and is now active in the market of the junior user.\textsuperscript{161} All these limitations had the object of forestalling trademark expansion so as not to award “trademark rights in gross.”\textsuperscript{162} The “natural expansion of business” doctrine is clearly ill-suited to address the problem of optimal goodwill internalization in trademark law especially due to its focus on plaintiff’s intent to enter a given market under a specific mark and its objective to keep the exclusionary effect of trademarks as narrow as possible.

This is not because the rights-holder has some kind of natural right to the goodwill he has created.\textsuperscript{163} The internalization of this intangible value takes place for the sake of promoting a dynamic competition with differentiated products by ensuring to the trademark holder that he will be able to capture the economic value of the marketable goodwill he has created. Goodwill protection is ultimately justified by the need to promote effective competition.\textsuperscript{164}

\textsuperscript{156} See also Paul R. Jackiewicz, Note, 29 NOTRE DAME L. REV. 132 (1953–1954).
\textsuperscript{157} G. B. Kent & Sons, Ltd. v. P. Lorillard Co., 114 F. Supp. 621, 630 (S.D.N.Y. 1953) (not dealing with the issue of whether likelihood of confusion is a condition precedent to the legal protection of expansion interests because it was not necessary for resolving the dispute).
\textsuperscript{159} ILC Indus., Inc. v. ILC, Inc., 175 U.S.P.Q. 623, 626 (T.T.A.B. 1972).
\textsuperscript{161} Thomas P. Deering, Trade-Marks on Noncompetitive Products, 36 OR. L. REV. 1, 7 (1956).
\textsuperscript{162} Marks, supra note 51, at 874.
\textsuperscript{163} Cf. Franklyn, supra note 37, at 139–40 (elaborating on how the labor theory of property rights provides a rationale for the protection of famous marks against free-riding).
\textsuperscript{164} Nicola Bottero, Andrea Mangâni & Marco Ricolfi, The Extended Protection of “Strong” Trademarks, 11 MARQ. INTELL. PROP. L. REV. 265 (2007) (emphasizing that expanded trademark protection should always be justified through some measure of consumer welfare); Mathias Strasser, The Rational Basis of Trademark Protection Revisited: Putting the Dilution Doctrine into Context, 10 FORDHAM INTELL. PROP. MEDIA & ENT. L.J. 375, 415 (2000) (arguing that there are several utilitarian arguments in favor of the dilution theory, such as that it provides additional incentives for rights-holders to market satisfactory products and that it prevents a situation of moral hazard where third parties market lower-quality goods while taking advantage of the quality assurance symbolized by a famous mark).
2. Protecting Locational Competition

As long as there are vacant locations in product space available for new entrants to occupy, the mere existence of incumbent trademarks would not by itself hinder the emergence of new competition. Nonetheless, to whatever extent trademark ownership interferes with locational competition, it should raise concerns about anticompetitive effects. An alleged violation of Section 5 of the FTC Act has been prosecuted under a relevant theory of competitive harm in the past.\textsuperscript{165} Suit was filed against three major producers of breakfast cereal, charging that they tacitly colluded in order to exclude potential competitors from the market. Among the unfair methods of competition allegedly deployed by the defendants was brand proliferation. Incumbent firms had been introducing many diverse brands throughout the product space, thus not allowing potential competitors to find market niches attracting a significant number of consumers that would allow them to take advantage of scale economies.\textsuperscript{166} New entrants were deprived of their potential to grow and their ability to compete was stifled from the outset. After having shielded the market for breakfast cereal against outsiders, the defendants were in fact sharing a position of monopoly with each other ("shared monopoly theory"). Suit was not successful in the end because the FTC reasoned that it would be possible for a potential competitor to penetrate the market and maintain a sustainable position of economic power by proliferating diverse brands himself in order to capture consumers situated across various locations of the product space.\textsuperscript{167} Because market entry was not actually precluded, no antitrust injury could be established. The FTC argued also that brand proliferation is not per se an exclusionary method of competition because it is directed at satisfying diverse consumer preferences.\textsuperscript{168} Scrutinizing the effects of respondents’ behavior on competition through the prism of a structure-conduct-performance analysis, the FTC found no evidence of monopoly behavior such as limitations of supply, supra-competitive prices or even innovative inertia, as the incumbent firms had been introducing new brands.\textsuperscript{169}

In terms of competition policy though, it makes sense to protect locational competition. If the point of protecting market niches is to provide a foothold to newcomers, which would assert competitive pressure to larger undertakings in the long run, then it becomes apparent that their freedom to locate themselves in a viable market niche of the product space should be protected. On the other hand, markets dominated by a "shared monopoly" would tend to bring about suboptimal variety, as the incumbent firms would differentiate to the extent of their own profit maximization once they have scared away new market entry. It would be a disproportional restriction of the right to participate in economic life to render market entry impossible for those economic operators that are not yet capable of competing

\textsuperscript{165} In re Kellogg Co., 99 F.T.C. 8 (1982).
\textsuperscript{167} In re Kellogg Co., 99 F.T.C. at 257, 276–77 (separate statement of Commissioner Clanton).
\textsuperscript{168} Id. at 256.
\textsuperscript{169} Id. at 267.
by brand proliferation. Under the competitive circumstances in *Kellogg*, market entry was not impossible but indeed very difficult. Enhancing the contestability of the market in a case like that would increase competitive pressure for incumbent firms without creating false positives.

The issue touches upon the more general problem of ascertaining the relationship between Section 2 of the Sherman Act and Section 5 of the FTC Act, which cannot be examined here in further detail. Rightfully, most commentators argue that the constitutionally mandated notion of unfairness allows the implementation of competition policy below the thresholds of antitrust harm set by the antitrust laws.170

3. Protecting Trademark and Communicative Interests of Competitors

Goodwill amounts to a protectable intangible value regardless of the type of mark it has been attached to. However, the assertion of trademark rights in words of common vocabulary in distant markets is highly likely to interfere with legitimate interests of third parties in language usage.171 The scholarly example refers to the word mark “AMAZON” used in connection with an electronic bookstore. A travel agency specializing in adventure holidays would have an obvious interest in being able to freely make use of the same word. But except for the referential use, the junior user may have a legitimate interest in using the word “AMAZON” as a trademark due to its suggestive nature. Due to their advertising value, suggestive marks constitute a very effective means of source identification and promotion.172 In such a case, the junior user is not attempting to free-ride upon the goodwill of the trademark holder but rather to build up his own goodwill through a suggestive trademark. It might well be that the junior user somehow profits from the distinctiveness173 of the famous senior mark in that he may find it easier to attract the attention of consumers to his services. This collateral advantage does not alter the


171 Franklyn, supra note 37, at 148–50; cf. Majestic Mfg. Co. v. Majestic Elec. Appliance Co., Inc., 79 F. Supp. 649, 650–51 (N.D. Ohio 1948) (arguing that non-competing uses could only be enjoined by owners of “original,” “arbitrary,” “fanciful,” or “strong” marks). These concerns indeed have merit. But instead of denying protection to goodwill attached in a “weak” mark, courts could distinguish between the market segments where the rights-holder should be able to exploit goodwill and those where junior uses should be permitted for communicative purposes. See Creamette Co. v. Conlin, 191 F.2d 108, 112 (5th Cir. 1951) (“We think it true that a name may be arbitrary or fanciful as applied to one or more products, but yet not be entitled to unlimited protection as against its good faith tradename adoption and use upon a product of which, because of its inherent properties, it is plainly and accurately descriptive in ordinary meaning.”).


