

# Exercise in Common Sense

*Understanding special considerations surrounding trademark licensing can improve efficiency of technology transfer*

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The licensing of trademarks is a relatively new phenomenon that has been generally recognized as a matter of law for less than 50 years. During this interval, trademark licensing has been embellished with a variety of formalistic procedures, a development which is, in itself, the hallmark of many professional specialties. These are based on a very few basic principles which, if appreciated, can go a long way toward removing the mystique surrounding this process.



*R. Goldscheider* Most problems concerning trademarks can be better understood by going back to the definition of the trademark concept. A trademark is a word, symbol, or combination thereof, which distinguishes the goods of a trader from those of its competitors. In those jurisdictions which recognize service marks (e.g. TWA or Roto-Rooter), substitute the word "service" for "goods."

Most rights to trademarks are acquired by obtaining a registration of the mark. In many jurisdictions which follow the British legal system, certain rights can be acquired by use of a mark, although enforceability of such rights is generally simplified by registration. A trademark is registered in respect to specified goods. Trademark licenses of a registered mark may either be in respect to "all goods covered by the registration," or be limited to specific goods that fall within the scope of the registration.

The key word in the definition is "distinguishes" because a trademark ceases to be legally enforceable when it does not point the way to a particular source of the article or service in question. This highlights the fact that the ownership of rights in trademarks carries with it substantial responsibility to protect the consuming public from deception. Thus, if a trademark ambiguously identifies the origin of the article or service, the owner of registrations of such mark is in danger of losing any property rights or other legal advantages conferred by virtue of obtaining a trademark registration.

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## Example

This is the fate suffered by the original proprietors in the United States of the words "cola" and "aspirin," "thermos," "cellophane" and "nylon," among others. It also explains why the proprietors of some very famous and valuable trademarks, whose universality of acceptance and use could adversely affect their distinctiveness, jealously police the public use of such marks to safeguard their continued distinctiveness. Trademarks falling within this category would be "COCA-COLA," "XEROX," "FRIGIDAIRE" and "BAND-AID."

With this background, it is not surprising that early court decisions considered the concept of trademark licensing to be a contradiction in terms. It was argued that permitting persons other than the proprietor to use a trademark destroyed the mark's distinctiveness since it misled purchasers into believing that goods came from the originator while, in point of fact, they would originate from a different source, albeit a party which had been selected by the originator.

As technology and the ability to transfer it precisely developed further, it became apparent that a compromise procedure was needed which would recognize licensing the use of trademarks, and also safeguard the public from being misled. The various legal requirements and practices governing trademark licensing which have evolved in different countries around the world are all designed to achieve that result.

Two elements may be identified as necessary to achieve this objective. One is the maintenance of controls by the licensor over the goods and/or services being marketed by the licensee. The other is the inclusion of a marking legend or some other reasonable form of publicity which is calculated to inform consumers of the existence of the license.

## Quality Control

The question of quality control is normally exercised on two levels. In the basic licensing agreement it should be expressly provided that the goods or services in relation to which the licensed trademark or service mark is proposed to be used will be manufactured in accordance with "standards, specifications and instructions approved by the proprietor." Furthermore, machinery should be established in the licensing contract to enable the proprietor to implement this principle by inspecting the relevant premises of the licensee during normal business hours and having the right to receive a realistic quantity of samples of the licensed products at reasonable intervals, or perhaps both.

It should be noted that the basic quality standard established for the licensee to meet need merely be "approved by" the licensor; they need not necessarily

be identical to those traditionally employed by the licensor in its activities which originally established the reputation of the mark. Thus, in certain licensing arrangements to developing countries, it may be recognized that various ingredients or skills may not be locally available, and the licensor could then approve a lesser standard, which is nonetheless the most satisfactory obtainable under the circumstances. In another case, a licensor might purposely wish to have certain variations in its product to conform to certain special customs or tastes which have been discerned in various markets, e.g. coffee brewed with different formulae by licensees located respectively in the United Kingdom, France, and West Germany, each of whom would be given the right to use the same, internationally-known trademark by a single licensor.

In other cases, it may be the commercial strategy to have exact uniformity wherever the trademark is used. This is apparently the policy of the soft-drink manufacturers, who want their product taste to be the same around the world. Such a policy also would be necessary for producers of precision equipment when components must be compatible, regardless of source.

