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Trademark Dilution Proof in Flux

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The federal law of trademark dilution has evolved significantly in the past year, with a split that developed between the Second and Fourth Circuit Courts of Appeal on the crucial aspect of whether a plaintiff must show "actual harm" in order to stop the offender. How this split is resolved will affect many businesses, whether they hold "famous" trademarks that they seek to protect, or whether they are setting up new trademarks that might be attacked by others as arguably diluting their own marks. Internet firms are likely to be active on both sides of the debate.

A federal cause of action for trademark dilution is relatively recent. Although some states, such as New York, have had trademark dilution statutes for nearly 50 years, the Federal Trademark Dilution Act (FTDA) was enacted only four years ago. The idea was to create a uniform federal standard that would supplement state law regarding trademark dilution cases.

But dilution always has been a nebulous concept, and the standards under various state laws have been less than clear. Congress did not help matters when it drafted the statute to require that the offending mark "causes dilution," while the hallmark of trademark infringement generally has been "likelihood of confusion." Just how much dilution or confusion must the senior trademark holder show?

Applying this "dauntingly elusive concept," the Fourth Circuit held in 1999 that the plaintiff must prove that the offending mark causes "actual harm" before it can be said to "cause dilution."[1] Since no actual harm was shown, the court allowed the State of Utah to continue to use the slogan "Greatest Snow on Earth," despite protests from Ringling Bros.-Barnum & Bailey, the owners of the "Greatest Show on Earth."

But a few months later, the Second Circuit explicitly rejected this interpretation, saying that it could be virtually impossible for a plaintiff to show the existence of "actual harm" even in a case where the dilution was obvious. Instead, it allowed the plaintiff to show dilution by circumstantial evidence, leading the court to enjoin Nabisco from making an orange, goldfish-shaped, bite-sized cheddar cracker that closely resembled the famous Pepperidge Farm goldfish crackers – even though the Nabisco cracker had not yet even been released on the market.[2]

More recent decisions have been less clear on the necessity of showing "actual harm." A Second Circuit decision in January 2000 strongly implied that the Federal Express Corporation had not suffered actual harm from two "Federal Espresso" coffee shops in Syracuse, N.Y., but ultimately relied on other factors when it affirmed the lower court's denial of a preliminary injunction motion.[3] Several other recent cases have involved Internet domain name disputes, but they provide little guidance as to whether "actual harm" must be shown for a court to find dilution. The most recent significant dilution case, *eToys.com v. etoy.com*, was settled at the end of January with etoy.com, a European artists' collective, obtaining the right to reopen the www.etoy.com Web site that had been shut down on a preliminary injunction obtained by eToys.com in November.

Federal Dilution Act

The FTDA became effective in January 1996 and amended §43 of the Lanham Act to provide a new cause of action for trademark "dilution." Specifically, the act provides the owner of a "famous mark" protection against another person's use of a mark "if such use begins after the mark has become famous and causes dilution of the distinctive quality of the mark."[4]

The FTDA defines dilution as "the lessening of the capacity of a famous mark to identify and distinguish goods or services, regardless of the presence or absence of (1) competition between the owner of the famous marks and other parties, or (2) likelihood of confusion, mistake, or deception."[5] In so doing, Congress sought to protect owners of famous, distinctive trademarks by prohibiting unauthorized, commercial "uses that blur the distinctiveness of [a famous] mark or tarnish or disparage it."[6] The hypothetical examples of "blurring" cited by Congress at the time the statute was enacted were "Buick aspirin," "Schlitz varnish" and "Kodak Pianos."[7] Whether or not there was confusion in the marketplace so as to constitute trademark infringement, these junior uses could effectively whittle away at each senior mark's unique, distinctive identity.

Since its inception, courts have struggled to determine what constitutes dilution under the FTDA. The essential elements of a dilution claim can be categorized as follows:

(1) The senior mark must be famous and distinctive.

(2) The junior use must be a commercial use in commerce that began after the senior mark became famous.

(3) The junior use must cause dilution of the senior mark's distinctive quality.

While courts have generally treated the first two categories consistently, they have struggled to develop a proper analysis for determining whether a junior use dilutes a senior mark's distinctive quality.

Ringling Bros. Go to Court

In *Ringling Bros.-Barnum & Bailey Combined Shows*, plaintiff Barnum & Bailey brought an action against the State of Utah under the FTDA, alleging that Utah's mark, "The Greatest Snow on Earth," diluted Barnum & Bailey's mark, "The Greatest Show on Earth." Barnum & Bailey introduced survey evidence that seemingly showed a mental association among consumers of the two marks. But the district court rejected the survey evidence and held that the FTDA requires proof of "actual harm" by the junior use.

Affirming the district court's decision, the Fourth Circuit held that dilution under the FTDA requires: (1) a sufficient similarity of marks to evoke in consumers a mental association of the two that (2) causes (3) actual harm to the senior mark's economic value as a product-identifying and advertising agent. Conceding that this interpretation does not "leap fully and immediately from the statutory text," the panel defended its interpretation by arguing that to hold otherwise would create a property right "in gross" for suitably "unique" marks, making them comparable to those protected by patent and copyright law. Apparently, the Fourth Circuit believed that if a junior use could be proscribed as dilutive without a showing of actual economic harm to the senior mark, then owners of senior marks could challenge any use of their marks, in any field, no matter how minor the junior use.

