

Holdover Trademark Licensees and the Counterfeiting Loophole*

I. Introduction

In today's decidedly consumerist America,¹ trademark law necessarily serves a critical function.² Trademarks decrease consumer search costs, allowing the public to distinguish quickly between products and services by relying on brand name as an indicator of consistent quality.³ Consumers need not examine the attributes of a product or service before each purchase; once a consumer has knowledge of a particular brand, the trademark provides a shorthand signal of those attributes.⁴ Trademark law also benefits producers, encouraging expenditures to maintain consistent quality and protecting producers' goodwill in their marks from free-riding competitors.⁵

Trademark protection, however, is being significantly weakened by substantial breakdowns in statutory and common law.⁶ One of these breakdowns—the subject of this Note—manifests when an entity formerly licensed to use a mark continues to do so after the license has expired or terminated. In such a scenario, because the license has lapsed, continued use of the mark reflects an improper connection to now unauthorized, unlicensed products or services. Although courts often impose trademark-infringement liability on these “holdover licensees”⁷ (as one might expect), infringement

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1. See, e.g., James Q. Whitman, *Consumerism Versus Producerism: A Study in Comparative Law*, 117 *YALE L.J.* 340, 394 (2007) (“Americans came to regard ‘consumer’ as their primary legal identity during the mid-twentieth century . . .”).

2. Protection of consumers is the primary policy justification underlying trademark law. Jessica Litman, *Breakfast with Batman: The Public Interest in the Advertising Age*, 108 *YALE L.J.* 1717, 1729 (1999).

3. William M. Landes & Richard A. Posner, *Trademark Law: An Economic Perspective*, 30 *J.L. & ECON.* 265, 268–69 (1987).

4. *Id.* at 269.

5. *Id.* at 269–70.

6. See, e.g., Arielle G. Lenza, Case Comment, *Rescuecom Corp. v. Google, Inc.*, 52 *N.Y.L. SCH. L. REV.* 137, 138 (2007–2008) (arguing that the interpretation of the Lanham Act's “use” requirement in *Rescuecom Corp. v. Google, Inc.*, 456 F. Supp. 2d 393 (N.D.N.Y. 2006), threatens to weaken trademark protection).

7. See, e.g., *U.S. Structures, Inc. v. J.P. Structures, Inc.*, 130 F.3d 1185, 1193 (6th Cir. 1997); *Pennzoil-Quaker State Co. v. Smith*, No. 2:05cv1505, 2008 WL 4107159, at *20 (W.D. Pa. Sept. 2, 2008) (both finding a holdover licensee liable for trademark infringement).

liability alone is typically insufficient to satisfy trademark law doctrine and policy.⁸ Instead, as this Note will argue, holdover licensees should generally incur liability for a more severe and more appropriate cause of action: trademark counterfeiting.

Imagine the following scenario. A young entrepreneur, holding a freshly minted business degree from a top university, wants to put his education to work immediately. He decides to open a business, but rather than facing the difficulties involved with creating a startup, he elects to open a franchise location of a well-established company—McDonald's. Under the franchise agreement, the entrepreneur agrees to give McDonald's a 15% royalty of his total sales. In exchange, McDonald's provides him with regular shipments of its "delicious cuisine," along with menus, signage, and other materials bearing the MCDONALD'S marks and trade dress⁹ to be installed at the location. McDonald's licenses the entrepreneur to use these marks and trade dress, conditioned upon continued fulfillment of his obligations under the franchise agreement.

Sometime later, things begin to sour. The entrepreneur begins to shortchange McDonald's on his required royalty payments. Due to this underpayment, McDonald's exercises its right to cancel the franchise, thereby terminating the entrepreneur's license to use the MCDONALD'S marks and trade dress. The entrepreneur, however, continues to operate a burger joint at the location. Because McDonald's has stopped food shipments, the entrepreneur buys burger patties, fries, and other menu items from a small local distributor—completely unaffiliated with McDonald's—who offers remarkably low prices. The entrepreneur takes down the large MCDONALD'S sign on the street, but to conserve time and money, he leaves up portions of the MCDONALD'S menus, wall decorations, and exterior building dressing.

The new burger joint is a success. Customers, some of whom are initially drawn to the location by the remnants of the well-known MCDONALD'S marks and trade dress, are ultimately quite satisfied with the entrepreneur's proprietary, non-McDonald's food. The entrepreneur, not wanting to disturb his good fortune, decides to leave the location as is, only

8. *See infra* Part IV.

9. Trade dress is the total image and overall appearance of a product or service, including features like size, shape, color combinations, textures, and graphics. *Two Pesos, Inc. v. Taco Cabana, Inc.*, 505 U.S. 763, 764 n.1 (1992). Trade dress is protectable under federal trademark law. *Traffix Devices, Inc. v. Mktg. Displays, Inc.*, 532 U.S. 23, 28–29 (2001); *see also* 15 U.S.C. § 1125(a)(3) (2006) (establishing specific rules for trade-dress-infringement actions). In the case of a McDonald's restaurant, trade dress would include the uniquely McDonald's building shape, interior wall dressing, and color scheme. *See Taco Cabana*, 505 U.S. at 764 n.1 (“[T]rade dress may include the shape and general appearance of the exterior of the restaurant, the identifying sign, the interior kitchen floor plan, the decor, the menu, the equipment used to serve food, the servers’ uniforms and other features reflecting on the total image of the restaurant.”).

removing some of the interior MCDONALD'S signage as it becomes outdated.

In this fact pattern—a prototypical holdover-licensee scenario—courts should generally impose liability for trademark counterfeiting. Liability for mere trademark infringement¹⁰ does not sufficiently serve trademark policy. Moreover, from a doctrinal standpoint, counterfeiting is the most appropriate cause of action. The leftover MCDONALD'S marks used by the entrepreneur are identical to those displayed at legitimate McDonald's restaurants. Yet unlike the marks at legitimate McDonald's restaurants, the marks at the entrepreneur's restaurant do not symbolize a genuine existing affiliation with McDonald's. Instead, the marks now represent a *false* connection to McDonald's: because the franchise has terminated, the marks are being used in connection with menu items that do not originate from McDonald's and services over which McDonald's has no control. This false connection leads to consumer confusion, the touchstone test for trademark counterfeiting.¹¹

Unfortunately, despite the cogent arguments for imposing counterfeiting liability on holdover licensees, certain courts have reached the opposite result.¹² Courts almost always levy liability for mere trademark infringement,¹³ but some courts refuse to go further.¹⁴ In these jurisdictions, holdover licensees are able to escape counterfeiting liability, even though their conduct—using *identical* versions of the former licensor's marks in connection with now inauthentic products or services—powerfully invokes both the doctrine and policy underlying trademark-counterfeiting prohibitions.¹⁵ This result imposes substantial costs on plaintiff mark owners, including the loss of almost-guaranteed treble damages and attorney's fees, or alternatively, statutory damages up to \$2 million per counterfeit mark.¹⁶

In arguing that holdover licensees should generally be liable for counterfeiting, this Note proceeds in several parts. Part II provides an overview of basic trademark law and policy, with a particular focus on

10. For a discussion of the distinction between trademark infringement and trademark counterfeiting, as well as other aspects of basic trademark law, see *infra* Part II.

11. See *infra* note 55 and accompanying text. Such confusion need not rise to the level of *actual* confusion—trademark counterfeiting requires only a *probability* of consumer confusion. See *infra* notes 48–49, 53, 59 and accompanying text. Further, even to the extent that customers very quickly realize the location is not a McDonald's, the brief initial confusion caused by the MCDONALD'S marks is sufficient to establish trademark counterfeiting. See *infra* notes 50–51 and accompanying text.

12. See, e.g., *U.S. Structures*, 130 F.3d at 1190, 1192 (upholding a lower court finding of trademark infringement against a holdover licensee, but denying a counterfeiting claim).

13. See Litman, *supra* note 2, at 1725–26 (describing courts' use of trademark law to “uphold claims to exclusive rights” in various proprietary marks); see also cases cited *supra* note 7.

14. See, e.g., *U.S. Structures*, 130 F.3d at 1192 (reversing a judgment of counterfeiting liability for a holdover licensee).

15. See *infra* subpart IV(B).

16. See *infra* notes 75–83 and accompanying text.

counterfeiting. Part III describes the holdover-licensee scenario more fully and explains the deficient precedents that have allowed holdover licensees in certain courts to escape counterfeiting liability. Part IV argues that courts should reject those precedents and recognize trademark counterfeiting as the most appropriate cause of action against holdover licensees. To advance this argument, Part IV posits three explanations sympathetic to current case law denying counterfeiting liability but ultimately rejects those explanations. Part V suggests two solutions, one legislative and one judicial, through which courts could more readily impose counterfeiting liability. The legislative solution is for Congress to amend the statutory definition of *counterfeit*¹⁷ to read: “A ‘counterfeit’ is a spurious mark that is identical to, or substantially indistinguishable from, a registered mark. A mark is ‘spurious’ if it is a physically inauthentic replica, or if it is an authentic mark used in connection with inauthentic products or services.” The judicial solution is for courts construing the definition of *counterfeit* to engage in a more nuanced process of statutory interpretation, using trademark policy to resolve ambiguous statutory language and legislative history.