The ability to inspect the premises of the licensee, provided by the laws relating to trademark licensing, is a potential asset to the licensor. The value of this asset should not be underestimated. This function can be discharged by "authorized representatives." They may be locally recruited engineers, lawyers or accountants, and thus need not impose an onerous burden on the licensor. The contacts which are promoted by these visits can, however, have a very positive influence on the efficiency of the licensing relationship, and foster better understanding and mutual esteem between the parties.

It might be argued that the right of regular inspection of the operations of the licensees might legitimize unnecessary control by the licensor over the licensee. This has been one of the arguments advanced by representatives of the lesser-developed countries in justification of legislative efforts to curtail trademark licensing. On the other hand, it may be argued that every type of dialogue between licensor and licensee on technical, commercial, and quality questions promotes greater understanding of the corpus of the license and should thus be encouraged.

### Samples

With regard to the analysis of samples, licensors should be organized to discharge this function promptly and thoroughly if it is to be meaningful. Regular dispatch of samples by the licensee to the licensor can be an onerous and expensive exercise and it therefore behooves licensees to be certain that the licensor indeed has the facilities to examine the samples adequately and expeditiously. It is also advisable from the licensee's point of view to insert a provision that samples shall be deemed approved unless the licensor comments adversely within a specified period, or even that the licensor shall be obliged to convey to the licensee the results of sample analyses in any event. If these arrangements are conscientiously discharged by the parties, experience has shown that the effectiveness and profitability of the licensing rela-

tionship can be enhanced.

There is no magic formula or language for marking legends other than that they should be truthful and not misleading. In the case of products manufactured in France by a local licensee of an American licensor, an ideal legend might read:

"Manufactured in France by  
Gallic Products S.a.r.l.  
under license from  
Yankee Products Corporation  
Bridgeport, Connecticut, U.S.A.  
Proprietor of the trademark ACME"

It is relatively rare that a legend as complete as this is utilized. Various elements can be deleted without distorting the message. Also, for esthetic or utilitarian reasons it is frequently not feasible to have the legend appear directly on the goods, or even the package. In such cases it is advisable, particularly from the licensor's point of view, to have the legend set forth in some package insert or even in some other reasonable way to inform purchasers of the goods or services in question of the existence of the licensing relationship.

Many jurisdictions decided to establish formalized recordation procedures whereby it was possible to require parties to trademark licenses to adopt specified standards of control over the use of the marks concerned. Another aim of these laws and regulations was to establish a register of existing trademark licensing relationships, open to public inspection. The first provisions of this type were enacted as part of the British Trade Marks Act of 1938 which established procedures for the entry of Registered Users of trademarks.

If the trademark licensee is unrelated to the licensor and obtained its rights pursuant to a license agreement, it is required to submit a copy of such agreement to the Trade Marks Registry as evidence of the terms and conditions under which the trademark is permitted to be used. If the licensee is a majority related company, no agreement need be submitted and it is merely necessary to recite the equity relationship.

This approach was rapidly adopted by virtually every jurisdiction in the British Commonwealth. Numerous civil law jurisdictions also enacted trademark license recordation procedures, many making recordal mandatory if the license was to be enforceable as a matter of law, or against third parties.

There have been decisions in the British courts in recent years to the effect that failure to enter a trademark licensee as a Registered User will not automatically vitiate the mark involved, as had been widely believed. Nevertheless, licensors of technology with respect to which trademarks are important, should be familiar with the variety of special legal requirements surrounding trademark licensing, and be prepared to pay the costs involved. The adroit use of trademarks can substantially enhance the value of the overall technology transfer.

### Improve With Age

While patents have a limited life, it has been said that trademarks "like good wine, often tend to get better with age." For example, many years ago Cluett Peabody & Company, Inc. widely and successfully licensed its patented process for reducing shrinkage in

cotton fabric. Part of the licensed package was the right to use the trademark SANFORIZED. When the patents eventually expired, virtually all of the licensees nevertheless opted to continue to pay royalties since they recognized the enormous good will which had accrued to the SANFORIZED mark, and wished to benefit from this.

