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COMBINING TRADEMARKS IN A JOINTLY OWNED IP HOLDING COMPANY*

*By Lanning Bryer** and Matthew Asbell****

I. INTRODUCTION

In 1999, Volvo spun off and sold its automobile division to Ford Motor Company, while retaining other automotive divisions, such as its truck business. As a result, Volvo then had to divide its VOLVO trademark rights between Ford and itself.¹ Volvo needed to continue controlling the VOLVO mark for trucks while giving Ford the right to control the VOLVO mark for cars. In a 2001 joint venture between Sony and Ericsson to make mobile telephones, the parties combined their respective trademarks, while maintaining their separate identities.² Similarly, SABMiller and Molson Coors Brewing Company are presently planning to use a new combined trademark in their joint venture, MILLERCOORS.³ Additionally, fast food franchises are leading the popular trend of co-branding, which often requires associating the trademarks and trade dress of multiple unrelated entities.⁴ For example, Kentucky

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1. Mike Osenga, *The Other Side of Ford-Volvo—Ford's Acquisition of the Passenger Car Business of Volvo AB*, DIESEL PROGRESS (North American Edition, March, 1999); Ford Motor Company website, <http://www.ford.com/en/company/about/brands/volvo.htm>; USPTO website, Trademark registration numbers 0636129 and 1182050, available at www.uspto.gov (assigned to Volvo Trademark Holding AB on Oct. 10, 2000).

2. Press Release, Sony Ericsson, Sony Ericsson Mobile Communications established today (Oct 1, 2001), available at http://www.sonyericsson.com/spg.jsp?cc=global&lc=en&ver=4001&template=pc3_1_1&zone=pc&lm=pc3_1&prid=110.

3. Aaron Back, *Justice Department Seeks More Information on Molson Coors-SABMiller Venture Plan*, Wall St. J., Nov. 21, 2007, at B3; *MillerCoors Creation Approved*, Denver Bus. J., Apr. 7, 2008, at 7 (available at http://www.bizjournals.com/denver/stories/2008/04/07/daily7.html?ana=from_rss).

4. Sonny Lufrano, *Co-Branding: Fast food finds strange bedfellows*, Atl. Bus. Chron., November 14, 2003, available at <http://atlanta.bizjournals.com/atlanta/stories/2003/11/17/focus9.html>; Jeffrey Tannenbaum, *Franchises Try New Fast-Food Combos*, Wall St. J., Oct. 16, 1996, at B1; Donald Kirk, *Franchise Dual-Branding: The Irony of Association*, 10 DePaul Bus. L.J. 1 (1997).

Fried Chicken, Pizza Hut and Taco Bell, which often operate in joint facilities, are all owned by a common parent.⁵

Whether one owner, like Volvo, partitions its brand for partial sale to an unrelated entity, or multiple diverse owners, such as McDonalds, CocaCola and Disney,⁶ elect to combine their goodwill in a joint venture, combination franchise or other co-branding relationship, joint use and joint ownership of multiple diverse trademarks have become more common in the globalized marketplace.⁷

Substantial risks may lie behind the sophisticated business transactions and the marketing strategies that accompany any sharing of trademark rights.⁸ It has been suggested that “co-branding may result in mixed consumer perceptions, leading to confusion, and eventually, a possible diminution in the value of the participating brands.”⁹ Without a central authority over their joint marks, or another means of coordinating strategy and execution with respect to the brand, independent companies may find it difficult to deliver a consistent experience to consumers on a global scale.¹⁰ This could result in a lack of control by these companies over their respective trademarks and trade dress, potentially resulting in the loss of such rights.¹¹

Furthermore, when separate entities attempt to improve market penetration by creating an association between their goods or services through a co-branding arrangement, a likelihood of confusion as to the origin of such goods and services may arise.¹² If consumers become confused over the source of products or services, the trademark rights could become vulnerable to third-party attack. Finally, when consumers identify multiple sources or products with inconsistent quality, the mark may lose distinctiveness or become diluted.¹³

5. Ann Hurwitz, *A Symposium on Franchise Law: Co-Branding: Managing Franchise Brand Associations*, 20 Okla. City U. L. Rev. 373 (1995); Yum Brands website, www.yum.com.

6. McDonalds, Coca-Cola, and Walt Disney have been allied for over 50 years, aligning their marks on tri-branded drinking cups among other products. Telephone Interview with Robert Lamb, Professor, Stern School of Business, New York University, in New York, N.Y. (December 1, 2006).

7. This article uses the term “sharing” to refer to any apportioning or combining of trademarks as described in the above examples.

8. Hurwitz, *supra* note 5, at 379.

9. *Id.* at 378-9.

10. Christian Dorffer & David Aaker, *Brand Papers—Dual Brand Ownership*, Brand Strategy, April 10, 2006, at 30.

11. *See infra*, Parts I.A.1. and 2.

12. Kirk, *supra* note 4, at 19. *But see* Steve Hartman, *Brand Equity Impairment—The Meaning of Dilution*, 87 TMR 418, 431 (1997). *See infra*, Part II.A.2.

13. *See infra*, Part II.A.3.

In an effort to mitigate these and other risks, brand owners have developed means to more safely share their marks. One frequently employed method has been dual trademarking, by which multiple owners license their respective trademark rights for use together without transferring any ownership.¹⁴ However, the resulting combined mark may not be registerable because no single entity wholly controls the combined mark. Furthermore, other benefits beyond the sharing of trademarks, such as tax savings, may be available to trademark owners that utilize alternative methods.

This article explores the risks and advantages involved in one such alternative, the combination of trademark rights of two or more entities into a holding company vehicle. The intellectual property holding company (IPHC)¹⁵ has primarily been used as a means of saving corporate income taxes. This has been accomplished by assignment of title in intellectual property (IP) rights from a parent company to a wholly owned subsidiary IPHC, which has then licensed back to its parent the right to use the IP. However, with the advent of increased trademark sharing between unrelated entities, IPHCs have been formed specifically to enable combined ownership of trademarks among multiple companies. Such a mutual trademark holding company (MTHC)¹⁶ is often formed as the jointly owned subsidiary of the multiple parent companies. With the goal of sharing trademarks while finding safer avenues toward at least some of the benefits of the wholly owned model, corporations may consider the formation of jointly owned MTHCs. One commentator has observed that “in the

14. See generally Saul Lefkowitz, *Double Trademarking—We’ve Come a Long Way*, 63 TMR 11 (1983). While there are numerous instances of double trademarking, a recent example is the cross-license in 2007 between Martha Stewart Living and Federated Merchandising (Macy’s) which resulted in “The Martha Stewart Collection Only at Macy’s” Licensing – Beyond the Basics, Association of the Bar of the City of New York, March 18, 2008.

15. These entities have come to be known by several other names: Intellectual Asset Management Companies, Intangible Holding Companies, Intangible Holding Subsidiaries, Trademark Holding Companies, Intangible Property Companies, Passive Investment Subsidiaries, Passive Investment Companies, Delaware Investment Holding Companies. See Christine Bauman & Michael Schadewald, *More States Challenge Trademark Holding Companies*, The CPA Journal, April 2004, at 38, available at <http://www.nysscpa.org/cpajournal/2004/404/essentials/p38.htm>; John Dull & Michael Bredahl, *Great Opportunities in an IP Holding Company Beyond Tax Savings*, *Intell. Prop. Today*, Jan. 2002, at 8; Susan Barbieri Montgomery & Leonard Schneidman, *Intellectual Property Transfers—Holding Companies in Intellectual Property Assets in Mergers and Acquisitions* 13.4 (L. Bryer ed., 2002); *State Income Tax Strategy*, 1-7 Taxation of Intellectual Property § 7.06 (2006).

16. This article uses the acronym MTHC to refer specifically to IPHCs that are mutually owned by multiple parent entities, which have transferred some or all of their respective trademark rights thereto. The acronym IPHC refers more generally to the corporate vehicle without specifying its singular or shared ownership or its specific type of IP assets.

absence of spinning off brands or mergers between the two parties, the only sustainable way to make dual brand ownership beneficial is to set up a trademark-holding company.¹⁷ For example, the Volvo Trademark Holding AB Corporation is 50% owned by Aktiebolaget Volvo Corporation and 50% owned by Ford Motor Company.¹⁸ This entity, organized as part of the sale of Volvo's automobile division to Ford, owns the VOLVO marks in order to coordinate global marketing and licensing initiatives for the benefit of both parent companies.

Regardless of whether an IPHC is wholly or mutually owned, its functions of acquiring, licensing, and enforcing IP are universal. Existing trademarks and other IP can be acquired via assignment(s) from the parent(s). In many instances, a parent will transfer its existing IP as an in-kind exchange for stock in a newly formed IPHC. Thereafter, the IPHC can adopt and register or acquire additional brands as necessary. No matter how the IP was acquired, the IPHC generally licenses the trademark rights back to the parent(s) for a reasonable royalty and enforces such rights against any third parties that use them without authorization.

II. THE RISKS OF IPHCs AND MTHCs

As mentioned at the outset of this article, the formation and maintenance of IPHCs create certain risks, especially when multiple owners are involved. There is concern that IPHCs may raise the possibility of the loss of trademark rights.¹⁹ Transferring trademarks to a shared subsidiary with a license back to the parents may, for example, result in a partial or total loss of quality control, and an increased likelihood of confusion, dilution or loss of distinctiveness. Certain jurisdictions complicate the formation or maintenance of MTHCs.²⁰ The incorporation of an MTHC by companies in a horizontal competitive relationship might raise antitrust concerns.²¹ Additional concerns arise with the possibility of multi-party and multi-district litigation stemming from cross-claims and countersuits in the event of disputes with third parties.²²

17. Dorffer, *supra* note 10, at 30.

18. Osenga, *supra* note 1.

19. Deborah Diehl, *Is the IP Holding Company Dead?* 37 Md. Bar. J. 43, 44 (2004).

20. *See infra*, Part II.A.6.

21. *See infra*, Part II.B.

22. David Vance Lucas, *Managing an IP Holding Company: IP Enforcement vs. Business Operations*, 2004 Spring Meeting (Amer. Intell. Prop. Lawyers Assoc.) (describing the multi-party and multi-district litigation concerns as well as increased administrative expenses arising from the duplication of certain costs and responsibilities and heightened disclosure requirements).

A. Risks to Trademark Rights

Several factors, such as insufficient quality control, an increased likelihood of confusion or dilution, a separation of the goodwill from the mark, a loss of distinctiveness, or jurisdictional bars to certain types of corporate vehicles, could have adverse impacts on trademark rights when utilizing an MTHC. Therefore, each factor should be examined.

1. Quality Control

Quality control is a critical component of the licensing aspect of a co-branding arrangement. Failure to exercise sufficient quality control may result in significant risks to trademark rights, including cancellation of or inability to enforce a trademark right against third parties.²³ While brand reliance by consumers is a well-established behavior,²⁴ the Trademark Law Revision Act of 1988 (TLRA) codified this perception in the United States by requiring that a trademark licensor control the quality of the goods on which the mark is used.²⁵ Failure to exercise quality control, deemed to be “naked licensing,” may result in the unintentional abandonment of the trademark.²⁶ Nonetheless, the TLRA does not

23. See *Dawn Donut Co. v. Hart's Food Stores, Inc.*, 267 F.2d 358, 367, 121 U.S.P.Q. 430 (2d Cir. 1959), accord *Huntington Nat'l Mattress Co. v. Celanese Corp. of America*, 201 F. Supp. 938, 132 U.S.P.Q. 395 (D. Md. 1962). See also 3 J. Thomas McCarthy, *McCarthy on Trademarks and Unfair Competition* § 18:48 (4th ed. 2003) [hereinafter *McCarthy*].

24. Frank Schechter, *The Rational Basis of Trademark Protection*, 40 Harv. L. Rev. 813 (1927) (arguing that the public had come to rely on the trademark primarily as representing a satisfactory level of product quality emanating from a common, though anonymous, source). The Lanham Act, 15 U.S.C. § 1055 (2007) (providing that the owner of a federal trademark registration or application could lawfully license the use of his mark if he controlled the nature and quality of the goods or services sold by the licensee under the mark.). See also 1 *McCarthy*, *supra* note 23, at § 3:3 B; *Siegel v. Chicken Delight, Inc.*, 448 F.2d 43, 171 U.S.P.Q. 269 (9th Cir. 1971), *cert. denied*, 405 U.S. 955 (1972); *Dawn Donut Co., Inc. v. Hart's Food Stores, Inc.*, 267 F.2d 358, 121 U.S.P.Q. 430 (2d Cir. 1959); *Edwin K. Williams & Co. v. Edwin K. Williams & Co.-East*, 542 F.2d 1053, 191 U.S.P.Q. 563 (9th Cir. 1976), *cert. denied*, 433 U.S. 908 (1977); *E. I. du Pont de Nemours & Co. v. Celanese Corp. of America*, 167 F.2d 484, 77 U.S.P.Q. 364 (C.C.P.A. 1948); *Arthur Murray, Inc. v. Horst*, 110 F. Supp. 678, 96 U.S.P.Q. 363 (D. Mass. 1953).

25. Trademark Law Revision Act, Pub. L. No. 100-667, § 107, 102 Stat. 3935, 3938 (1988) *codified as amended* at 15 U.S.C. § 1055 (2007) (adding the sentence, “If first use of a mark by a person is controlled by the registrant or applicant for registration of the mark with respect to the nature and quality of the goods or services, such first use shall inure to the benefit of the registrant or applicant, as the case may be.”).