Turning to case law evolution under state dilution statutes, the circuit court noted frequent allusion to a mark's selling power and the "whittling away" of that power as being the primary focus of dilution law. Thus, the court concluded that it was the selling power of a mark and its economic value – rather than its distinctiveness – which dilution law sought to prevent. And by specifically defining dilution as "the lessening of the capacity of a famous mark to identify and distinguish goods or services," the panel concluded that the FTDA "makes plain what the state statutes arguably may not: that the end harm at which it is aimed is a mark's selling power, not its 'distinctiveness' as such." The court held, accordingly, that the FTDA requires actual proof of the lessening of the senior mark's selling power.

The real interpretive problem, the Fourth Circuit opined, has been how harm to the senior mark's selling power resulting from the junior mark's use could be proved. But because the state statutes contained text which required only a "likelihood" of dilution, the courts did not have to resolve this issue. The court also cited the FTDA's omission of the term "likelihood" in its definition of "dilution" as further evidence that the federal statute "provides remedy only for actual, consummated dilution and not for the mere likelihood of dilution."

In so holding, the panel conceded that this rule is a stringent interpretation of dilution, which confines the federal dilution claim to a more narrow scope than that generally accorded state law dilution claims. The court also recognized the extreme difficulty or near impossibility of proving actual economic harm caused by dilution, but replied, "though proof of those elements . . . may tax the skills of advocacy . . . [I]f they do exist, there are means of proving them by normal evidentiary processes. Impossibility or near-impossibility of proving them does not support their judicial presumption."

Second Circuit Speaks

In *Nabisco Inc. v. PF Brands Inc.*, the Second Circuit agreed that proving actual economic harm from trademark dilution is virtually impossible, but expressly rejected the Fourth Circuit's ruling that the FTDA requires proof of actual dilution. In that case, Nabisco was ordered to recall and cease selling certain cheese crackers, which were manufactured in accordance with a joint promotion agreement between Nickelodeon and Nabisco to promote a Nickelodeon cartoon program entitled "CatDog."

Pursuant to the agreement, Nabisco developed a CatDog snack consisting of small orange crackers in three shapes, including a fish that closely resembled Pepperidge Farm's Goldfish cracker in color, shape, size and taste. But the Nabisco fish cracker was somewhat larger and flatter, and had markings on one side.

Based upon Pepperidge Farm's federal and state dilution claims, the district court preliminarily enjoined Nabisco from marketing the CatDog crackers. Affirming the district court's decision, the Second Circuit rejected Nabisco's argument, based on the *Ringling Bros.* decision, that proof of actual consummated dilution was required to show dilution of the Pepperidge Farm mark.

In rejecting the Fourth Circuit's decision, the Second Circuit noted that it was not clear which of two positions the Fourth Circuit had adopted when it required proof of actual dilution:

(1) that courts may not infer actual damage from contextual factors (degree of mark and product similarity, etc.), but instead must rely on evidence of "actual loss of revenues" or the "skillfully constructed consumer survey;" or (2) that the FTDA requires that dilution be proved not only by a showing of lost revenues, but also that the junior user must be already established in the marketplace before the senior can seek an injunction. In any event, the Second Circuit took issue with both positions.

Requiring proof of actual revenue loss resulting from dilution, the court argued, was virtually impossible. If, for example, the senior mark was being exploited with continually growing success, the senior user might never be able to show diminished revenues, no matter how obvious the dilution was. And even if diminished revenue could be shown, the court opined that it would be extraordinarily speculative and difficult to prove that the loss was necessarily due to the mark's dilution. The court also pointed out the expense and unreliability of consumer surveys, which are prone to manipulation.

The Second Circuit noted that ordinarily plaintiffs are "free to make their case through circumstantial evidence that will justify an ultimate inference of injury." And, therefore, the court concluded that if a junior user began to market Buick aspirin or Schlitz shellac, the senior users should also be able to rely on "persuasive circumstantial evidence of dilution of their distinctiveness of their marks without being obligated to show lost revenue or engage in an expensive battle of surveys." The panel also reasoned that because contextual factors have long been used to establish infringement, it saw no reason why such factors should not be used to prove dilution.

The court also attacked the broader second reading of the Fourth Circuit's decision, which would impose an additional requirement that the junior user be already established in the marketplace before the senior could seek an injunction. While conceding that the statute lends some support to this interpretation in that it uses the language "causes dilution," rather than referring to "likelihood of dilution," the Second Circuit maintained that this excessively literal reading would defeat the intent of the statute. The panel found it significant that Nabisco has an established distribution and marketing infrastructure; if the Nabisco crackers had been allowed on the market, the dilution of Pepperidge Farms' trademark would have been immediate, and an injunction at that time would have been too late.

Thus, the Second Circuit concluded that the Fourth Circuit's interpretation risked leaving senior mark owners with uncompensable injury, as the FTDA could not be invoked until after injury had occurred. Because the statute generally provides for injunctive relief without damages, the injury would never be compensated.