II. Trademark Law Overview

A. General Principles and Policy

A trademark is an identifying symbol.¹⁸ Under the Lanham Act¹⁹—the federal trademark statute—a *trademark* is defined as a designation that identifies and distinguishes a producer’s goods or services and indicates their source.²⁰ In essence, a mark must answer the question: “Who are you?”²¹ Beyond this prerequisite, there are no technical limitations on the allowable subject matter that may form a mark.²² Words, such as WAL-MART, remain the most common types of marks,²³ but trademark protection also extends to

17. See 15 U.S.C. § 1127 (2006) (defining *counterfeit* as “a spurious mark which is identical with, or substantially indistinguishable from, a registered mark”).

18. 1 J. THOMAS MCCARTHY, MCCARTHY ON TRADEMARKS AND UNFAIR COMPETITION § 3:4, at 3–14 (4th ed. 2009).

19. 15 U.S.C. §§ 1051–1141n.

20. *Id.* § 1127. The term *trademark* technically refers only to marks used on goods. JANE C. GINSBURG ET AL., TRADEMARK AND UNFAIR COMPETITION LAW: CASES AND MATERIALS 17 (4th ed. 2007); see also 15 U.S.C. § 1127 (defining a *trademark* as a designation used to identify and distinguish goods). However, the term is often used as a blanket definition covering other types of marks, such as service marks (marks used in connection with services, rather than goods). 1 MCCARTHY, *supra* note 18, § 3:1. Accordingly, this Note will use the terms *trademark* and *mark* as inclusive of all subject matter protectable under the federal trademark statute. *Cf.* 15 U.S.C. § 1127 (“The term ‘mark’ includes any trademark, service mark, collective mark, or certification mark.”).

21. 1 MCCARTHY, *supra* note 18, § 3:6.

22. RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 9 cmt. g (1995); see also 15 U.S.C. § 1127 (providing that a trademark may consist of “any word, name, symbol, or device, or any combination thereof”).

23. RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 9 cmt. g.

other designations, including logos,²⁴ sounds,²⁵ trade dress,²⁶ and in some instances, even single colors.²⁷

Trademark law promotes several policy rationales. First, trademarks protect consumers from confusion.²⁸ Because trademarks must identify and distinguish source, trademarks reduce the potential for misunderstanding and deceit in the marketplace, allowing consumers to proceed with confidence in the truth of the information presented.²⁹

Second, trademarks lower consumer search costs.³⁰ As a consumer gains experience with a product or service, the attached marks (i.e., the brand) “become associated with expectations of a particular quality.”³¹ This economizes the cost of information about anticipated performance, leading to more efficient future purchases—rather than fully investigating a product or service before each purchase, a consumer can use his past experience with the brand to make a decision.³²

Third, trademarks create optimal quality-based incentives for producers. Producers must build and maintain a consistent quality over time and across consumers, or else the producers’ marks will cease to embody any particular level of quality.³³ A producer’s failure to maintain that consistent quality destroys the marks’ search-cost-economizing function, thereby devaluing the marks to the consumer.³⁴ Moreover, beyond simply promoting consistency at any level of quality (e.g., consistently low-quality products), trademark

24. See, e.g., *In re Corning Glass Works*, 6 U.S.P.Q.2d (BNA) 1032, 1033 (T.T.A.B. 1988) (“A design which has ornamental value may nevertheless be registered if it also functions as a trademark.”).

25. See, e.g., U.S. Trademark No. 3,288,274 (filed May 30, 2005) (issued Sept. 4, 2007) (establishing a federal trademark registration for a sound comprising a C eighth note, E-flat eighth note, B-flat eighth note, G quarter note, C eighth note, and C quarter note for use by Nokia on various communication devices).

26. See *supra* note 9.

27. See, e.g., *Qualitex Co. v. Jacobson Prods. Co.*, 514 U.S. 159, 159 (1995) (holding that when a single color has come to indicate a particular source of goods or services, “no special legal rule prevents color alone from serving as a trademark”).

28. See *Dart Drug Corp. v. Schering Corp.*, 320 F.2d 745, 748 n.10 (D.C. Cir. 1963) (“[C]onfusion to the public is the essence of both trademark infringement and unfair competition.” (citations omitted)); *Safeway Stores, Inc. v. Safeway Prods., Inc.*, 307 F.2d 495, 497 (2d Cir. 1962) (“The keystone in that portion of the law of unfair competition which relates to trademarks is the avoidance of confusion in the minds of the buying public.”).

29. *Falcon Rice Mill, Inc. v. Cmty. Rice Mill, Inc.*, 725 F.2d 336, 348 (5th Cir. 1984). The importance of preventing consumer confusion is further illuminated by the fact that the touchstone test for trademark infringement and trademark counterfeiting is likelihood of confusion. See *infra* subpart II(B).

30. ARMEN ALCHIAN & WILLIAM R. ALLEN, *EXCHANGE AND PRODUCTION: COMPETITION, COORDINATION, AND CONTROL* 193 (2d ed. 1977); Landes & Posner, *supra* note 3, at 268–69.

31. ALCHIAN & ALLEN, *supra* note 30, at 193.

32. *Id.*

33. Landes & Posner, *supra* note 3, at 269.

34. *Id.*

law actually encourages producers to *improve* quality.³⁵ Because marks identify and distinguish source, producers cannot evade associations between their marks and the quality of their products or services.³⁶ Thus, producers are incentivized to improve quality as much as consumers are willing to pay for it.³⁷ In contrast, without trademark law, consumers would be unable to recognize high- or low-quality brands, so producers would have little motivation to improve quality.³⁸ Sales would simply go to the producers who cut quality and offered the lowest prices.³⁹

Finally, trademark law protects a producer's goodwill in his marks from free-riding competitors.⁴⁰ Given that it is exponentially more expensive to build up goodwill in one's own marks than to simply duplicate and use another's, a lack of trademark protection would disincentivize expenditures to develop goodwill and instead incentivize simply copying and using marks already established by others.⁴¹

B. Trademark Infringement

The essence of trademark infringement is *likelihood of confusion*.⁴² Under the Lanham Act, the touchstone test for whether a defendant has infringed a plaintiff's mark is whether the defendant's use of the allegedly infringing mark is likely to confuse the consuming public.⁴³ Generally, likelihood of confusion can occur in two broad scenarios.⁴⁴ In the first scenario, the defendant's use of the mark confuses the public into believing that the defendant's products or services originate from the plaintiff.⁴⁵ In the second scenario, the defendant's use confuses the public into believing that there is some other affiliation, association, or sponsorship between the plaintiff and the defendant.⁴⁶ Most circuits utilize a multifactor balancing test to determine whether a defendant's use of a mark has created likelihood of

35. 1 MCCARTHY, *supra* note 18, § 2:4.

36. *See* Landes & Posner, *supra* note 3, at 269 (describing how trademarks allow consumers to associate quality levels with brands).

37. *Id.*

38. *Id.*

39. *Id.*

40. *Id.* at 270.

41. *See id.* (arguing that the incentive for producers to incur the expense of creating a trusted trademark will be destroyed if such marks are not protected by trademark law).

42. *Internet Specialties W., Inc. v. Milon-DiGiorgio Enters.*, 559 F.3d 985, 990 (9th Cir. 2009); *see also* 15 U.S.C. §§ 1114(1)(a), 1125(a)(1)(A) (2006) (prohibiting use of a mark where such use is "likely to cause confusion, . . . mistake, or to deceive"). Likelihood of confusion is also known as "confusing similarity." 4 MCCARTHY, *supra* note 18, § 23:4.

43. 4 MCCARTHY, *supra* note 18, § 23:1, at 7.

44. 2 ANNE GILSON LALONDE, *GILSON ON TRADEMARKS* § 5.01[3] (Karin Greene ed., 2008) [hereinafter *GILSON*].

45. *Id.*

46. *Id.*

confusion.⁴⁷ Likelihood of confusion requires only a *probability* of consumer confusion;⁴⁸ evidence of *actual* confusion is not required.⁴⁹

Likelihood of confusion can occur at various points in the commercial process. Confusion often manifests at the point of sale—i.e., at the time of the consumer’s purchase—but need not necessarily arise then.⁵⁰ Under the doctrine of initial-interest confusion, likelihood of confusion (and therefore infringement) may also stem from confusion that creates initial customer interest in a product or service, even though such confusion never actually results in a sale.⁵¹ Confusion may also occur postsale, among individuals other than the purchaser.⁵²

C. Trademark Counterfeiting

Trademark counterfeiting is a subset of trademark infringement.⁵³ All counterfeiters infringe, but all infringers do not necessarily counterfeit.⁵⁴ In both counterfeiting and infringement cases, likelihood of confusion is the critical inquiry.⁵⁵ The key difference is that, in counterfeiting cases, the defendant’s mark is impossible or extremely difficult to tell apart from the plaintiff’s.⁵⁶

The cause of action for counterfeiting is created by Lanham Act provisions 15 U.S.C. § 1117(b) and (c). Referencing § 1117(a), which

47. *See, e.g.*, *Polaroid Corp. v. Polarad Elecs. Corp.*, 287 F.2d 492, 495 (2d Cir. 1961) (establishing eight factors for evaluating likelihood of confusion: strength of the plaintiff’s mark; degree of similarity between the plaintiff’s and defendant’s marks; proximity of the products or services attached to the marks; likelihood that the plaintiff will “bridge the gap”; evidence of actual confusion; defendant’s good faith in adopting the mark; quality of the defendant’s product or service; and sophistication of the buyers); *see also* RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 21 cmt. b reporter’s note (1995) (“The evolving views of the Second Circuit have been influential in the approach adopted by most courts to the likelihood of confusion issue The fact-oriented approach adopted in *Polaroid* has been followed by other courts, although the enumeration of relevant factors varies among jurisdictions.”).