26. 1 *McCarthy*, *supra* note 23. For a case finding trademark rights owned by a holding company to be invalid for lack of quality control, see *CNA Fin. Corp. v. Brown*, 922 F. Supp. 567 (M.D. Fla. 1996); *but see* Kevin Parks, “Naked” is not a Four-Letter Word: *Debunking the Myth of the Quality Control Requirement in Trademark Licensing*, 82 TMR 531 (1991) (questioning the reasoning behind the quality control requirement as a legal fiction lacking theoretical basis, practical benefit, or consistency with modern commerce). See also Michael A. Lisi, *Intracorporate Licensing: A Domestic Trademark Holding Company Example*, 510 PLI/PAT 381, 391-3 (1998).

adequately address whether ownership by a subsidiary that is licensing the rights to its parent could satisfy the quality control requirement.²⁷ The United States Patent and Trademark Office (USPTO) does not scrutinize the sufficiency of control by the parent for applications for registration by wholly owned subsidiaries,²⁸ and the only relevant case law to date has avoided the question.²⁹

Supporting the position that a wholly owned IPHC can have sufficient control over its parent to permit trademark ownership are the following factors, *inter alia*: (1) the leverage gained by the subsidiary over the parent arising from the risk of abandonment of the mark; (2) the parent's voluntary acquiescence to the control by the subsidiary for their mutual benefit; (3) the special relationship between the licensor and licensee creating a presumption that the licensee's intent is to protect the interests of the licensor; (4) the separate existence of the parent and the subsidiary being ignored for purposes of trademark ownership; and (5) the parties having a unity of interest, with trademark ownership benefiting the enterprise as a whole.³⁰ All of these factors, however, offer significantly weaker support for commonly owned MTHCs, whose interests cannot be so easily aligned with those of their multiple parents, and whose relationship with those parents is more tenuous. There is a risk that actions brought by or against the MTHC may result in a loss of trademark rights because of the MTHC's inability to exercise adequate control over its parent licensee. It is safe to conclude that there is no bulletproof strategy or structure for setting up and operating IPHCs.³¹ Nevertheless,

27. Pamela Chestek, *Control of Trademarks by the Intellectual Property Holding Company*, 41 IDEA 1, 5-7 (2001) (describing how the TLRA amended the definition of "related company" while leaving open the question of whether a subsidiary can control a parent); Trademark Law Revision Act, Pub. L. No. 100-667, § 134, 102 Stat. 3935, 3947 (1988) *codified as amended* at 15 U.S.C. § 1127 (2007).

28. U.S. Patent & Trademark Office, *Trademark Manual of Examination Procedures* § 1201.07(b)(i) (Mary Hannon, ed., 4th Ed. 2005) (hereinafter "TMEP") stating:

If the applicant or the applicant's attorney represents that either the applicant or the registrant owns all of the other entity, and there is no contradictory evidence, then the examining attorney should conclude that there is unity of control, a single source and no likelihood of confusion. This would apply to an individual who owns all the stock of a corporation, and to a corporation and a wholly owned subsidiary. In this circumstance, additional representations or declarations should generally not be required, absent contradictory evidence.

29. *In re Wella A.G.*, 787 F.2d 1549, 1552-53, 229 U.S.P.Q. 274, 276-77 (Fed. Cir. 1986), *on remand*, 5 U.S.P.Q.2d 1359, 1361 (T.T.A.B. 1987), *rev'd on other grounds*, 858 F.2d 725, 8 U.S.P.Q.2d 1365 (Fed. Cir. 1988). However, the increasing number of cases of fraud on the Trademark Office since *Medinol Ltd. v. Neuro Vasx, Inc.*, Opposition No. 92040535 (TTAB, Sept. 23, 2003) suggests at least the possibility that a U.S. trademark registration could be challenged on the grounds that an assertion of control was fraudulent.

30. See Chestek, *supra* note 27.

31. Lisi, *supra* note 26, at 413.

despite these uncertainties, companies continue to establish and rely on IPHCs, whether singularly or jointly owned.

Although a subsidiary can control and thus license the use of company trademarks to its parents and other licensees, it must exercise caution that competing uses by different related entities do not create a likelihood of confusion, dilution, separation from the associated goodwill, or loss of the distinctive character of the mark.

2. Confusion

Likelihood of confusion as to source is a bar to registration of a trademark in many countries, including pre-registration examination countries, such as the United States and Mexico.³² The U.S. Trademark Office may properly deny registration of a trademark if it is similar to the mark of an existing registration, and if the use of the trademark in commerce would be likely to cause confusion as to the source of the goods.³³ This is true even if the cited registration is owned by a company related to the applicant. It should be noted that actual confusion need not exist to bar registration.³⁴ Likelihood of confusion is determined on a case-by-case basis with consideration of factors, such as: (1) the strength of the marks; (2) the similarity of the appearance, sound, and meaning of the marks as a whole; (3) the similarity of the goods and services sold in association with the marks; (4) the similarity of marketing channels used; (5) the degree of care

32. TMEP, *supra* note 28, at 1207.01; The Lanham Act, 15 U.S.C. § 1052(d) (2007); *Ley de la Propiedad Industrial* [L.P.I.] [Industrial Property Law], *as amended*, Art. 90.XV, 27 de Junio de 1991 (Mex.).

33. TMEP, *supra* note 28, at § 1201.07(b)(iv), stating:

In contrast to those circumstances where the relationship between the parties may support a presumption of unity of control or at least afford an applicant the opportunity to demonstrate unity of control, some relationships, by their very nature, contradict any claim that unity of control is present. For instance, if the relationship between the parties is that of licensor and licensee [sic], unity of control will ordinarily not be present. The licensing relationship suggests ownership in one party and control by that one party over only the use of a specific mark or marks, but not over the operations or activities of the licensee generally. Thus, there is no unity of control and no [sic] basis for concluding that the two parties form a single source. Precisely because unity of control is absent, a licensing agreement is necessary. The licensing agreement enables the licensor/owner to control specific activities to protect its interests as the sole source or sponsor of the goods or services provided under the mark. Therefore, in these situations, it is most unlikely that an applicant could establish unity of control to overcome a § 2(d) refusal.

See also Chestek, *supra* note 27 at 16. But, in many countries including the United States, entities, particularly business associations, can register collective or certification marks, which allow multiple member companies to jointly use a trademark while control of the mark is vested in the association. *See* 37 C.F.R. § 2.44-5 (2007).

34. *A & H Sportswear v. Victoria's Secret*, 166 F.3d 197 (3d Cir. 1999).

exercised by consumers in making a purchase; (6) any evidence of actual confusion; and (7) the intent of the junior party.³⁵

Consumer confusion may arise when businesses combine their existing marks into a new composite mark for which the MTHC then seeks trademark registration.³⁶ Steps that may be taken by the joint owners to lessen the possibility of such confusion include: (1) setting forth the relationship of the parties to establish that their actions are in tandem; (2) establishing control and supervisory guidelines over the use of the composite mark; (3) discontinuing use of the composite mark, including its possible use as a corporate or trade name, upon termination of the business; (4) prohibiting the use of any of the elements of the composite marks in a stand-alone fashion; and (5) requiring licensing and demarcation of the ownership rights and registration status of individually owned elements whenever the composite mark is used.³⁷

Alternatively, the parents can elect to assign their pre-existing marks to the MTHC. When trademarks are owned by one entity, there may be fewer obstacles to establishing rights in a composite mark,³⁸ at least in circumstances where the individual marks have equal strength or fame.³⁹ The subsidiary owner must, of course,

35. *Polaroid Corp. v. Polarad Elec. Corp.*, 287 F.2d 492 (2d Cir.), *cert. denied*, 368 U.S. 820 (1961); *AMF, Inc. v. Sleekcraft Boats*, 599 F.2d 341, 351 (9th Cir. 1979); *J.B. Williams Co. v. Le Conte Cosmetics, Inc.*, 523 F.2d 187 (9th Cir. 1975), *cert. denied*, 424 U.S. 913 (1976); *Earth Technology Corp. v. Environmental Research of Tech., Inc.*, 222 U.S.P.Q. 585, 588 (C.D. Cal. 1983); *American Home Prods. Corp. v. Johnson Chem. Co.*, 589 F.2d 103 (2d Cir. 1978).

36. Saul Lefkowitz, *Double Trademarking—We've Come a Long Way*, 63 TMR 11, 15 (1983). *But see In re Diamond Walnut Growers, Inc., and Sunsweet Growers Inc.*, 204 U.S.P.Q. 507, 511 (T.T.A.B. 1979) (holding it appropriate to grant a registration of a composite mark to the two owners of the separate parts of the composite). However, in that case, the parents retained ownership and licensed the composite to the joint venture. Here, the joint entity owns the marks and licenses back to the parents.). *See In re Hercofina*, 207 U.S.P.Q. 777 (T.T.A.B. 1980) (holding that the joint venture was the proper owner of the composite mark). On the question of whether there is less likelihood of confusion where a composite mark incorporates a well-known house mark, *compare E. & J. Gallo Winery v. Consorzio del Gallo Nero*, 782 F. Supp 457 (N.D. Cal. 1991); *Vitarroz Corp. v. Borden, Inc.*, 644 F.2d 960 (2d Cir. 1981).

37. *Chestek*, *supra* note 27 at 16-17. Regarding the discontinuance of the mark upon termination of the business, see Thomas McCarthy, *Joint Ownership of a Trademark*, 73 TMR 1, 5-6 (1983) (suggesting that "to preserve the identity of a trademark, the parties to a joint enterprise . . . should contract that only one of the participants will receive the trademark and associated good will upon dissolution").

38. TMEP, *supra* note 28, at § 1201.07(b).;

Of course, in many of these situations, the applicant may choose to attempt to overcome the § 2(d) refusal by submitting a consent agreement or other conventional evidence to establish no likelihood of confusion. . . . Another way to overcome a § 2(d) refusal is to assign all relevant registrations to the same party.

39. *Kirk*, *supra* note 4, at 19 (arguing in the context of dual-branding and trade dress, that where a weaker mark becomes associated with a well-known mark, consumers may

take care that its licensees continue to use the individual marks on their own to avoid abandonment and maintain their separate existence from the composite mark.⁴⁰ Careful contract drafting will minimize confusion regarding ownership of trademarks upon dissolution of the IPHC.⁴¹ If the transfer includes a company's "house" mark to a partially owned subsidiary, this decision should not be made lightly, as the level of legal and business risk would increase.

3. Dilution

Dilution may arise when a famous trademark is used by multiple parent licensees. In the United States, the Trademark Dilution Revision Act of 2006 defines two types of dilution.⁴² Dilution by blurring is defined as "association arising from the similarity between a mark or trade name and a famous mark that impairs the distinctiveness of the famous mark."⁴³ Dilution by tarnishment is defined as an "association arising from the similarity between a mark or trade name and a famous mark that harms the reputation of the famous mark."⁴⁴ Several countries outside the United States also recognize the concept of dilution in one form or another.⁴⁵

begin to perceive the product source as that of the strong mark, resulting in an absence of distinctiveness). *See, e.g.*, *Conopco, Inc. v. May Dep't Stores Co.*, 46 F.3d 1556 (Fed. Cir. 1994), *cert. denied*, 514 U.S. 1078 (1995); *L.A. Gear, Inc. v. Thom McAn Shoe Co.*, 988 F.2d 1117, 1134 (Fed. Cir. 1993), *cert. denied*, 510 U.S. 908 (1993); *Bristol-Myers Squibb Co. v. McNeil-P.P.C., Inc.*, 973 F.2d 1033, 1046 (2d Cir. 1992); *Turtle Wax, Inc. v. First Brands Corp.*, 781 F. Supp. 1314, 1326 (N.D. Ill. 1991); *Estee Lauder Inc. v. The Gap, Inc.*, 108 F.3d 1503 (2d Cir. 1997).

40. John R. Morrissey, *Double Trademarking in Canada*, 73 TMR 28, 44 (1983).

41. 1 *McCarthy*, *supra* note 23, at 5-6.

42. Trademark Dilution Revision Act, 109 P.L. 312, 120 Stat. 1730 (2006).

43. *Id.*

44. *Id.*

45. *Adidas-Salomon v. Fitnessworld Trading*, 2003 E.C.R. I-12537 (holding that the protection of well-known marks in Europe must be at least as extensive for identical and similar goods as for dissimilar goods and therefore also provide dilution protection in cases of similar goods.); *General Motors v. Yplon*, 1999 E.C.R. I-05421. Aside from the United States and Europe, many countries offer some form of antidilution law, including Canada, Argentina, South Africa, India, Japan, Singapore, New Zealand, and Australia. *See The Protection of Well-Known Marks in the European Union, Canada and the Middle East*, International Trademark Association website, http://www.inta.org/images/stories/downloads/ref_protection.pdf; and *The Protection of Well-Known Marks in Asia-Pacific, Latin America and Africa*, International Trademark Association website, http://www.inta.org/images/stories/downloads/ref_Aasian.pdf. *See also* Markus H. H. Luepke, *Taking Unfair Advantage or Diluting a Famous Mark — A 20/20 Perspective on the Blurred Differences Between U.S. and E.U. Dilution Law*, 98 TMR 789 (2008); South Africa with § 10(17) and § 34(1)(c) of its 1993 Trade Marks Act, which is based on Art. 5(2) of the 1988 E.U. Trademark Directive; Canada allows protection under the "Depreciation of Goodwill" theory, which is not limited to famous or well-known marks but requires goodwill.

