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Irreconcilable Differences: Who Gets Custody of the Trademarks When a Business is Dissolved?

Five years ago Violet and Petunia formed a partnership and opened a florist shop called Everything's Rosy. Business is booming and the shop has developed a reputation for its striking arrangements and fresh cut flowers. Customers ask for Everything's Rosy arrangements by name. Unfortunately, for the last six months, things between Violet and Petunia have been everything but rosy, and the two have decided to call it quits. Violet wants to open a new shop called Everything's Rosy, but she is concerned because she understands that Petunia intends to do the same thing. Violet calls your office in a panic, "Petunia can't be allowed to use the store's name. I am the talent! I'll lose all my customers if she sells her mediocre arrangements using the same store name. How can I stop Petunia from opening a new store called Everything's Rosy?" After explaining the situation to your colleague in the Intellectual Property Group, you drop into a chair in her office as you ask, "Is there anything I can do?" Your colleague responds, "This is an all or nothing scenario—all of the rights in the mark and its good will must be assigned to one of the partners or neither partner will be able to use Everything's Rosy."[1]

Violet and Petunia have developed trademark rights for the name Everything's Rosy over the five years they operated the shop. They used the mark in connection with the partnership, and it is associated with the good will of the partnership; therefore it is a partnership asset. Although, generally upon dissolution, partnership assets are apportioned among the partners pursuant to state statute or the partnership agreement, distribution is a unique challenge when the asset is a trademark. The value of a trademark stems from consumers' ability to associate the goods or services offered in connection with the mark with a single source. A companion principle is that consumers expect that the goods and services offered in connection with the mark will be of the same quality.[2] In order to maintain that quality, a trademark owner must exercise control over use of the mark or risk losing trademark rights. Both of these factors allow consumers to rely on the mark to designate the quality of the goods or services they associate with it.

It might seem that the best solution is to allow both partners to use the mark. However, that result would, at best, weaken and, at worst, destroy the validity of the mark altogether. Violet and Petunia want to use the identical mark in connection with identical goods and services to designate two separate sources. Because the mark and the goods and services are the same, consumers are bound to be confused regarding the source of the goods or services. Furthermore, with two independent users of the Everything's Rosy mark, the quality of goods and services offered in connection with the mark would be different. Consumers would not know what level of quality to expect when purchasing goods or services associated with the mark. If a third user were to enter the market with a similar mark, Violet and Petunia would have a hard time stopping the third user. It would be difficult, if not impossible, to argue that the third user was causing confusion among consumers when two independent users of the mark already existed in the marketplace.

A second issue is the relationship between the trademark and the good will of the partnership. It is impossible for consumers to see the Everything's Rosy mark and not think of the good will developed in the partnership. For this reason, the mark and the good will associated with the business using the mark are inseparable.[3] A mark is assignable with the good will of the business in which the mark is used, or with that part of the good will of the business connected with the use of and symbolized by the mark.[4] If one of the partners attempts to use the mark in connection with a new business without the permission of the other partner, it would be an attempt to capitalize on the good will developed in the partnership and would violate the fiduciary duty each partner owes to the partnership. A partner may not exploit the unique assets of the partnership to the detriment of the other.[5] Moreover, if a contractual agreement exists between the partners, such unauthorized use could violate that agreement as well.

The issues at hand are no different if Violet and Petunia had formed a different type of entity. Regardless of whether the original entity was a partnership, limited liability company, or corporation, a likelihood of confusion would exist if both Violet and Petunia were allowed to use the mark in association with new separate entities. Similarly, a mark and its good will are inseparable no matter what type of entity owns the mark. In addition, just as officers and directors of a corporation owe a fiduciary duty to the corporation and its shareholders,[6] so too members of limited liability companies owe the company a fiduciary duty.[7] If one officer or member used the mark to the detriment of the other, that person would violate his or her fiduciary duty to the business and to the other shareholders or member.

If Violet and Petunia cannot agree that one or the other of them can use the trademark, a court is likely to stop both of them from using the name Everything's Rosy.[8] Allowing both partners to use the mark would lead to consumer confusion and an impermissible split of the business good will and the trademark used in that business. In order to secure rights in the mark and stop Petunia from using it, Violet should negotiate to obtain the trademark and business goodwill while Petunia receives other partnership assets. Another option for Violet, if she is financially able, is to attempt to buy Petunia's portion of the business. Ideally, Violet and Petunia should have included a provision in their partnership agreement providing for distribution of the trademark and associated good will to one of the partners in the event of the dissolution of the partnership. Unfortunately, if the two partners cannot resolve the dispute, Everything's Rosy will be pushing up daisies. **TFL**

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Endnotes

[1]*See generally* J. Thomas McCarthy, McCarthy on Trademarks and Unfair Competition, § 16.44 (4th ed. 2007).

