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## IBM v. Comdisco: Are Modified 3090 Computers Counterfeit?, 13 J. Marshall J. Computer & Info. L. 93 (1994)

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## CASENOTES

# **IBM v. COMDISCO: ARE MODIFIED 3090 COMPUTERS COUNTERFEIT?**

### INTRODUCTION

The recent settlement in *IBM v. Comdisco* seems to preserve the competitive market for IBM 3090 Computers.<sup>1</sup> The 3090 processor supports many of the large scale, high performance mainframe computers<sup>2</sup> upon which modern business depends. In fact, for many applications, there is no realistic alternative to 3090 technology.<sup>3</sup> Its popularity derives in part from the ability of IBM 3090 memory to be readily modified.<sup>4</sup> Adding or removing memory cards, called "reconfiguring,"<sup>5</sup>

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1. Stipulation and Order for Permanent Injunction, *IBM v. Comdisco*, No. 91 C 6777 (N.D. Ill., filed Aug. 30, 1994) [hereinafter Settlement].

Following industry practice, throughout this Comment the acronym "IBM" will be used for the International Business Machines Corporation. The name "IBM" will also be used for the corporation's subsidiaries, including IBM Credit Corporation (ICC), which actually owns and leases most IBM 3090 systems.

2. IBM 3090 computers are among the most powerful computers ever made available in the commercial market. Complaint, *IBM v. Comdisco* (Ct. Chan. Del. filed Jan. 14, 1991) (No. 11922) [hereinafter Complaint (Del.)]. They support databases for large corporate accounts, customer lists, and other significant amounts of information which must be processed rapidly. Answer and Affirmative Defenses at 9, *IBM v. Comdisco* (N.D. Ill. filed Nov. 25, 1991) (No. 91 C 6777) [hereinafter Answer].

3. COMDISCO, INC., THE IBM vs. COMDISCO LAWSUIT: WHAT IT MEANS TO COMPUTER USERS, at 1-8 (1992) [hereinafter Comdisco White Paper].

4. IBM describes this capability as follows:

IBM main memory and expanded storage consists of memory "cards" that are, in turn, mounted in "gates", which are mounted into "frames". The frames, which, along with frames containing other types of components, make up the processor "boxes" in a 3090 system. The actual memory circuits are contained on "chips" that are housed in "modules", which are, in turn, soldered onto the "cards". . . . Main memory boards for the 3090 family come in three capacities — two megabyte cards, four megabyte cards, and eight megabyte boards (*i.e.*, two million, four million, and eight million bytes of storage capacity). Expanded storage boards come in six capacities — two megabyte, four megabyte, eight megabyte, sixteen megabyte, twenty-four megabyte and thirty-two megabyte cards. The differences in the amount of memory per board are governed by the number of memory modules soldered onto the card.

Verified Complaint for Preliminary and Permanent Injunctive Relief at 8-9, *IBM v. Comdisco*, (N.D. Ill. filed Oct. 25, 1991) (No. 91 C 6777) [hereinafter "Complaint"].

enables those who sell or lease 3090 computers to precisely tailor these

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IBM alleged that Comdisco and other independent brokers both moved boards from one "box" to another and also:

engaged in an ongoing program of removing memory modules, or causing modules to be removed, from IBM-manufactured memory boards and re-soldering those modules (or having them re-soldered) onto other IBM-manufactured boards for the purpose of creating different capacity cards. In this way, for example, defendant has removed (or caused to be removed) the memory modules from two megabyte boards and re-soldered those modules onto other two megabyte boards to create four megabyte cards. A similar process can be followed to create eight megabyte boards from two four megabyte cards.

*Id.* at 11.

IBM also contended that the defendants tried to conceal their actions by counterfeiting IBM's part-number labels. *Id.* at 12. These were used for reconfigured or remanufactured equipment to denote the equipment's new capabilities. *Id.* IBM alleged:

Defendant has removed, or caused others to remove, the part number labels from the bogus boards and replaced them with labels that contain the part number of the board that IBM would have affixed to each board had IBM manufactured the card. Defendant has intentionally done that, or caused that to be done, in order to avoid detection and to reinforce the misconception on the part of both users and IBM maintenance personnel that these boards are genuine, IBM-manufactured cards. That misconception is further reinforced by the fact that the IBM trademark appears on each module.