Blurring can be further described as the use of a famous mark in a manner that creates inconsistent associations and images with the established equity of a brand, regardless of the relationship between those using it.⁴⁶ There are concerns that an IPHC “can dilute [its] own mark” and that “[t]he use of a mark in a manner that impairs the equity is dilutive regardless of who is responsible for the impairing use.”⁴⁷ There may also be risks of dilution in transferring a famous house mark to a commonly owned entity.⁴⁸

While concerns over self-dilution may be legitimate, they are not likely to prevent the registration or use of famous marks by an MTHC subsidiary. For example, U.S. trademark examiners will not cite a likelihood of dilution as a bar to registration. The possibility of self-dilution therefore is more a theoretical than a practical issue, because neither of the related users/owners of the mark will likely assert such a claim against the other. However, dilution can act as a bar to registration in other countries, for example, Mexico.⁴⁹ In these countries, the parent companies should take care that the trademark prosecution efforts of the MTHC do not, in effect, dilute any famous marks retained by the parent because their trademark offices may either refuse to register a mark to the MTHC, or possibly, in subsequent disputes, recognize the dilution as impairing the notoriety of the parent’s famous mark.

46. Hartman, *supra* note 12, at 421-22, claiming that:

[D]ilution is the impairment of brand equity caused by a use of the mark that creates associations and images inconsistent with the equity. Dilution erodes or (in the words of the [Federal Trademark Dilution Act of 1995]) “lessens” the brand’s identity, and in so doing, weakens the brand’s pricing power, ability to command market share, and durability, those qualities of brand equity that account for its selling power and marketing value.

47. *Id.*

48. Lefkowitz, *supra* note 35, at 17 (“A party ought not to commit a mark that has achieved public acceptance and recognition for use in a joint venture which involves operations unrelated to the field(s) of expertise of its owner, or to one that entails a measure of risk.”). Because different countries apply different thresholds for the requirement of fame, the risk that the IPHC or its parents might dilute their mark likely depends on the jurisdiction in which the mark was created. See Markus H. H. Luepke, *Taking Unfair Advantage or Diluting a Famous Mark — A 20/20 Perspective on the Blurred Differences Between U.S. and E.U. Dilution Law*, 98 TMR 789 (2008) (describing the lower threshold for fame in the E.U. compared to the United States as resulting from the need to address trademark misuse on dissimilar goods under the concept of dilution rather than confusion).

49. “A mark considered to be well-known is a bar to registration of an identical or similar mark, if use of the junior mark would result in . . . an unauthorized exploitation of the well-known mark, tarnishment of the well-known mark, or dilution of the distinctive character of the well-known mark. *Ley de la Propiedad Industrial* [L.P.I.] [Industrial Property Law], as amended, Art. 90.XV, 27 de Junio de 1991 (Mex.). See also Indonesia: Law No. 19 of 1992, State Gazette 1992 No. 81, Law No. 15 on August 1, 2001; China: Article 13 of the Trademark Law.

4. Distinctiveness

Transferring a trademark to an MTHC could jeopardize its validity if the trademark loses its distinctive character. An MTHC created for the purposes of co-branding may risk losing its exclusive right to use its marks as a result of a loss of distinctiveness caused by allowing its licensees to use multiple marks on a single product or service. The licensor must restrict the use of each of its marks so that each mark creates a separate and distinct impression from any others used, and each mark serves as a means to identify and distinguish the product or service from those of others in the market.⁵⁰ “The use of each mark applied to the product must not confuse the purchasing public as to its function or purpose, or derogate the trademark rights of anyone who contributed to the creation of the product, or those who handle the product during its journey to the market place.”⁵¹ As such, licenses from an MTHC back to its parents, or out to third parties, must restrict the licensees’ use in conjunction with other marks. Ford Motor Company, which owns the FORD trademark for use on or in connection with motor vehicles and related goods and services, and is licensed to use the VOLVO trademark to identify vehicles and related goods and services, might jeopardize both famous marks if Ford affixed both of them on its cars. Consumers might be confused as to the source of manufacture of Ford’s vehicles. However, the likelihood of confusion may be far less substantial today than it was in the past because consumers have become more sophisticated as a result of the increasing practice of using trademarks outside of the normal context of a simple sale of goods or services. For example, there is a growing awareness among consumers of the current use of trademarks in product placements in film and television.⁵²

5. Separation of Trademarks From Their Associated Goodwill

An additional problem arising from the transfer of trademarks from multiple unrelated entities to a jointly held subsidiary IPHC

50. Lefkowitz, *supra* note 36, at 13.

51. *Id.* at 14.

52. See Nancy Cohen, *Virtual Product Placement Infiltrates TV, Film, Games*, Ecommerce Times, February 23, 2006, <http://www.ecommercetimes.com/story/48956.html> (last visited Nov. 19, 2007); Robin Good, *Product Placement And Hypercommercialism Pervade Hollywood Film Industry: But No-One Seems To Notice*, Master New Media, January 9, 2007, http://www.masternewmedia.org/news/2007/01/09/product_placement_and_hypercommercialism_pervade.htm# (last visited Nov. 19, 2007); *Product Placement Comes to the Fore*, BBC News, Nov. 14, 2005, <http://news.bbc.co.uk/1/hi/entertainment/film/4435776.stm> (last visited Nov. 19, 2007).

is the separation of the marks from the goodwill that is associated with them. Goodwill is the advantage of reputation in connection with a business.⁵³ In the United States, and elsewhere, the rights in a mark cannot usually exist apart from the business whose product or service it identifies.⁵⁴ However, some countries allow assignment in gross of trademark rights independent of any transfer of goodwill.⁵⁵ Others, including the United States, require transfer of the goodwill associated with the mark along with the mark.⁵⁶ Thus, where a mutual IPHC is intended to manage a diverse portfolio of marks worldwide, certain assignments from a parent must be accompanied by a recitation of the transfer of goodwill, while the transfer of goodwill may not be required for others. In order to minimize the risks of challenge by third parties to trademark rights stemming from the transfer, IPHC management should be mindful of those jurisdictions that require that goodwill be included in an assignment of trademarks and file accordingly.

6. Jurisdictional Bars

Establishing an IPHC in a tax-friendly or “offshore” jurisdiction may limit its ability to register, assign and enforce the associated marks, as well as to take advantage of multinational trademark conventions such as the Madrid Agreement and Protocol.⁵⁷

Some jurisdictions may prevent entities from registering marks based upon prior pending applications or granted registrations belonging to related foreign entities. Section 44(c) of the Lanham Act prevents registration of a U.S. mark by a foreign

53. Mark A. Greenfield, *Good Will as a Factor in Trademark Assignments—A Comparative Study*, 60 TMR 173 (1970).

54. *Id.* (quoting *Pinto v. Badman*, 8 RPC 181, 194 (1891) (“[I]f you transfer the indication of origin, without transferring the origin itself, you are transferring a right, if any right at all, to commit a fraud upon the public.”)).

55. Greenfield, *supra* note 53, at 178-79 (“the goodwill of a business frequently is inherent in the trade mark itself.”). *Id.* at 181 (describing non-British-law countries as permitting assignments either without any restrictions as to good will or only with good will by some definition.), and *id.* at 186 (suggesting a trend outside the U.S. toward recognizing a trademark as an independent form of property capable of alienation without good will).

56. The Lanham Act, 15 U.S.C. § 1060 (2007); Greenfield, *supra* note 53, at 175-6 (“A transfer of the entire business of the assignor is not required unless the assignee cannot produce the same products without it.”). See International Trademark Association website, www.inta.org (under Information and Publishing, click Country Guides, then click Advanced Search, select question 23 and search all jurisdictions). See generally James R. Olsen, Spyros M. Maniatis, and Cristina Garrigues, *Trade Marks, Trade Names and Unfair Competition: World Law and Practice* (Tina Loverdou, Daphne Zografos, and Elaine Simpson-Long, eds., 2006) at Table 22/1.

57. See Michelle Dillon, *Offshore: Before you go*, Legalweek, Oct. 12, 2006, <http://www.legalweek.com/Articles/130960/Offshore+Before+you+go.html>.

entity whose country of origin is party to a trademark treaty with the United States until such mark has been registered in the applicant's country of origin, unless the applicant alleges in the alternative a basis for registration based on use in commerce.⁵⁸ Based on this statute, the U.S. Trademark Trial and Appeal Board determined that a Swedish corporation could not register a mark in the United States based on prior registrations obtained by its wholly owned subsidiaries in Austria and Denmark that were subsequently assigned to the applicant. Neither Austria nor Denmark qualified as the applicant's country of origin under the statutory definition.⁵⁹ An IPHC may therefore face difficulty trying to register marks in the United States on applications that claim priority back to earlier foreign registrations by its parents located in another jurisdiction. Similarly, parent companies may not be able to claim priority to foreign applications for marks filed by the IPHC.

A parent company must ensure that it is indeed the record owner of the marks it seeks to transfer and that assignment to another entity is permissible.⁶⁰ Some countries will not recognize or permit ownership of trademarks by holding companies, or alternatively, they charge transfer taxes upon their assignments.⁶¹ A Canadian trademark might be endangered by the transfer to an IPHC. The Supreme Court of Canada has stated,

[A]n assignment would not invariably support the assignee's claim to trade mark protection if there was a deception of the public in the message that the trade mark conveyed in its use by the assignee, that is, if the public would take from it that the trade mark was still distinctive of the origin of the goods

58. 15 U.S.C. § 1126(c) (2007) provides:

No registration of a mark in the United States by a person described in subsection (b) of this section shall be granted until such mark has been registered in the country of origin of the applicant, unless the applicant alleges use in commerce. For the purposes of this section, the country of origin of the applicant is the country in which he has a bona fide and effective industrial or commercial establishment, or if he has not such an establishment the country in which he is domiciled, or if he has not a domicile in any of the countries described in subsection (b) of this section, the country of which he is a national.

59. *In re Aktiebolaget Electrolux*, 182 U.S.P.Q. 255, 256 (T.T.A.B. 1974) (holding:

[T]he relationship of parent company and wholly-owned subsidiary does not, per se, mean that the non-resident parent company is doing business in the forum in which the wholly owned subsidiary is located, and that the existence of a wholly owned subsidiary in a foreign forum does not mean that the non-resident parent company has a "bona fide and effective or commercial establishment" in that foreign forum).

60. Dillon, *supra* note 57.

61. Lisi, *supra* note 26, at 386. *See generally* Olsen, *supra* note 55 (countries that may restrict or prohibit ownership by holding companies or impose transfer taxes upon assignment include: Bulgaria, Czech Republic, Ecuador, El Salvador, Fiji, Japan, Mexico, New Zealand, The Slovak Republic, Spain, Surinam, Turkey, Uzbekistan, and Yemen).

being in the assignor rather than being distinctive merely of the place of manufacture.⁶²

However, a recent Canadian case has distinguished the unregistered transfer of trademark registrations from a parent to a subsidiary where there is evidence that consumers identified the subsidiary as the source of goods.⁶³ In *Cross-Canada*, a more-than-twenty-year delay in registration of an assignment of trademarks from the Korean parent company to its Canadian subsidiary was held not to have caused consumer confusion in light of the subsidiary's extensive advertising and expert evidence that consumers perceived the source of goods to be the dealers controlled by the subsidiary.⁶⁴

Licensing between parent and subsidiary may be similarly problematic in some countries unless the licensee provides notice of the licensing relationship on its products or packaging (*i.e.*, it recites the licensed use).⁶⁵ Despite the previous availability in Canada of registered user records, which treated licensed use as if it was made by the owner, at least one author at the time suggested there was "no guarantee" of distinctiveness.⁶⁶ "The licensee should not be permitted to use the mark as if it were his own, but should always mark the goods to indicate that they were made under the authority of a named trade mark owner."⁶⁷ It is therefore prudent to understand how the trademark law of a particular jurisdiction views the concepts of ownership, assignment, and licensing.

While determinations of ownership and transferability usually can be readily obtained in the case of registered marks, unregistered or "common law" trademarks may pose greater difficulty because their legal ownership is a matter of local law, and some jurisdictions impose restrictions on their assignment separate from related business assets.⁶⁸

62. *Breck's Sporting Goods Co. Ltd. v. Magder*, 17 CPR.2d 201, 207 (Sup. Ct. of Canada 1975). See also *Wilkinson Sword (Canada) Ltd. v. Juda*, 51 CPR 55 (Ex. Ct., 1966).

63. *Cross-Canada Auto Body Supply (Windsor) Limited v. Hyundai Motor Am.*, 2007 FC 580 (June 1, 2007).

64. *Id.* at 592.

65. See generally Olsen, *supra* note 55 (for example, licensees in Taiwan must mark their licensed uses to avoid being subject to cancellation).

66. Morrissey, *supra* note 39, at 36.

67. *Id.* at 35.

68. See Dillon, *supra* note 57; see generally Olsen, *supra* note 55 (countries that may impose such restrictions specifically on unregistered marks include: Anguilla, Antigua and Barbuda, Australia, Bahamas, Bahrain, Bangladesh, Hong Kong, Ireland, Kenya, Lithuania, Malawi, Malta, Namibia, Singapore, South Africa, St. Lucia, Switzerland, Thailand, and United Kingdom) and accompanying text in Part II.A.5.