48. 4 MCCARTHY, *supra* note 18, § 23:3, at 18.

49. *E. & J. Gallo Winery v. Consorzio Del Gallo Nero*, 782 F. Supp. 457, 465 (N.D. Cal. 1991); 4 MCCARTHY, *supra* note 18, § 23:12; *see also, e.g.*, *Polaroid*, 287 F.2d at 495 (holding that evidence of actual confusion is merely one factor in the likelihood-of-confusion analysis).

50. 4 MCCARTHY, *supra* note 18, § 23:5, at 22.

51. *Mobil Oil Corp. v. Pegasus Petroleum Corp.*, 818 F.2d 254, 260 (2d Cir. 1987); 4 MCCARTHY, *supra* note 18, § 23:6, at 30.

52. 4 MCCARTHY, *supra* note 18, § 23:7, at 39; *see also* *Mastercrafters Clock & Radio Co. v. Vacheron & Constantin-Le Coultre Watches, Inc.*, 221 F.2d 464, 466 (2d Cir. 1955) (finding likelihood of confusion where imitation ATMOS-marked clocks were likely to confuse visitors at purchasers’ homes, even though the purchasers likely knew the clocks were not genuine Atmos products).

53. 2 GILSON, *supra* note 44, § 5.19[2][a].

54. *Id.*

55. *Id.*; *see also* 15 U.S.C. § 1117(b) (Supp. 2008) (establishing the counterfeiting cause of action by referencing § 1117(a), which in turn incorporates the core infringement provisions of § 1114(1)(a), for registered marks, and § 1125(a)(1)(A), for unregistered marks, both of which center upon likelihood of confusion).

56. 2 GILSON, *supra* note 44, § 5.19[2][a].

establishes remedies for normal infringement claims, § 1117(b) provides for special remedies against a defendant who “intentionally [uses] a mark or designation, knowing such mark or designation is a counterfeit mark.”⁵⁷ Similarly, § 1117(c) provides for statutory damages “[i]n a case involving the use of a counterfeit mark.”⁵⁸

A counterfeiting claim under § 1117(b) and (c) requires everything that an infringement claim does⁵⁹ but also entails four additional requirements. First, the defendant’s mark must be *counterfeit*: “a spurious mark which is identical with, or substantially indistinguishable from, a registered mark.”⁶⁰ The Lanham Act’s legislative history defines *spurious* to mean “not genuine or authentic” but does not further explain the term’s significance.⁶¹ The requirement that the defendant’s mark be identical to or substantially indistinguishable from the plaintiff’s differs significantly from a mere infringement case, where the similarity between the marks is only one factor in evaluating likelihood of confusion.⁶² Second, the plaintiff’s mark must be registered on the U.S. Patent and Trademark Office’s principal register for use on the exact same goods or services as those to which the defendant applied the mark.⁶³ In contrast, an infringement claim can be brought for either registered or unregistered marks,⁶⁴ and the similarity between the plaintiff’s and defendant’s goods or services is merely a factor in determining infringement.⁶⁵ Third, to establish counterfeiting, the defendant must not have been authorized to use the plaintiff’s mark at the time of the manufacture or production of the goods or services in question.⁶⁶ Fourth,

57. 15 U.S.C. § 1117(b).

58. *Id.* § 1117(c).

59. *See supra* notes 53–54 and accompanying text.

60. 15 U.S.C. § 1127 (2006). Some clarification is helpful regarding the interplay between the Lanham Act’s substantive counterfeiting prohibitions in § 1117(b) and (c) and the definition of *counterfeit* in § 1127. In establishing remedies against counterfeiters, § 1117(b) and (c) both expressly incorporate the definition of *counterfeit mark* found in another Lanham Act provision, § 1116(d). *See id.* § 1117(b); *id.* § 1117(c) (both referring to a *counterfeit mark* “as defined in section 1116(d) of this title”). Section 1116(d), then, circularly defines a *counterfeit mark* as a “counterfeit of a mark.” *Id.* § 1116(d)(1)(B)(i). In turn, § 1127 ultimately defines *counterfeit* as quoted above: “a spurious mark which is identical with, or substantially indistinguishable from, a registered mark.” *Id.* § 1127. For further discussion regarding the Lanham Act’s statutory language and the *counterfeit* requirement, see 2 GILSON, *supra* note 44, § 5.19[3][b][i].

61. *Joint Statement on Trademark Counterfeiting Legislation*, 130 CONG. REC. H31,675 (1984).

62. *See supra* note 47.

63. 15 U.S.C. §§ 1116(d)(1)(B)(i), 1127; *see also* 2 GILSON, *supra* note 44, § 5.19[3][b][iv] (“In order for a claim of counterfeiting to prevail, the plaintiff or complainant’s trademark must be registered on the U.S. PTO’s principal register for use on the same goods to which the defendant applied the mark.”).

64. *Compare* 15 U.S.C. § 1114(a)(1) (providing a cause of action for registered marks), *with id.* § 1125(a)(1) (providing an essentially identical cause of action but without requiring registration).

65. *See supra* note 47.

66. 15 U.S.C. § 1116(d)(1)(B); *see also* 2 GILSON, *supra* note 44, § 5.19[3][b][v], [3][c][i] (“The term ‘counterfeit mark’ does not include a mark used when the manufacturer or producer of

counterfeiting generally arises only when a defendant acts with knowledge and intent.⁶⁷ Although unintentional counterfeiting is possible,⁶⁸ it is relatively rare⁶⁹ and has little relevance to the argument advanced by this Note.⁷⁰ Accordingly, unintentional counterfeiting is not considered in the discussion below, and this Note does not argue that unintentional or negligent holdover licensees should be subject to counterfeiting liability.

As a subset of trademark law, counterfeiting law promotes many of the same policy rationales: protecting consumers from confusion, minimizing consumer search costs, optimizing quality-based incentives for producers, and protecting producers' goodwill in their marks.⁷¹ Counterfeiting prohibitions, however, promote these policies in situations where the defendant's conduct especially threatens trademark protection, as the defendant's mark is extremely similar (or identical) to the plaintiff's and the goods or services are necessarily the same.⁷² The automatic presence of these two factors makes likelihood of confusion more probable in a counterfeiting case than an infringement case.⁷³ Further, because counterfeiting requires that the defendant's mark be identical to or substantially indistinguishable from the plaintiff's, it is far less likely that the defendant arrived at the mark by accident.⁷⁴

the good was, at the time of manufacture or production, authorized by the trademark owner to use the mark on that type of goods.”).

67. See 15 U.S.C. § 1117(b) (providing a cause of action where a defendant intentionally uses a mark he knows to be counterfeit); *id.* § 1117(c)(2) (establishing statutory damages for “willful” counterfeiting).

68. See *id.* § 1117(c)(1) (providing for statutory damages without mentioning any mental-state requirement, in contrast to § 1117(b) or (c)(2)); see also 2 GILSON, *supra* note 44, § 5.19[4][a][ii] (discussing the existence of unintentional counterfeiting).

69. Unintentional counterfeiting typically arises in only one specific factual scenario. See 2 GILSON, *supra* note 44, § 5.19[4][a][ii] (noting that unintentional counterfeiting primarily occurs when a retailer sells goods he does not know are counterfeit).

70. In the types of holdover-licensee cases with which this Note is concerned, the holdover licensee knows that he is continuing to use the former licensor's mark after termination of the license and has been asked to stop. These facts preclude any colorable argument that the holdover licensee is not acting intentionally and knowingly. See *Int'l Korwin Corp. v. Kowalczyk*, 855 F.2d 375, 380–81 (7th Cir. 1988) (holding that willfulness exists where a defendant is provided notice of his infringing conduct).

71. See 2 GILSON, *supra* note 44, § 5.19[1] (“Counterfeiting . . . thwarts . . . the trademark owner's ability to assure its customers of quality products [and services.]”); GINSBURG ET AL., *supra* note 20, at 958 (“[Counterfeiting] remedies exist to combat . . . the normal harms trademark owners can suffer, such as diverted sales, reputation loss and potential injury to mark distinctiveness and goodwill, and that potential purchasers can suffer, such as obtaining the wrong goods or increased search costs . . .”).

72. See *supra* notes 56, 60 and accompanying text.

73. While there is no logical necessity that likelihood of confusion will always be present in counterfeiting cases, the weight of these two factors makes confusion more likely than in an infringement case. See, e.g., *Polaroid Corp. v. Polarad Elecs. Corp.*, 287 F.2d 492, 495 (2d Cir. 1961) (establishing similarity between the marks and similarity between the underlying products or services as two factors for evaluating likelihood of confusion).