*Id.*

Note that though the IBM trademark appeared on the modules, it did not appear on the counterfeit parts labels themselves. *Id.* Though Comdisco disputed IBM's characterization of the parts as "bogus" and the activities as misleading, it does not appear to have disputed the underlying facts themselves:

Comdisco states that it has, on occasion, purchased modified IBM 3090 memory boards from third party vendors or had IBM 3090 memory boards Comdisco owns reconfigured or modified by a third party. It also has modified IBM 3090 boards that it owns. These reconfigurations or modifications were accomplished by adding IBM parts so as to increase the memory storage capacity of IBM 3090 memory cards. To the best of Comdisco's knowledge, to the extent that any parts on these modified 3090 memory boards contain the letters "IBM," each of those parts was so marked by or at the direction of IBM and was manufactured by or for IBM. The part number on some of these modified IBM 3090 memory boards was changed and reflects the increased capacity of these cards.

Answer, *supra* note 2, at 2.

5. The term "reconfiguring" is used in the industry to refer to changes in a 3090 system which were intentionally provided for in the design, such as "moving around plug-in modules," for instance. *IBM-Comdisco Legal Conflicts Crawl Toward Resolution*, TECHNOLOGY NEWS OF AMERICA CO, INC., Feb. 1992, at 7. The IBM-Comdisco dispute also involves another process, sometimes called "remanufacturing." *Id.* This involves unintended modifications, such as soldering together two small memory boards to make one larger one. *Id.* Remanufactured 3090 equipment can be rebuilt using either all-IBM parts or some parts which were never produced by IBM. *Id.*

The IBM-Comdisco dispute, however, seems limited to parts reconfigured or remanufactured from pieces originally created by IBM. Complaint, *supra* note 4, at 6-8. In this Comment, the term "remanufactured" will refer only to such altered but all-IBM parts except where specifically indicated otherwise.

systems to the needs of each user.<sup>6</sup> IBM competes with independent "brokers" to lease 3090's. Up until 1991, both IBM and independents<sup>7</sup> modified 3090 systems using equipment taken from other computers.<sup>8</sup>

IBM filed suit against Comdisco<sup>9</sup> and three other independent brokers<sup>10</sup> to restrict the leasing of modified IBM equipment. This litigation threatened to give IBM monopolistic control over the used 3090 mar-

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6. Reconfiguration creates an extremely efficient use of 3090 systems. The author's interview with a former Comdisco broker (who prefers not to be identified) indicates that he was expected to "turn around" (re-lease or resell) 3090 equipment within a few days. Equipment rarely remains unused for any length of time since the cost of leasing unused equipment is thousands of dollars a day. Such costs would quickly erode the profits earned by those who reconfigure 3090 systems and arrange for their transfer from one user to another.

7. Comdisco is apparently the largest of these independents. Answer, *supra* note 2, at 6.

8. According to Comdisco:

If a third-party company such as Comdisco does upgrade or modify the equipment during the lease, it is immediately tested and recertified for maintenance by IBM. Furthermore, Comdisco immediately allocates identical IBM parts from our inventory to ensure that the right parts will be available when the equipment is to be restored to its original configuration. At the end of the lease, when this restoration occurs, IBM once again recertifies the equipment.

Comdisco White Paper, *supra* note 3, at 4.

In the current litigation, IBM denied that Comdisco and other independent brokers always followed this procedure. Stipulation and Order, *IBM v. Comdisco*, at 2 (N.D. Ill. filed Nov. 6, 1991) (No. 91 C 9777) [hereinafter Stipulation]. Since the instigation of the IBM-Comdisco law suit, IBM has refused to certify systems unless they are returned in exactly the same condition (down to the exact parts numbers) in which they were leased out. *Id.*

9. Technology, a British trade magazine which appears in the Financial Times, asks whether IBM's true target in the Comdisco litigation may not be Comdisco and other independent lessors, but that in fact Fujitsu. *IBM Widens Legal Battle*, TECHNOLOGY, July 19, 1992, at 1. Is the litigation "IBM's way of warning off Fujitsu, the Japanese company which is resolved to overtake IBM as the world's largest computer manufacturer, from making a bid for a U.S. leasing company?" *Id.*

Other possible "real targets" of the IBM litigation are Hitachi and Amdahl. *ES/9000 Installation Plan Cuts Secondary Market Opportunities*, EQUIPMENT LEASING TODAY, Sept. 1991, at 10. Such speculation is bolstered by the fact that IBM has ended litigation as an ally of Comdisco, *infra* note 15, rather than an enemy and thus in a stronger position in the domestic market.