Keeping careful record of licenses and arranging for the registration thereof could be crucial for certain tax, IP and financial considerations.⁶⁹ For example, written licenses may need to be produced to support tax positions regarding transfer pricing. A failure to document licenses could jeopardize the trademarks based on non-use or may prevent a licensee from enforcing its rights.⁷⁰ Indeed, a failure to record a written license with the trademark office in some countries serves to invalidate the license.⁷¹ Some jurisdictions also have currency or banking controls that prevent royalty payments from leaving the country without evidence and recordal of a written license.⁷² The need to document and record licenses results in increased transaction costs when transferring trademarks to an offshore IPHC.⁷³

Some countries may prevent MTHCs from taking effective action to suppress infringements.⁷⁴ By separating ownership from exploitation of trademark rights, an MTHC may suffer less damage from infringements than its licensed parents, and therefore be entitled to limited recovery,⁷⁵ while the parents may not have standing to sue because they do not own the marks.⁷⁶

Last, it is important to consider whether the target country is a member of, and may take advantage of, certain international IP harmonization and protection treaties, such as the Madrid Agreement and/or Protocol.⁷⁷ Under the Madrid Agreement, international registration of a mark is only available to a trademark owner that has registered the mark in the owner's

69. *See id.*

70. *See id.*

71. Examples include Thailand and Russia. *See* § 68 of the Trademark Act, B.E. 2534 (1991) (Thailand); *New Russian IP Law Has Serious Deficiencies for Trademark Owners*, INTA Bulletin, Vol. 62, No. 2 (Jan. 15, 2007) (describing the newly enacted Part IV of the Civil Code in Russia as requiring “mandatory recordal of all trademark licenses against the registration of the licensed mark, an extremely burdensome and costly requirement that serves no legitimate purpose and has been abandoned by all but a handful of countries around the world.”) (emphasis in original). *See generally* Olsen, *supra* note 55.

72. *See* Dillon, *supra* note 57.

73. *Id.*

74. *Id.*

75. *Id.* However, depending on the decision as to which entity is to assume the risk of liability, it may be possible to include an indemnity or other term in the license between the MTHC and its parents to make the MTHC responsible for the full damages incurred by the parents in anticipation of an argument by an alleged infringer that the damages to a plaintiff MTHC are reduced.

76. *Id.*

77. *Id.* Madrid Agreement Concerning the International Registration of Marks, Art. 1, April 14, 1891 (“The Agreement”); Protocol Relating to the Madrid Agreement Concerning the International Registration of Marks, Art. 2, June 27, 1989 (“The Protocol”); The Agreement and The Protocol are jointly referred to as “The Madrid System.”

“country of origin,” which must be a member of the Agreement.⁷⁸ Under the Madrid Protocol, international registration of a mark is available to an applicant or registrant in their country of origin.⁷⁹ Thus, if an MTHC is located in a non-member country, it may be unable to apply under the Madrid System, regardless of whether it acquired the mark on which an international registration application would be based by prosecution or assignment. In addition, after an international registration is obtained, it cannot be transferred to an entity in a non-member country.⁸⁰ Companies therefore should consider whether the location of the MTHC will prevent it from transferring existing international registrations or the filing of future trademark registration applications via the Madrid System.

B. Antitrust Issues

Before utilizing an MTHC, U.S. and foreign parent entities, especially competitors, should take into account all relevant antitrust laws and regulations. In the United States, combining substantial assets of two or more companies into a single entity may qualify as a merger and lend itself to federal antitrust scrutiny as an anticompetitive collaboration among potential or actual competitors.⁸¹ Such collaborations also may be scrutinized

78. *Id.* at Art. 1(2) (Under The Agreement, the country of origin is considered “the country of the Special Union where the applicant has a real and effective industrial or commercial establishment; if he has no such establishment in a country of the Special Union, the country of the Special Union where he has his domicile; if he has no domicile within the Special Union but is a national of a country of the Special Union, the country of which he is a national.”).

79. *See* The Protocol, *supra* note 77, at Art. 2(1)(i) (Under The Protocol, “the person in whose name that application or registration stands [must be] a national of that Contracting State, or is domiciled, or has a real and effective industrial or commercial establishment, in the said Contracting State”).

80. *See* The Agreement, *supra* note 77, at Art. 9*bis*(2) (“No transfer of a mark registered in the International Register for the benefit of a person who is not entitled to file an international mark shall be recorded.”) *See also* Art. 9*bis*(3) (“When it has not been possible to record a transfer in the International Register, either because the country of the new proprietor has refused its consent or because the said transfer has been made for the benefit of a person who is not entitled to apply for international registration, the Office of the country of the former proprietor shall have the right to demand that the International Bureau cancel the mark in its Register.”). *See* The Protocol, *supra* note 77, at Art. 9 (“At the request of the person in whose name the international registration stands, or at the request of an interested Office made ex officio or at the request of an interested person, the International Bureau shall record in the International Register any change in the ownership of that registration, in respect of all or some of the Contracting Parties in whose territories the said registration has effect and in respect of all or some of the goods and services listed in the registration, provided that the new holder is a person who, under Article 2(1), is entitled to file international applications.”).

81. *See* Federal Trade Commission & U.S. Department of Justice, Antitrust Guidelines for Collaborations Among Competitors, § 1.3 (2000) [hereinafter Antitrust Guidelines].

at the state level, although state antitrust laws, despite their lack of uniformity, tend to be more narrow and lenient.⁸²

In the United States, the primary federal antitrust laws are Section 7 of the Clayton Act, Section 1 of the Sherman Act, and Section 5 of the Federal Trade Commission Act.⁸³ The Clayton Act proscribes mergers whose effects substantially lessen competition.⁸⁴ The Sherman Act prohibits agreements or conspiracies in restraint of interstate or foreign commerce.⁸⁵ Case law has generally held that only “unreasonable” restraint violates the Sherman Act.⁸⁶ The Federal Trade Commission Act proscribes “unfair methods of competition.”⁸⁷ Additionally, the Hart-Scott-Rodino Antitrust Improvements Act of 1976 sets out certain pre-merger notification and reporting requirements for larger transactions.⁸⁸ Federal law applies different standards of scrutiny to mergers than to mere collaborations among competitors.⁸⁹ Merging parties completely and permanently end any competition between them in a relevant market.⁹⁰ Mere collaborations among competitors are typically for limited durations and for different markets.⁹¹

1. Mergers

In 1992, the Federal Trade Commission and the U.S. Department of Justice jointly issued the Horizontal Merger Guidelines to describe the principles employed in determining when a merger violates federal antitrust laws.⁹² These agencies inquire into the facts of each case to determine “whether the merger may increase market power by facilitating coordinated interaction among rival firms and whether the merger may enable the merged firm unilaterally to raise price or otherwise exercise

82. Sheryl Brown & Christopher Kim, *Antitrust Violations*, 43 Am. Crim. L. Rev. 217, 248-50 (2006).

83. The Clayton Act, 15 U.S.C. § 18 (2007); The Sherman Act, 15 U.S.C. § 1 (2007); The Federal Trade Commission Act, 15 U.S.C. § 45 (2007).

84. The Clayton Act, 15 U.S.C. § 18 (2007).

85. The Sherman Act, 15 U.S.C. §§ 1-7 (2007).

86. *See, e.g.*, *Nynex Corp. v. Discon, Inc.*, 525 U.S. 128, 133 (1998).

87. The Federal Trade Commission Act, 15 U.S.C. § 45 (2007).

88. The Hart-Scott-Rodino Act of 1976, 15 U.S.C. § 18a (2007).

89. *See* Antitrust Guidelines, *supra* note 81, at § 1.3.

90. *Id.*

91. *Id.*

92. *See* Federal Trade Commission and the U.S. Department of Justice, Horizontal Merger Guidelines (1992) *as amended* (1997) [hereinafter Horizontal Merger Guidelines]; Federal Trade Commission and the U.S. Department of Justice, Commentary on the Horizontal Merger Guidelines (2006) [hereinafter Commentary on Horizontal Guidelines].

market power.”⁹³ These Guidelines are designed to identify the mergers that are “likely to create or enhance market power in any market.”⁹⁴ They define a market, based on a “hypothetical monopolist test,”⁹⁵ as follows:

[A] product or group of products and a geographic area in which it is produced or sold such that a hypothetical profit-maximizing firm, not subject to price regulation, that was the only present and future producer or seller of those products in that area likely would impose at least a small but significant and nontransitory increase in price [(“SSNIP”)], assuming the terms of sale of all other products are held constant.⁹⁶

If a violation is found, the combined entities may be separated and a penalty could be assessed.⁹⁷

U.S. courts uphold agency determinations when a merger is “de facto” or “virtual.”

a. “De Facto” Mergers

A “de facto” merger may exist where a court finds the sum and substance of a collaboration to be akin to a merger. This could result in the application of the higher level of scrutiny applied to formal mergers without concern for whether or not the parties had intended such collaboration to be considered a merger. Cases successfully invoking the doctrine have involved an actual sale of assets, a shift in management control, and dissolution of the transferring corporation.⁹⁸ As an MTHC obtains its initial

93. Commentary on Horizontal Guidelines, *supra* note 92.

94. *Id.* at 5.

95. *Id.*

96. Horizontal Merger Guidelines, *supra* note 92, at § 1.0.

97. *Id.* In some cases, a merger may be allowed to proceed if certain assets are excluded.

98. See, e.g., *Rath v. Needham*, 136 N.W.2d 410, 412 (Iowa 1965) (reversing a decision that what was titled a “Plan and Agreement of Reorganization,” in which “Needham agreed to: (1) transfer all its assets to Rath; (2) cease using its name; (3) distribute the new Rath-Needham shares to its stockholders, liquidate and dissolve; and (4) turn over to Rath its corporate and business records,” did not amount to a merger in fact for the purpose of requiring a certain shareholder vote.); *Farris v. Glen Alden Corp.*, 143 A.2d 25 (Pa. 1958) (affirming a decision that a “reorganization agreement” in which the Glen Alden Corporation would acquire all of the assets of a Delaware Holding Company called List, which would be dissolved, but would occupy eleven of seventeen directorships on the board of the renamed corporation, amounted to a merger in fact requiring notice of a right to dissent to be issued to shareholders.); *Knapp v. North Am. Rockwell Corp.*, 506 F.2d 361 (3d Cir. 1974) (reversing summary judgement in favor of a defendant corporation which acquired substantially all of the assets of a predecessor which had agreed to dissolve as soon as practicable where the predecessor’s negligence resulted in an injury to the plaintiff after the de facto merger transaction.); *Stuart R. Cohn, The Non-Merger Virtual Merger: Is Corporate Law Ready for Virtual Reality?*, 29 Del. J. Corp. L. 1, 5 (2004).

trademark assets from its parent entities, which continue to exist after the transfer, the transaction creating the MTHC would not likely be considered to be a “de facto” merger.

b. “Virtual” Mergers

A collaboration not deemed to be a “de facto” merger, but functionally serving the same purpose, may qualify as a “virtual” merger if it expressly provides for a termination, whereupon assets would revert to the contributing parent.⁹⁹ A virtual merger may arise where each corporation allocates a significant percentage of its assets to joint control, while simultaneously retaining a residuary interest in the assets.¹⁰⁰ For example, when two hospitals in Poughkeepsie, New York, decided to integrate their services beyond an initial successful joint venture agreement, while retaining their separate identities and ownership structures, the New York Antitrust Division applied state antitrust laws to defeat this “virtual” merger on the grounds that it was really a horizontal collusion that decreased consumer choice and price competition.¹⁰¹

The creation of a jointly owned MTHC may be characterized as a “virtual” merger if the parent entities expressly require assignment of their marks back to them when the MTHC is later dissolved. However, if the trademarks residing in the MTHC are not “house” marks, or otherwise do not constitute a significant percentage of each parent’s assets, the possibility that the intended collaboration could be construed as a “virtual” merger is minimized.

No decisions to date have found a “virtual” merger involving publicly held U.S. companies.¹⁰² Perhaps they will arise in the context of MTHCs.

2. Collaborating Competitors

Even if the allocation of assets to a jointly owned MTHC is not considered a “de facto” or “virtual merger,” collaborating competitors may still find they are subject to antitrust scrutiny.¹⁰³ Collaborations may be scrutinized under merger law when: (1) the participants are competitors in a particular market; (2) their

99. Cohn, *supra* note 98, at 8.

100. *Id.* at 5.

101. New York *ex rel.* Spitzer v. Saint Francis Hosp., 94 F. Supp. 2d 399 (S.D.N.Y. 2000).

102. Cohn, *supra* note 98, at 7; Mr. Cohn expects that collaborations in the high tech, pharmaceutical, oil, and communications industries may soon be scrutinized as virtual mergers.

103. See Antitrust Guidelines, *supra* note 81, at § 1.3.

integration of economic activity would enhance efficiency in the relevant market; (3) the integration would eliminate all competition among the participants in the relevant market; and (4) the collaboration does not terminate within a sufficiently limited time period.¹⁰⁴

More frequently, however, collaborations are evaluated for their effects on competition via a different legal framework: anti-competition law. At the federal level, some combinations have been identified as being so likely to be anti-competitive and to be lacking in pro-competitive benefits that they have been *per se* illegal.¹⁰⁵ Most, however, are analyzed under the “rule of reason” approach by inquiring whether the combination “likely harms competition by increasing the ability or incentive profitably to raise price above or reduce output, quality, service, or innovation below what likely would prevail in the absence of the agreement.”¹⁰⁶ The agencies have considerable discretion in determining whether the collaboration fails under the “rule of reason” analysis.¹⁰⁷

Whether an MTHC could be analyzed under merger or anti-competition law depends on the facts of each particular case. Potential collaborators in the United States should consider the risk of antitrust scrutiny before proceeding.

3. Absence of Single Entity Defense

One of the main tenets of Section 1 of the Sherman Act is that it requires a plurality of actors.¹⁰⁸ Due to that limitation, related entities sometimes escape antitrust liability on the basis of the “single entity defense.” Under this defense, established by the U.S. Supreme Court in *Copperweld v. Independence Tube*, merging companies may claim that their close relationship prior to the merger renders the antitrust claim impossible.¹⁰⁹ According to *Copperweld*, there can be no intra-enterprise conspiracy between an entity and its wholly owned subsidiary.¹¹⁰ The question arises whether that case would be limited only to a parent and its wholly

104. *Id.* (According to the Guidelines, the typical period for which a collaboration is expected to terminate is ten years.).