173 Goodwill is not transferable to the market of the junior user in this example.
fact that the overall balance of competitive interests involved in the example is in favor of allowing the junior use of the mark.\textsuperscript{174} The attempt to balance the diverse interest positions involved in trademark disputes should also include the aspect of whether the junior user is in any respect reliant upon the use of a specific mark, given the unlimited availability of other signs that are appropriate for identifying and differentiating that trade.\textsuperscript{175}

The distinction between the use of a word as a trademark for the source identifying purposes of the rights-holder and other referential uses left at the disposal of competitors for communicative purposes is meant to strike a balance between competitive interests of multiple market operators. Sometimes though, this legal construction would not do justice to the communicative interests of competitors.\textsuperscript{176} Some laudatory terms connoting brand reliability such as “performance,” “authentic” and “genuine brand,” for example, should not be trademarked because all competitors have an equally legitimate interest in their unconstrained use. The freedom to make referential use of these terms does not adequately address competitors’ communicative interests in connoting brand reliability because the trademark holder would be in an unjustifiably advantageous position in regard to this specific parameter of competition. The Sixth Circuit has opposed such an anticompetitive monopolization by holding the respective terms to be \textit{de jure} functional.\textsuperscript{177}

4. Free-Riding Upon the Distinctiveness of a Senior Mark in Markets With Low Levels of Differentiation

As already noted, senior marks with a high degree of recognition and distinctiveness in the marketplace may be used by third parties for dissimilar products in distant markets in order to increase the level of differentiation in these markets. These would be hard cases to decide. When the trademark holder provides evidence of intent to exploit the distinctive character of the mark in connection with the unrelated goods at issue, he should be able to prevail. Otherwise, he would have

\textsuperscript{174} The conflict between the interest of the rights-holder in exploiting his goodwill in related or distant markets and the communicative interests of competitors and the public is difficult to resolve in such cases. Polaroid Corp. v. Polaraid, Inc., 319 F.2d 830, 835 (7th Cir. 1963). “POLARAIM” is a composite mark which is suggestive of the services offered by the defendant in connection with refrigerating and heating systems. Plaintiff’s goodwill is not transferable to defendant’s products. The defendant is making use of two descriptive terms as elements of a suggestive mark. There is some collateral free-riding upon the high degree of distinctiveness of the senior mark. Overall, the balance of interests involved indicates that the junior use should be allowed. The court ruled for the plaintiff on the grounds of dilution.


\textsuperscript{176} Cf. Stephen L. Carter, \textit{The Trouble with Trademark}, 99 \textit{Yale L.J.} 759, 768 (1990) (considering the protection of communicative interests of competitors, rather than the possible anticompetitive effects of product differentiation as the most important concern about overbroad trademark protection).

to establish a dilution claim. Nike, Inc. v. Nikepal International, Inc. seems to be an illustration of this type of trademark litigation. Defendant used the mark “NIKEPAL” for syringes and sought actively to create consumer associations to the senior famous mark. The court found for the trademark holder on the dilution claim.

It is not very clear how the issue of free-riding on the distinctiveness of a famous mark should be dealt with in such cases. If we allow free-riding with the purpose of facilitating the market entry of the junior user, we will encourage third parties to adopt marks that are similar to famous trademarks when deciding to enter a market. Allowing the generalization of this business practice would provide fertile ground for dilution of famous marks by blurring. Trademark owners should at least be allowed to argue likelihood of dilution arising from the cumulative effect of such uses. Given that the circle of marks qualifying as famous is narrow, the firms that would not be able to engage themselves in such a form of competition would be unjustifiably disadvantaged against the free-riders. The appropriation of a famous mark’s distinctive character should, on a balance of the competitive interests involved, not be enjoined where the junior user is simultaneously asserting an interest in using words of common vocabulary as an element of a suggestive mark. Coined trademarks would generally be broader in scope than other types of marks.

5. Further Limitations of Goodwill Protection Dictated by Consumer Interests

Generating goodwill through product differentiation might not always be pro-competitive. In markets for generic pharmaceuticals, branding activities may undermine the effectiveness of competition. Consumer welfare depends primarily on static efficiency and quality assurance in relation to the healing properties of the product. Pharmaceutical companies have an incentive to invest in brand loyalty in order to suppress competition from generics and to impede new market entry. Protecting the goodwill attached to trademarks in markets for generic pharmaceuticals would not only reduce consumer welfare in terms of productive efficiency but would also provide incentives for companies to spend large sums on brand equity instead of investing in R&D. Therefore, no protection against misappropriative associations should be available for the rights-holder in this context. By virtue of his trademark rights he should only enjoy reputational advantages related to his capabilities as a producer of good quality pharmaceuticals.

Restrictions on the protection of goodwill may also arise from the regulation of advertising content. Recently, the promotion of cigarettes has been subjected to serious limitations on suggestive advertising. Extended goodwill protection in the tobacco industry would be contrary to public policy. Because trademarks are part of,


and therefore teleologically subjected to, the broader complex of norms regulating the competitive process, legal restrictions on advertising set out in unfair competition laws should have normative implications for the scope of trademark rights.

V. Goodwill Appropriation in Unfair Competition Law

A. Is There a Misappropriation Doctrine in Unfair Competition Law?

Unfair competition theory has long grappled with the question of whether competitors are under a duty to compete by deploying their own effort and skill instead of appropriating business values created by another. The starting point of this discussion is the Supreme Court opinion in International News Service v. Associated Press.180 Associated Press (AP) was an east coast news wire service provider, who had been investing time and resources to obtain news from the European front during World War I. Competitor International News Service (INS), situated on the opposite coast, was wiring these stories to customers in their own territory. Due to the respective time span, the newspapers belonging to the network of INS were able to deliver the news at the same time or, in some instances, even earlier than the competing AP papers. The Supreme Court ruled for the appellant and condemned INS for misappropriating the labor and skill of another, emphasizing the unethical approach of trying to “reap where [one] has not sown” or to appropriate “the harvest of those who have sown.”181 No matter how plastic and colorful these metaphors might be, they do not reveal the actual ratio decidendi of the case. The court reached its conclusion by inquiring upon the competitive situation that would arise if protection were to be denied. It seemed highly likely that AP would not manage to survive the competition with a rival that bore no cost of collecting the news information.182 That would result in the collapse of the market, because AP was the sole undertaking in the position to provide the service demanded by the market.183

A sweeping unfair competition theory that would effectively rule out any appropriation of subject matter attributed to the business efforts of another has to be rejected mainly for the purpose of avoiding undue restrictions on competition. Its broad formulation and the lack of clarity regarding the requirements of protection render the misappropriation doctrine undesirable from the perspective of competition policy.184 Nevertheless, it would be much more sensible to narrow down the propositions of INS following the directions that the Supreme Court itself gave us, rather than completely eradicating the doctrine. The opinion deployed a “but for” approach, which took into account the competitive consequences of allowing the appellant to appropriate the news information generated by his competitor. Following the intellectual process of narrowing down the scope of the tort theory described in INS, one might encounter situations where the effectiveness of competition

180 248 U.S. 215 (1918).
181 Id. at 239–40.
182 Id. at 240–41.
183 Id. at 241.
would be promoted if third parties were prohibited from free-riding upon business values created by another.\(^\text{185}\) It is submitted that such a case of actionable misappropriation arises when a free-ride is taken upon the goodwill of the trademark holder. Awarding protection aims at stimulating dynamic competition with differentiated products.

B. Misappropriation of Goodwill as a Category of Unfair Competition

Case Law

The reluctance of contemporary courts to recognize goodwill appropriation, or free-riding, as an independent theory of trademark liability correlates to their skepticism towards the misappropriation doctrine in unfair competition law. Nevertheless, an anti-free-riding impulse can already be discerned, for example, in the infamous “Odol” case,\(^\text{186}\) which is usually reported as the cradle of protection against dilutive harm.\(^\text{187}\) Being famous for mouthwash products, the mark “Odol” had been used for bathtubs. The junior user was held liable in tort for inflicting economic harm to the claimant by tarnishing his trademark. In the court’s view, the interference with the semantic content of the trademark was endangering its capacity to connote a positive association regarding the quality of the trademarked goods to the minds of the consumers. The claimant would therefore suffer economic loss due to the diminished selling power of its mark. The court subsumed the set of facts under Article 826 of the German Civil Code (BGB), pursuant to which the intentional cause of harm to another in a manner contrary to bonos mores gives rise to tortious liability.\(^\text{188}\) The diluting use was held to be unlawful in the sense of violating bonos mores because it allowed the defendant to avail himself of the positive consumer associations incorporated in the “Odol” trademark and thereby transfer them to his own products. The judgment contains therefore a condemnation of free-riding upon the goodwill of another although it does not provide for a general theory of goodwill misappropriation.

