

THE ECONOMICS OF TRADEMARKS

*By Nicholas S. Economides**

ABSTRACT

Trademarks facilitate consumers' choice among experience goods and transmit quality signals for infrequently consumed goods. Trademarks are indispensable for the efficient provision of products with the wide range of variety and quality combinations demanded in a modern economy. Nevertheless, they can also sometimes have anticompetitive effects. Trademarks allow firms to tie in desired mental images with the advertised goods and to compete in perception advertising. The resulting possible distortions of competition fall into three categories. First, competition in perception advertising may result in a larger number of brands at equilibrium than is optimal. Second, the tie in produces an allocative distortion. Third, resources are wasted in the effort to link desired mental images with advertised goods.

The effects of trademarks on barriers to entry are ambiguous. The intertemporal effects of perception advertising may create barriers to entry for newcomers. Such barriers will be beneficial to society when they tend to decrease the number of brands toward optimality. With sequential entry, however, perception advertising may tend to increase the number of brands.

Firms may acquire some small market power from first use of the most appropriate symbol and words as trademarks. Such monopoly power is limited by restrictions against use of generic and descriptive terms.

I. INTRODUCTION

Man lives, thinks and dies using symbols. From the cross of the delivery hospital to the cross on the grave, man's life is lived by learning symbols, using them and creating new ones. Symbols are concrete and relatively simple representations of ideas and objects. A symbol is used instead of the detailed mental image it invokes because it is simple and can be quickly grasped. Use of

* Assistant Professor of Economics, Columbia University, New York, N.Y. The author has written extensively on questions of competition in variety and quality features of goods. The author wishes to thank Susan Rose-Ackerman for many helpful suggestions, Douglas Goodfriend and Judy Kim for diligent research assistance, Rosemarie Bowie for helpful comments and Jerre B. Swann, Allan S. Pilson and Robert C. Sorensen from The United States Trademark Association for their extensive suggestions and comments. Financial support from the Center for Law and Economics of Columbia University, under a grant from The United States Trademark Association, is gratefully acknowledged. The opinions expressed herein are solely the responsibility of the author.

advantage from the monopoly right of the use of the "best" symbol can only be temporary and small. This is true under the assumption that the trademarked name was not generic or descriptive of the item sold. If the name were generic or descriptive, its protected exclusive use could create significant difficulties in the effective functioning of the market. Competitors could be substantially disadvantaged and the monopoly power of the "trademark" holder could be considerable.²⁶ The law has provided insurance against such potential distortions through the exclusions of generic and descriptive names from trademark protection.²⁷ Not only is the protection of merely descriptive names limited under the Lanham Act,²⁸ but also designations that, in the eyes of the relevant public, primarily come to denote a product rather than the product's producer cease to be valid trademarks.²⁹ However, if a descriptive term has acquired a "secondary meaning" (or "distinctiveness") through identification in use with a particular brand, it qualifies for full statutory trademark protection under the Lanham Act.³⁰

VIII. CONCLUSION

I have shown that trademarks play an indispensable role in the efficient provision of experience goods with the variety and quality characteristics consumers desire. A similar role is played

26. In *Anti-Monopoly*, supra note 9, 611 F2d at 301, 204 USPQ at 982, the court explains that "[t]he genericness doctrine . . . is designed to prevent such anti-competitive misuse of trademarks." It affirms the rationale offered in *Bada Co. v. Montgomery Ward & Co.*, 426 F2d 8, 11, 165 USPQ 483, 485 (CA 9 1970), cert denied 400 US 916, 167 USPQ 513 (1970): "one competitor will not be permitted to impoverish the language of commerce by preventing his fellows from fairly describing their own goods."

27. Section 14(c) Lanham Act, 15 USC §1064(c) (providing for cancellation of a trademark which has become the common descriptive name of an article or substance), and §15(4) Lanham Act, 15 USC §1065(4) (no incontestable rights shall inhere in a mark which is a common descriptive name of the good); see also *Kellogg Co. v. National Biscuit Co.*, 305 US 111, 39 USPQ 296 (1938); *Nestle Company v. Chester's Market, Inc.*, 571 F Supp 763, 219 USPQ 298 (D Conn 1983). In the *Nestle* case, the district court ruled that TOLL HOUSE had become a generic term for chocolate chip cookies; however, note that the status of TOLL HOUSE as a generic term is unclear because the parties settled while appeal from the trial court was pending, and the appellate court then vacated the judgment and dismissed the complaint.

28. Section 2(e) Lanham Act, 15 USC §1052(e), states that marks that are merely descriptive are not registrable on the Principal Register unless, as provided in §2(f) Lanham Act, 15 USC §1052(f), the mark has become distinctive of the applicant's goods in commerce. See also *In re Work Wear Corp.*, 169 USPQ 501 (TTAB 1971).

29. However, "[a] registered mark shall not be deemed to be the common descriptive name of goods or services solely because such mark is also used as a name of or to identify a unique product or service. The primary significance of the registered mark to the relevant public rather than purchaser motivation shall be the test for determining whether the registered mark has become the common descriptive name of goods or services in connection with which it has been used." Section 14(c) Lanham Act, 15 USC §1064(c), as amended by Pub L No 98-620, §103, 98 Stat 3335 (1984).

30. Section 2(f) Lanham Act, 15 USC §1052(f); under this section, proof of substantially exclusive and continuous use of a mark for five years prior to the date of filing an application for registration of a mark constitutes prima facie evidence that the mark has become distinctive. A mark acquires "secondary meaning," or "distinctiveness," when "the primary significance of the term in the minds of the consuming public is not the product but the producer." *Kellogg Co. v. National Biscuit Co.*, supra note 27 at 118, 39 USPQ at 299.