105. *Id.* at § 3.1 (If a collaboration is determined to be so anti-competitive that it is *per se* illegal, there is no need to scrutinize it under the less strict, “rule of reason” approach.).

106. *See id.*

107. *Id.*

108. *See* Brown, *supra* note 82, at 219; the Sherman Act, *supra* note 85.

109. *See* Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 771 (1984).

110. *Id.* *See* Michael D. Belsley, *Comment: The Vatican Merger Defense—Should Two Catholic Hospitals Seeking to Merge be Considered a Single Entity for Purposes of Antitrust Merger Analysis?* 90 Nw. U. L. Rev. 720, 739-742 (1996).

owned subsidiary or would be expanded to allow less closely related entities to assert the defense. As discussed earlier, an MTHC is jointly owned by multiple unrelated parents. Because the parent companies and the MTHC have separate structures, and independent board members and officers, it may not be possible for the owners of the MTHC to assert successfully the single entity defense.¹¹¹

4. U.S. Reporting Requirements

Combining entities in the United States also may be required to notify the Federal Trade Commission (FTC) and the Antitrust Division of the Department of Justice (DOJ) before contributing substantial trademark assets to and acquiring their respective shares of an MTHC.¹¹² The Hart-Scott-Rodino Act requires a 30-day advance notification to the FTC and DOJ generally for proposed mergers involving assets worth more than a certain threshold amount.¹¹³ IP qualifies as an asset covered by the Act.¹¹⁴ The regulations promulgated under the Act require only the parent entities that contribute IP to report.¹¹⁵ A parent is subject to mandatory reporting if, at the time of formation of the IPHC, the parent's percentage of the value of the IPHC exceeds an annually adjusted threshold (currently \$239.2 million).¹¹⁶ The

111. Brown, *supra* note 82, at 231.

112. The Hart-Scott-Rodino Act, 15 U.S.C.S. § 18a (2007).

113. *Id.*

114. Exclusive licenses of patents are reportable under the Hart-Scott-Rodino Act if the two parties are of sufficiently large size and the transaction is considered a legal transfer with a value of \$ 50 million or more. David Balto & Andrew Wolman, *Intellectual Property and Antitrust: General Principles*, 43 IDEA 395, 421 (2003); Antitrust Guidelines for the Licensing of Intellectual Property, § 1.0 (April 6, 1995) [hereinafter Licensing Guidelines] available at <http://www.usdoj.gov/atr/public/guidelines/0558.htm>. See U.S. v. S.C. Johnson Inc. and Bayer AG, 1995-1 CCH Trade Cases 70,884 (1994) (enjoining any exclusive patent licenses between S.C. Johnson and patentees of insecticide chemicals without notification to the U.S. Department of Justice Antitrust Division).

115. 16 CFR § 801.40(a) (2007) provides:

In the formation of a joint venture or other corporation (other than in connection with a merger or consolidation) even though the persons contributing to the formation of a joint venture or other corporation and the joint venture or other corporation itself may, in the formation transaction, be both acquiring and acquired persons within the meaning of § 801.2, the contributors shall be deemed acquiring persons only, and the joint venture or other corporation shall be deemed the acquired person only.

16 CFR § 801.41 (2007) further requires only the parents of the IPHC and not the IPHC itself to file a notification, stating:

Whenever any person(s) contributing to the formation of an entity are subject to the requirements of the Act by reason of § 801.40 or § 801.50 of this chapter, the new entity need not file the notification required by the Act and § 803.1 of this chapter.

116. 16 CFR § 801.40(b) (2007) provides:

parent also may be required to notify the FTC of its intended formation of an IPHC even if its ownership percentage does not exceed the \$239.2 million threshold.¹¹⁷

5. European Anticompetition Laws

MTHCs formed by European parents and/or incorporated in Europe are likely to be subject to European as well as national anticompetition law. The treaty establishing the European Community seeks to encourage competition among companies and to ensure the free flow of goods, services, people, and capital between member states.¹¹⁸ In relevant part, it prohibits “all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the

Unless exempted by the act or any of these rules, upon the formation of a joint venture or other corporation, in a transaction meeting the criteria of Section 7A(a)(1) [of the Clayton Act, currently codified as 15 U.S.C. 18a(a)(1) and requiring that either the acquiring person or the acquired person be engaged in commerce or in any activity affecting commerce] and 7A(a)(2)(A) [currently codified as 15 U.S.C. 18a(a)(2)(A) and requiring that acquiring persons that would hold an aggregate total amount of the voting securities and assets of the acquired person (A) in excess of \$200,000,000 (as adjusted and published for each fiscal year beginning after September 30, 2004, in the same manner as provided in section 8(a)(5) to reflect the percentage change in the gross national product for such fiscal year compared to the gross national product for the year ending September 30, 2003)] (other than in connection with a merger or consolidation), an acquiring person shall be subject to the requirements of the act.

16 CFR § 801.40(b) (2007); 15 U.S.C. § 18a(a) (2007). For adjusted threshold amounts, see 72 Fed. Reg. 2692 (Jan. 22, 2007).

117. 16 CFR § 801.40(c) (2007) provides:

Unless exempted by the act or any of these rules, upon the formation of a joint venture or other corporation, in a transaction meeting the criteria of Section 7A(a)(1) [requiring engagement in commerce or activities affecting commerce] and the criteria of Section 7A(a)(2)(B)(i) [describing the acquiring person’s holdings as in excess of \$50,000,000 (as so adjusted [to \$59.8 million in 2007] and published) but not in excess of \$200,000,000 (as so adjusted [to \$239.2 million] and published)] (other than in connection with a merger or consolidation), an acquiring person shall be subject to the requirements of the act if: (1)(i) The acquiring person has annual net sales or total assets of \$100 million (as adjusted [to \$119.6 million]) or more; (ii) The joint venture or other corporation will have total assets of \$10 million (as adjusted [to \$12 million]) or more; and (iii) At least one other acquiring person has annual net sales or total assets of \$10 million (as adjusted [to \$12 million]) or more; or (2)(i) The acquiring person has annual net sales or total assets of \$10 million (as adjusted [to \$12 million]) or more; (ii) The joint venture or other corporation will have total assets of \$100 million (as adjusted [to \$119.6 million]) or more; and (iii) At least one other acquiring person has annual net sales or total assets of \$10 million (as adjusted [to \$12 million]) or more.

16 CFR § 801.40(c) (2007); 15 U.S.C. § 18a(a) (2007). For adjusted threshold amounts, see 72 Fed. Reg. 2692 (Jan. 22, 2007).

118. Valentine Korah, *The Federal Circuit and Antitrust: The Interface Between Intellectual Property and Antitrust: The European Experience*, 69 *Antitrust L. J.* 801 (2002).

common market.”¹¹⁹ While Article 81, similar to Section 1 of the Sherman Act, is limited to multiple entities, Article 82 allows the European Commission to scrutinize individual companies that abuse a dominant position within the common market.

Though there are certain exceptions allowing for IP transactions, the European Community limits these to technology transfer agreements, which typically only apply to patents, know-how, and software copyrights.¹²⁰ Trademarks are not exempt from the European anti-competition rules, and a combination of trademark rights in an MTHC within the EU may trigger antitrust scrutiny. Moreover, European Community Merger Regulations expand the powers of the European Commission to

119. Treaty establishing the European Community, art. 81, Dec. 29, 2006, Official J. of the E.U. C 321 E/41 provides:

1. The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market, and in particular those which: (a) directly or indirectly fix purchase or selling prices or any other trading conditions; (b) limit or control production, markets, technical development, or investment; (c) share markets or sources of supply; (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage; (e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts. 2. Any agreements or decisions prohibited pursuant to this article shall be automatically void. 3. The provisions of paragraph 1 may, however, be declared inapplicable in the case of: any agreement or category of agreements between undertakings, any decision or category of decisions by associations of undertakings, any concerted practice or category of concerted practices, which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not: (a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives; (b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

120. Treaty establishing the European Community, art. 81(3), Dec. 29, 2006, Official J. of the E.U. C 321 E/41, stating:

The provisions of paragraph 1 may, however, be declared inapplicable in the case of: any agreement or category of agreements between undertakings, any decision or category of decisions by associations of undertakings, any concerted practice or category of concerted practices, which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not: (a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives; (b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

Technology Transfer Block Exemption, Commission Regulation 772/2004, Apr. 27, 2004, 123 OJ L 11.

review mergers and acquisitions that are potentially antitrust violations.¹²¹

6. Corporate Governance and Shareholder Voting

Where the parents are publicly held, the structure of the transaction could determine whether shareholder approval is required in the United States.

Transactions transferring trademark assets to an MTHC may not be subject to shareholder vote. Under the general rule, unless state statute or articles of incorporation provide otherwise, business decisions are not subject to shareholder vote.¹²² While the Model Business Corporation Act (MBCA), upon which many states have based their corporation statutes, expressly states that mergers are subject to shareholder vote, it does not include virtual mergers.¹²³ Hence, unless deemed a “de facto” merger, creation of an MTHC may not require shareholder consent.

A “virtual” merger still may be subject to other statutory provisions requiring a shareholder vote to approve proposals to “sell, lease, exchange, or otherwise dispose” of all or substantially all of the corporate assets.¹²⁴ The MBCA expressly excludes from shareholder approval the transfer of assets only to a wholly owned subsidiary, not to one that is jointly owned.¹²⁵ As the parents typically retain most of their non-IP assets, including any real property, equipment, inventory, etc., when transferring trademark assets to an MTHC, the creation of an MTHC may not include substantially all of the corporate assets. Hence, a shareholder vote is not usually required to create an MTHC.

C. Business Concerns

In addition to the aforementioned legal risks, establishing an MTHC raises serious business concerns. The MTHC is somewhat inflexible to the changing business environment because restructuring may require a substantial number of transactions to wind up the subsidiary business, including assignment of trademarks and other IP, sale of real property, equipment and other physical assets, distribution of profits to shareholders, and revision of employment agreements. The co-branding relationship

121. Charles W. Smitherman III, *The Future of Global Competition Governance: Lessons from the Transatlantic*, 19 Am. U. Int'l L. Rev. 769, 789 (2004); Commission Regulation 4064/89; Commission Regulation 1310/97; Commission Regulation 139/2004.

122. Cohn, *supra* note 99, at 18; Securities Exchange Act of 1934, 15 U.S.C. § 78n (2001).

123. Cohn, *supra* note 99, at 19; Model Business Corporations Act, American Bar Association.

124. *Id.* at 20.

125. *Id.* at 20-21.

has been likened to that of marriage,¹²⁶ the termination of which is known to be complex, especially when there is a child: an MTHC. Accordingly, mere compatibility between the parents may not be sufficient to warrant formation of an MTHC.¹²⁷

III. THE BENEFITS OF IPHCs AND MTHCs

Despite the risks, certain benefits, including the centralized control over IP, arise from the transfer of trademarks to an IPHC enabling more focused efforts to license and enforce,¹²⁸ better managerial oversight,¹²⁹ and more efficient valuation.¹³⁰ The use of IPHCs have also traditionally yielded tax advantages.¹³¹ IPHCs further may add another layer of protection against creditors, litigation, and hostile takeovers.¹³² It should be noted, however, that certain of the advantages described above may not apply in the context of mutual ownership.

A. *Centralized Control of Trademarks and Other IP*

A major benefit of utilizing an IPHC is the consolidation of IP management.¹³³ Many companies fragment their overall IP operation into various responsibilities in different organizations, or otherwise authorize business managers with limited understanding of the potential value of the assets to make decisions regarding their licensing and enforcement. In contrast, the IPHC structure facilitates centralization, increased focus on IP, and greater accountability.¹³⁴ As an independent business without competing priorities, an IPHC seems to elevate the visibility and importance of IP within the overall corporate structure.¹³⁵ Focusing on IP, IPHCs can assist in maximizing the value of IP while minimizing maintenance and enforcement costs.

126. Hurwitz, *supra* note 5, at 379.

127. *Id.* at 381 (suggesting that some form of common control of co-branding participants must exist in order for a franchising alliance to be effective).

128. Xuan-Thao N. Nguyen, *Holding Intellectual Property*, 39 Ga. L. Rev. 1155, 1190 (2005).

129. Lucas, *supra* note 22.

130. Peter L. Faber, *Planning for the Use of Intangibles Holding Companies*, 14 State Tax Notes 1931 (1998); Nguyen, *supra* note 128, at 1190.

131. Chestek, *supra* note 27, at 2.

132. *Id.* at 3 (For a plaintiff to be able to litigate against a defendant parent company with regard to the IP, States generally require the subsidiary IPHC “to be so dominated and controlled by its parent that it is a mere instrumentality or alter ego of the parent”).

133. Dull, *supra* note 16, at 8.

134. *Id.*

135. *Id.*

In addition, dedicating employees solely to IP matters allows for more efficient oversight. IPHCs also allow for greater assessment of the economic benefits of IP.¹³⁶ Separate tracking of expenses and separate profit and loss statements further enable improved current and future valuation of IP.¹³⁷

Use of an MTHC adds another dimension to centralized control. Because the MTHC manages trademark assets of multiple entities, it is possible to align more efficiently the branding goals of the several parents. “Creating a holding company can give all trademark owners a proportional influence on brand investment and brand management decisions.”¹³⁸ Moreover, “[b]rand experience must be delivered consistently to build a dominant brand with the global customer; this requires both a global brand strategy and a highly coordinated execution.”¹³⁹ Though centralized control has not typically served as the primary reason for the creation of wholly owned IPHC subsidiaries, its importance is augmented when the MTHC and its trademark assets are shared.