The Fourth Circuit's interpretation also would prevent a junior user from seeking declaratory relief to determine the permissibility of a proposed use before investing significant time and capital in launching and promoting its mark. The Second Circuit persuasively reasoned that such implications hardly could have been the intent of Congress when it passed the FTDA, and in fact, it was Nabisco as a junior trademark user that had brought the goldfish cracker case as a declaratory judgment action.

Further Developments

Since the Fourth Circuit's ruling in *Ringling Bros.-Barnum & Bailey Combined Shows*, several district courts have followed its ruling,[8] including at least one decision that came after the

Second Circuit's *Nabisco* decision.[9] However, the Second Circuit's decision clearly better reaches the intent of the statute. The Second Circuit's decision also is in conformance with a First Circuit case rejecting the requirement that the diluting mark cause a lessening in demand for the plaintiff's product although the First Circuit did not clearly articulate any test for evaluating dilution claims.[10]

The Second Circuit also stepped away from an overly-tight focus on "actual harm" by developing a 10-factor test to determine whether dilution has occurred. In the *Federal Express v. Federal Espresso* decision in January, the Second Circuit reapplied and reinforced the use of these facts, which are:

- the distinctiveness of the senior mark;
- the similarity of the marks;
- the proximity of the products, and the likelihood that if they are not presently similar, that the senior trademark holder might "bridge the gap" and sell products similar to the junior user;
- the "interdependent relationship" of the first three factors;
- the extent of overlap among consumers of the senior user's products and the junior user's products;
- sophistication of consumers;
- whether there is actual confusion;
- whether the senior user's mark is indeed descriptive of the junior user's product;
- whether the senior user acted promptly or allowed the junior user to develop goodwill in the mark; and
- whether the senior user has been lax in the past in protecting its mark against dilution.

Analyzing all of these factors, the Second Circuit found no basis to enjoin "Federal Espresso" from the operation of its two coffee shops in Syracuse.

The most remarkable recent dilution case was brought by eToys.com against etoy.com, reportedly after the toy company received complaints from parents whose children found themselves at the Web site of the group of European conceptual artists. The toy manufacturer obtained a preliminary injunction on a dilution theory last November, but the case was settled at the end of January with eToys.com agreeing to allow etoy.com back on the Web and reimbursing etoy.com $40,000 in legal expenses. Etoy.com had mounted an online protest and e-mail campaign against eToys.com, and the artists claimed credit for the recent drop in the toy seller's stock price.

Undoubtedly eToys.com would have had a tough time at trial proving "actual harm" under the Fourth Circuit standard. Yet even under the Second Circuit factors, the toy seller would have had great difficulty at trial – if for no other reason than that eToys.com was not the senior trademark holder. The artists had been on the Internet since 1995, two years before the launch of the eToys.com site.

Many more dilution cases will be brought, and courts will continue to wrestle with the concept of dilution. We think it more likely that the Second Circuit's factors will gain widespread acceptance, just as the Second Circuit's landmark decision in the "Lexis v. Lexus" case in 1989[11] has set the tone for analysis for dilution claims under the New York Anti-Dilution statute.

(1) *Ringling Bros. Barnum & Bailey Combined Shows, Inc. v. Utah Div. of Travel Dev.*, 170 F.3d 449, 450 (4th Cir. 1999).

(2)*Nabisco, Inc. v. PF Brands, Inc*., 191 F.3d 208 (2d Cir. 1999).

(3) *Federal Express Corp. v. Federal Espresso, Inc*., No. 98-9430, 2000 WL 6084 (2d Cir., Jan. 5, 2000).

(4) Codified at 15 U.S.C. §1125(c)(1).

(5) Lanham Act §45, 15 U.S.C. §1127.

(6) H.R. Rep. No. 104-374, at 2 (1995), U.S. Code Cong. & Admin. News at 1029.

(7) These examples, as well as "DuPont shoes" and "Bulova gowns," previously appeared in the New York State legislative history when New York enacted its state dilution law, N.Y. Gen. Bus. Law §360-1 (formerly §368-d). See 1954 N.Y. Legis. Ann. 49-50.

(8) *Planet Hollywood (Region IV), Inc. v. Hollywood Casino Corp.*, No. 96 C 4660, 1999 WL 1131887, at *68 (N.D. Ill. Dec. 3, 1999); *Playboy Enterprises, Inc. v. Netscape Communications Corp.*, 55 F.Supp.2d 1070, 1075 (C.D.Ca. 1999); *American Cyanamid Co.v. Neutraceutical Corp.*, 54 F. Supp.2d 379, 391 (D.N.J. 1999); *World Gym Licensing, Ltd. v. Fitness World, Inc.*, 47 F. Supp.2d 614, 625 (D.Md. 1999).

(9) *See Planet Hollywood*, supra.

(10) *I.P. Lund Trading ApS v. Kohler Co.*, 163 F.3d 27, 49 (1st Cir. 1998).

(11) *Mead Data Central, Inc. v. Toyota Motor Sales, U.S.A., Inc.*, 875 F.2d 1026 (2d Cir. 1989).

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