Judgments awarding injunctions against uses of senior marks on non-competing goods that were held to be confusing as to source or affiliation have simultaneously disapproved the defendant’s effort to get the benefit of the reputation of

\(^{185}\) In the context of trade dress, see Apostolos Chronopoulos, *Trade Dress Rights as Instruments of Monopolistic Competition: Towards a Rejuvenation of the Misappropriation Doctrine in Unfair Competition Law and a Property Theory of Trademarks*, 16:1 MARQ. INTELL. PROP. L. REV. 119, 137–38 (2012).


the trademark owner.\textsuperscript{189} An early example is the English case of \textit{Eastman Photographic Materials v. John Griffiths Cycle Corp.},\textsuperscript{190} which was eventually decided on the grounds of passing-off. The trademark in suit, “Kodak,” had been used in connection with cameras long enough to develop to a symbol of reputation for its holder. The defendant was successful in registering the mark for bicycles. The court was convinced that allowing the junior user to conduct business under the claimant’s mark would cause confusion to consumers who might assume that the defendant’s bicycles were emanating from the trademark holder or that there was some kind of connection between the parties of the dispute.\textsuperscript{191} An act leading to such type of confusion in the marketplace was deemed by the court to be indicative of an intention to capitalize upon the reputation of the senior mark.\textsuperscript{192}

Similarly, in the landmark case of \textit{Aunt Jemima Mills Co. v. Rigney & Co.},\textsuperscript{193} a producer of syrup and sugar cream adopted a word mark that was already being used by the claimant in connection with baking flour. The court emphasized that it was due to the proximity of the goods that the consumers would be induced to believe that the syrup or sugar cream products bearing the “Aunt Jemima’s” mark had been produced by the claimant.\textsuperscript{194} Additionally, the junior use was held as allowing the defendant to take advantage of the reputation and the advertisement of the trademark holder, which were to be treated as property rights protectable in equity.\textsuperscript{195} Free-riding would basically take place due to the proximity of the goods. In other words, this was an example where goodwill was transferable to other non-competing goods.

In a similar vein, a great deal of cases have condemned the act of adopting a senior trademark for non-competing goods, as a business practice that has no other purpose or effect than to cause confusion as to source or affiliation and thereby allows the junior user to appropriate the reputation and the advertising value created by the trademark holder. These rulings seem to proceed on the assumption that the confusion requirement is automatically met whenever the defendant uses the senior mark for products that were similar to those marketed by the trademark holder. The similarity of the products referred generally to a situation where the goodwill of the products marketed under the senior mark was transferable to the goods of the junior

\textsuperscript{189} \textit{See generally} Deering, \textit{supra} note 161, at 2–15 (discussing this particular extension of the confusion theory); \textit{cf.} John Wolff, \textit{Non-Competing Goods in Trademark Law}, 37 COLUM. L. REV. 582 (1937) (ignoring the free-riding rationale that underlies these cases and treating them as precedents that establish the theory of confusion as to sponsorship or affiliation).

\textsuperscript{190} \textit{Eastman Photographic Materials Co. Ltd. v. John Griffiths Cycle Corp. Ltd.}, (1898) 15 R.P.C. 105 (U.K.).

\textsuperscript{191} \textit{Id.} at 111–12.

\textsuperscript{192} \textit{Id.} at 110–11.

\textsuperscript{193} \textit{Aunt Jemima Mills Co. v. Rigney & Co.}, 247 F. 407 (2d Cir. 1917).

\textsuperscript{194} \textit{Id.} at 409–10.

\textsuperscript{195} \textit{Id.} at 410.
user. Further, the confusion requirement was in a certain sense circumvented by lowering the threshold for its affirmation sometimes also by referring to an alleged goal of the unfair competition law to protect even the most naive of the consumers from deception. Even where there was a finding of some actual confusion occurred in the marketplace, the courts were proceeding on the assumption that the non-competing use of a senior mark is as such an act of fraudulent nature aiming at the appropriation of advertising value. After a light-handed administration of the confusion requirement, the court would present the appropriation of goodwill as the commercial wrong it sought to prevent in the most adamant terms. In essence, the courts were condemning free-riding. In some instances the courts would not only condemn free-riding, but they would even explicitly admonish the junior user for entering the market without generating his own goodwill.

196 Because trademark infringement only came into play under the 1905 Trademark Act in the case of goods sharing the same descriptive properties, the cases were decided by recourse to the unfair competition cause of action. See, e.g., Yale Elec. Corp. v. Robertson, 26 F.2d 972 (1928).
198 Aetna Causalty & Surety Co. v. Aetna Auto Finance, Inc., 123 F.2d 582, 583–84 (5th Cir. 1941); Del Monte Special Food Co. v. California Packing Corp., 34 F.2d 774, 776–77 (9th Cir. 1929); Buckspan v. Hudson’s Bay Co., 22 F.2d 721, 722 (5th Cir. 1927).
199 See, e.g., Rosenberg Bros. & Co. v. Elliot, 7 F.2d 962, 967 (3d Cir. 1925); British-Am. Tobacco Co., Ltd., 211 F. at 935.
200 See, e.g., R. H. Macy & Co., Inc. v. Macy’s Drug Store, Inc., 84 F.2d 387, 388 (3d Cir. 1936) (“[The non-competing use of the senior mark] was intended to, and had a tendency to, mislead and deceive the public into the belief that the defendants’ business was connected with that of the plaintiff. Indeed, the entire atmosphere surrounding the acquisition of the name ‘Macy’s’ by the defendants justifies a conclusion that there was a palpable attempt to make use of the plaintiff’s reputation and good will, acquired through many years of advertising, and appropriate it to the benefit of the defendants and deceive the Public.”); Aetna Cas. & Sur. Co., 123 F.2d at 584 (“The name itself coupled with the advertising defendant began with, . . . leaves us in no doubt that it was the purpose of defendant to build itself upon the established reputation and business strength of plaintiff and to reap such benefit from it as it could. . . [W]here as here it plainly appears that there is a purpose to reap where one has not sown, to gather where one has not planted, to build upon the work and reputation of another, the use of the advertising or trade name or distinguishing mark of another, is in its nature, fraudulent and will be enjoined.”); Acme Chem. Co. v. Dobkin, 68 F. Supp. 601 (W.D. Pa. 1946) (“Though there has been shown but slight confusion, it requires nothing but comparison of the names and the fundamental character of the business done to demonstrate that there is a likelihood of future confusion. I, therefore, believe that there exists a threat, if not a promise, of growing confusion to the detriment of the plaintiff’s reputation in an area in which its patrons are in part drawn. The public could very easily be confused and think that they are dealing with the plaintiff in violation of the principle that a name and reputation like a face is the symbol of its possessor and creator, and another can use it only as a mask. It also appears to me there is a purpose to reap where one has not sown, to gather where one has not planted, to build upon the work and reputation of another, the use of the advertising or trade-name of the plaintiff and, under such circumstances, it is the duty of the court to grant injunctive relief.”); see also Standard Oil Co. of N.M., Inc. v. Standard Oil Co. of Cal., 56 F.2d 973, 980 (10th Cir. 1932); Kroll Bros. Co. v. Rolls-Royce, Ltd., 126 F.2d 495, 497 (C.C.P.A. 1942).
201 Aetna Cas. & Sur. Co., 123 F.2d at 584 (“[The purpose of the junior user entering the market] is to project itself into that business arena panoplied in a name already favorably known, rather than to come into it on its own merits, and slowly building, here a little, there a little, establish its own place.”).
This line of case law is better understood if we recall the threefold purpose of the pristine unfair competition cause of action to promote honesty and fair dealing in the marketplace as well as to protect competitors and consumers from deceptive acts. The disapproved practices were scrutinized for their potential, and not actual, capacity to cause confusion. Case law was thereby providing consumers and competitors an absolute protection against deception, while enforcing honesty and fair dealing in a rigorous manner. The courts were determined to oppose free-riding while at the same time striving to customize their judgments within the traditional framework of the unfair competition cause of action. By drastically lowering the threshold for affirming the confusion requirement, the courts were practically applying a theory of misappropriation.