B. Taxation

Among the principal benefits of employing an IPHC have been certain tax advantages.¹⁴⁰ In fact, until recently, the decision to use an IPHC was largely tax-driven. For example, Volvo was able to avoid paying any taxes on its creation of an MTHC with Ford.¹⁴¹ The structure has the advantage over other IPHCs of further distancing the parent companies from the subsidiary, making it harder for tax authorities to impute the income of parents to them. However, the use of the IPHC for tax planning has become considerably more complex.¹⁴² The nature of the tax benefit could

136. Lucas, *supra* note 22.

137. *Id.*

138. Dorffer, *supra* note 10, at 30.

139. *Id.*

140. Chestek, *supra* note 27, at 2 (“Of the various benefits arising from the establishment of an IP holding company, the greatest is the reduction in the enterprise’s total obligation for state taxes.”); Ashley B. Howard, *Comment: Does the Internal Revenue Code Provide a Solution to a Common State Taxation Problem?: Proposing State Adoption of § 367(d) to Tax Intangibles Holding Subsidiaries*, 53 *Emory L.J.* 561, 565 (2004) (describing avoidance of state income taxes as “the central benefit of the use of the intangibles holding subsidiary.”).

141. Press Release, AB Volvo, Advanced Income Tax Ruling on the Sale of Volvo Cars (Apr. 1999), available at <http://www.volvo.com/group/global/en-gb/newsmedia/pressreleases/1999/pr468.htm>.

142. It is highly recommended that companies hoping to reduce their tax burdens through the use of an IPHC seek the advice of competent tax counsel. See generally Report on IP Holding Company Case Law in the United States, International Trademark Association website, http://www.inta.org/images/stories/downloads/tap_holdingcompany.pdf.

depend upon the jurisdiction(s) in which the parent entities reside and in which the IP is created, the place of incorporation of the subsidiary IPHC, and the particular structure and contractual arrangements.

In certain instances, U.S. companies may be able to avoid federal taxes if the formation of a U.S.-based IPHC is structured as an exchange of assets for stock.¹⁴³ More importantly, many enterprises have been able to save substantial state taxes on royalties and other income by incorporating an IPHC in a state that does not recognize that income, such as in Delaware or Nevada.¹⁴⁴ Placement of the subsidiary outside of the United States may also enable significant tax arbitrage,¹⁴⁵ especially for IP created under the laws of countries other than the United States. Finally, non-United States parents may be able to benefit from other tax advantages.¹⁴⁶

1. U.S. MTHCs

The formation of an MTHC in the United States may result in tax advantages at the federal level initially, followed by long-term tax savings on royalties at the state level. Corporations, whether domestic or foreign, may be able to set up MTHCs in the United States without incurring any U.S. federal taxes under Section 351(a) of the Internal Revenue Code.¹⁴⁷ That Code section requires that the Internal Revenue Service (IRS) not recognize the transfer of property in exchange for controlling stock for income tax purposes.¹⁴⁸ Such exchanges frequently have been employed in the creation of wholly owned IPHCs.¹⁴⁹

Despite the requirement of control, which Section 368(c) of the Internal Revenue Code defines as requiring at least 80 percent of the stock,¹⁵⁰ multiple unrelated entities also may be able to

143. See Part III.B.1., *infra*.

144. *Id.*

145. In this article, “tax arbitrage” is employed to mean intentional tax avoidance; see Part III.B.2., *infra*.

146. See Part III.B.3., *infra*.

147. 26 U.S.C. § 351(a) (2007) providing:

No gain or loss shall be recognized if property is transferred to a corporation by one or more persons solely in exchange for stock in such corporation and immediately after the exchange such person or persons are in control (as defined in section 368(c)) of the corporation.

See Montgomery, *supra* note 14, at 13.2 (explaining that intellectual property likely falls within the meaning of property and that an exchange likely falls within the meaning of transfer in the statute).

148. *Id.*

149. Chestek, *supra* note 27, at 2.

150. 26 U.S.C. § 368(c) (2007).

contribute their U.S. and non-U.S. trademark assets to an MTHC in exchange for stock without incurring any federal tax liability.¹⁵¹ Although neither parent is likely to own more than 80 percent of the MTHC's stock, the concerted contribution by each may qualify under Section 351, which allows "one or more persons" to contribute assets in exchange for joint control of the subsidiary.¹⁵² As a result, the parent companies may be able to provide their pre-existing trademarks to a mutually controlled subsidiary without incurring any U.S. federal tax.

However, there are no federal tax savings on the subsequently generated royalty income, which is recognized as taxable income by the Internal Revenue Code.¹⁵³ The more significant tax advantage of a U.S.-based IPHC traditionally has been its ability to avoid state income taxes through incorporation in tax-free jurisdictions.¹⁵⁴ In certain states, royalty income derived by the IPHC is usually not taxable while, at the same time, the parent companies may deduct those royalty payments as business expenses.¹⁵⁵ Further state tax advantages may arise when income from the MTHC is funneled back to the parent in the form of loans, whose interest payments to the MTHC are deductible,¹⁵⁶ or as domestic dividends.¹⁵⁷

For example, Delaware Investment Holding Companies (DIHCs) engaged exclusively in the maintenance and management of intangible investments located outside of the state are exempt from Delaware income tax.¹⁵⁸ As a result, IPHCs typically have been incorporated in Delaware as DIHCs.¹⁵⁹ However, there may be some risks to trademark rights, as the state's limitation on DIHCs of only permitting management of intangible assets could be perceived as inconsistent with a trademark owner's duty to

151. 26 U.S.C. § 351 (2007).

152. *Id.*

153. 26 U.S.C. § 61(a) (2007) ("Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items . . . (6) Royalties.").

154. Chestek, *supra* note 27, at 2 ("Of the various benefits arising from the establishment of an IP holding company, the greatest is the reduction in the enterprise's total obligation for state taxes."); Howard, *supra* note 140, at 565 (describing avoidance of state income taxes as "the central benefit of the use of the intangibles holding subsidiary").

155. See Del. Code Ann. tit. 30, § 1902(b)(8) (1997); Dull, *supra* note 14, at 8.

156. 26 U.S.C. § 163(a) (2007); George T. Bell et al., *A State Tax Strategy for Trademarks*, 81 TMR 445, 456 (1991).

157. 26 U.S.C. § 243 (2007).

158. Del Code Ann. tit. 30, § 1902(b)(8) (1997) (*available at* http://delcode.delaware.gov/title30/c019/index.shtml#P31_1655); Montgomery, *supra* note 14, at 13.4.

159. Montgomery, *supra* note 15, at 13.4.

actually exercise quality control.¹⁶⁰ It has been suggested that Delaware should be avoided because it may raise a “red flag” for state auditors.¹⁶¹ As an alternative, Delaware also allows for the formation of a Headquarters Management Corporation (HMC) for the lawful purpose of maintaining and managing intangible rights.¹⁶²

Nevada has also established tax laws favorable to MTHCs. The state does not require its corporate residents (or individuals) to pay any income tax whatsoever.¹⁶³

States that do not offer similar tax advantages could still be appropriate places of incorporation for MTHCs if they apply a lower rate of taxation on royalty income.¹⁶⁴ Those that require combined reporting for related entities will not tax the subsidiary on income for which the parent has already paid, and vice versa,¹⁶⁵ and they may still permit the MTHC to avoid state taxation in other states.¹⁶⁶

160. Chestek, *supra* note 27 (describing licensing and enforcement efforts as beyond the mere management of intangibles).

161. Lisi, *supra* note 26 at 414 (suggesting that incorporation of an IPHC in Delaware raises suspicions that the subsidiary structure is a sham, created solely or primarily for tax avoidance, and as such state auditors may likely target those entities).

162. 74 Del. Laws, c. 256 § 1 (2004) *as amended by* 75 Del. Laws, c. 123 § 1 (2005) codified at Del. Code Tit. 30 § 6402 (2007). For 2003 only, a Delaware Headquarters Management Corporation was subject to a four percent tax on its income derived from intangibles. For subsequent tax years, these corporations are subject to a tax of eight point seven percent. Del. Code Tit. 30 § 6403 further provides that: “Copyright, patent, service mark, trademark and trade name royalties (less applicable or related expenses) shall be allocated to this State,” *State Income Tax Strategy*, 1-7 Taxation of Intellectual Property § 7.06 (2006).

163. Nevada Secretary of State website, http://sos.state.nv.us/comm_rec/whyinc.htm (last visited, April 17, 2007); *State Income Tax Strategy*, in 1-7 Taxation of Intellectual Property § 7.06 (2006). In addition, Michigan did not recognize royalties as income until the Michigan Business Tax Act became effective on January 1, 2008. *See* Michigan Business Tax Act, MCLS § 208.1305 (2007); Michigan Single Business Tax Act, MCLS § 208.7 (2007) (repealed 2007).

164. Howard, *supra* note 140, at 563.

165. Lisi, *supra* note 26; Bauman, *supra* note 15, stating:

[O]nly about a dozen states (including California, Illinois, Maine, and New Hampshire) require unitary affiliates to file returns on a combined group basis. Five states—Delaware, Maryland, Pennsylvania, Texas, and Wisconsin—do not permit consolidated returns or combined reporting under any circumstances. The other states that impose corporate income taxes either give affiliated corporations the option of filing separate returns or electing to file a state consolidated return (e.g., Alabama, Florida, Georgia, Massachusetts, and South Carolina), or generally allow affiliated corporations to file separate returns but under certain conditions may require or permit the filing of a combined unitary report (e.g., New Jersey, New York, North Carolina, and Virginia).

166. *State Income Tax Strategy*, 1-7 Taxation of Intellectual Property § 7.06 (2006):

Partial benefits may be obtained by establishing the [IPHC] in one of these states. Since the [IPHC] will be included in the combined report in a unitary state regardless of what state it is located in, it is tax neutral to place the [IPHC] in the unitary state.

Incorporation of the subsidiary in the same state as its parent may offer additional advantages. For example, the existing infrastructure of the parent may be utilized to provide office space and resources to the MTHC. Also, there is an increased likelihood that the MTHC will be regarded by state tax commissions as a legitimate business entity,¹⁶⁷ which can be an important factor in avoiding taxation in other states.

Despite the historic availability of state tax benefits, a U.S. MTHC may still be susceptible to taxes on its royalty income in states other than the state in which it was incorporated.¹⁶⁸ Non-resident U.S. IPHCs have been held liable for income tax through the finding of an “economic nexus” with their licensed products sold within the state.¹⁶⁹ Determinations that the relationship between the IPHC and its parent company is a “sham,” lacking any real purpose or substance, have also resulted in tax liability.¹⁷⁰

Increasingly, state courts have recognized the “substantial nexus” necessary between out-of-state IPHCs and their licensed products in the state to permit taxation under the Commerce Clause of the U.S. Constitution.¹⁷¹ These opinions adopt a

At the same time, the income earned by the [IPHC] would not be taxed in separate company reporting states where the taxpayer is subject to tax unless the state disallows the related party expenses deducted by the taxpayer. . . . Nevertheless, two unitary states do have measures that preclude taxpayers from deducting royalty payments made to related entities outside the combined report. 35 Ill Laws Cons Stat 5/203; Ore Admin Code § 150-314.295. These measures are intended to prevent taxpayers from obtaining a tax benefit for royalties paid to non-US related parties (in both states, only US entities are included in the unitary group. This is commonly referred to as “the water’s edge.”

167. Faber, *supra* note 130, at 1934; John E. Gaggini, *State Taxation of Passive Income Subsidiaries*, 540 PLI/TAX 169, 179 (2002).

168. *Geoffrey, Inc. v. S.C. Tax Comm’n*, 437 S.E.2d 13 (S.C. 1993), *cert. denied*, 114 S. Ct. 550 (1993); Diehl, *supra* note 18, at 44; Montgomery, *supra* note 15, at 13.5; Bauman, *supra* note 15, at 38.

169. See *Geoffrey*, 437 S.E.2d at 13; Bauman, *supra* note 15, at 38; Michael A. Lisi, Trademark Ownership, and Creation of an IP Holding Company, Presentation at the Annual Meeting of the International Trademark Association (2000) (on file with author) (describing three separate bases for a finding of nexus: (1) the presence of IP and accounts receivable in the taxing state; (2) the parent conducting activities in the taxing state as an agent of the IPHC; (3) the employees of the IPHC performing functions in the taxing state); *State Income Tax Strategy*, 1-7 Taxation of Intellectual Property § 7.06 (2006) (“This nexus of taxing the [IPHC] has been adopted primarily by regulations in Arkansas, Florida, Iowa, New Jersey, Massachusetts, Oklahoma and Wisconsin. Also, in addition to the *Geoffrey* case in South Carolina, courts in New Jersey, New Mexico, Oklahoma and North Carolina, and Louisiana have issued opinions allowing taxation of the out-of-state entity.”).

170. *Syms Corp. v. Comm’r of Revenue*, 765 N.E.2d 758 (Mass. Sup. Jud. Ct., 2002); *Comptroller of the Treasury v. SYL, Inc.*, 825 A.2d 399 (Md. 2003); *Sherwin-Williams Co. v. Tax Appeals Tribunal*, 784 N.Y.S.2d 178 (App. Div. 3d Dept., 2004), *appeal denied*, 4 N.Y.3d 709 (2005); *but see Sherwin-Williams Co. v. Commissioner of Revenue*, 778 N.E.2d 504 (Mass. 2002).

