



Trademark Owners Must Exercise Sufficient Control over the Quality of Licensed Merchandise or Risk Losing Rights in Their Valuable Brands

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by [Phillip Barengolts](#), [Trademark Attorney](#)

Merchandise and character licensing is big business, generating billions of dollars in revenue for the most valuable brands.¹ Under U.S. law, the licensor of a brand must maintain real control over the quality of the products licensed for sale under the brand. Without such control, the brand owner could lose its rights forever. Many business people, however, treat brand licensing like patent licensing – prepare the written agreement, get it signed, and enjoy the royalties. Such was the case in *Eva’s Bridal Ltd. v. Halanick Enterprises, Inc.*, 1:07-cv-01668 (N.D. Ill. Aug. 4, 2010) – a dispute between a licensor and its licensee.

Disputes over the use of a brand between a licensor and licensee are the most frequent context for claims of abandonment through uncontrolled licensing of a mark (often referred to as “naked licensing” or “licensing in gross”). Here, the licensee counterclaimed that the licensor/brand owner abandoned its trademark for a bridal shop through naked licensing of the trademark to the licensee.

“The critical question [in such cases] is whether the [brand owner] sufficiently policed and inspected its licensees’ operations to guarantee the quality of the products they sold under [the brand owner’s] trademarks to the public.” *Universal City Studios, Inc. v. Nintendo Co.*, 578 F. Supp. 911, 929 (S.D.N.Y. 1983) *aff’d* 746 F.2d 112 (2d Cir. 1984) (finding that original owner of KING KONG mark had abandoned its rights through uncontrolled licensing). In this case, the defendants had taken over the daily operations of the bridal shop that bore the plaintiff’s trademark – EVA’S BRIDAL – pursuant to an agreement between the parties.

¹ For example, DORA THE EXPLORER has generated over \$11 billion in revenue since 2001. See <http://www.licensing.biz/news/5018/BRAND-PROFILE-Dora-the-Explorer>. Merchandise licensing of the SHREK brand has generated over \$2 billion in revenue at retail. See <http://www.licensing.biz/brand-profiles/196/Shrek>.



The agreement contemplated that the defendants would run the bridal shop as they saw fit, while the plaintiffs reviewed a management report, monitored the monthly sales and paid rent on the storefront. The court found this insufficient to demonstrate plaintiffs' control over the operations of the store, "especially with respect to quality." Moreover, this evidence was insufficient even to raise a genuine question of fact on the issue, so the court granted summary judgment to the defendants, holding that the plaintiffs had abandoned their trademark.² The plaintiff has appealed the ruling, so stay tuned for the Seventh Circuit's review.

The level of control necessary to maintain trademark rights, and the evidence sufficient to establish "real" control, varies from case to case. *Eva's Bridal* reveals that control merely over the finances involved in a licensing relationship likely is insufficient. Furthermore, merely having the right to exercise control likely also is insufficient.

Marketers, licensing executives and brand counsel should work together to ensure that valuable rights are not lost. The *Eva's Bridal* case is instructive about what minimum levels of quality control may be required, and a licensor should consult with counsel before and during a licensing relationship to avoid any pitfalls. In almost every instance, the effort of establishing a quality control program will be well worth the cost if an issue arises in later litigation.

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Phillip Barengolts is a partner with [Pattishall, McAuliffe, Newbury, Hilliard & Geraldson LLP](#), a [leading intellectual property law firm](#) based in Chicago, Illinois. Pattishall McAuliffe represents both plaintiffs and defendants in [trademark](#), [copyright](#), and [unfair competition trials and appeals](#), and advises its clients on a broad range of domestic and international intellectual property matters, including [brand protection](#), [Internet](#), and [e-commerce](#) issues. Mr. Barengolts' practice focuses on litigation, transactions, and counseling in domestic and international [trademark](#), [trade dress](#), [Internet](#), and [copyright law](#).

² The Court's opinion has limited analysis, but one glaring omission from the discussion is licensee estoppel – the doctrine that a licensee is estopped from claiming any rights against the licensor which are inconsistent with the terms of the license. See, e.g., *Creative Gifts, Inc. v. UFO*, 235 F.3d 540, 548 (10th Cir. 2000). Perhaps the parties did not brief it.