WESTERN NEW YORK
THE DAILY RECORD
YOUR TRUSTED SOURCE FOR LEGAL AND REAL ESTATE NEWS
NYDAILYRECORD.COM
SEPTEMBER 15, 2020

# IP Frontiers: The fallacy of 'free-floating' trademarks as a distinct business asset

By ALANA M. FUIERER, ESQ

A trademark (or service mark) is a business asset akin to other forms of intellectual property (e.g., patents, copyrights) and tangible business assets. And, yes, it is true that, just like other tangible or intangible business assets, trademarks frequently are bought, sold, transferred, licensed, and even used as security interest. However, under U.S. law, there is a significant distinction between trademarks and other forms of intellectual property — a trademark is wholly dependent on another intangible asset. Goodwill. This oft-forgot dependency can result in a business owner inadvertently losing trademark rights regardless of how many federal trademark registrations are in its portfolio.

**The relationship between trademarks and goodwill**

Goodwill is an intangible asset that represents the value of a business by virtue of its quality and reputation with consumers. It can add significant value to a business when it comes time to sell or otherwise transfer it, and this value is usually set forth in the valuation of a business. Similarly, the goodwill of a trademark or service mark represents the inherent value of the mark — that is, the recognition of a company's mark among consumers and the value it generates. Under U.S. law, it is well established that a "trade name or mark is merely a symbol of goodwill; it has no independent significance apart from the goodwill it symbolizes." Marshak v. Green, 746 F.2d 927, 929 (2d Cir. 1984).

This trademark principle stems from the fact that, in the U.S., all rights in a trademark originate via use in commerce. Actual use is a prerequisite to acquire rights, and continuous use is required to maintain them. Therefore, unlike patents or copyrights, trademarks "are not property rights apart from their use in connection with a business." United Drug Co. v. Theodore Rectanus Co., 248 U.S. 97 (1918) (holding it is a "fundamental error [to suppose] that a trademark right is a right in gross or at large" and that there is "no such thing as property in a trademark except as a right appurtenant to an established business or trade in connection with which the mark is employed"). A company builds up goodwill in both its business and trademarks through years of use, advertising and marketing. It is through this use that a trademark becomes a source identifier and gains value. As explained by the Second Circuit:

"[T]rademarks are 'incidents and appurtenances to businesses and trades. They have no independent existence.' … Put another way, '[t]rademark rights do not exist in the abstract, to be bought and sold as a distinct asset.'"

Berni v. Int'l Gourmet Rest. of Am., Inc., 838 F.2d 642, 646 (2d Cir. 1988); see 1 J. Thomas McCarthy, McCarthy on Trademarks and Unfair Competition § 2:15 (4th ed. 2014) ("Trademarks, unlike patents and copyrights, have no existence independent of the good will of the products or services in connection with which the mark is used.")

So while a business may accumulate goodwill as a business asset without any trademarks, the reverse is not true. It is not possible for a trademark or service mark to exist as mere chattel unless it is also accompanied by the goodwill associated with the ongoing business that created it. This article explores how this longstanding legal principle can result in at least one misstep when a business owner attempts to retain and exploit its trademark(s).

**The sale of business and its goodwill voids any attempt to retain marks**

Although this misstep can happen in the sale of any business, it typically takes place under the following scenario: A business owner provides a service, e.g., a restaurant, a dog groomer, or a plumbing business and owns (and perhaps registers) a service mark, and then eventually, after several years of building the business, the owner decides to sell its ongoing business to a third party. In doing so, the business owner intends to retain all trademarks with the goal of licensing or otherwise generating future income from them.

Under the principles outlined above, regardless of the business owner's expressed intent or the language of the sales agreement(s), rights in a trademark cannot be transferred or retained "in gross" or apart from an ongoing business. See Marshak, 746 F.2d at 929 ("There are no rights in a trademark apart from the business with which the mark has been associated; they are inseparable."); see also Berni, 838 F.2d at 646-47. The problem is that when an ongoing business is sold, it frequently is sold complete with its goodwill. When this happens, courts have held the buyer necessarily acquires ownership of any trademarks the seller owned and under which the buyer continued to operate its business, even if not expressly stated as such. This transfer occurs as a matter of law. See Stagecoach Properties, Inc. v. Wells Fargo & Co., 199 USPQ 341, 347 (TTAB 1978) (presumption is that rights to the marks and name were transferred with the business); see also Dairymen's League Co-Operative Ass'n v. Weckerle, 160 Misc. 866, 875, 291 N.Y.S. 704, 711 (Sup. Ct. 1936) ("[A]s a general rule, [the sale of good will of a business] includes the name under which the business is conducted and by which it is known.")

