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## **Tastes As Good As It Looks: The Quality Function and Product Regulation**

**Intellectual Property**

**Litigation and Dispute Resolution**





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## CHEAT SHEET

- **The quality function of the trademark.** Trademark protection may also prove to be a useful line of argument in the context of ingredients and flavouring bans.
- **The US Supreme Court.** It could be argued the Lanham Act trumps regulatory requirements that require significant modification of branded products.
- **The EU context.** An EU measure seeking to reconfigure consumer products would give great weight to public health interests.
- **International legal protection.** Article 20 of the Trade-Related Aspects of Intellectual Property Rights (TRIPS) Agreement prohibits encumbrances on the use of a trademark in the course of trade.

One of the most important roles of in-house counsel is to closely watch regulatory trends that may affect their companies. This is no less the case when considering consumer goods. When watching for trends, it is wise to take a wide view and consider adjacent industries. Not only does it help avoid being blindsided, but it may also offer some guidance on how to go about developing effective strategies to deal with challenges.

While it is probably wrong to say that every measure that has come to apply to tobacco products will inevitably extend to all other consumer goods, it is probably fair to say that the tobacco industry's experience with regulation offers other manufacturers of consumer goods helpful insight. Particularly relevant is the apparent conflict between public health-based regulation versus IP protection that happened when Australia introduced plain packaging for tobacco products in 2011. The growing requirement to place ever-larger graphic health warnings on tobacco packaging (well over 50 percent of the pack in many jurisdictions) inevitably lead to plain packaging. And plain packaging, in turn, led to litigation before domestic courts, bilateral investment treaty arbitration (alleging expropriation), as well as a dispute resolution panel of the World Trade Organisation to consider whether plain packaging violates international trade rules, including international IP protections under TRIPS.

The driving objective of this new wave of labeling regulation is no longer to warn consumers but rather to make packaging less attractive. The idea is that the product branding should be minimised and replaced by ugly images designed to deter use of the products.

This denormalization policy objective has also begun to emerge in relation to tobacco product regulation. The idea is that risky products should not be marketed in an attractive manner because this arguably minimizes the perception of risk in the mind of the public. Some proponents of this approach would argue that dangerous products that also taste good encourage use so it follows that only unpalatable products should be permitted. Some countries have either banned or are proposing to ban the use of ingredients and flavours on the basis of attractiveness.

Brazil, for example, banned the use of menthol in tobacco products on the basis that menthol might be considered too attractive by certain consumer segments. Germany has banned cigarettes with menthol capsules, [Administrative Court Braunschweig \(Germany\), Press Release, September 26, 2012](#) (translation) on the basis that the innovative flavour capsules were too appealing to consumers. This line of thinking figured very prominently in the EU's work on revising the Tobacco Product

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Directive last year. Earlier drafts of the revised directive called for the outright ban of all flavoured products (including menthol) as well as attractive packaging and product formats such as slims.

No one can seriously question a regulator's power to regulate ingredients used in consumer products. However, this latest tobacco product regulation trend is interesting because it does not require showing that flavourings and other ingredients somehow make products more toxic or dangerous. Indeed the argument is that “attractiveness” itself is toxic. The reasoning is that by making a risky product more appealing, it might make some people smoke more, or more people try smoking or make it harder to quit, which some would argue makes that product potentially more dangerous. This is reminiscent of the attractive advertising class actions cases that have so far been unsuccessful against fast food chains. Similar claims are being made about [the obesity epidemic and the use of sugar](#), high fructose corn syrup and hydrogenated vegetable oils in many consumer goods. Given the growing clamour, there is a risk that this type of regulation may begin to extend beyond the tobacco industry on the basis that by making dangerous or unhealthy consumer products less attractive, consumption patterns can be redirected to healthier alternatives.