10. IBM sued Comdisco, Inc. (Case No. 91 C 6777); Allen-Myland, Inc. [hereinafter called AMI] (Case No. 92 C 2896); Datanon, Inc. (Case No. 92 C 2897); and BSM Corporation (Case No. 92 C 2898). Order of Consolidation, *IBM v. Comdisco*, (N.D. Ill. filed June 9, 1992) (No. 91 C 6777). The settlement announced on August 26, 1994 appears to cover only Comdisco, *infra* note 15; presumably the other defendants remain in litigation.

IBM has sued these same defendants on prior occasions. Most of the same issues were raised in *IBM v. Comdisco*, No. 11922 (Ct. Chan. Del. filed Jan. 24, 1991). This case was dismissed for lack of jurisdiction. Order Granting Motion to Dismiss, No. 11922 (Ct. Chan. Del. filed July 2, 1991) [Hereinafter "Dismissal Order"]. See also *AMI v. IBM*, 693 F. Supp. 262 (E.D. Penn. 1988) *supplemental claims* 746 F. Supp. 520 (E.D. Penn. 1990).

ket.<sup>11</sup> Since many users have no real alternatives to the 3090, preventing third parties from leasing 3090's would have given IBM an ability to fix prices.<sup>12</sup> The important role played by 3090 computers in the computer industry means that IBM's attack on its independent competitors could have substantially increased the cost of high-powered computers to individual users and to the U.S. economy as a whole.<sup>13</sup>

The recent settlement of *IBM v. Comdisco*<sup>14</sup> kept IBM from driving its competitors from the market. However, the settlement fails to resolve whether leasing modified computer equipment under the original trade-

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11. The U.S. Supreme Court has recognized that the after-market for a single brand of equipment constitutes a marketplace susceptible to illegal monopolistic control when consumers have no realistic alternatives to that brand. *Eastman Kodak Company v. Image Technical Services, Inc.*, 112 S. Ct. 2072, 2079-82 (1992).

12. The leasing industry does not take a unified stand towards IBM's suit. Maxwell Lemming, *Reconfiguration Lawsuit Yields Villains Galore, But No Heroes*, *COMPUTER LEASING TODAY*, Nov. 1991, at 6. "The independent community, on an individual basis, has been less supportive of Comdisco's position than one would have expected." *Id.*, at 7. Other independent brokers compete with Comdisco, and this competition sometimes makes tempers rise. *Id.* But most commentators seem to agree with Comdisco's view that IBM seeks to drive competition from the field.

[IBM] is the aggressor here, not Comdisco. . . . There is more to the [IBM]-Comdisco lawsuit than meets the eye. It is about time for everyone in the independent community to take the blinders off their eyes and recognize what is at stake. It is your future. . . . If Comdisco wins, you will have lucked out. If they lose, you will be out of luck.

*Id.*

13. The IBM-Comdisco "disputes have rubbed salt into the wounds caused by a depressed market." Lemming, *supra* note 12, at 1. The current weakened state of the economy has forced businesses to scale back new equipment purchases and to depend more heavily on releasing, making an IBM monopoly over the industry especially dangerous. *Id.*

According to the Computer Dealers and Lessors Association (CDLA), Comdisco alone serves more than 60,000 business locations around the world, including nearly every major manufacturer, and netted 2.2 billion dollars in 1991. *Id.* at 6-7. The entire releasing industry had more than 26 billion dollars in sales that year. *Id.*