The courts had been drawing a distinction between uses of senior marks on competing goods, which were misleading as to source for the purpose of diverting trade from the trademark holder, and uses of senior marks on non-competing goods, which were misleading as to source for the purpose of appropriating the goodwill of the trademark holder so as to promote the sales of the junior user.

One of the most cited cases decided upon this particular misappropriation theory is that of Wall v. Rolls-Royce of America, Inc. A company selling radio tubes by mail used the senior mark “Rolls-Royce” as part of its trade name. The junior user’s products were touted in advertisements as being of significant quality, just like their name was suggesting. The court opined that such actions were objectively directed at utilizing the trade reputation and the earned good will of the trademark holder by making a misrepresentation of being affiliated with the “Rolls-Royce” group. Because the senior user was operating a business involving electrical appliances, the consumer might suppose that they had extended their business to radio tubes. According to the court, this association with potentially inferior quality products would endanger the rights-holder’s goodwill.

By enjoining the junior use of the “Rolls-Royce” mark, the court felt that it was promoting commercial morality in the marketplace.

---

202 See, e.g., Rosenberg Bros. & Co. v. Elliot, 7 F.2d at 965–66.
204 Callmann, Property Concept, supra note 151, at 448.
205 Stork Rest., Inc. v. Sahati, 166 F.2d 348, 356 (9th Cir. 1948).
206 Wall v. Rolls-Royce of Am., Inc., 4 F.2d 333 (3d Cir. 1925).
207 Id. at 334 (“Upon no other theory than a purposed appropriation to himself, and an intent to convey to the public a false impression of some supposed connection with the Rolls-Royce industries, can Wall’s actions and advertisements be explained.”).
208 Id.
209 Id. (“Indeed, from the standpoint of commercial integrity, fair business, and trade equity, we feel the court below, sitting in equity, was justified in preventing the defendant from veiling his business under the name of ‘Rolls-Royce,’ for he had, and could have had, but one object in view, namely, to commercially use as his own a commercial asset that belonged to others, the continued use and abstraction of which is so fraught with such possibilities of irremediable injury that the only way to remedy it is to stop it at the start.”).
The defendant was held to have used the senior mark for the purpose of trading on the reputation and the goodwill of the trademark holder.\textsuperscript{211} The defendant was in fact seeking a trade name for his corporation selling shirts that would associate his products with England’s “great reputation [for] turning out well-dressed men.”\textsuperscript{212} According to the Fifth Circuit in \textit{Buckspan v. Hudson’s Bay Co.}, the adoption of a name that was very similar to the trade name of an already established firm could do nothing but give rise to an inference of an intention of the junior user to secure the advantages of an association with a well-reputed business.\textsuperscript{213}

Other examples of junior uses on non-competing goods that were enjoined as “fraudulent misappropriation” are readily available. In one case, a distilling company used as part of its corporate name and on its whiskey labels the senior mark “Churchill Downs,” which had become a symbol of goodwill for an undertaking that maintained a racing plant. The court opined that the exclusive use of the mark was a property right in a qualified sense, which would be protected from another’s intentionally exploitative use.\textsuperscript{214} In another case, the appellant was held to have attempted to take advantage of the trademark holder’s goodwill by labeling his oleo-margarine with the senior mark “Del Monte” which had, in the meantime, acquired a good reputation for foodstuffs.\textsuperscript{215} The junior use was considered to have been calculated so as to create source confusion.\textsuperscript{216} And in a third case, \textit{Armour & Co. v. Master Tire & Rubber Co.}, a developing company producing goods incident to the use of automobiles was held to be entitled to enjoin the junior use of its trade name in the business of manufacturing and selling tires.\textsuperscript{217}

Another group of precedents condemning free-riding upon the goodwill of another refers also to the potential of non-competing uses to cause dilutive harm.\textsuperscript{218} Permitting such uses would place the reputation of the trademark holder in the hands of the junior user, who might tarnish it if he decides at some point to market goods of inferior quality or to advertise in a manner that is dilutive for the senior mark.

Nevertheless, these precedents do not really stand for the proposition that extended trademark protection without the need for showing consumer confusion of some kind presupposes dilutive harm. Rather, the courts were trying to fit their misappropriation theory in the traditional unfair competition cause of action, which could only be maintained if the parties to the dispute were in a competitive relation-

\textsuperscript{211} Id. (“The only conceivable reason for the use of the name ‘Dunhill’ by the defendant is to trade on the reputation and good will of the plaintiff.”).

\textsuperscript{212} Id.

\textsuperscript{213} Buckspan v. Hudson’s Bay Co., 22 F.2d 721, 722–23 (5th Cir. 1927).

\textsuperscript{214} Churchill Downs Distilling Co. v. Churchills Downs, Inc., 90 S.W.2d 1041, 1044 (6th Cir. 1936).

\textsuperscript{215} Del Monte Special Food Co. v. California Packing Corp., 34 F.2d 774, 775, 777 (9th Cir. 1929).

\textsuperscript{216} Id. at 777.


\textsuperscript{218} Stork Rest., Inc. v. Sahati, 166 F.2d 348 (9th Cir. 1948); Bulova Watch Co., Inc. v. Stolzberg, 69 F. Supp. 543 (D. Mass. 1947); Tiffany & Co. v. Tiffany Prods., Inc., 264 N.Y.S. 459 (Sup. Ct. 1932).
ship. Therefore, the field of applicability of the unfair competition doctrine was extended so as to cover non-competing uses of senior marks because this commercial practice was likely to injure the plaintiff and as such it was an act that should fall under the ambit of the common law of unfair competition.\textsuperscript{219}

In \textit{Stork Restaurant, Inc. v. Sahati},\textsuperscript{220} for example, both parties to the dispute were engaging in the same business. Since they were restaurants in different states, remotely located from another, there was no possibility of fraudulent trade diversion. For this reason this case bore an analogy to those related to junior uses on non-competing goods because the applicability of the unfair competition cause of action had to be established through the principle that the goodwill of a trader should not become dependent on the quality of the goods offered by the junior user or the argument that dilutive harm was likely to occur. The courts have enjoined the misappropriation of the advertising value under the aforementioned application of the unfair competition doctrine.\textsuperscript{221}

In some of the cases, the aspect of dilution is expressly mentioned in a part of the judgment that was ruling on the applicability of the unfair competition laws. The cases were not awarding damages for dilutive harm, but they were focused on enjoining goodwill misappropriation.\textsuperscript{222} The proscription of dilutive harm in these cases that in effect established a common law theory of misappropriation probably did promulgate the idea that dilution laws are meant to combat free-riding.\textsuperscript{223}

\section*{VI. Goodwill Appropriation in Trademark Law}

\subsection*{A. A Free-Riding Rationale for the Dilution Doctrine}

The misappropriation theory developed through the common law of unfair competition found its way to the interpretation of dilution laws by the courts. The dilution statute of New York identified the three elements of a successful dilution claim as follows: a) a senior mark of high distinctive quality attributed either to its inherent or acquired distinctiveness; b) a junior use that dilutes the distinctiveness