[2]*Id.*, §§ 3.10–3.11

[3]*Durango Herald Inc. v. Riddle,* 719 F. Supp. 941, 945 (D. Colo. 1988); *see also Visa, U.S.A. Inc. v. Birmingham Trust Nat. Bank*, 696 F.2d 1371, 1375 (Fed. Cir. 1982).

[4]*See* 15 U.S.C. § 1060(a).

[5]*Durango*, 719 F. Supp, at 945.

[6]18B Am. Jur.2d *Corporations* § 1460 (2004).

[7]New Topic Service Am. Jur.2d *Limited Liability Companies* § 11 (2005).

[8]*See, e.g., Durango*, 719 F. Supp. at 953.

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under the ADEA after they were terminated because of a reduction in force, claiming that the fact that 30 of the 31 employees who were laid off were over the age of 40 supported their disparate-impact allegations. Originally, the Second Circuit held that the plaintiffs had been successful at both proving a prima facie case for disparate-impact liability and in refuting the employer's "facially legitimate business justification" for their discharge under the "business necessity" test. However, the Supreme Court, in light of new precedent, reversed the Second Circuit's ruling and remanded the case. The current appeal stems from the Second Circuit's decision on remand to apply the new "reasonableness" test and place the burden of persuasion for such test on the employees' shoulders. In placing the burden on the employees, the court stated that "[i]t is therefore hard to see how an ADEA plaintiff can expect to prevail on a showing of disparate impact based on a factor that correlates with age without also demonstrating that the factor is unreasonable." Plaintiff employees appealed this decision, and the Supreme Court heard oral argument on April 23, 2008. **TFL**

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Endnotes

[1]Chief Justice William H. Rehnquist, Remarks at the University of Guanajuato, Mexico, Sept. 27, 2001.

[2]*Id.*

[3]128 S. Ct. 1020 (Feb. 20, 2008).

[4]*Larue v. DeWolff, Boberg & Associates Inc.*, 450 F.3d 570 (4th Cir. 2006), *rev'd by* 128 S. Ct. 1020 (Feb. 20, 2008).

[5]128 S. Ct. 978 (Feb. 20, 2008).

[6]546 U.S. 440 (2006).

[7]9 U.S.C. § 1 et seq. (2008).

[8]128 S. Ct. 1146 (Feb. 26, 2008).

[9]*Sprint/United Management Co. v. Mendelsohn*, 466 F.3d 1223 (10th Cir. 2006), *rev'd by* 128 S. Ct. 1146 (Feb. 26, 2008).

[10]128 S. Ct. 1147 (Feb. 27, 2008).

[11]29 U.S.C. § 626(d) (2008).

[12]*Federal Express Corp. v. Holowecki*, 440 F.3d 558 (2nd Cir. 2006), *aff'd by* 128 S. Ct. 1147 (Feb. 27, 2008).

[13]467 F.3d 571 (6th Cir. en banc Oct. 31, 2006), *cert. granted*, 76 U.S.L.W. 3153 (U.S. Sept. 25, 2007) (No. 06-1037).

[14]476 F.3d 54 (1st Cir. 2007), *cert. granted*, 76 U.S.L.W. 3154 (U.S. Sept. 25, 2007) (No. 06-1321).

[15]29 U.S.C. § 633a (2008).

[16]463 F.3d 1076 (9th Cir. 2007), *cert. granted*, 76 U.S.L.W. 3273 (U.S. Nov. 20, 2007) (No. 06-939).

[17]211 Fed. Appx. 373 (6th Cir. 2006), *cert. granted*, 76 U.S.L.W. 3391 (U.S. Jan. 18, 2008) (No. 06-1595).

[18]42 U.S.C. § 2000e-3 (2008).

[19]461 F.3d 134 (2nd Cir. 2006), *cert. granted*, 76 U.S.L.W. 3391 (U.S. Jan. 18, 2008) (No. 06-1505).