74. See *supra* notes 60–62 and accompanying text.

As counterfeiting is especially grievous conduct, the law provides several enhanced remedies beyond those available for mere infringement. First, special monetary damages are available to the plaintiff.⁷⁵ When a defendant intentionally uses a mark he knows to be counterfeit, the plaintiff is entitled to mandatory treble damages and attorney's fees, unless the court finds extenuating circumstances.⁷⁶ Alternatively, the plaintiff may elect to receive statutory damages of up to \$2 million per counterfeit mark.⁷⁷

A hypothetical example illustrates the potential for immensely divergent damages awards between infringement and counterfeiting cases. Suppose a plaintiff suffers \$100,000 of actual damages from a defendant's use of his mark. The plaintiff succeeds on an infringement claim but fails on counterfeiting. To start, injunctions are often the only remedy available in infringement cases;⁷⁸ without establishing counterfeiting, a plaintiff typically cannot expect any monetary damages whatsoever.⁷⁹ Assume for the sake of argument, though, that the hypothetical plaintiff here is entitled to \$100,000, even on the infringement-only claim. The plaintiff accrues \$25,000 of attorney's fees while litigating the case. Absent exceptional circumstances, a court cannot award attorney's fees for a mere infringement claim.⁸⁰ Although the court may adjust damages or profits upward, the decision to do so is entirely discretionary.⁸¹ Thus, the plaintiff's likely net gain is \$75,000: \$100,000 in actual damages minus \$25,000 owed to his attorney.

A successful counterfeiting claim on the same facts yields a much higher net gain. If the court finds that the defendant intentionally and knowingly counterfeited, the plaintiff will almost certainly be entitled to mandatory treble damages and attorney's fees, or \$300,000 plus \$25,000, for a net gain of \$300,000: \$325,000 minus \$25,000 owed to the attorney.⁸²

75. 15 U.S.C. § 1117(b)–(c) (Supp. 2008).

76. *Id.* § 1117(b). A finding of extenuating circumstances is very rare. Once the mental state requirements of knowledge and intent are established, the vast majority of cases will not entail the sort of extenuating circumstances necessary to negate an award of mandatory treble damages and attorney's fees. *Joint Statement on Trademark Counterfeiting Legislation*, 130 CONG. REC. H31,680 (1984).

77. 15 U.S.C. § 1117(c)(2). Section 1117(c)(2) actually refers to "willful" counterfeiting, rather than utilizing the intent-knowledge language of § 1117(b). *See id.* (allowing for an award of statutory damages "if the court finds that the use of the counterfeit mark was willful"). Nevertheless, there is no indication in the statute or its legislative history that the word *willful* was intended to mean something other than knowledge and intent, so this provision seemingly refers to the same mental state as § 1117(b). *See* N.A.S. Import, Corp. v. Chenson Enters., 968 F.2d 250, 252 (2d Cir. 1992) (defining *willful* in terms of knowledge and intent); 2 GILSON, *supra* note 44, § 5.19[4][a] (discussing the distinction between *willful* and *nonwillful* in terms of "intent").

78. *See* GINSBURG ET AL., *supra* note 20, at 917 (identifying injunctive relief as the usual remedy in trademark cases, given that actual damages are usually difficult to quantify and prove).

79. *Id.*

80. 15 U.S.C. § 1117(a).

81. *Id.*

82. *See id.* § 1117(b) (providing for mandatory treble damages and attorney's fees in cases of intentional and knowing counterfeiting, except in extenuating circumstances).

Alternatively, the plaintiff could elect to receive statutory damages, which would yield up to \$2 million per counterfeit mark.⁸³ Either way, the plaintiff's net gain would be substantially higher than the \$75,000 he would receive for the infringement-only claim, or perhaps even more likely, the \$25,000 net loss he would sustain if the court granted only an injunction against the infringement.

Finally, beyond the sizable increase in monetary remedies, counterfeiting claims provide two additional benefits. First, a plaintiff in a civil counterfeiting case can apply for ex parte seizure of the counterfeit marks and goods.⁸⁴ This allows the court to seize the counterfeit materials without providing notice to the defendant.⁸⁵ Second, unlike defendants in mere infringement cases, counterfeiters are subject to criminal penalties.⁸⁶ All things considered, the difference in liability between infringement and counterfeiting can be substantial.

III. Holdover Licensees: Avoiding Counterfeiting Liability

As the previous Part described, trademark-counterfeiting law serves the same core functions and policies as trademark law at large.⁸⁷ The Lanham Act and federal criminal law establish enhanced penalties for counterfeiting beyond those available in infringement cases—including civil remedies that may immensely affect what a plaintiff receives on a successful claim—because counterfeiting is a particularly egregious form of infringement.⁸⁸

Certain defendants, however, are avoiding the augmented penalties for counterfeiting, notwithstanding the alignment of their conduct with counterfeiting doctrine and policy. These defendants are holdover trademark licensees—entities formerly licensed to use another's marks who continue to use those marks without authorization after their license has terminated.⁸⁹ This Part describes more fully the holdover-licensee scenario and identifies the deficient precedents that have allowed holdover licensees to escape counterfeiting liability. In particular, this Part details two cases—including a key Sixth Circuit decision—in which holdover licensees have questionably defeated counterfeiting claims. This Part also describes one Ninth Circuit decision that reached the opposite result but notes the subsequent failure of that decision to gain widespread adoption. The next Part then advances the

83. *See id.* § 1117(c)(2) (setting the statutory maximum recovery at \$2 million per counterfeit mark where the defendant's use was willful).

84. *Id.* § 1116(d)(1)(A).

85. 2 GILSON, *supra* note 44, § 5.19[4][b][i].

86. *See* 18 U.S.C. § 2320 (2006) (establishing criminal sanctions against trafficking in counterfeit goods or services).

87. *See supra* notes 28–41, 71–74 and accompanying text.

88. *See supra* notes 71–86 and accompanying text.

89. *See* 4 MCCARTHY, *supra* note 18, § 25:31, at 78–79 (defining a *holdover* as a franchisee, dealer, or licensee who continues to use a mark after the license agreement has terminated and authorization to use the mark has thus lapsed).

central normative claim of this Note: courts should overcome the deficient precedents and recognize trademark counterfeiting as generally the most appropriate cause of action against holdover licensees.

It is well established that holdover licensees are liable for trademark infringement.⁹⁰ Nevertheless, certain courts refuse to go further by imposing counterfeiting liability.⁹¹ In one of the few circuit decisions considering the issue, the Sixth Circuit has expressly ruled that holdover licensees are not counterfeiters.⁹² In that case, *U.S. Structures, Inc. v. J.P. Structures, Inc.*,⁹³ the defendants entered into a franchise agreement allowing them to use the plaintiff's ARCHADECK mark in connection with a deck-construction business.⁹⁴ After six years of operation, the plaintiff terminated the franchise for the defendants' failure to pay required royalties.⁹⁵ Following termination, the defendants continued to use the ARCHADECK mark within their business and in an advertising program through which they received numerous customer referrals.⁹⁶ The Sixth Circuit affirmed the district court's finding of trademark infringement⁹⁷ but reversed an award of treble damages and attorney's fees under the Lanham Act's counterfeiting provisions:

We agree with defendants that [15 U.S.C.] § 1117(b) does not apply where, as in this case, a holdover franchisee continues to use the franchisor's original trademark after the franchise has been terminated. *Although the use of an original trademark is without authorization, it is not the use of a counterfeit mark.* Thus, the district court erred in awarding attorneys' fees pursuant to § 1117(b).⁹⁸

The court did not elaborate further on its reasoning.⁹⁹ It also failed to cite any authority in support of the proposition that holdover licensees are not counterfeiters.¹⁰⁰

Relying on the unreasoned precedent of *U.S. Structures*, other courts have similarly exonerated holdover licensees from counterfeiting claims.¹⁰¹

90. *Id.*

91. *See, e.g.*, *U.S. Structures, Inc. v. J.P. Structures, Inc.*, 130 F.3d 1185, 1192 (6th Cir. 1997); *Pennzoil-Quaker State Co. v. Smith*, No. 2:05cv1505, 2008 WL 4107159, at *20–22 (W.D. Pa. Sept. 2, 2008) (both absolving a holdover licensee from a counterfeiting claim).

92. *U.S. Structures*, 130 F.3d at 1192.

93. 130 F.3d 1185 (6th Cir. 1997).

94. *Id.* at 1187.

95. *Id.*

96. *Id.*

97. *Id.* at 1193.

98. *Id.* at 1192 (emphasis added).

99. *Id.*

100. *Id.*

101. *See, e.g.*, *Pennzoil-Quaker State Co. v. Smith*, No. 2:05cv1505, 2008 WL 4107159, at *22 (W.D. Pa. Sept. 2, 2008); *Motor City Bagels, L.L.C. v. Am. Bagel Co.*, 50 F. Supp. 2d 460, 489 (D. Md. 1999) (both citing *U.S. Structures*, 130 F.3d at 1192, to deny counterfeiting liability for a holdover licensee). On the other hand, one circuit court decision since *U.S. Structures* has decided the issue correctly, finding a holdover licensee liable for counterfeiting. *See Idaho Potato Comm'n*

In a recent case, *Pennzoil-Quaker State Co. v. Smith*,¹⁰² a federal district court cited *U.S. Structures* to deny counterfeiting liability for a holdover licensee whose conduct was considerably more egregious than the defendants' in *U.S. Structures*.¹⁰³ In *Pennzoil*, the defendant Smith owned Lube Pro, a retail oil-change center.¹⁰⁴ At his Lube Pro facility, Smith displayed various exterior and interior signage prominently bearing the PENNZOIL marks.¹⁰⁵ This signage included a massive road sign stating, "We Feature PENNZOIL products," and another large PENNZOIL sign on the front of the facility's exterior.¹⁰⁶ Smith had obtained the PENNZOIL signage from the facility's previous owner, who had signed an agreement with Pennzoil to become an authorized distributor.¹⁰⁷ Under that agreement, Pennzoil was required to loan genuine PENNZOIL signage to the facility for installation there.¹⁰⁸ The signage remained the property of Pennzoil, and the agreement required the facility owner to remove and return the signage if he ever discontinued featuring Pennzoil-brand products.¹⁰⁹