\textsuperscript{219} Tiffany & Co., 264 N.Y.S at 461–62.
\textsuperscript{220} 166 F.2d 348.
\textsuperscript{221} Tiffany & Co., 264 N.Y.S at 463: “[The acts of the junior user] were deliberately intended to obtain, and in fact did obtain, an unfair advantage for defendant from the good will created by plaintiff in the name. The purpose of these acts was wrongfully and unfairly to appropriate for defendant’s pecuniary gain the value plaintiff had created in plaintiff’s own name and plaintiff’s unique business and financial reputation.” Bulova Watch Co., 69 F. Supp. at 547 (D. Mass. 1947); “Defendant has little cause to complain since he has been riding the coattails of the plaintiff’s good will, and he had available to him a wide range of choice to name his products.” \textit{Stork Rest., Inc.}, 166 F.2d at 357 (explicitly referring to the ‘reaping where one has not sown’ metaphor).
\textsuperscript{222} Stork Rest., Inc., 166 F.2d at 364 (issuing an injunction against an unfair trade practice—misappropriation—that would cause dilutive harm if continued); Tiffany & Co., 264 N.Y.S at 461–64.
\textsuperscript{223} See, e.g., Allied Maint. Corp. v. Allied Mech. Trades, Inc., 369 N.E.2d 1162, 1165 (N.Y. 1977) (“The evil which the Legislature sought to remedy was not public confusion caused by similar products or services sold by competitors, but a cancer-like growth of dissimilar products or services which feeds upon the business reputation of an established distinctive trade-mark or name.”).
and/or the reputation of claimant’s mark; and c) a predatory intent of the defendant to take an unfair advantage of the trademark holder’s goodwill through the adoption of an identical or similar mark. While the courts remained obstinate in their interpretation that the third factor relating to misappropriation is not dispositive, the judicial administration of the dilution action was essentially providing trademark protection against free-riding upon the goodwill of another. The relevant opinions were presuming dilutive harm whenever the similarity of the marks was likely to prompt consumers to associate the defendant with the senior mark. Having established so easily that trademark dilution was about to occur, the courts would then examine whether there was predatory intent in the adoption of the junior mark and eventually enjoin the misappropriative practices of the defendant. Establishing predatory intent required simply a showing that the defendant had been aware of the senior trademark at the time he adopted his own mark. The rulings reach a conclusion that impermissible trademark dilution has come to pass, although there has been no real examination as to whether the mark at issue was impaired by blurring of its distinctiveness or tarnishment of its reputation.

Typical of this judicial approach to the dilution cause of action is McDonald’s Corp. v. McBagel’s Inc.224 The defendant made use of the “Mc” prefix in combination with the name of a generic food item as a trade name for a bagel bakery and restaurant. The court held that the second element of the respective cause of action was present and referred to previous cases litigated in the Second Circuit, where the courts have not hesitated to find a “whittling down” of the trademark’s identity whenever a junior similar use created associations with the senior mark of the claimant.225 Immediately thereafter, the opinion condemns the predatory intent of the junior user, who has attempted to capitalize on business values of the trademark holder.226 The conclusive finding of dilution is reached without any substantial proof of dilutive harm, indicating that the principal concern of the court was to prevent the defendant from taking an unfair advantage of the goodwill of another.

Toys “R” Us, Inc. v. Canarsie Kiddie Shop, Inc.227 emphasizes that it would suffice for a finding of dilution if the junior user succeeds in evoking favorable associations for his products through the adoption of a similar mark. The defendant, a retailer in the business of children’s apparel including toys and clothing, used the mark Kids “r” Us in connection with his products. The junior use was directed at calling into consumers mind the image of a large warehouse store offering a wide variety of child related products at low prices symbolized in the claimant’s mark. In its concluding, and probably decisive, remarks the opinion holds that the defendant’s adoption of a similar mark was performed in predatory intent.

225 Id. at 1281.
226 Id.
B. Misappropriative Associations as Actionable Type of Confusion

1. Confusion and Misappropriation as Parallel Theories of Trademark Infringement

Third parties may attempt to exploit the commercial attractiveness of a senior successful trademark in order to increase consumer demand for their own products. By adopting a similar mark the junior user endeavours to trigger the positive associations generated by the established trademark and effectively incorporate them in his product bundle. He actually borrows something from the senior trademark’s capacity to function as a symbol of product desirability. The similarity of the marks causes the consumer to associate the products of the junior user with those marketed under the senior mark. As the products bear some common symbol of product desirability, consumers subconsciously identify the characteristics of one product with those of the other. In this manner the junior user manages to poach upon the commercial magnetism of another’s trademark and to take a free-ride upon the differentiation strategy of another. Justice Frankfurter seems to have justified the authority of the rights-holder to enjoin such uses on the grounds of the nature of trademarks as property rights. The proprietor is, according to the view of the judge, rightfully exploiting the goodwill attached to a trademark because he created the respective intangible value himself.

The S.D.N.Y. has, on the other hand, developed its own theory of trademark liability against goodwill misappropriation under the Lanham Act. In particular, the court has opined that the association between two products of different commercial origins implanted into the minds of consumers due to a mark similarity is a type of confusion that should be considered actionable within the meaning of Sections 32(a) and 43(a) of the Lanham Act. For example, Justice Macmahon affirmed that the use of the trademark “GROTRIAN-STEINWEG” on pianos was likely to precipitate subliminal confusion in regard to the senior mark “STEINWAY,” registered for the same products. It was immaterial that no actual confusion as to the source of the goods existed. Thus, this theory extends the protection of commercial goodwill beyond the prevention of confusion and establishes a misappropriation cause of ac-

---

228 Mishawaka Rubber & Woolen Mfg. Co. v. S. S. Kresge Co., 316 U.S. 203, 205 (1942) (“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 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. Once this is attained, the trade-mark owner has something of value. If another poaches upon the commercial magnetism of the symbol he has created, the owner can obtain legal redress.”) (emphasis added).

229 Id.

On appeal the Second Circuit did affirm the judgment, but it provided a slightly different account of the wrong committed against the rights-holder when subliminal consumer confusion takes place. The junior user was actually successful in capturing the attention of consumers who were already acquainted with the incumbent mark, while saving the advertising costs of making his product known to the public. The use of a similar mark, albeit not causing any confusion as to source, confers upon the new entrant an undeserved competitive advantage. By borrowing something from the senior trademark’s likeness, the newcomer is basically locating himself very closely to the point of the fictitious product space, where the incumbent firm is already residing. In other words, the junior user seeks to compete by imitation, expecting that the cost advantages he possesses would allow him to undercut his competitor.

The opinions subscribing to the subliminal confusion theory impute trademark liability for predatory intent while putting emphasis on the strength of the senior mark. The anticompetitive nature or the unfairness of trademark imitation does not actually rest on its alleged exclusionary effect. Sellers cannot claim protection from price competition of highly substitutable products. Neither should a relevant trademark action be recognized on the grounds of protecting the investment of the rights-holder in creating goodwill. It is rather necessary to inquire into the effect of defendant’s imitative activity on competition. Creating a product bundle which is substantially similar to that of a competitor instead of differentiating one’s own product undermines consumer welfare, as it prevents the emergence of dynamic competition with differentiated products. To exempt subliminal confusion from trademark liability may in a given case lead to suboptimal product variety. The S.D.N.Y. has been more successful in describing the misappropriative nature of the subliminal confusion theory, even if it did not precisely identify the essence of the competitive harm. Finally, it becomes apparent that, apart from the classic infringement scenario involving a junior use causing consumer confusion, there are other ways to trespass upon trademark rights, especially by misappropriating their