This was such the case in Moloney v. Centner. See Moloney v. Centner, 727 F. Supp. 1232, 1239 (N.D. Ill. 1989). In Moloney, the plaintiff had owned a business and a federally registered service mark for several years. The federal service mark registration was for the "stylized" version of the service mark (i.e. the logo). When it came time to sell the business, the owner expressly retained ownership of the registered logo. The asset purchase agreement, however, provided for the sale of the business, including all goodwill. Some years later, the original owner sued the new owner for trademark infringement, asserting the retained federal registration. In granting the new owner's motion to dismiss the infringement claims, the Moloney court held that because the asset purchase agreement provided for the sale of the business's goodwill, the sale of the business effectively transferred all trademarks and/or service marks to the defendants. Moloney, 727 F. Supp. at 1239. Thus, although the prior owner of the business still held a federal registration for the stylized logo, the court found the prior sale of underlying goodwill and business name divested the original owner's standing to bring suit under the federally registered mark. Id. Furthermore, given this ruling, the federal registration would be subject to

Reprinted with permission of The Daily Record © 2020

cancellation.

More recently, "[a]n attempt to simultaneously sell a restaurant and license associated intellectual property has led to ten years of litigation in state and federal court." Uptown Grill, L.L.C. v. Camellia Grill Holdings, Inc., 920 F.3d 243 (5th Cir. 2019). In this case, Michael Shwartz owned and operated the Camellia Grill restaurant for decades. He also owned a separate holding company for the sole purpose of owning federally registered Camellia Grill trademarks. In 2006, Shwartz sold his only brick and mortar Camellia Grill restaurant to Uptown Grill, LLC. Under the bill of sale, Schwartz sold all:

"right, title and interest in and to the… tangible property located within or upon" the restaurant, including "all furniture, fixtures and equipment, cooking equipment, kitchen equipment, counters, stools, tables, benches, appliances, recipes, trademarks, names, logos, likenesses, etc., and all other personal and/or movable property… located within or upon the property."

Id. In a separate license agreement, Schwartz's holding company licensed the right to use the trademarks, including "all 'Camellia Grill' marks on file with the USPTO" and "all 'trade dress' associated with the 'Camellia Grill' Restaurant," as well as blueprints, menus, and recipes. The license agreement also provided that the "Licensee acknowledges and agrees that all of the Licensor's right, title and interest in and to the Marks shall remain the property of the Licensor." Id. at 246.

On paper, all would appear to be in order. Schwartz's intent clearly was to sell the physical restaurant and business but retain the ability for his holding company to license the trademarks and other intangibles (i.e., receipts, menus) as a future income stream. Despite his intent, the question that resulted in 10+ years of litigation was this: Did Schwartz properly retain any interest in the Camellia Grill trademarks when he sold his restaurant? According to the 5th Circuit, the answer is a resounding "No."

"As a technical matter, a trademark cannot be separated from the goodwill of a business. So, when an entire business is sold, as here, the goodwill and associated trademarks are necessarily transferred absent certain conditions not present here … we cannot look to parol evidence to find otherwise."

Id. at 248. The Court went on to explain that to retain ownership after the sale of the business associated with the trademark, "some portion of the goodwill of the previous business must remain with the owner, and resumption of operations must occur within a reasonable time." Id. at 248 (emphasis added). In this case, the only Camellia Grill business was at the location that Schwartz sold. Since all goodwill associated with Camellia Grill was connected to the business that was sold, no goodwill remained to which otherwise "free-floating trademark rights" could attach. Id. at 249.

These two cases provide business owners with a valuable lesson that should not be ignored. Trademarks are not a right in gross that can be divorced from their goodwill, and therefore are not a distinct business asset that can be bought and sold like other forms of property. The ownership of a federal trademark registration does not change this fact. In practice, if one wishes to retain a registered (or unregistered) trademark when selling a business for future licensing or other financial opportunities, it is not enough to ensure the sales agreement reserves rights in the mark. More importantly, the seller must retain at least a portion of the business's goodwill, or risk losing any rights in the mark altogether.

*Alana M. Fuierer, Esq. is a partner in the Rochester office of Heslin Rothenberg Farley & Mesiti, PC. Ms. Fuierer can be reached at (585) 288-4832 or alana.fuierer@hrfmlaw.com.*