171. *Geoffrey*, 437 S.E.2d at 13; *Kmart Properties, Inc. v. Taxation and Revenue Department of New Mexico*, 131 P.3d 27 (N.M. Ct. App. 2001), *cert. granted*, 40 P.3d 1008

“business situs theory wherein the presence of [IP] is sufficient to justify the substantial nexus between the taxing jurisdiction and the foreign [IPHC].”¹⁷² That is to say, they find that an “economic nexus” is “substantial” enough to enable taxation beyond state borders.¹⁷³ It has been argued, however, that this categorical assignment of a business situs to IP wherever the products associated with them are sold may violate the Commerce Clause of the U.S. Constitution.¹⁷⁴ In applying this doctrine, courts would not likely distinguish between wholly owned IPHCs and jointly owned MTHCs. Unless the U.S. Supreme Court declares the finding of substantial nexus based solely on IP an unconstitutional over-extension,¹⁷⁵ U.S. IPHCs must beware of the possibility of taxation in states other than where they were incorporated.

Other states have successfully challenged the wholly owned IPHC structure as a sham corporation or phantom entity,¹⁷⁶ claiming the parent and subsidiary have “no real economic substance as separate business entities.”¹⁷⁷ However, states may find it difficult to characterize MTHCs as sham corporations because they are less closely related to their parents than those

(N.M. 2002), *cert. quashed*, 131 P.3d 22 (N.M. 2005); *Lanco, Inc. v. Dir., Div. of Taxation*, 908 A.2d 176 (Sup. Ct. N.J. 2006), *cert. denied*, No.06-1236 (June 18, 2007); *Geoffrey v. Tax Commission*, 132 P.3d 632 (Ok. Ct. Civ. App. 2005); *A&F Trademark, Inc. v. Sec’y of Revenue*, 605 S.E.2d 187 (N.C. App. 2004), *aff’g* *Sec’y of Revenue v. A&F Trademark, Inc.*, N.C. Sup. Ct., Wake City (May 22, 2003); *J.C. Penney Natl. Bank v. Johnson*, 19 S.W.3d 831 (Tenn. Ct. App., 1999); *America Online v. Johnson*, No. M2001-00927-COA-R3-CV, 2002 Tenn. App. LEXIS 555 (Tenn. Ct. App. 2002); *Dept. Rev. v. Gap*, 886 So. 2d 459 (La. Ct. App. 1st Cir. 2004); *but see* *Acme Royalty Co. v. Director of Revenue*, 96 S.W.3d 72 (Mo. 2002).

172. Nguyen, *supra* note 128, at 1180.

173. Andrew W. Swain, *A Taxing Question*, 15 Bus. Law Today 51 (2006).

174. Nguyen, *supra* note 128, at 1181-84; David Cowling, *Nexus from Intangibles—Geoffrey*, 10 State Tax Notes 129 (1996); Craig J. Langstraat, *Economic Nexus: Legislative Presumption or Legitimate Proposition?* 14 Akron Tax J. 1, 23 (1999); Diehl, *supra* note 18, at 44.

175. Thus far, the Supreme Court has denied *certiorari* in all cases that raised the issue since its decision in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), which subsequent lower court decisions have argued does not apply to income taxes. *See* Diehl, *supra* note 18, at 46; *see* Swain, *supra* note 173.

176. States including Massachusetts, Maryland, and New York, have found IPHCs, often consisting only of a post office box and a single part-time attorney or paralegal, to be sham corporations that exist only in name for the unlawful avoidance of state taxes; *Syms Corp. v. Comm’r of Revenue*, 765 N.E.2d 758 (Mass. Sup. Jud. Ct. 2002); *Comptroller of the Treasury v. SYL, Inc.*, 825 A.2d 399 (Md. 2003); *Sherwin-Williams Co. v. Tax Appeals Tribunal*, 784 N.Y.S.2d 178 (App. Div. 3d Dept. 2004), *appeal denied*, 4 N.Y.3d 709 (2005). *But see* *Sherwin-Williams Co. v. Commissioner of Revenue*, 778 N.E.2d 504 (Mass. 2002).

177. Diehl, *supra* note 19, at 45 (quoting *Comptroller of the Treasury v. SYL* and *Comptroller of the Treasury v. Crown Cork & Seal Company (Delaware), Inc.*, SYL, 825 A.2d 399 (Md. 2003)); Bauman, *supra* note 15 (describing judicial doctrines requiring economic substance and business purpose under *Gregory v. Helvering*, 293 U.S. 465 (1935)).

that are wholly owned.¹⁷⁸ An MTHC is far more likely to have a real purpose beyond that of tax avoidance if it oversees use and the enforcement of shared trademark rights. Nonetheless, states may attempt to counteract the tax advantages by other means, including: (1) pursuing the parent company's deductions;¹⁷⁹ (2) requiring consolidated reporting;¹⁸⁰ and/or (3) utilizing apportionment formulas.¹⁸¹

Congress has thus far been unsuccessful in addressing the disparity among the states concerning non-resident domestic IPHC taxation.¹⁸² Along with several predecessor bills, the U.S. Business Activity Tax Simplification Act of 2007 proposed to amend 15 U.S.C. § 381 to remove the jurisdiction of states to levy income tax against businesses not physically present in the state.¹⁸³ It would have allowed IPHCs that cannot be characterized as sham

178. Nguyen, *supra* note 128, at 1192-3 (“Evidence of a sham arrangement may include the parent company holding majority control of the stock in an IP holding company. . . .”).

179. States sometimes seek the parent or related company's deductions. *State Income Tax Strategy*, 1-7 Taxation of Intellectual Property § 7.06 (2006); Ohio Rev. Code § 5733.042 (1991); Conn. Gen. Stat. § 12-218c (1998); Ala. Rev. Stat. § 40-18-35 (2001); Miss. Code Ann. § 27-7-17(2) (2001); N.C. Gen. Stat. § 105-130.7A (2001); N.J. Rev. Stat. § 54:10A-4.4 (2002); Mass. Gen. Law, Ch. 63, §§ 31I and 31J (2003); N.Y. Tax Law § 208(9)(O) (2003); Ark. Code § 26-51-423(g)(1) (2003); D.C. Code § 47-1803.03(b)(7)(A); Ga. Code § 48-7-28.3, *as amended by* Ga. HB 191; Ky. Rev. Stat. § 141.205(2) and (4), *as amended by* Ky. HB 272; HB 297, codified at Ch. 56, Md. Tax-Gen Code Ann. §§ 10-109 and 10-306.1; Va. Code § 58.1-402. *See also* 35 ILCS 5/203 (D-17) and (D-18); Or. Admin Code R 150-314.295; 2005 SCH 3767. *See* Faber, *supra* note 130, at 1933; Nguyen, *supra* note 128, at 1192; Diehl, *supra* note 18, at 46; and Bauman, *supra* note 15.

180. Other states have required consolidated reporting of parents and affiliates on tax returns to eliminate the shifting of income outside of the jurisdiction. *State Income Tax Strategy*, 1-7 Taxation of Intellectual Property § 7.06 (2006). *But see* Nguyen, *supra* note 128, at 1193-94 (“States cannot tax the royalty income when the [IPHC] is a legitimately separate business entity.” Therefore, combined reporting may not be applicable to jointly held MTHCs, which have less difficulty than wholly owned IPHCs in justifying their separateness from parent companies.)

181. An additional concern regarding the taxation of non-resident domestic IPHCs is the use of apportionment formulas by several states. Lisi, *supra* note 26, at 416. However, several states elect to consider only the single factor of licensing activities when calculating apportionment for holding companies. IPHCs lacking any non-IP assets or operations in a particular state may be subject to higher taxes there. Incorporation of the IPHC as a DIHC, where strict limitations on the business' functions and properties are imposed, does not likely protect it from such unbalanced apportionment by other states. Chestek, *supra* note 27. *But see* Del. Code Tit. 30 § 6403 (apportioning state taxes for Delaware Headquarters Management Corporations based on the average of three ratios between in-state and total values: (1) real and tangible personal property, (2) compensation paid, and (3) revenues from sales of personal property and other gross income without regard to IP royalties. Based on this apportionment formula, a Delaware Headquarters Management Corporation serving as an IPHC might be able to pay all of its state taxes to Delaware.)

182. Business Activity Tax Simplification Act, S. 1726, 110th Cong. (2007); S. 2721, H.R. 1956, 109th Cong. (2006); H.R. 4845, 109th Cong. (2005); S. 2721, 109th Cong. (2005); H.R. 3220, 108th Cong. (2003).

183. *Id.*

corporations to avoid taxation based solely on their economic nexus with a state.¹⁸⁴

From a practical perspective, companies seeking to form domestic MTHCs should consider taking several precautions with the help of tax counsel.¹⁸⁵ First, corporations should expressly formulate the non-tax-related, business purposes for incorporating the MTHC.¹⁸⁶ Second, MTHCs should establish a substantial, independent presence in their states of incorporation, with their own locations, staff, bank accounts, executives, and boards of directors.¹⁸⁷ Third, they should execute license agreements in their home states under that state's law.¹⁸⁸ They also should seek independent valuations in order to set arm's-length rates on licenses back to their parents, and seek to license to third parties, as well.¹⁸⁹ Next, they should perform and pay for all maintenance of trademarks and other IP.¹⁹⁰

Aside from the potentially unconstitutional application of the economic nexus doctrine, and the need to take great care in the establishment of domestic IPHCs, the risk of state taxation seems lower for those IPHCs that are commonly owned. In any event, because uncertainty exists, many companies may prefer to move their trademarks to offshore subsidiaries.

2. Incorporation of a Non-U.S. MTHC

For U.S. companies, the risks of establishing a domestic IPHC subsidiary have resulted in a trend toward incorporating IPHCs abroad for the limited purpose of holding their foreign IP.¹⁹¹ By transferring non-U.S. IP to a subsidiary incorporated in a non-U.S. jurisdiction where little or no tax is imposed on royalty income, U.S. parent companies may be able to avoid or defer recognition of

184. *Id.*

185. Richard W. Giuliani, *Intellectual Property Holding Companies: Current Tax Issues*, Presentation at the Conn. Intell. Prop. Law Assoc. (December 2, 2003).

186. Lisi, *supra* note 26, at 415; Montgomery, *supra* note 15, at 13.3.

187. Giuliani, *supra* note 185; Lucas, *supra* note 22; Montgomery, *supra* note 15, at 13.2.

188. Giuliani, *supra* note 185.

189. *Id.*

190. *Id.*

191. Howard, *supra* note 140, at 567-8; Avi M. Lev, *Offshore Migration of U.S. Intellectual Property: An Unintended Effect of Transfer Pricing Regulations*, 28 Tax Notes Int'l 285, 285 (2002); John I. Forry, "Domiciling Intellectual Property Overseas," presented to the Joint Intellectual Property Entertainment and Media Law Committee Meeting of the New York County Lawyers' Association, Oct. 16, 2007 (recommending transfer of foreign IP rights to an offshore IPHC).

income.¹⁹² However, U.S. federal tax laws attempt to discourage this offshore migration by offsetting the deferral with imputed income. Thus, consultation with an experienced tax attorney is recommended.

The U.S. Internal Revenue Code normally does not recognize the transfer of intangibles in exchange for controlling stock as taxable gain under Section 351.¹⁹³ However, U.S. transfer-pricing provisions under Section 367(d) may deem the offshore migration as a taxable sale rather than a non-recognition transaction.¹⁹⁴ As a result, the domestic parent is required to include in its annual income fictitious payments called “super royalties,” for the useful life of the IP up to 20 years.¹⁹⁵ Subject to retrospective yearly adjustment by the IRS to reflect “arm’s length rates” based on the actual income earned through the use of the IP, these amounts essentially offset the deductible royalty payments by adding equivalent sums back to the parent’s taxable income.¹⁹⁶

While Section 367(d) effectively eliminates some real tax benefits in the contribution of IP to a wholly-owned IPHC abroad, it is questionable whether application of that section may be avoided when the subsidiary is jointly owned. Where a U.S. entity does not transfer intangible property to a foreign corporation in an exchange described in Section 351 or Section 361, Section 367(d) does not apply.¹⁹⁷ Though Section 351 normally applies to MTHCs where the parent entities’ concerted contribution of trademarks results in the requisite control of the newly created MTHC, the creation of the foreign subsidiary prior to any contribution of trademarks by a U.S. parent, which on its own receives less than a

192. Montgomery, *supra* note 15, at 13.7. Additional federal tax savings may be available to U.S. parents that share the costs of developing IP assets other than trademarks with a foreign IPHC. See Lev, *supra* note 191, at 288.

193. 26 U.S.C. § 351 (2007).

194. Howard, *supra* note 140, at 569; Montgomery, *supra* note 15, at 13.3; Tira Greene & Michael Ward, *Offshore Corporations*, Intell. Prop. Assets in Mergers and Acquisitions 14.1, 14.2-14.3 (L. Bryer ed., Wiley 2002) (describing “a tendency to attribute value to intellectual property leaving the [high-taxing] country and tax the value as though it were a disposition, whether an actual disposition takes place or not. This concept is employed in the United States and Canada.” The authors therefore advocate isolating U.S. income from that earned worldwide and bringing IP offshore “before it even exists” or at least early in the development cycle.). Professor John Forry similarly recommends transfer of only foreign IP rights to offshore entities. Forry, *supra* note 191.