Robert Lustig of the University of California, San Francisco, says [sugar should be regulated like tobacco and alcohol](#): “Both of those are toxic and addictive. And we regulate them and we keep them out of the hands of children. Well, sugar meets the same criteria of ubiquity, toxicity, abuse and negative impact on society that tobacco and alcohol also achieve.”

The likely outcome is that these bans may significantly alter the brand experience of many consumer goods. The goodwill of many trademarks will suffer the brunt of this assault, when consumers discover that the brands they know and want no longer guarantee that the related product is indeed the product they know and want. Trademarks on reconfigured products will be converted from guarantees of quality to vehicles for consumer deception and confusion. It is the legal protection afforded trademarks, both domestic and internationally, that may provide the strongest and soundest legal defence against unjustified product regulation. This article argues that this latest wave of product regulation (and the emerging “attractiveness” rationale for such regulation) runs directly against the quality assurance function of trademarks giving rise to both domestic as well as international legal grounds for challenge.

## **The quality function of the trademark**

In jurisdictions that do not benefit from US-style constitutional protection for commercial speech, trademark protection is often the most compelling legal argument against regulatory labelling measures such as plain packaging and large graphic health warnings. As we will see further on, trademark protection may also prove to be a useful line of argument in the context of ingredients and flavouring bans.

When considering the trademark, one good starting point is to consider the following advice: “Of each particular thing, ask: What is it in itself? What is its nature?”

Book 8, Meditation X, Marcus Aurelius.

We might think we understand what a trademark is, but actually what we learn is how it interacts with other things, i.e., what it does. Only from such action can we learn what attributes we can assign to it, and we know these only through their interactions. It's only through interacting with the product to which it is affixed, and through the consumers who purchase those products, that we discover anything about the nature of the trademark. The interaction between the trademark and product

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speaks to origin and differentiation. The interaction between the consumer and the trademarked product speaks to quality.

Almost all trademark scholars define trademarks as indicators of a product's source and as guarantors of its quality. By quality, we mean quality "as perceived by the consumer." This does not refer to the quality or health benefits of the product ingredients. Rather, the quality of the experience to the consumer, with the brand serving as shorthand, and this draws the consumer back to the product instead of alternatives.

The quality function enables owners of brands to create goodwill. Indeed some writers on trademark law have long asserted the importance of the quality assurance function of trademarks stating that "the true functions of the trademark is, then, to identify a product as satisfactory. Indeed as one such writer noted in the *Fordham Law Review* article, "The Quality Assurance Function of Trademarks":

One can readily make the argument that in the world of modern marketing the primary function of a trademark is to indicate degree of quality, and only secondarily to indicate origin or source. Consumers rarely know or care about the origin of a product. ... Their concern is to be able to relate trademarks to their own personal measure of quality. In short, a consumer wishes to match a trademark with what he likes and dislikes. If the origin of a product is of concern to a consumer, it is only because the manufacturer's products have come to be associated with a certain level of quality.

The European Union has also acknowledged the trademark quality function. The EU Court of Justice in its *L'Oréal* case considered whether a trademark may be jeopardized although its function as a source-identifier for the designated goods or services was not affected. The CJEU held that:

[The trademark's] functions include not only the essential function of the trademark, which is to guarantee to consumers the origin of the goods or services, but also its other functions, in particular that of guaranteeing the quality of the goods or services in question and those of communication, investment or advertising.

This trademark extends legal protection to the very product itself. Interference with the product is interference with the brand experience. This, in turn, may come to undermine the brand as a guide enabling consumers to make a choice. In other words, consumers associate a given quality with a brand and react negatively to changes in that promised quality. It is not about the best possible quality, it is about the brand specific quality that consumers care.

## **Attractiveness and the quality function**

Possibly the most compelling legal counterargument against attractiveness-based ingredients bans derives from the quality function of the trademark. In very simple terms, to redesign a product to be "unattractive" by law is to directly encumber and impair the quality function of the trademarks attached to that product.