233 Critical stances of the doctrine rest on the notion that free-riding should not be restrained when confusion about source is not likely. See Chi-Ru Jou, The Perils of a Mental Association Standard of Liability: The Case Against the Subliminal Confusion Cause of Action, 11 VA. J.L. & TECH. 2, 17–23 (2006) (bringing forward the argument that making the consumer search for an imitation product by triggering an association with a well-known brand does not amount to a cognitive consumer harm, which should be remedied, if no confusion as to source takes place in the end).
advertising value. Confusion as to source or affiliation and misappropriation theories of liability are therefore complementary.\textsuperscript{234}

2. Limiting the Scope of the Misappropriation Rationale

Conspicuously, the courts have applied the doctrine without any qualification, even in markets for generics\textsuperscript{235} and tobacco,\textsuperscript{236} where brand differentiation should not be promoted. In Ortho Pharmaceutical Corp. v. American Cyanamid Co.,\textsuperscript{237} the junior trademark “RHO-GEST” was held to be infringing of the senior trademark “RhoGAM” on the basis of goodwill misappropriation. In its analysis the court considered the prefix “Rho” as being suggestive of a medicament treating Rh hemolytic disease.\textsuperscript{238} Defendant was held to have adopted the junior mark for the purpose of taking advantage of the goodwill attached to the products of the trademark holder.\textsuperscript{239} The court seems also to have been influenced by the fact that the plaintiff had been the first organization to develop the specific medicament and the fact that there were some technical differences between the two brands. In any event, the absence of confusion as to source and the possibility of keeping consumers aware of the manufacturer’s identity through informative advertising would be adequate in serving the interests of the trademark holder.

In the pharmaceutical industry, permitting newcomers to adopt similar marks reduces incentives to differentiate and promotes competition on price, output and therapeutic effects. Mark similarity facilitates market entry in that the junior user can draw the attention of the consuming public to his generic product by free-riding on the distinctiveness of the incumbent mark. Consequently, exonerating the junior use from trademark liability would promote static efficiencies and thereby enhance consumer welfare. The effectiveness of competition in markets for generic pharmaceuticals depends on competitors’ ability to share in the goodwill of a medicament, which is no longer under patent protection. Goodwill appropriation facilitates price competition because it increases the degree of substitutability between the products belonging to the same relevant market. In order to effectively share in the goodwill of the no-longer-patented pharmaceutical, competitors need also to share in the goodwill of the name the article was known during the term of the patent exclusivity through the use of a similar mark.\textsuperscript{240}

\textsuperscript{234} Rudolf Callmann & Louis Altman, Trademarks and Monopolies, (4th ed, 2004), § 17:9 to 17-64 (citing for that proposition Hugo Stein Cloak Co. v. S.B. Stein & Son, Inc., 58 Ohio App. 377, 382 (6th Cir. 1937): “[T]he appellant is entitled to protection against the use, by another, of its established trade name and trade mark in such manner as to mislead the trade and the public to believe that when they are dealing with one they are dealing with the other, or in such manner that such use results, or may result, in appropriation of the good will, a property right of the other—in the first case a fraud upon the public; in the second an infringement of a property right.”


\textsuperscript{238} Id. at 1035.

\textsuperscript{239} Id. at 1044–45.

VII. The Suppression of the Free-Riding Rationale in Modern Trademark Law

A. The Process of Trademark Propertization

Contemporary trademark law theory has been pervaded by the notion that the purpose for awarding exclusive rights in trademarks is to ensure an undistorted flow of reliable information about source or affiliation in the marketplace (information-transmission model).

Trademark protection is intended to prevent market failures, which are likely to arise as a result of misrepresentations to consumers in the context of passing-off activity. In this sense it has been argued that, because trademark protection is justified by these tort principles, the proprietary rights of exclusion reserved for the trademark holder should not extend beyond the level necessary to implement the policy against misrepresentations as to source or affiliation.

Further expansions of the exclusive authorities available to the rights-holder in regard to his mark would create additional property rights and eventually give rise to monopolistic positions that would unduly restrict competition.

Mainstream trademark theory recognizes that trademark owners may have an economic interest in prohibiting uses other than those causing consumer confusion. But goodwill misappropriation has been rejected as rationale for trademark propertization. Internalizing the intangible asset of goodwill would be tantamount to awarding copyrights thereto.

Competition would then be unduly burdened by an increase in the exclusive legal positions being operative in the market.

Coupling expanded trademark protection with dilutive harm foresees many of the competitive interests involved in trademark disputes, such as the rights-holder’s interest in competing monopolistically or consumer demand for differentiated products. It also disregards the actual effect of trademark rights on competition. The analogy to copyright goes amiss because trademarks would only be able to internalize goodwill in those markets where it is economically exploitable so as to promote

241 See Bone, supra note 35, at 549.
dynamic competition with differentiated products. Concerns about increasing the cumulative monopolistic effect of property rights in the marketplace are not justified to the extent that they do not consider that property is not an absolute and limitless legal position but a bundle of authorities with respect to a specific subject matter, which could be carefully designed\textsuperscript{245} so as to promote effective competition. Competition would therefore not necessarily be promoted by reducing the exclusive authorities of the rights-holder to a minimum but by optimally calibrating trademark scope.\textsuperscript{246}

Yet, contemporary trademark theory focuses on finding methods to restrict protection.\textsuperscript{247} Particularly, commentators argue that the threshold of protection should be raised so that only a close circle of trademarks would be able to form the basis of a dilution claim.

B. Narrow Definitions of Goodwill

The intangible value of goodwill is comprised of the positive consumer associations prompted by the mark. These may be based on the reputation of the trademark holder as a manufacturer or seller of quality goods, the likeness of the products or services offered under the mark and even irrational beliefs attributed to suggestive advertising.\textsuperscript{248} Case law and commentary have in many instances attempted to narrowly define the exclusionary scope of trademark rights by distinguishing the specific types of goodwill that should be protectable. In\textsuperscript{249}\textit{Qualitex Co. v. Jacobson Products Co., Inc.}, the Supreme Court opined that the functionality doctrine bars trade dress protection for product features the monopolization of which would put competitors at a significant non-reputation related disadvantage.


\textsuperscript{246} Cf. Walter J. Derenberg, \textit{The Problem of Trademark Dilution and the Antidilution Statutes}, 44 CALIF. L. REV. 439, 451 (1956) (considering trademark protection without any finding of consumer confusion as an extension of unfair competition principles regarding misappropriation into trademark law and not as a patent- or copyright-like treatment of trademarks).


\textsuperscript{248} The tort of misappropriation presupposes a broad definition of goodwill, encompassing all factors contributing to consumer patronage and especially branding. Michael Spence, \textit{Passing-Off and the Misappropriation of Valuable Intangibles}, 112 L.Q. REV. 472, 475–77 (1996) (proposing the term “valuable intangibles” instead of “goodwill” but rejecting the misappropriation doctrine in the end due to the lack of a convincing justification).

\textsuperscript{249}\textit{Qualitex Co. v. Jacobson Prods. Co., Inc.}, 514 U.S. 159, 169 (1995) (“The functionality doctrine thus protects competitors against a disadvantage (unrelated to recognition or reputation) that trademark protection might otherwise impose, namely, their inability reasonably to replicate important non-reputation-related product features.”).
The case has been invoked for the proposition that trademark law should only protect goodwill arising from the reputation of the trademark owner as manufacturer or seller. Another way to reach the same legal effect has been to consider that “product goodwill” encompassing all characteristics contributing to the likeness of a product should remain free from trademark restraints. The Supreme Court made this point in *Kellogg Co. v. National Bisquit Co.*, while it sought to establish the freedom to imitate articles that are no longer under patent protection. The purpose behind the conceptualization of “product goodwill” as a public good was to foster competition by imitation and to avoid the creation of positions of economic power based on product differentiation. More recently, “inherent goodwill” was systematically analyzed as another legal species of goodwill that trademark law should not protect. The term refers to the attractiveness of the mark itself contrasted with the goodwill of the trademark holder as a supplier of goods or services. In view of that, trademark norms should not restrain third parties from capitalizing on the likeness of a trademark.