After Smith's purchase of the Lube Pro facility, Pennzoil contacted Smith to request that he sign a contract, similar to the one the previous owner had signed, to become an authorized Pennzoil distributor.¹¹⁰ Smith declined, believing that Pennzoil charged too much for its bulk oil.¹¹¹ Despite his refusal to sign the agreement, however, Smith did not take down the PENNZOIL signage.¹¹²

Yet rather than "featuring" Pennzoil products, Smith sold very little: 95% of his oil came from bulk containers, which he never purchased from Pennzoil.¹¹³ In 2005, Smith sold approximately 5,000 gallons of oil, only 100 to 150 of which were Pennzoil products.¹¹⁴ Smith performed oil changes

v. G & T Terminal Packaging, Inc., 425 F.3d 708, 720–22 (9th Cir. 2005) (affirming a counterfeiting claim against a holdover licensee who continued to use a certification mark after expiration of the license). Still, that lone decision does not absolve the need, as this Note argues, for other courts to distance themselves from *U.S. Structures* and its progeny. Indeed, at least one court has already distinguished *Idaho Potato* on relatively dubious grounds in order to follow *U.S. Structures*' perplexing rule. See *Pennzoil*, 2008 WL 4107159, at *21 & n.33 (distinguishing *Idaho Potato* on the grounds that it concerned a certification mark, not a trademark or service mark, but failing to connect that distinction to the issue of why holdover licensees should not be liable for counterfeiting).

102. No. 2:05cv1505, 2008 WL 4107159 (W.D. Pa. Sept. 2, 2008).

103. See *id.* at *22 (referring to *U.S. Structures* as "instructive" despite its factual differences).

104. *Id.* at *5.

105. *Id.*

106. *Id.*

107. *Id.* at *5–6.

108. *Id.* at *5.

109. *Id.* at *6.

110. *Id.*

111. *Id.*

112. *Id.*

113. *Id.* at *7.

114. *Id.*

with Pennzoil only when the customer specifically requested that he do so.¹¹⁵ Such requests occurred less than once a week, possibly as infrequently as once a month.¹¹⁶ Smith estimated that less than 1% of his customers requested a specific brand of oil.¹¹⁷ In short, despite not being an authorized Pennzoil distributor and despite selling only a miniscule amount of Pennzoil products (and only when specifically requested), Smith continued to display the prominent PENNZOIL signage at his Lube Pro location.¹¹⁸

Ignoring this confluence of culpable behavior, the district court rejected Pennzoil's trademark-counterfeiting claim.¹¹⁹ Reasoning that Smith's use of the PENNZOIL signage was not use of a counterfeit mark, the court held that Pennzoil could not establish an essential element of its claim.¹²⁰ The court asserted that the term *counterfeit* in the Lanham Act refers to the defendant's marks themselves, not the underlying goods or services.¹²¹ The PENNZOIL marks at the Lube Pro were genuine—loaned by Pennzoil itself—not counterfeits or copies.¹²² Thus, the court evidently found it irrelevant that the overwhelming majority of Smith's oil-change products were not Pennzoil brand. Further, the court held that even if *counterfeit* in the Lanham Act could potentially refer to the defendant's underlying goods or services, Smith had not “attached” the genuine PENNZOIL marks to his overwhelmingly non-Pennzoil products¹²³ (even though one sign stated, “We Feature PENNZOIL products,” at a facility that sold only 5% or less Pennzoil).¹²⁴ The court attempted to support its holding by citing *U.S. Structures* for the bare proposition that holdover licensees are not counterfeiters.¹²⁵

In contrast, one circuit has rejected *U.S. Structures*, affirming counterfeiting liability against a holdover licensee. In *Idaho Potato Commission v. G&T Terminal Packaging, Inc.*,¹²⁶ the defendant continued to use the IDAHO and GROWN IN IDAHO certification marks on bags of potatoes after his license to do so had expired.¹²⁷ Upholding statutory damages for counterfeiting under § 1117(c),¹²⁸ the Ninth Circuit prudently

115. *Id.* at *8.

116. *Id.*

117. *Id.*

118. *Id.* at *5–8.

119. *Id.* at *21–22.

120. *Id.* at *21; *see also supra* notes 56–58 and accompanying text.

121. *Pennzoil*, 2008 WL 4107159, at *21.

122. *Id.*

123. *Id.*

124. *Id.* at *5, *7 (emphasis added).

125. *Id.* at *22.

126. 425 F.3d 708 (9th Cir. 2005).

127. *Id.* at 711–13.

128. *See supra* note 75 and accompanying text.

rejected *U.S. Structures*' rule that holdover licensees are not counterfeiters.¹²⁹ Unfortunately, like the Sixth Circuit in *U.S. Structures*, the Ninth Circuit did little to explain its holding.¹³⁰ Although the Ninth Circuit seemed to implicitly reject *U.S. Structures*, it did not confront the Sixth Circuit's rule head on.¹³¹ Perhaps for those reasons, the Ninth Circuit's decision has not been universally followed: *Pennzoil*, decided three years after *Idaho Potato*, instead chose to adopt the *U.S. Structures* rule.¹³²

While *Idaho Potato* lacks a particularly compelling discussion of the counterfeiting issue, its result finds substantial support in trademark doctrine and policy.¹³³ *U.S. Structures*, *Pennzoil*, and similar cases,¹³⁴ on the other hand, concede an unjust victory to holdover-licensee defendants. This victory is significant. Even when a holdover licensee remains liable for infringement, exculpation on a counterfeiting claim provides a tremendous boon because the defendant avoids the enhanced counterfeiting penalties.¹³⁵ The next Part argues that holdover licensees generally should not enjoy this windfall. Courts should reject *U.S. Structures* and regularly impose counterfeiting liability on holdover licensees.

IV. Holdover Licensees Are Counterfeiters

The previous Part described how current law allows holdover licensees to elude counterfeiting liability. This Part argues that courts should reject the deficient precedent of *U.S. Structures* (and the cases following it) to adjudge holdover licensees as counterfeiters. Most notably, this Part suggests that holdover licensees are counterfeiters because they purposefully use the former licensor's actual marks to generate false associations with the former licensor.

In advancing the argument against *U.S. Structures* and its progeny, this Part will take a two-pronged approach. First, this Part will attempt to decipher the rationale behind the *U.S. Structures* rule, advancing three potential explanations for its undeveloped holding. Then, this Part will reveal why all three explanations should ultimately be rejected as unpersuasive arguments

129. See *Idaho Potato*, 425 F.3d at 721 (citing the conclusion of *U.S. Structures, Inc. v. J.P. Structures, Inc.*, 130 F.3d 1185, 1192 (6th Cir. 1997), as contradictory authority on the counterfeiting issue).

130. See *id.* at 720–22 (analyzing the counterfeiting issue in terms of likelihood of confusion and quality control, but failing to substantially discuss counterfeiting specifics).

131. See *id.* at 721 (citing *U.S. Structures*, 130 F.3d at 1192, as contradictory authority on the counterfeiting issue, but failing to explain why *U.S. Structures* was not followed).

132. *Pennzoil-Quaker State Co. v. Smith*, No. 2:05cv1505, 2008 WL 4107159, at *22 (W.D. Pa. Sept. 2, 2008).

133. See *infra* subpart IV(B).

134. See, e.g., *Motor City Bagels, L.L.C. v. Am. Bagel Co.*, 50 F. Supp. 2d 460, 489 (D. Md. 1999) (denying counterfeiting liability for a holdover licensee without performing any analysis of the issue beyond a cursory citation to *U.S. Structures*, 130 F.3d at 1192).

135. See *supra* notes 75–86 and accompanying text.

for the case's result. In doing so, this Part will show that, even under the most sympathetic readings possible, decisions denying counterfeiting liability for holdover licensees are generally fundamentally inconsistent with counterfeiting doctrine, trademark law policy, and the weight of better reasoned circuit authority.

A. *Attempting to Decipher U.S. Structures*

The *U.S. Structures* opinion is puzzling. Although its rule is clear—holdover licensees are not counterfeiters—the court did not even briefly explain its reasoning.¹³⁶ Consequently, any inquiry into the court's rationale must involve some speculation. With that in mind, one could hypothesize at least three explanations potentially justifying *U.S. Structures*.

1. *Narrow Interpretation of "Spurious."*—The first explanation, and likely the most viable, is that *U.S. Structures* reflects a narrow interpretation of the term *spurious* as used in the Lanham Act. As discussed above, one essential element of a counterfeiting claim is that the defendant's mark be counterfeit: "a spurious mark which is identical with, or substantially indistinguishable from, a registered mark."¹³⁷ The Lanham Act's legislative history defines *spurious* to mean "not genuine or authentic" but does not further clarify the term's significance.¹³⁸ In denying the plaintiff's counterfeiting claim, the *U.S. Structures* court may have believed that the defendants' ARCHADECK marks were not spurious and therefore were not counterfeit.