Thus, parties to licensing negotiations should recognize the long-run implications of using a licensor's trademark. If the mark is unknown in the licensed territory at the outset of the relationship but acquires substantial good will as a result of the licensee's efforts, the licensee will have been building up an asset of the licensor and thereby become more dependent upon perpetuation of the licensing relationship, even after the underlying patents have expired or licensed trade secrets may have entered into the public domain. The power acquired by trademark licensors has proven to be a sensitive issue in many developing countries. They have therefore recently enacted defensive legislation intended to limit the ability to license trademarks. The Mexican law has been particularly worrisome to trademark proprietors. Care should be taken to check the current legal situation whenever trademark licenses are contemplated to a developing country — particularly to Mexico, Brazil, the Andean Pact Nations and India.

Sometimes a prospective licensee has a valuable trademark of its own and proposes that its mark and that of the proprietor both be used in relation to the licensed products. This can be a risky business, since a combination of the two marks (particularly in a hyphenated form or with an oval encircling them) would tend to dilute the distinctiveness of each mark. This approach is therefore usually inadvisable. At the very least, the marks should be kept separate, and ought possibly be printed in different colors. There should also be a special marking legend indicating the ownership of the respective marks.

#### Sublicensing

Sublicensing of trademarks is not recognized by many jurisdictions — including those who follow the British lead — and should generally be avoided. This is because lack of contractual privity between the proprietor and a sublicensee can prevent effective control over use of trademarks, and hence result in the public being misled. Thus, assume A licenses the ACME mark to B who sublicenses to C. If A doesn't like the quality of goods being marketed by C, A's only recourse is to request B to intervene. If B disagrees on A's assessment of quality, A may have a cause of action against B but cannot forthwith stop C from continuing its actions. If sublicensing of the technology is contemplated, provision should thus be made for direct trademark licenses from the trademark proprietor to the sublicensee.

A special question in this area relates to the inclusion of the licensor's trademark in the company name of the licensee. For instance, in the circumstances of the illustrated marking legend, if the ACME trademark is widely known in the field, it might be very advantageous, from the commercial point of view, for "Gallic Products, S.a.r.l." to change its name to "ACME Products S.a.r.l." This also creates certain

### Trading Name Agreement

*This is usually in the form of a special contract which specifies the conditions under which the licensee is permitted to include the sensitive word in its corporate name and which gives the owner of the name the unequivocal right to cause such name to be deleted from the licensee's corporate title. These agreements are frequently read into the corporate minutes of the licensee and also recorded at the local Corporations Registry to put creditors and subsequent shareholders on notice of the limitation on the right to use the name. Such agreements also frequently contain provisions for sizable liquidated damages. (e.g. \$10,000 per day) in the event the licensee fails to change its company name to remove the sensitive word upon request and within the notice period specified in the agreement.*

dangers to the proprietor of the ACME mark, since the proprietor would not wish the licensee to be able to use the mark, especially in its name, if the underlying licensing relationship should terminate. This problem can be anticipated by a so-called "Trading Name Agreement." (See Insert)

Finally, there is the question whether trademark licenses should be separate agreements or incorporated in larger technical assistance agreements which also include licenses to patents and/or know-how. Absent special tax or recordation considerations, the writer is inclined to include all those aspects of what is essentially a single commercial transaction in a single internally consistent document. This is particularly true since the relative value of the patents, know-how and trademarks may vary over the life of the agreement, with the value of the marks being sufficiently great at the end of the initial term of the agreement to justify continuation of royalty payments thereafter to permit use of the trademarks without interruption. If a license is to a foreign jurisdiction which requires recordation of "the trademark license agreement" the full agreement and not some synopsis thereof should be recorded. In either event, a request usually may be made to the recording authorities to keep royalty rates and other commercial information of a confidential nature in such agreements away from access by third parties without a special order.

#### Conclusion

Practitioners of the technology transfer process can increase their efficiency by understanding the special considerations surrounding trademark licensing. These are based on principles designed to prevent misleading impressions from being given to the consuming public, the intended beneficiaries of trademark laws. Careful observance of such guidelines can help clarify much of the jurisprudence that has developed. Furthermore, adroit use of trademarks can do more than generate significant royalties. It can also improve the commercial viability of the technology involved.