C. Raising the Threshold of Protection

1. The Notion of Famousness as Quantitative Barrier to Extended Trademark Protection

   a. Nation-Wide Recognition as Trademark

   The concept of famousness represents an attempt to reduce the exclusionary effect arising from protecting trademarks beyond the source confusion paradigm by constructing a narrow category of marks entitled to such overbroad protection. Accordingly, the extended protection should attach to the commercial value resulting from the actual use of the mark in commerce, as it is reflected in its famousness. The law should therefore reward long lasting and successful commercial activity conducted under a specific mark and not construe broad property rights in trademarks with the purpose of internalizing goodwill as intangible property for the benefit of the rights-holder.

   In the same vein, the Trademark Dilution Revision Act (TDRA) has set a very high threshold in regard to the famousness requirement. For a mark to qualify as famous it has to be widely recognized by the general consuming public within the US as an identification of source. The most decisive of all factors set out by the Act

250 NIMS, supra note 6, § 43, at 79.
251 *Kellogg Co. v. Nat’l Biscuit Co.*, 305 U.S. 111, 122 (1938) (“Sharing in the goodwill of an article unprotected by patent or trade-mark is the exercise of a right possessed by all—and in the free exercise of which the consuming public is deeply interested.”).
252 Bone, supra note 35, 551–53.
253 See also Derenberg, supra note 246, at 451 (proposing to restrict extended trademark protection only to “celebrated” marks).
as relevant to the famousness inquiry is the extent of the actual recognition of the mark. Both the extent of the advertising and the sales of goods made under the mark are simply indications that this mark might be famous. The omission to file an application to register a mark might provide a hint about the rights-holder’s low valuation of that mark and vice versa, but it cannot affect any factual finding on famousness. The legislator has strictly linked famousness with quantitative criteria related to the recognition of a mark as an indication of source. The inquiry of famousness should hence remain a matter of plain empirical evidence. In practice, the extended protection of Section 43(c) of the Lanham Act is reserved for few truly famous house marks.

b. Abolishment of the Niche-Fame Theory

During the period that preceded the TDRA, courts had already been interpreting the famousness requirement in a very restricting manner. In particular, case law has been largely repugnant to the theory of niche-fame, which posits that a trademark having a reputation within the boundaries of some specific market should be eligible for dilution protection. If this theory were to be sustained, it would supposedly stifle the freedom of competition by creating trademark rights in gross. The denial of extended protection for marks famous only within the boundaries of a specific market has in quite a few cases unwarrantedly allowed the defendant to make use of the goodwill of the trademark holder. In Breuer Electric Manufacturing Co. v. The Hoover Co., for instance, the trademark holder was a supplier of vacuum cleaners in commercial and industrial markets. One of his trademarks consisted of the word mark “TORNADO” along with a stylized design of a tornado. The defendant, who was selling his own vacuum cleaners, both in the commercial and the domestic market, used graphic depictions of tornados for the labels of his products and in his advertising. Injunctive relief was denied on the dilution claim. The high recognition degree of his mark in the narrow niche of the commercial market for vacuum cleaners was not enough to render it famous for the purposes of the dilution laws.

The junior user was actually able to adopt the marketing concept of the trademark holder through an imitation of the mark that symbolized his advertising message. It would make sense for trademark law to allow the trademark holder an injunction in order to force the defendant to compete on the merits of his own advertising message. As already explained, this is important from the perspective

256 Id.
260 Id. at 16.
of consumer preference for product variety. The competitive practice of the defendant also has a significant exclusionary potential. Because the defendant, in contrast to the trademark holder, is active in both the commercial and the domestic market for vacuum cleaners and therefore serves a larger market, he would probably have the capacity to undercut his competitor in price after he has eliminated other non-price parameters of competition between them. The junior user was also interfering with the possibility of the trademark holder transferring his goodwill to the market for domestic use vacuum cleaners.

2. The Cumulative Requirements of Famousness and Inherent Distinctiveness

The competition policy decision to drastically reduce the amount of marks that might become eligible for extended protection has found its way into the judicial statutory interpretation of federal dilution law. As amended by the Federal Trademark Dilution Act (FTDA), Section 43(c)(1) of the Lanham Act provided that injunctive relief based on dilution claims is directed against junior uses that cause dilution to the distinctive quality of a trademark. The same provision referred to the degree of the inherent or acquired distinctiveness of the senior mark as one of the determinants of its eligibility for dilution protection. Ambiguity was raised about whether the Lanham Act was imposing a requirement for dilution protection that the trademark at issue should be not only famous but also inherently distinctive.

The issue came before the Second Circuit in *Nabisco, Inc. and Nabisco Brands Co. v. PF Brands, Inc. and Pepperbridge Farm, Inc.*,261 where the trademark holder invoked dilution protection for his goldfish-shaped crackers as trade dress. The mark was undoubtedly famous. Its inherent distinctiveness was very weak though, as the sale of crackers or candies in the shape of an animal had been a common marketing practice. The capacity of the mark to signify source had been acquired through extensive use. Dilution protection was denied because the court interpreted the FTDA as awarding protection for marks that are both famous and inherently distinctive.262 The argument rested upon a substantive valuation derived from the Abercrombie scale of distinctiveness, according to which the worthiness of a sign to be protected as a trademark is proportional to its inherent capacity to connote commercial source.263 Arbitrary marks are deemed to be the most worthy of such protection, as they bear no semantic reference to the nature of the products they distinguish and could only be apprehended by the consumer as indications of source. Because the dilution protection has an exclusionary effect that spreads over the whole commerce without restricting itself to confusing uses, it interferes with the freedom of new entrants to adopt a mark of their liking. To avoid undue restrictions of competition, the extended protection should in the spirit of *Abercrombie* only be granted to marks that originally possess a high distinctive quality.264 The opinion is

261 Nabisco, Inc. v. PF Brands, Inc., 191 F.3d 208, 212 (2d Cir. 1999).
262 Id. at 215–16.
263 Id.
264 Id. at 216.
also justified by reference to Schechter’s views on the need to protect the selling power of those trademarks that are unique, singular, or particular in semantic content.\textsuperscript{265}

In \textit{TCIP Holding Co., Inc. v. Haar Communications Inc.},\textsuperscript{266} the Second Circuit had the opportunity to elaborate on its restrictive theory regarding the scope of dilution protection. The case was about a dilution claim based on the famous mark “CHILDRENS PLACE” for children’s clothing. Protection was refused due to the weakness of the mark’s inherent distinctiveness. The fact that famousness and inherent distinctiveness were mentioned in Section 43(c) of the Lanham Act meant, in the Second Circuit’s view, that it established two separate hurdles for a trademark to qualify as eligible for dilution protection, namely a wide recognition as source indicator (famousness) and an element of creativity in coining the mark that contributes to its fancifulness or arbitrariness (inherent distinctiveness).\textsuperscript{267} These two factors should not be seen as alternatives but rather as complementary elements of a very high threshold for dilution protection.

In opposition to these rulings, the Third Circuit was of the opinion that the legislative history of the FTDA reveals an intention to protect the source-designation value of famous trademarks and not to make dilution claims contingent on the inherent distinctiveness of the mark at issue. The evolving circuit split was resolved by the enactment of the TDRA, which set out the high standard for nation-wide recognition as a trademark.

Limiting extended trademark protection to “coined” or “fanciful marks” makes sense for those who believe that putting trademarks on an equal footing with copyrights and patents in terms of their exclusionary scope would require some degree of originality or inventfulness in coining or selecting the mark.\textsuperscript{268} Goodwill protection is more about protecting the advertising value as information codified in the mark from misappropriation rather than rewarding the creativity of the rights-holder in choosing his mark on its own merit.\textsuperscript{269}

\textsuperscript{265} Id. at 217; cf. Elliot B. Staffin, \textit{The Dilution Doctrine: Towards a Reconciliation with the Lanham Act}, \textit{6 FORDHAM INTELL. PROP. MEDIA & ENT. L.J.} 105, 164–67 (1995).