In reaching this conclusion, the court may have applied either of two narrow interpretations of *spurious*. First, if the defendants' ARCHADECK marks were physically genuine—i.e., the physical marks had been provided by the plaintiff itself at the outset of the license—the court may have believed that the marks inherently could not be spurious. This was likely the driving rationale in *Pennzoil*, where Pennzoil itself had loaned physical signage to Lube Pro.¹³⁹ Second, even if the defendants' physical ARCHADECK marks had not been provided by the plaintiff, the court may have nevertheless felt that the marks were not spurious because they had originally, under the former license, reflected a legitimate association with the plaintiff. Because of a general lack of precision throughout the opinion,

136. See *U.S. Structures*, 130 F.3d at 1192 (holding, without elaboration, that unauthorized continued use of a mark by a former licensee is not trademark counterfeiting).

137. 15 U.S.C. § 1127 (2006).

138. *Joint Statement on Trademark Counterfeiting Legislation*, 130 CONG. REC. H31,675 (1984).

139. *Pennzoil-Quaker State Co. v. Smith*, No. 2:05cv1505, 2008 WL 4107159, at *5–6 (W.D. Pa. Sept. 2, 2008).

it is unclear which (if either) of these two possibilities—physical genuineness or original legitimacy—informed *U.S. Structures*.¹⁴⁰

In its exceptionally brief treatment of the counterfeiting issue, *U.S. Structures*' language supports the possibility that the court applied a narrow interpretation of *spurious*. To dispense with the plaintiff's counterfeiting claim, the court held, "Although [the defendants' holdover use] of an original trademark is without authorization, *it is not the use of a counterfeit mark*."¹⁴¹ Because the Lanham Act defines *counterfeit mark* with reference to the key term *spurious*,¹⁴² this language suggests that the court believed the defendants' ARCHADECK marks were not spurious either because of physical genuineness or original legitimacy. Further, although decided eleven years after *U.S. Structures*, a narrow interpretation of *spurious* certainly governed in *Pennzoil*, where the court held that the term *counterfeit* "refers to the mark itself, not the nature of the goods or services."¹⁴³ In other words, the *Pennzoil* court narrowly interpreted *spurious* to hold that a mark is counterfeit only when the mark itself is inauthentic, regardless of the authenticity of the underlying goods or services.¹⁴⁴

2. *Authorization*.—The second explanation for *U.S. Structures* is rooted in another required element of a trademark-counterfeiting claim: lack of authorization. To establish counterfeiting, a plaintiff must show that the defendant was not authorized to use the mark at the time of the manufacture or production of the goods or services in question.¹⁴⁵ The *U.S. Structures* court may have concluded that the defendants in that case were not counterfeiters because they had previously been authorized to use the ARCHADECK mark under the license agreement.

3. *Judicial Pragmatism*.—The third explanation is that *U.S. Structures* was simply the result of judicial pragmatism. As Justice Oliver Wendell Holmes once proclaimed, "[H]ard cases make bad law."¹⁴⁶ Although the *U.S. Structures* defendants admittedly benefitted from their holdover use of

140. See *U.S. Structures*, 130 F.3d at 1187–88 (describing the facts at issue without mentioning where the defendants' ARCHADECK marks originated); *id.* at 1192 (failing to provide any rationale in ruling that holdover use of a mark does not give rise to a counterfeiting claim).

141. *Id.* at 1192 (emphasis added).

142. See 15 U.S.C. § 1117(b)–(c) (Supp. 2008) (referencing § 1116(d), which defines a *counterfeit mark* as a "counterfeit of a mark" registered with the U.S. Patent and Trademark Office or as "spurious"); *id.* § 1127 (2006) (defining *counterfeit*, as utilized in § 1116(d), as a "spurious mark").

143. *Pennzoil*, 2008 WL 4107159, at *21.

144. *Id.*

145. 15 U.S.C. § 1116(d)(1)(B) (2006); 2 GILSON, *supra* note 44, § 5.19[3][b][v], [3][c][i].

146. *N. Sec. Co. v. United States*, 193 U.S. 197, 400 (1904) (Holmes, J., dissenting).

the ARCHADECK mark,¹⁴⁷ their conduct was surely not the most egregious form of counterfeiting imaginable. Perhaps the *U.S. Structures* court did not wish to impose the weighty counterfeiting penalties on defendants whose conduct the court believed did not morally align with such hefty consequences.

B. Rejecting the Explanations for U.S. Structures

1. Narrow Interpretation of “Spurious.”—The first explanation potentially supporting *U.S. Structures*—a narrow interpretation of the term *spurious*—is deficient for several reasons. To start, a narrow interpretation of *spurious*, which would exclude from the term’s gambit any physically genuine or originally legitimate mark, defies common sense. As a matter of plain intuition, it is considerably more egregious to sell inauthentic products or services under the guise of a physically genuine or originally legitimate mark than to sell the same under an inauthentic replica mark. An inauthentic replica mark at least gives consumers some chance, however small, of detecting the mark’s lack of authenticity. When a physically genuine or originally legitimate mark is used, on the other hand, the chance of detection necessarily drops to zero—there is no inauthenticity in the mark to detect. Still, one need not stop at intuition when arguing against a narrow interpretation of *spurious*. Beyond simply eschewing practical sensibilities, a narrow interpretation of *spurious* defies several strands of trademark law itself.

First, it is inconsistent with well-established circuit precedent to hold that a mark is not spurious, and therefore not counterfeit, simply because it is physically genuine or was originally legitimate at some prior point.¹⁴⁸ Similarly, the *Pennzoil* holding, which couched its counterfeiting discussion solely in terms of the marks’ physical authenticity and paid no regard to the inauthentic nature of the attached goods and services,¹⁴⁹ defies reasoning found in many circuit decisions.

In terms of on-point authority contravening *U.S. Structures* and *Pennzoil*, the Ninth Circuit in *Idaho Potato* rejected a narrow interpretation of *spurious*.¹⁵⁰ By affirming counterfeiting liability against the holdover licensee in that case, the Ninth Circuit established that a genuine, originally

147. See *U.S. Structures, Inc. v. J.P. Structures, Inc.*, 130 F.3d 1185, 1187 (6th Cir. 1997) (noting that the defendants received numerous customer referrals through an advertising program in which they continued to use the ARCHADECK mark after termination of the license).

148. See *infra* notes 150–157 and accompanying text.

149. See *Pennzoil*, 2008 WL 4107159, at *21 (“The plain language of the statute indicates that the term ‘counterfeit’ refers to the mark itself, not the nature of the goods or services associated with the mark . . .”).

150. See *supra* notes 126–31 and accompanying text.

legitimate mark can still be spurious for purposes of the counterfeiting statute.¹⁵¹

Other circuit decisions in counterfeiting cases lend substantial support to the Ninth Circuit's approach, refuting the viability of interpreting *spurious* narrowly. Although these other decisions do not specifically address the holdover-licensee context—which is exactly why *U.S. Structures*' problematic rule still carries weight¹⁵²—their rules and rationales inform counterfeiting law as a whole, including holdover-licensee cases. For instance, some circuits expressly hold that a genuine mark becomes spurious when attached to inauthentic products or services. Thus, in *United States v. Petrosian*,¹⁵³ the Ninth Circuit held that genuine COCA-COLA marks on genuine bottles became spurious—and therefore counterfeit—when the defendants filled the bottles with a beverage that was not Coca-Cola.¹⁵⁴ The marks were rendered spurious, despite being technically genuine, because they “falsely indicated that Coca-Cola was the source of the beverage in the bottles and falsely identified the beverage in the bottles as Coca-Cola.”¹⁵⁵ Following the same logic, the Fifth Circuit held in *Rolex Watch USA, Inc. v. Meece*¹⁵⁶ that genuine ROLEX marks could be deemed spurious when placed on watches partially containing non-Rolex parts.¹⁵⁷ At least two circuits have similarly noted that, although *counterfeit* literally implies an unauthorized reproduction or duplication, counterfeiting actually does not require the defendant to have physically duplicated the plaintiff's mark—it is irrelevant whether the defendant uses the plaintiff's genuine mark or a replica.¹⁵⁸ These precedents, if applied in *U.S. Structures* and *Pennzoil*, would have defeated any argument that the holdover licensees' marks were not spurious because of physical genuineness or original legitimacy. Once the licenses were terminated and the underlying goods and services became unauthorized, the attached marks would have been rendered spurious, regardless of their physical genuineness or then-lapsed original legitimacy.

151. See *supra* notes 126–31 and accompanying text. *Idaho Potato* may also stand for the proposition that a physically genuine mark can still be spurious, but it is unclear from the opinion whether the IDAHO and GROWN IN IDAHO marks were physically provided by the plaintiff. See *Idaho Potato Comm'n v. G & T Terminal Packaging, Inc.*, 425 F.3d 708, 711 (9th Cir. 2005) (reciting that the licensee was licensed to use the plaintiff's marks without discussing the source of the physical marks used by the licensee).

152. See, e.g., *Pennzoil*, 2008 WL 4107159, at *21 (electing to follow *U.S. Structures*).

153. 126 F.3d 1232 (9th Cir. 1997).

154. *Id.* at 1234.

155. *Id.*

156. 158 F.3d 816 (5th Cir. 1998).

157. *Id.* at 826–27.

158. See *Westinghouse Elec. Corp. v. Gen. Circuit Breaker & Elec. Supply, Inc.*, 106 F.3d 894, 899–900 (9th Cir. 1997); *Gen. Elec. Co. v. Speicher*, 877 F.2d 531, 534 (7th Cir. 1989) (both concluding that when a defendant attaches a plaintiff's mark to inauthentic goods, whether the mark is genuine or an unauthorized reproduction has no legal relevance).