14. According to terms announced on August 26, 1994, Comdisco agreed to pay seventy million dollars (fifty million in cash, plus twenty million in a convertible note) but did not concede any wrongdoing. *Comdisco Settles Suit*, *WALL STREET JOURNAL*, Aug. 29, 1994, at 4. *Id.* Announced at the same time was a separate agreement whereby IBM shifted from a Comdisco foe to a Comdisco "ally"; the two companies agreed to provide "mutual backup support" for one another's customers in case of disaster and to discuss distribution agreements. *Id.*

The settlement translated into a Comdisco fourth-quarter loss of about \$1.05 per share. *Id.* For the quarter ending Sept. 30, Comdisco would have earned about 58 cents per share without the charge against earnings caused by the settlement. *Id.* The agreement cut this to a net loss of 47 cents. *Id.* Nonetheless, the value of Comdisco stock on the New York Stock Exchange shot up by \$1.25 (or 6.1%) on the day of the announcement. *Id.* The market apparently regarded the IBM-Comdisco alliance and the lifting of a "cloud of uncertainty" over Comdisco's business activities as a Comdisco victory. *Id.*

mark by a third party violates the rights of the mark holder.<sup>15</sup> IBM claimed that modified 3090 computers are not genuine,<sup>16</sup> and thus the

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15. "Under the terms of the settlement agreement, Comdisco has agreed to label altered memory and other parts as not being IBM parts. . . eligible for IBM maintenance." COMDISCO, *News Release*, Aug. 26, 1994. The terms of the settlement include:

1. Comdisco. . . is hereby permanently enjoined from making, in connection with the sale, lease or other marketing of any part, any of the following representations, either in writing or orally and whether explicit or implicit, unless each is true and accurate when made:

(i) that the part in its present form was manufactured by or on behalf of IBM, or under IBM supervision by the use of IBM manufacturing and testing processes (any computer part that meets the definition of Altered IBM Parts as defined below is not manufactured by IBM or on behalf of IBM or under IBM supervision by the use of IBM manufacturing and testing processes);

(ii) that the part in its present form had been maintained by IBM; or

(iii) that the part is eligible for IBM's standard maintenance agreement or any other IBM maintenance service (any part that meets the definition of Altered IBM Parts as defined by paragraph 2 below is not eligible for IBM's standard maintenance agreement service or any other IBM maintenance service).

In any proceeding before the Court arising from an assertion by IBM that Comdisco has violated this paragraph, Comdisco shall not be deemed to have violated it if Comdisco is able to prove, by a preponderance of the evidence, that, in connection with the subject transaction, Comdisco took reasonable steps to insure that each of the above representations was true and accurate. Notwithstanding such a determination by the Court, IBM shall be free at the trial of the action to seek damages in connection with the subject transaction under applicable legal standards.

2. Any part originally manufactured by or on behalf of IBM but which in its present form has been altered by someone not acting by or on behalf of IBM, or not acting under IBM's supervision using IBM manufacturing and testing processes, or acting without IBM's prior explicit written permission is an "Altered IBM Part" except that if Comdisco reconfigures IBM equipment using IBM Maintenance Parts or incidental hardware (e.g., bolts, screws, covers, light bulbs), the resulting equipment will not result in an Altered IBM Part. IBM Maintenance Parts are parts that are or have been available for purchase from IBM CEs can replace in the field. If Comdisco has any question as to whether a particular item is a maintenance part, it should direct any such question to IBM's Assistant General Counsel for Litigation and IBM will promptly respond.

3. Comdisco is hereby enjoined from selling, leasing or otherwise marketing or disposing of Altered IBM Parts unless it: (1) attaches to such Altered IBM Parts in a reasonably permanent manner to which the parties agree, a label [stating "This part was not manufactured by IBM, has not been maintained by IBM in its present form and is not eligible for IBM maintenance."] and (2) discloses that parts are Altered IBM Parts and are not eligible for IBM standard maintenance agreement service or any other IBM maintenance service.

Settlement, *supra* note 1, at 2-4.