195. Howard, *supra* note 140, at 569-70; Montgomery, *supra* note 15, at 13.8.

196. *Id.*

197. 26 U.S.C. § 367(d)(1) (2007); Bruce N. Davis, *U.S. Taxation of Foreign Joint Ventures*, 46 Tax L. Rev. 165, 189 (1991); Howard, *supra* note 140, at 583; § 361 is inapplicable here unless both the subsidiary and parent are parties to a plan of reorganization; 26 U.S.C. 361 (2007).

controlling share of the MTHC, may not be subject to Section 351 in certain special circumstances.¹⁹⁸

If the IP does not yet have a high value, an alternative is to sell it to the MTHC at an arm's-length price, rather than be subject to continuing "deemed royalties" to the U.S. parent under Section 367(d).¹⁹⁹ Where the IP has not yet been developed in a new, non-U.S. market, a U.S. parent and its foreign MTHC may be able to enter into a cost-sharing agreement in which the MTHC develops and owns the non-U.S. IP while the U.S. parent reduces its income tax by limiting the amount of income imputed to it.²⁰⁰

Aside from the initial transfer of trademarks by the parent, royalty income collected by the foreign MTHC may be subject to taxation in its home country as well as being subject to taxation against the U.S. parent.²⁰¹ If U.S. IP is transferred and then licensed back to the U.S. parent, U.S. withholding tax against the U.S. parent may be avoided if the MTHC is placed in a country that has an income tax treaty with the United States.²⁰² However, with the addition of a provision to all U.S. tax treaties restricting third-party benefits, MTHCs in non-treaty countries can no longer take advantage of U.S. tax treaties by licensing U.S. trademarks to an affiliate in a treaty country, which in turn sublicenses them to the U.S. parents.²⁰³

The key to the most effective limitation of income taxes applied against a U.S. parent and/or its foreign IPHC subsidiary

198. See Davis, *supra* note 197, at 192-196 (describing means by which U.S. parties to foreign joint ventures can avoid U.S. source income treatment resulting from 26 U.S.C. 367(d)). But see 26 U.S.C. § 482 (2007) (providing that the amount for which a U.S. parent sells its IP to the foreign IPHC may be subject to adjustment to "arm's length rates" for federal tax purposes if the companies are under common control). See Montgomery, *supra* note 15, at 13.7 (describing the different methods of assessing arm's length rates and the substantial penalties for failing to accurately meet the standard); Treas. Reg. § 1.482 (as amended in 2003). See also Dr. Harold McClure, *Alternative Approaches To Determining An Arm's Length Royalty Rate*, 43 *Idea* 111, 112 (2002). See also Davis, *supra* note 197, at 205-6 (warning that common control may exist even if the U.S. parent does not own a majority interest in the foreign subsidiary and proposing that in the absence of common control, the U.S. parent can sell its IP to the foreign subsidiary for a reduced price in order to avoid a taxable gain. However, concerns regarding double taxation may compel the company itself to assert that it has such control).

199. See Forry, *supra* note 191 (Professor Forry suggests that low-value IP can be sold to an MTHC to avoid imputed royalties).

200. See *id.*

201. See Davis, *supra* note 197, at 209-10. See generally Keith Engel, *Tax Neutrality to the Left, International Competitiveness to the Right, Stuck in the Middle with Subpart F*, 79 *Tex. L. Rev.* 1525 (2001); J. Clifton Fleming, *Exploring the Contours of a Proposed U.S. Exemption (Territorial Tax System)*, 41 *Tax Notes Int'l* 217 (2006); Montgomery, *supra* note 15, at 13.8 (describing a 30 percent withholding tax imposed on the parent making royalty payments to the foreign licensor).

202. Montgomery, *supra* note 15, at 13.9; Forry, *supra* note 191.

203. See Davis, *supra*, note 197.

on exploitation of non-U.S. IP appears to be the determination under the Internal Revenue Code and Treasury Regulations of whether the non-U.S. subsidiary entity is a “Controlled Foreign Corporation” (CFC).²⁰⁴ Passive income of a CFC is taxed as if it were distributed to the U.S. parent. However, exceptions exist for income from certain types of foreign entities that have most of the beneficial characteristics of corporations, but who under the so-called “check-the-box regulations,” may choose their classification for U.S. tax purposes.²⁰⁵ If, as in the case of Volvo and Ford, the MTHC is not a CFC because it is not owned more than 50 percent by U.S. shareholders, then the passive income rules do not apply.

Running an IPHC from abroad does not necessarily avoid U.S. state taxes. In *Zebra Technologies v. Topinka*, the U.S. district court affirmed that a parent corporation had to include income earned by its two IPHCs, which were incorporated in Delaware and headquartered in Bermuda, in its Illinois combined state income tax return, because substantial business activity relating to development, protection, and quality control of intellectual property took place in the United States.²⁰⁶ Most states, however, tend to follow federal law regarding their treatment of non-U.S. entities’ international income.²⁰⁷

Regardless of the methods employed to migrate trademarks and other IP abroad, serious consideration must be given to determining in which country to establish the MTHC, preferably with the assistance of local and international tax and trademark counsel. Some offshore jurisdictions operate as pure tax havens, where neither persons nor corporations, whether local or foreign, are subject to income tax.²⁰⁸ These are believed to provide greater flexibility in exploiting trademarks and other IP.²⁰⁹ Non-pure tax havens, on the other hand, distinguish between local entities and certain special categories of foreign entities; and as a result, they

204. A controlled foreign corporation is any foreign corporation in which more than 50 percent of the total combined voting power of all classes of stock entitled to vote is owned directly, indirectly, or constructively by U.S. shareholders on any day during the taxable year of such foreign corporation or more than 50 percent of the total value of the stock is owned directly, indirectly or constructively by U.S. shareholders on any day during the taxable year of the corporation. 26 § C.F.R. 1.957-1 (2007).

205. 26 C.F.R. § 7701 (2007). The U.S. parent can reduce double taxation by claiming a foreign tax credit upon repatriation of the earnings under 26 U.S.C. § 902 if it owns at least 10 percent of the voting stock in the foreign venture. 26 U.S.C. § 902(a)(1) (2007); U.S. parents of foreign IPHCs may further benefit by the enactment of federal tax reforms which cease to recognize as passive income of a CFC dividends paid by foreign affiliates to their foreign CFC. See Tax Notes Intl, Vol. 41, No. 2 (January 16, 2006).

206. *Zebra Tech. Corp. v. Topinka*, 799 N.E.2d 725 (1st Dist. 2003).

207. Forry, *supra* note 191.

208. Greene, *supra* note 194, at 14.1.

209. *Id.*

have been targeted by the Organization for Economic Cooperation and Development's (OECD) campaign against harmful tax regimes.²¹⁰ Most jurisdictions will likely have their own federal income taxes in addition to local taxes and withholdings of taxes on distributions abroad, all of which may apply differently depending on the corporate structure utilized.

Some of the most popular foreign sites to which U.S. companies have transferred their trademarks and other IP are Bermuda, the Cayman Islands, Barbados, Ireland, Hong Kong, Mauritius, and Singapore.²¹¹ In these jurisdictions, the enterprises commonly employ a multi-tier structure in which the IPHC does not license back to the parent, but rather licenses to a subsidiary in a third country. The subsidiary collects royalties from other foreign subsidiaries who sell products identified by the trademarks and protected by other IP.²¹²

When a U.S. entity seeks to acquire non-U.S. trademarks and/or other IP to be exploited in non-U.S. markets, a foreign IPHC may be employed in order to protect against high U.S. tax rates.²¹³ A typical jurisdiction is the Netherlands Antilles, which has an advance tax ruling system and an extensive tax treaty network.²¹⁴ Switzerland also has been called "one of the most favourable jurisdictions in which to establish [a] holding [company]."²¹⁵ Danish holding companies are not subject to any tax

210. *Id.* The OECD is an organization of 30 national governments which share information in order to promote world trade and economic development; see generally, OECD website, http://www.oecd.org/pages/0,3417,en_36734052_36734103_1_1_1_1_1,00.html.

211. Stepping Up and Withdrawing from Crusade Against Tax Evasion, 1-Intro Tax Havens of the World 9 (Matthew Bender 2005); Mauritius has a growing number of double taxation treaties, particularly with Asian countries. It taxes corporations at a flat rate of 15 percent and has no capital gains or withholding taxes. See Naiken Gopalla, *Mauritius and Africa Investments*, Bright Ideas, Fall 2007, at 8; Forry, *supra* note 191. See also Elisabeth A. Langworthy, *Tax Planning and Structuring Strategies for Global Trademark Portfolios*, INTA Bulletin, Vol. 63 (February 1, 2008) (describing some of the pros and cons of setting up IPHCs in Ireland or Brazil).

212. *Id.*

213. Montgomery, *supra* note 15, at 13.10.

214. *Id.* The percentage of total receipts of CFCs by country of incorporation for Tax Years 1988 and 2002 shows that the Netherlands increased the most, from 4.4 percent to 11 percent. Internal Revenue Service, Statistics of Income Studies of International Income and Taxes, available at <http://www.irs.gov/pub/irs-soi/intertax.pdf>. For a discussion of the tax benefits of incorporating an IPHC in the Netherlands, see 2-Netherlands Antilles and aruba Foreign Tax & Trade Briefs § 1. See also Danish Holding Companies, <http://www.lowtax.net/lowtax/html/offon/denmark/denadv.html> (last visited, March 8, 2007) (comparing Danish with Dutch holding companies). See Greene, *supra* note 194, at 14.2 and 14.9.

215. See Christian H. Kalin, *Swiss Companies in International Tax Planning*, Tax Planning Intl. (2005); MB Group GmbH Business Dialog Website, <http://www.business-dialog.com/holding-company.htm>; Thierry Boitelle, *Switzerland increasingly popular in US Tax Planning*, http://www.amcham.ch/publications/content/us_tax_planning.pdf; Toni Amonn, Taxation of Companies in Switzerland (2004), <http://www.taxation.ch/index.cfm/fuseaction/show/temp/default/path/1-535.htm>.

on the issue or transfer of shares, but the cost of incorporation through an agent can be \$4,000 or more, and can take 8-14 weeks if a more expensive off-the-shelf company is not employed.²¹⁶ Until very recently, Malta allowed the creation of foreign-owned “International Trading Companies,” which were entitled to preferential tax treatment with an effective rate of 4.17 percent.²¹⁷

3. Non-U.S. Parents

If a non-U.S. MTHC is wholly or majority owned by non-U.S. parents, then royalties or other income from its exploitation of non-U.S. IP may not be subject to U.S. taxation. Thus, utilization of the MTHC structure may still facilitate substantial tax savings for non-U.S. parents in their home countries and abroad.

However, as a result of the advanced globalization of business activities, other developed nations aside from the United States may begin to implement similar strategies to tax income from intangibles located outside of the country. For instance, the Japanese tax authorities have published revised Transfer Pricing Administration Guidelines, which suggest attribution of income to a Japanese company that developed certain intangibles including brands when foreign related parties earn profits based on those intangibles.²¹⁸

C. Protection from Creditors, Litigation, and Hostile Takeover

Vesting ownership of trademarks in an MTHC may also shield them from the parent companies’ creditors, insulate the parent entities from liability, and/or protect the parents from hostile takeovers.²¹⁹ As parents are mere licensees, whose licenses may be structured to prevent transfer, and/or automatically terminate in anticipation of bankruptcy,²²⁰ their creditors cannot usually obtain

216. Danish Holding Companies, <http://www.lowtax.net/lowtax/html/offon/denmark/denadv.html> (last visited, March 8, 2007) (describing Denmark’s withholding tax on trademark and some other types of IP royalties and characterizing the country as among the top 10 worldwide jurisdictions in terms of the number of double taxation treaties negotiated).

217. <http://www.lowtax.net/lowtax/html/jmacos.html>. Income in Malta is currently taxed at 12% or less.

218. See Yoshiyasu Okada, *Japan Tax Update: Transfer Pricing Issues and Intangible Assets*, Int’l Fin. & Treasury, Nov. 15, 2007 at 1, 17.

219. Chestek, *supra* note 27, at 3; Howard, *supra* note 140, at 566.

220. For a detailed treatment of the ways in which the anti-assignment and automatic termination clauses of IP licenses may be upheld even in the event of bankruptcy, see William M. Goldman & Charles G. Klink, *Bankruptcy and Intellectual Property in Intell. Prop. in the Global Marketplace Volume II: Commercial Exploitation and Country-by-Country Profiles* 28.20 (M. Simenksy, L. Bryer, & N. Wilkof eds., Wiley 1999).

the licensed rights, let alone the trademark assets themselves. Furthermore, because the MTHC owns the trademarks and warrants in its license agreements that it alone has the right to grant licenses on those rights, parent licensees cannot be held liable to third parties for the parent's proper licensed use of such rights. Additionally, potential predator companies face substantial obstacles in their efforts to buy out a parent, whose goodwill is tied to trademark rights owned by a largely independent entity.

IV. CONCLUSION

In its infancy, the concept of IP was primarily about individual ownership, and trademarks denoted a single source. In the interest of avoiding consumer confusion, by definition, trademark law sought to discourage multiple entities from sharing trademarks.

Today, owners may benefit from sharing their trademarks as a result of the growing sophistication of consumers. The law surrounding the use of new and different IP ownership vehicles has been slow to adapt to present-day collaborative practices. Owners have thus found creative ways to allow them to share their trademarks. One way has been the MTHC.

In this era of cooperation and competition among multiple brand owners, MTHCs may provide a sensible means for companies either to partition and sell off portions of their goodwill, or to find opportunities for synergy with others that can help their brands grow. The increased focus and centralized control over trademarks that accompanies employment of an MTHC helps companies to accurately assess and improve the value of these assets, while potentially providing tax and other additional benefits. However, corporate law, tax law, antitrust law, IP law, and other laws may not have been fully adapted to the use of MTHCs. Thus, the decision to employ an MTHC should only be made on a case-by-case basis and only with the advice of experienced counsel.