This is because when a consumer purchases a chocolate bar he or she does so with the understanding that the premium paid is in exchange for a product of the standard and quality warranted by the trademark. This works for premium and non-premium products. There is a minimum guarantee that the product will taste, smell and crunch the way it is supposed to. This is the quality

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function of the trademark at work. It is not so much a matter of whether any given product is of quality or not in terms of the objective (healthful, etc.) attributes of its ingredients, or whether its ingredients are of the highest standard of ingredients of that type (e.g., containing genuine cacao, not cheap sweeteners), but rather if it is the quality that a consumer expects in terms of the consumer experience.

Subjective ingredient bans operate in a manner that directly interferes with the interaction between the product and the consumer. While the consumer may seem unimpeded in differentiating products among manufacturers or in determining origin, that choice is ultimately frustrated because the trademark is impeded from delivering the “quality” signal warranted to the consumer. Indeed, where trademarks can no longer guarantee or signify “quality,” consumers will learn that trademarks do not enable them to relate their past and future consumption experience, and the branded product will be like a good without a trademark.

In many countries, determining the quality of its product in terms of the consumer experience is one of the core rights and obligations of the owner of a trademark. Imposing a certain quality for the product on brand owners deprives them of a core right that comes along with the ownership of a trademark. While the trademark can still be used to distinguish goods from other goods, its function to inform consumers about the quality of the product (and with it the consumer’s desire to repurchase the product he or she “knows,” which represents the value of the goodwill incorporated in the trademark) will be severely impaired.

## **The quality function and product regulation**

Several US courts have considered the trademark quality function in the context of regulatory challenge. For the present purposes, the most interesting is the June 2013 Fourth Circuit Court of Appeals ruling involving a regulatory challenge brought by the American Petroleum Institute. In that case the Court considered the conflict between the protection of trademark quality under the Lanham Act and a North Carolina regulation requiring gasoline to be blended with ethanol. The American Petroleum Institute, on behalf of gasoline brand owners argued that the mandatory modification of branded products threatened the brands. It was argued, among other things, that the change in the fuel blending could damage certain engines and confuse consumers, who had come to expect certain qualities from the brand of gasoline they purchase. This, they argued, would undermine the quality guarantee of their brands. The Court held that the Lanham Act, which codifies US trademark law, could preempt the North Carolina statute due to the interference of the blending law with the quality assurance function of the related trademarks. The Court remanded the case to district court to conduct further fact-finding whether the blending statute has a “significant negative impact” on the supplier’s ability to ensure that blended gasoline bearing their trademarks meets the level of quality needed to safeguard their trademark rights and prevent consumer confusion.

While the case involves the unique US doctrine of “pre-emption” (applicable in the case of conflicts between federal and state legislation), the case supports the view that trademark law not only protects trademark holders from infringement but also from regulatory interference. The case also demonstrates that such protection extends not only to questions of origin, and product differentiation, but also to product quality itself.

The implications of this ruling offer important clarity for all brand owners faced with regulatory driven changes to their products. If the quality of branded gasoline is protected, then so too might many other products with strong brand equity. A mandatory ban on fructose or corn syrup from a breakfast cereal might, for example, benefit from this argument if it could be shown that the removal of the

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ingredient would so change the brand experience of that cereal so as to interfere with the quality assurance function of the related brand. Indeed, if consumers no longer trust their brand of cereal to taste and crunch as they expect, the brand no longer conveys the quality it always has. Under US law, the Lanham Act could be argued to trump such a regulatory requirement.

## **Pom wonderful**

Although it is not a case directly involving the trademark quality function, the recent US Supreme Court ruling in *Pom Wonderful LLC v. Coca-Cola Co.* may provide further clarity. The question before the Court was whether a private action may be brought under the Lanham Act for deceptive labeling and marketing, even when the product's labeling complies with FDA regulations that govern deception and confusion in food labeling. As discussed previously, the protections against misleading trademark use contained in the Lanham Act are the means by which the trademark quality function is protected (or, as the case may be, not protected).