16. The IBM-Comdisco dispute under the Lanham Act might be reduced to differing interpretations of the term "genuine." Comdisco appeared to claim, as this Comment suggests, that under trademark law the word "genuine" means more or less: "1. Actually possessing or produced by the alleged or apparent attribute, character, or source. . . . 2. Not spurious or counterfeit; authentic. 3. Free from hypocrisy or dishonesty." AMERICAN HERITAGE DICTIONARY 550 (New College Ed. 1969). Note that the key element of this definition is *truthfulness*. IBM's position seems to depend on a less basic aspect of the term's meaning: "4. Being of pure . . . stock." *Id.* This Comment contends that this aspect of the definition is not relevant to trademark law. Genuine means *honest*, not *unmixed* or *unchanged*.

use of the IBM trademark for such computers is a trademark violation.<sup>17</sup> At various stages of litigation, IBM challenged its competitors on numerous grounds.<sup>18</sup> This Comment will focus on Comdisco's alleged violations of the Federal trademark law, commonly called the "Lanham Act."<sup>19</sup> Additionally, this Comment will discuss to what degree does originally genuine trademarked equipment become "counterfeit" when it is altered and then re-leased?

This Comment will first focus on the factual background of the IBM-Comdisco dispute. Second (because there is no direct precedent on this issue), this Comment will discuss the policies which support trademark protection. Third, this Comment will discuss the degree to which anti-trust policies should affect questions of genuineness. Fourth, this Comment will draw analogies from the question of genuineness which arises

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17. The IBM complaint does not clearly distinguish between reconfigured and remanufactured 3090 systems. Complaint, *supra* note 4. It appears, however, that IBM denied the authenticity of both. Comdisco denied that it ever remanufactured computers or that it intentionally sold or leased them. Answer, *supra* note 2, at 2-3, and Stipulation, *supra* note 8, at 2. But at least one of the other defendants, BSM Corporation, seems to have conceded that it does so, BSM's Answer at 3, *IBM v. BSM Corp.*, No 92 C 2896 (N.D. Ill., filed Mar. 9, 1993):

BSM, at its customers' request, has removed genuine IBM memory chips from genuine IBM memory boards owned by BSM or the customers and reinstalled the genuine IBM memory chips into other genuine IBM memory boards owned by the customers. Defendants [BSM] specifically deny that they have ever created imitation IBM memory cards.

*Id.*

Because much of the technical evidence being developed by both IBM and the Comdisco defendants is not public, it is not clear exactly to what degree or in what ways IBM alleges that the systems have been altered. Given this uncertainty, this Comment will assume that the authenticity of both reconfigured and remanufactured 3090 systems were, or could have been, issues necessary for resolution of *IBM v. Comdisco*.

18. In the Complaint filed in the original Delaware case of *IBM v. Comdisco*, IBM alleged that Comdisco's activities constitute unjust enrichment, conversion, interference with contractual rights, interference with business relations, breach of contract, unfair competition, interference with contract, and deceptive business practices. Complaint (Del.) *supra* note 2, at 15-23. In the Complaint filed in the current federal case in Illinois, the allegations were for state and federal trademark violations, unfair competition, interference with business relations, and deceptive business practices. Complaint, *supra* note 4. Many of these claims were dismissed or withdrawn. Order Granting Defendant's Motion, *IBM v. Comdisco*, No. 91 C 6777 (N.D. Ill. filed Feb. 25, 1992) [hereinafter, Order Dismissing Count]. The remaining counts (federal trademark violations, unfair competition, and deceptive business practices) refer, at least in part, to the degree to which consumers might be confused by vendors other than IBM who use the IBM trademark. Complaint, *supra* note 4, at 13-20.

19. 15 U.S.C. § 1114, 1125(a) (1988). Under the Lanham act, it is unlawful to sell or lease trademarked goods which are not genuine. *Id.* IBM raised this issue in the federal suit in Illinois but not in the state suit in Delaware. Complaint, *supra* note 4; Complaint (Del.), *supra* note 2.

in the "gray market."<sup>20</sup> This Comment concludes that "genuine" means "truthful" rather than "pure."<sup>21</sup> Lessors of modified goods must inform consumers that the goods have been altered.<sup>22</sup> However, unless goods are so drastically modified as to lose their original identity, they must be regarded as genuine under the Lanham Act, so that honest use of their trademark when leased is lawful.<sup>23</sup>

## II. BACKGROUND

First, this background will discuss the role played by the 3090 Computer System in the current economy. Subsequently, this background discusses the specific issues around which recent litigation between IBM and its competitors have revolved.