More broadly, the circuit decisions rejecting a narrow interpretation of *spurious* reveal the overarching trademark law principles that invalidate such an interpretation. The value of a trademark lies not in its physical incarnation or any since-lapsed relationship; rather, a trademark's value lies in the connection it *presently* represents to a particular producer of goods or services.¹⁵⁹ Accordingly, a mark should rightfully be regarded as genuine when, at the time and in the context of the allegedly unlawful use, it represents a legitimate association with the mark's owner. If, as in the holdover-licensee scenario, the mark owner no longer bears any connection to the products or services sold under the mark, the mark cannot reasonably be regarded as genuine in any meaningful sense of the word. The mark has become nothing more than a genuine Coca-Cola bottle that now contains a disappointingly flavorless discount-brand cola.¹⁶⁰ Even if the mark is physically genuine, it is not genuine in the sense relevant to trademark law. It is spurious.

In addition to defying well-established circuit precedent, a narrow interpretation of *spurious* also defeats the functions and policy rationales underlying trademark-counterfeiting law. Source identification, the fundamental purpose of a trademark,¹⁶¹ is greatly impeded when a holdover licensee continues to use a physically genuine or originally legitimate mark to advertise or sell now-inauthentic products and services. Further, regardless of whether a mark is physically genuine, originally legitimate, or merely an imitation created illicitly by the counterfeiter, the policies underlying counterfeiting prohibitions are equally pervasive.¹⁶² In fact, a physically genuine or originally legitimate mark is actually more likely to create consumer confusion than an unauthorized replica because "the imitation is not merely colorable, but perfect."¹⁶³ In other words, attachment of genuine marks to inauthentic products and services—the mainstay of the holdover licensee¹⁶⁴—is particularly conducive to consumer confusion

159. See, e.g., *Rolex*, 158 F.3d at 826 (holding that ROLEX marks were potentially rendered spurious because they did not represent watches made of 100% genuine Rolex parts); *Petrosian*, 126 F.3d at 1234 (finding genuine COCA-COLA marks spurious where they no longer bore any connection to Coca-Cola because the marks had been affixed to an imitation beverage); cf. *El Greco Leather Prods. Co. v. Shoe World, Inc.*, 806 F.2d 392, 395 (2d Cir. 1986) (holding that even where certain physical goods were originally authorized by a trademark owner, those goods may lose their genuine nature if not inspected for quality before they are sold to ensure they accurately represent a genuine connection to the mark owner).

160. Cf. *Petrosian*, 126 F.3d at 1234 (holding that bottles bearing genuine COCA-COLA marks became counterfeit when filled with a non-Coca-Cola imitation beverage).

161. See *supra* notes 18–21 and accompanying text.

162. See *Speicher*, 877 F.2d at 534 (finding no difference, for counterfeiting-prohibition purposes, between an infringing mark made by the mark owner and an infringing mark made by the infringer himself).

163. *Id.*

164. See, e.g., *U.S. Structures, Inc. v. J.P. Structures, Inc.*, 130 F.3d 1185, 1187 (6th Cir. 1997) (describing the defendants' original use of the ARCHADECK marks under the license agreement, which represented a legitimate connection to the plaintiff); *Pennzoil-Quaker State Co. v. Smith*, No.

precisely because the mark is, or was at some point, genuine: it is perfectly identical to the mark used by the mark owner itself. This heightened potential for confusion detrimentally affects the various objectives of trademark policy, including protecting consumers,¹⁶⁵ reducing consumer search costs,¹⁶⁶ providing optimal incentives for producers,¹⁶⁷ and protecting producers' goodwill.¹⁶⁸

Lastly, interpreting *spurious* narrowly in the holdover-licensee context puts the mark owner in a highly precarious position. As with a typical infringement case, the potential for consumer confusion in the holdover-licensee scenario creates a risk that the mark owner will be attributed as the source of the holdover licensee's products or services.¹⁶⁹ In the holdover-licensee context, however, this risk is particularly dangerous. The holdover licensee's marks are identical to the ones used by the mark owner itself.¹⁷⁰ Consequently, there is an especially strong chance of consumer confusion, leading to an increased risk that the holdover licensee's commercial shortcomings will be attributed to the mark owner.¹⁷¹ But because the license has terminated, the mark owner has already lost all ability to control the quality of the holdover licensee's products or services—a control so critical to trademark law that it is actually *required* to maintain a valid license in the first place.¹⁷² As a result, the mark owner faces a significant chance of being negatively associated with product or service deficiencies over which it has absolutely no control. For example, a customer at an oil-change center prominently bearing genuine “We Feature PENNZOIL” signage may attribute a subsequent car problem to Pennzoil, even though the products

2:05cv1505, 2008 WL 4107159, at *5–7 (W.D. Pa. Sept. 2, 2008) (noting that the defendant Smith used physically genuine signage loaned by Pennzoil itself).

165. See *supra* notes 28–29 and accompanying text.

166. See *supra* notes 30–32 and accompanying text.

167. See *supra* notes 33–39 and accompanying text.

168. See *supra* notes 40–41 and accompanying text.

169. Cf. 15 U.S.C. § 1125(a)(1)(A) (2006) (creating a cause of action for infringement where the defendant's use is likely to cause confusion “as to the origin” of the defendant's goods or services).

170. See, e.g., *Pennzoil-Quaker State Co. v. Smith*, No. 2:05cv1505, 2008 WL 4107159, at *5–7 (W.D. Pa. Sept. 2, 2008) (describing the defendant Smith's use of PENNZOIL signage provided directly by Pennzoil itself).

171. See *Burger King Corp. v. Mason*, 710 F.2d 1480, 1492–93 (11th Cir. 1983) (“Common sense compels the conclusion that a strong risk of consumer confusion arises when a terminated franchisee continues to use the former franchisor's trademarks. A patron of a restaurant adorned with the Burger King trademarks undoubtedly would believe that [Burger King] endorses the operation of the restaurant. . . . Any shortcomings of the franchise therefore would be attributed to [Burger King].”).

172. A licensor has an affirmative duty to monitor and control the quality of goods and services offered by licensees under the licensor's marks. 3 MCCARTHY, *supra* note 18, § 18:48, at 101–04. A license agreement that does not control quality in this way is known as a “naked license” and is invalid. *Id.* This rule promotes the central trademark function of source identification: without quality control standards, the licensee's use of the marks represents a false connection to the licensor, and the licensee's goods or services offered under the mark are not truly genuine. *Id.*

provided were not Pennzoil-brand and Pennzoil could not enforce its quality-control standards.

2. *Authorization.*—The second possible explanation for *U.S. Structures*, that the court believed the plaintiff had not established the authorization element of a counterfeiting claim, is equally unpersuasive. Although it is true that an essential element of counterfeiting is that the defendant must not have been authorized to use the plaintiff's marks at the time of the manufacture or production in question,¹⁷³ that provision does not apply to holdover licensees.¹⁷⁴ Indeed, the relevant statutory provision was purposely revised during the drafting process to avoid creating a grace period for holdover licensees.¹⁷⁵ Rather, the authorization element was meant to target a different situation, known as the “overrun” scenario, where a *current* licensee produces more goods or services than the license permits and then eventually sells those goods or services.¹⁷⁶ For example, the authorization element would preclude counterfeiting liability for a manufacturer who is licensed to make 500,000 umbrellas bearing a licensor's marks but instead manufactures and sells 1 million.¹⁷⁷ This protection against counterfeiting claims extends to sales occurring after the license has terminated, but only when the overruns were actually produced while the license was still valid.¹⁷⁸

By definition, then, an overrun producer is distinct from the prototypical holdover licensee. An overrun producer is merely selling off a finite quantity of extra products or services, all of which were produced during a period of authorization.¹⁷⁹ In contrast, holdover licensees in cases like *U.S. Structures* and *Pennzoil* do more than simply liquidate a fixed, limited stock. The holdover-licensee defendant in *Pennzoil*, for example, was not merely selling off some finite overrun inventory of Pennzoil lubricants. Rather, he continued to use PENNZOIL signage, without a license, to sell and advertise overwhelmingly non-Pennzoil products and services.¹⁸⁰ Given this critical distinction, the authorization element cannot sensibly be used to absolve holdover licensees from counterfeiting claims in cases like *U.S. Structures* and *Pennzoil*.

173. See *supra* note 66 and accompanying text.

174. *Joint Statement on Trademark Counterfeiting Legislation*, 130 CONG. REC. H31,676–H31,677 (1984).

175. *Id.*

176. *Id.*

177. *Id.*

178. *Id.*

179. *Id.*

180. See *Pennzoil-Quaker State Co. v. Smith*, No. 2:05cv1505, 2008 WL 4107159, at *6–8 (W.D. Pa. Sept. 2, 2008) (explaining that the defendant Smith continued to use PENNZOIL signage without a license, including a sign stating, “We Feature PENNZOIL products,” despite selling only 5% or less Pennzoil).