The *Pom Wonderful* case involved a challenge against Coca-Cola's Minute Maid Pomegranate Blueberry juice blend, which although labeled as a blend of those two juices, actually contains 99.4 percent apple and grape juices, 0.3 percent pomegranate, 0.2 blueberry juice and 0.1 percent raspberry juice. The label complied with the US Federal Food and Drug Administration (FDA) regulations that allow juice manufacturers to identify their juice products with a non-primary, characteristic juice. The district court granted summary judgment to Coca-Cola, concluding that the FDA had, through its regulations, spoken directly to the issue. On appeal, the US Court of Appeals for the Ninth Circuit ruled that Pom Wonderful's Lanham Act claim was barred because "as presumption or a general principle," claims under the Lanham Act may not "usurp, preempt or undermine FDA authority."

The US Supreme Court held that the Federal Food, Drug, and Cosmetic Act (FDCA) and the Lanham Act are complementary, and that suits by competitors under the Lanham Act are not precluded by the FDCA. Indeed, the Court stated: "An agency may not reorder federal statutory rights without congressional authorization."

The ruling is important because it stands for the proposition that administrative regulation cannot trump the trademark rights codified by the Lanham Act. Indeed, the outcome of the case is that the Court has, in effect, disallowed a brand owner from using a trademark in a manner that deceives the public as to the nature of the underlying product, even where such deceptive use might comply with federal regulations. It remains to be seen, but wouldn't this reasoning also apply where federal regulation banning the use of "attractive ingredients" renders use of the related trademark deceptive? Brand owners faced with regulatory driven changes to their products might be able to invoke *Pom Wonderful LLC v. Coca-Cola Co.* to argue that regulatory measures may not override Lanham Act legal protections, which include the trademark quality function. A challenge to a ban on a soda colouring, for example, might prevail under this argument if it could be shown that the brand experience was so dramatically changed so as to interfere with the quality assurance function of the related brand.

## **The EU context**

In the European Union, where the parameters of protection afforded the quality function are still under development, the answer is less clear. While the *L'Oreal* case demonstrates the ECJs recognition of the quality function as a stand-alone function, the facts of that infringement case did



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not permit the court the opportunity to explore further. Indeed, as one commentator noted:

In *L’Oreal* the ECJ made it plain that Article 5(1) (a) infringement could arise from damage to any one of the newly specified functions. Despite treating each function separately as potentially conferring a standalone right, the ECJ gave no further guidance on the meaning and scope of these functions.

It is most likely that a case along the lines of the American Petroleum Institute case would have been approached very differently in the European Union. It is likely the Court would have employed a “proportionality” test to weigh the degree of interference with the quality function versus the public interest in requiring gasoline to be blended with ethanol. Under the proportionality test the Court would likely consider whether there were better-tailored and less onerous means of achieving the regulatory goal. The Court would likely query whether there was any regulatory alternative that would interfere less with the rights of brand owners.

In the case of a public health-based measure, the same weighing test would be applied, but with great weight given to the interest in protecting public health. That said, an EU measure seeking to reconfigure consumer products with little or no scientific basis for doing so might not fare as well.

## **Protecting the quality function – international legal protection**

The trademark quality assurance function also benefits from international legal protection. As trademarks on reconfigured products are converted from guarantees of quality to vehicles for consumer deception and confusion, governments that pass such laws risk running afoul of international legal obligations.

One of the most compelling international arguments derives from Article 20 of the Trade-Related Aspects of Intellectual Property Rights (TRIPS) Agreement, which prohibits encumbrances on the use of a trademark in the course of trade.

The use of a trademark in the course of trade shall not be unjustifiably encumbered by special requirements, such as use with another trademark, use in a special form or use in a manner detrimental to its capability to distinguish the goods or services of one undertaking from those of other undertakings.