\textsuperscript{266} TCPIP Holding Co., Inc. v. Haar Communications Inc., 244 F.3d 88, 93–100 (2d Cir. 2001).

\textsuperscript{267} Id. at 95–96.


\textsuperscript{269} In any case, if the purpose of dilution laws is to protect the selling power of a trademark, there is no apparent reason why such protection should be restricted to inherently distinctive marks. Gary Myers, \textit{Statutory Interpretation, Property Rights, and Boundaries: The Nature and Limits of Protection in Trademark Dilution, Trade Dress, and Product Configuration Cases}, \textit{23 COLUM.-VLA J.L. & ARTS} 241, 281–87 (2000); cf. Julie Arthur Garcia, \textit{Trademark Dilution: Eliminating Confusion}, \textit{85 TRADEMARK REP.} 489, 504–05 (1995) (explaining that courts have developed multiple factors to assist in determining the strength and distinctiveness of a particular mark).
3. Making it Almost Impossible: Actual Dilution

Perhaps the most radical attempt to curtail the scope of trademark protection on the basis of a non-confusion-based theory of trademark liability has been the decision of the Supreme Court in *Moseley v. V. Secret Catalogue*.

There the issue was whether the use of the mark “Victor’s Little Secret” as a trade name of an adult novelty store was dilutive of the trademark “Victoria’s Secret,” owned by a corporation that marketed lingerie. The goodwill generated by the trademark holder is transferable to the market where the junior user is commercially active. The adoption of a similar trade name creates a misappropriative association to the senior mark. In this specific case, there are compelling reasons why the goodwill attached to the trademark should be internalized for the benefit of the rights-holder. The semantic content conveyed by the trademark is prone to generate demand in the market for the junior user’s products. The trademark holder should not only have the opportunity of exploiting his goodwill in the market for erotic products himself, but he should also be able to control the context in which it would be commercialized within the same market. Enjoining the junior user from adopting a trade name so similar to the senior trademark would further compel him to compete on the merits of his own logo and enrich competition with a brand new goodwill. There is also no compelling reason for permitting the junior user to make use of the distinctiveness and advertising capacity of the senior mark in order to enter the market. The advertising costs of market entry are not of such amount, that the junior user finds himself in some kind of competitive need to free-ride on another famous mark. In other words, the distinctive and advertising capacity of the mark should not be considered as a positive trademark externality in this case.

In favor of the defendant, it could be argued that he is marketing a parody product and that trademark rights would suppress the production of such goods, which are actually demanded by consumers, since the rights-holder would usually not allow the junior use of the mark in that context. On the other hand, the rights-holder could argue that the parody product is likely to substitute demand for his own goods if he decided to transfer his goodwill to the market for erotic products. Notably, such a thorough analysis of the interests involved can only take place under the free-riding theory.

In any event, called upon to rule on the requirements of the dilution cause of action under the FTDA, the Supreme Court opined that it is necessary for the claimant to prove actual dilution. Therein lies a competition policy decision to render extended trademark protection a rare exception within a legal framework that primarily seeks to protect the public interest against confusion as to the source of

---

The stringent requirement was not substantially ameliorated by the fact that the court ruled that dilution might be proven by circumstantial evidence where the junior use is an identical one.274

In fact, the likelihood of dilution test for determining trademark infringement may practically allow trademark holders to prevent the appropriation of their goodwill by claiming that a certain junior use will in all likelihood turn out to be dilutive.275 On the other hand, there is an actual need to protect the rights-holder before the harm of dilution actually occurs.276 It seems that the TDRA sought to resolve this tension by raising the quantitative threshold for the famousness requirement.

Finally, the theories that make extended trademark protection contingent upon a finding of actual or likely dilutive harm are in essence an offspring of the notion that trademarks are solely dedicated to facilitating purchasing decisions by connoteing commercial source and economizing consumer search costs.277

---


274 Moseley, 537 U.S. at 434.


277 Stacey L. Dogan & Mark A. Lemley, A Search-Costs Theory of Limiting Doctrines in Trademark Law, 97 TRADEMARK REP. 1223, 1229–30 (2007); Mark A. Lemley & Mark P. McKenna, Owning Mark(et)is, 109 Mich. L. REV. 137, 162–66 (2010) (recognizing that non-competing junior uses may eventually take a free-ride on the goodwill of the trademark holder, but contending that rights-holders should not have the authority to oppose these junior uses so that trademarks remain faithful
D. Further Theories Restrictive of Dilution Protection

In the name of avoiding undue restrictions of competition, some commentators have developed their own theories narrowing down the scope of dilution protection. One view understands the doctrine of dilution as protecting trademarks solely in their already certified capacity to identify one single particular product according to its commercial origin. The purpose of dilution laws is accordingly to protect the source designation function of those trademarks that have become famous while being used in connection with a specific product category. Non-competing uses dilute this special bond between the famous mark and the trademarked goods or services. This theory would accordingly suggest for instance, that the distinctiveness of the famous trademark “Rolls-Royce” should be protected against dilution only in respect with automobiles.

Another theory contemplates that the expressive content of a famous mark should not be allocated to the rights-holder by virtue of a property right for reasons appertaining to the creation of communicative efficiencies in the marketplace. The prefix “Mc” of the famous trademark “McDonald’s” for example has eventually come to connote the meaning of standardized, consistent, and pleasurable services. In the absence of another semiotic or linguistic term conveying exactly the same meaning, the sign “Mc” should be freely used for expressive purposes (“expressive genericity”). Because the legitimate business interests of the trademark owner would have been given enough consideration through an extended dilution protection in the field of his actual commercial activity, other economic operators should for the sake of the freedom of competition be allowed to use the semantic content of the “Mc” prefix for their remoted products (“competitive genericity”).

VIII. Conclusion

Beyond connoting commercial source, trademarks affect the process of competition as instruments of brand differentiation. As part of the group of norms regulating the competitive process, trademark law should account for business interests in the internalization of advertising value and consumer welfare arising from dynamic competition with differentiated products. The economics of product variety offer a valid rationale for the controversial misappropriation doctrine of unfair competition law and indicate that goodwill appropriation should be regarded as a distinct theory to their mission of serving as source designators); Stacey L. Dogan & Mark A. Lemley, The Trademark Use Requirement in Dilution Cases, 24 Santa Clara Computer & High Tech. L.J. 541 (2008) (arguing that the imposition of a trademark use requirement on dilution claims would ensure that trademarks remain dedicated to economizing search costs of consumers and would not end up being anticompetitive property rights). In the past, some opinions treated consumer confusion as a prerequisite for a successful dilution claim. See, e.g., Haviland & Co. v. Johann Haviland China Corp., 269 F. Supp. 928, 957 (S.D.N.Y. 1967); Field Enters. Educ. Corp. v. Grosset & Dunlap, Inc., 256 F. Supp. 382, 390–91 (S.D.N.Y. 1966); Cue Publ’g Co., Inc. v. Colgate-Palmolive Co, 256 N.Y.S.2d 239 (Sup. Ct. 1965).
of trademark liability standing next to confusion-based infringement theories on an equal footing. Promoting dynamic competition with differentiated products requires the development of non-confusion-based theories of liability that would conceptualize infringing uses as practices undermining product variety. Instead of trimming the scope of the exclusive right through categorical exclusions by confining expanded trademark protection to certain types of marks and the degree of their famousness or inherent distinctiveness, it would be much more fruitful for trademark analysis to identify the goodwill at issue and inquire further on its protectability in a given case. Such an approach makes it possible to introduce into the calculus of trademark scope definition parameters related to the effectiveness of competition.