3. *Judicial Pragmatism.*—Finally, couching *U.S. Structures* in terms of judicial pragmatism is considerably unsettling. Setting aside the interminable clash between formalism and realism,¹⁸¹ it is troubling to envision a judge who uses supposedly common-sense principles to decide cases without even mentioning those principles. While there may exist judges who “select[] the result that best comports with personal values and then enlist[], sometimes brutally, whatever doctrines arguably support the result,”¹⁸² those judges’ decisions, even the most radical among them, presumably have a modicum of support in sound legal doctrine, policy, or at the very least, common sensibilities. Yet if such a basis existed for the *U.S. Structures* rule that holdover licensees are not counterfeiters, the court neglected to articulate that basis.¹⁸³

If, as hypothesized above,¹⁸⁴ the *U.S. Structures* court simply did not wish to levy the enhanced counterfeiting penalties on the defendants in that case, the court could have made an attempt to ground its decision in counterfeiting doctrine. For instance, the court could have construed the facts to find “extenuating circumstances,” which would have allowed the imposition of counterfeiting liability in name, but without the penalties that essentially distinguish counterfeiting from infringement.¹⁸⁵ Although this application would have pushed the envelope of the extenuating-circumstances exception,¹⁸⁶ it likely would not have been any less reasonable than the undeveloped holding actually written. In the end, rather than carefully considering the issue and weighing the relevant authorities, doctrines, and policies, the court in *U.S. Structures* did not undertake any significant effort to support its decision on the counterfeiting issue.

V. Correcting *U.S. Structures* and Its Progeny

The defective rule of *U.S. Structures* should be rejected. Future holdover-licensee cases outside the Sixth Circuit need not emulate *Pennzoil* by following *U.S. Structures*’ prohibitive rule. A number of mechanisms could be used to overcome the troublesome decision, depending on which explanation for the court’s rationale is most accurate—a narrow

181. See, e.g., Brian Leiter, *Rethinking Legal Realism: Toward a Naturalized Jurisprudence*, 76 TEXAS L. REV. 267, 277–78 (1997) (contrasting common perceptions of legal formalists and legal realists).

182. Jon O. Newman, *Between Legal Realism and Neutral Principles: The Legitimacy of Institutional Values*, 72 CAL. L. REV. 200, 203 (1984).

183. See *U.S. Structures, Inc. v. J.P. Structures, Inc.*, 130 F.3d 1185, 1192 (6th Cir. 1997) (ruling that holdover licensees are not counterfeiters but without providing any reasoning or citing to any authority in support of that proposition).

184. See *supra* section IV(A)(3).

185. See 15 U.S.C. § 1117(b) (Supp. 2008) (providing enhanced civil remedies for intentional and knowing counterfeiting, except where a court finds extenuating circumstances).

186. *Joint Statement on Trademark Counterfeiting Legislation*, 130 CONG. REC. H31,680 (1984).

interpretation of *spurious*, authorization, or judicial pragmatism.¹⁸⁷ This Part assumes the narrow-interpretation explanation, given its (albeit scant) support in the language of *U.S. Structures*,¹⁸⁸ as well as the subsequent holding of *Pennzoil*, which implicitly applied a narrow interpretation of *spurious*.¹⁸⁹ In assuming a narrow interpretation of *spurious* as the basis for *U.S. Structures*, this Part suggests two solutions, one legislative and one judicial, for reversing course on the flawed proclamation that holdover licensees are not counterfeiters.

The first solution is for Congress to redraft the Lanham Act's ambiguous definition of *counterfeit*. If courts are disregarding the weight of authority and errantly interpreting the requirement that a counterfeit be spurious to mean that the mark must literally be a physically inauthentic replica with no legitimate original association,¹⁹⁰ Congress could redraft the statute to better align with trademark policy. For example, Congress could alter the definition of *counterfeit* to read: "A 'counterfeit' is a spurious mark that is identical to or substantially indistinguishable from, a registered mark. A mark is 'spurious' if it is a physically inauthentic replica, or if it is an authentic mark used in connection with inauthentic products or services."¹⁹¹

The second solution is more feasible¹⁹² but also more complex: courts should engage in a more nuanced interpretation of the term *spurious*. Under well-established principles of statutory interpretation, courts should first rely on a statute's literal language if that language is plain and unambiguous.¹⁹³ If the statutory language is ambiguous, courts may then consider the legislature's intent, as derived from extrinsic materials like legislative history.¹⁹⁴ Finally, if an inquiry into legislative intent does not reveal a clear interpretation, courts should look to the policies and purposes underlying the statute.¹⁹⁵

The Lanham Act requires that a counterfeit mark be "spurious."¹⁹⁶ This language is ambiguous. Even given additional guidance from the Lanham

187. See *supra* subpart IV(A).

188. See *supra* notes 137–41 and accompanying text.

189. See *supra* notes 143–44 and accompanying text.

190. See *supra* notes 139–44, 148–52 and accompanying text.

191. Cf. 15 U.S.C. § 1127 (2006) (providing the current statutory definition of *counterfeit*).

192. See Patrick M. Garry, *The Unannounced Revolution: How the Court Has Indirectly Effected a Shift in the Separation of Powers*, 57 ALA. L. REV. 689, 696 (2006) (acknowledging the difficulty in acting legislatively in a system of checks and balances).

193. *Caminetti v. United States*, 242 U.S. 470, 485 (1917).

194. See *Exxon Mobil Corp. v. Allapattah Servs., Inc.*, 545 U.S. 546, 568 (2005) ("Extrinsic materials have a role in statutory interpretation only to the extent they shed a reliable light on the enacting Legislature's understanding of otherwise ambiguous terms.").

195. See *Negusie v. Holder*, 129 S. Ct. 1159, 1171 (2009) (Stevens, J., concurring in part and dissenting in part) ("[S]tatutory interpretation is a multifaceted enterprise, ranging from a precise construction of statutory language to a determination of what policy best effectuates statutory objectives.").

196. 15 U.S.C. § 1127.

Act's legislative history, which explains that *spurious* means "not genuine or authentic,"¹⁹⁷ courts still face significant uncertainty. Perhaps *spurious* refers to a mark that is physically inauthentic and lacks any original legitimacy, an interpretation assumed here to be the driving force behind *U.S. Structures*. Yet this is not the only possible interpretation. *Spurious* could also reflect the pervasive trademark law principle of source identification—a spurious mark is one that misrepresents source by suggesting an inauthentic connection to a particular producer of goods or services. This latter interpretation of *spurious* finds substantial support in the circuit authority holding that a genuine mark becomes spurious when attached to inauthentic products or services.¹⁹⁸

Due to these conflicting interpretations, courts must look to trademark policy to determine unequivocally what is a spurious mark under the ambiguous text of the Lanham Act. Specifically, courts' interpretations should be couched in the policy objectives of protecting consumers from confusion, lowering consumer search costs, optimizing quality-based incentives for producers, and protecting producers' goodwill in their marks.¹⁹⁹

With those policies in mind, interpreting *spurious* narrowly, such as to include only physically inauthentic marks with no original legitimacy, is inadequate. Even more so than an inauthentic replica mark, improper use of a physically genuine or originally legitimate mark is highly conducive to consumer confusion.²⁰⁰ This heightened likelihood of confusion then compromises other trademark policy objectives: when consumers are confused, they cannot rely on the search-cost-economizing function of trademarks; when consumers have trouble distinguishing between products or services, producers have less incentive to provide high- and consistent-quality products or services, as their efforts may be attributed to another producer; if consumer confusion is present, marks cannot clearly indicate source, so producers have less incentive to develop goodwill and more incentive to simply infringe others' marks.²⁰¹

Accordingly, given the Lanham Act's underlying policies, the superior interpretation of *spurious* is the one suggested by the weight of circuit authority:²⁰² a spurious mark is one that falsely represents a connection to a producer because it attaches to goods or services bearing no relationship to that producer, even if the mark itself is physically genuine or was at some prior point originally legitimate.

197. *Joint Statement on Trademark Counterfeiting Legislation*, 130 CONG. REC. H31,675 (1984).

198. *See supra* notes 153–58 and accompanying text.

199. *See supra* notes 28–41 and accompanying text.

200. *See supra* notes 159–64 and accompanying text.

201. *See supra* notes 28–41 and accompanying text.

202. *See supra* notes 149–61.

VI. Conclusion

Holdover trademark licensees are unjustly avoiding liability for trademark counterfeiting.²⁰³ These defendants continue to use genuine marks, which they were formerly authorized to use under a valid license, after that license has terminated.²⁰⁴ In doing so, holdover licensees use the former licensor's genuine marks to sell products and services that no longer bear any connection to the former licensor.²⁰⁵ This conduct implicates the very core of prohibitions against trademark counterfeiting.²⁰⁶ Yet due to a small number of unreasoned court decisions, holdover licensees in certain jurisdictions are able to escape counterfeiting liability in favor of the less stringent—and less appropriate—remedies for mere trademark infringement.²⁰⁷

Courts should now reject this approach. Holdover licensees, at least in most circumstances, should be adjudged as trademark counterfeiters. Decisions absolving holdover licensees from counterfeiting liability lack a rational basis in trademark law doctrine or policy and also run contrary to the persuasive weight of better reasoned judicial authority.²⁰⁸ Either through legislative modification of statutory counterfeiting provisions or via a more nuanced process of statutory interpretation,²⁰⁹ courts should begin to consistently ensure that holdover licensees incur the form of liability most suitable under the scope of trademark law.

—Travis R. Wimberly

203. *See supra* Parts III and IV.

204. *See supra* notes 94–96, 107–18 and accompanying text.

205. *See supra* notes 94–96, 107–18 and accompanying text.

206. *See supra* notes 159–72 and accompanying text.

207. *See supra* subparts I(B)–(C) and Part III.

208. *See supra* subpart IV(B).

209. *See supra* Part V.