Encumbrance of the use of a trademark in the meaning of Article 20 refers in its ordinary meaning to any kind of requirement that would have the effect of “impeding” or “hampering” the function of a trademark. As stated earlier, to redesign a product to be “unattractive” by law is to directly encumber and impair the quality function of the trademarks attached to that product. An ingredient ban that changes the product works only to frustrate the choice of consumers when differentiating products among manufacturers or in determining origin because the trademark is impeded (or in the case of plain packaging entirely removed) from delivering the quality of the brand signal warranted to the consumer. These encumbrances on the trademark quality function constitute an encumbrance of the use of a trademark under Trips Article 20.

A measure can only be justified when the member state pursues a goal that is seen as just and suitable to achieve the announced objective. A mere invocation of public policy goals such as public health cannot be considered sufficient justification, as it would open up the possibility to circumvent

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Article 20 by just naming a legitimate goal. In addition to this suitability test, a regulation must be limited to requirements that are not disproportionate or arbitrary.

TRIPs article 20 does not bar governments from banning the use of ingredients in consumer goods in the interest of public health. It does, however, require a robust inquiry as to the justification (“necessity”) of the measure. The complete impairment of the trademark quality function and consequent consumer confusion cannot be justified by a simple invocation of the public health and vague assertions about the “attractiveness” of fast-moving consumer goods.

Any discussion on international legal protection must be done so with the caveat that any rights before domestic courts will depend on the manner and degree by which international obligations are transposed into national law. In some cases individuals will not benefit directly from their nation’s international obligations, and in other cases they will. Regardless, nations that do subscribe to international agreements such as TRIPS can be lobbied to address infringements of those rights by other signatories before technical committees and dispute resolution panels of the World Trade Organization.

## Conclusion

Many consumer goods are facing or will soon face product reconfigurations that will radically change the brand experience for many consumers. The goodwill of many trademarks will be destroyed when consumers discover that the brands they know and want no longer guarantee the quality they expect. Brand owners may claim that trademarks will be transformed from guarantees of quality to vehicles for consumer deception and confusion.

As discussed earlier, the potential for consumer deception, and failure of the quality function, would render trademarks useless. As consumers abandon their brands and good will is destroyed, significant economic impact is certain. Wittingly or unwittingly, brand owners may be regulated into a situation of forced trademark forfeiture, which, in turn, could be argued to be a form of regulatory taking.

Indeed where a product no longer tastes as a consumer expects due to an unjustified ingredient bans, trademark owners are legislated into a situation where they may only use their marks in a misleading or deceptive manner. The result is a forced situation of trademark cancellation and forfeiture. This is most certainly a de facto deprivation of rights giving rise to an inherent right to compensation.

The legal protection afforded trademarks, both domestic and internationally, may promise a sound legal defence against such forms of regulation. Indeed, the direct conflict between product regulation (particularly the emerging “attractiveness” rationale for such regulation), and the trademark quality assurance function, may provide the strongest grounds for both domestic as well as international legal challenge.

## Further Reading

*Hakki v. Zima Company*, No. 03-9183, 2006 WL 852126 (DC Super. March 28, 2006); *Tomberlin v. Adolph Coors Company*, No. 05 CV 545, slip op. (Wis. Cir. Ct. Dane County Feb. 20, 2006); *Eisenberg v. Anheuser-Busch*, No. 1:04 CV 1081, 2006 WL 290308 (ND Ohio Feb. 2, 2006); *Kreft v.*

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*Zima Beverage Co.*, No. 04CV1827, slip op. (Colo. Dist. Ct. Jefferson County Sept. 16, 2005).

Noah D. Genel, "Keep it Real: A call for a broader quality control requirement in trademark law", 8 Ford. Intel Property, Media and Entertainment L.J. 269, 274 (1997).

Schechter, The Rational Basis of Trademark Protection, 40 Harv. L. Rev. 813, 818 (1927).

W. Landes and R Posner, Trademark Law: An Economic Perspective" 30 J.L and Econ. 265 (1987).

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