### A. THE IBM 3090 COMPUTER MARKETPLACE

Large scale, high performance computers form the infrastructure of today's information age.<sup>24</sup> One of the most important groups of such

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20. The "gray market" refers to trademarked goods imported to the United States though intended for retail sale abroad. Jacob Laufer, *Good Faith And Fair Dealing With The American Consumer*, 1987 COLUM. BUS. L. REV. 167, 167-68 (1987). When nearly identical goods are sold at lower prices abroad than in the United States, the opportunity to profit through arbitrage is strong. *Id.* Section 42 of the Lanham Act and section 526(a) of the Tariff Act of 1930 have been invoked by trademark holders to attempt to shut down the gray market, with limited success. *Id.* This extensive litigation culminated in *K Mart Corp. v. Cartier, Inc.* 486 U.S. 281 (1988).

In *K-Mart*, the U.S. Supreme Court drew a complicated line between legal and illegal gray market imports. *Id.* Generally, gray market imports are illegal if an independent American firm holds a trademark which happens to be identical to one used abroad. *Id.* However, gray market imports are legal when the American trademark holder is identical or closely associated with the foreign manufacturer. *Id.*

21. See *supra* note 16 for a discussion of the meaning of the term "genuine". The IBM-Comdisco settlement terms conform to this Comment's conclusion, since the terms allow Comdisco to use the trademark IBM in connection with altered (impure) goods so long as Comdisco gives notice that the goods are altered and ineligible for IBM maintenance. Settlement, *supra* note 1, at 3-4.

22. IBM was especially concerned with maintenance agreements, claiming that it was sometimes forced to maintain degraded equipment under agreements which legally obligated IBM to work on IBM equipment. *News Release, supra* note 15. The questions of whether altered equipment is "genuine" under the Lanham Act (for trademark purposes) and whether it is truly "IBM equipment" under maintenance agreements were intertwined during litigation, but only the former (trademark) question is addressed in this Comment. The parties agreed as to the first question fairly early in the litigation; in 1991 Comdisco agreed that IBM was not obliged to maintain altered parts and that it should notify customers to this effect. Stipulation, *supra* Note 8.

23. *Id.*

24. The information age depends on high powered computers in the same way that the industrial revolution depended on railroads. THE ENCYCLOPEDIA BRITANNICA, v. 18, *Railway*, 927-928 (1965). During the industrial revolution, America's business relied on trains



computers are those based on IBM's 3090 processor.<sup>25</sup> For example, IBM 3090 systems are used for military applications, weather forecasting, high volume financial transaction processing, and for many other applications demanding enormous computer power.<sup>26</sup> IBM 3090 system prices often reach the tens of millions of dollars;<sup>27</sup> the 3090 central processing unit alone can cost millions of dollars.<sup>28</sup>

Part of the enormous utility of 3090 systems derives from their "modular"<sup>29</sup> design. By adding or removing various component modules

to deliver mail and goods to everyone. *Id.* Now we rely on electronic mail and wire transfers for the same purposes. Information is the basic commodity of the information age. It is created by and transported in and through computers:

IBM's 3090 customers often use their computers to perform critical, on-line applications such as airline reservations, retail point of sale, banking and manufacturing control. Numerous government agencies use 3090 computers to perform a variety of applications critical to the national interest.

Complaint, *supra* note 4, at 7.

The railroads required special regulation because after the civil war "abuses such as rate wars, rate discrimination and financial piracy became more widespread. BRITANNICA, *supra*, at 929. In these things railways were probably no worse offenders than many other businesses of that era, but since they had by then attained almost a monopoly over domestic transportation, the public could not tolerate these abuses." *Id.*

It is surprising that the computer industry has been subject to so little regulation (at least by comparison with railroads), given the importance it has for the economy.

25. According to IBM:

IBM 3090 systems are among the most powerful and sophisticated computers in the world and they are used to perform a broad array of applications including, for example, military applications, weather forecasting, advanced research applications, computer aided design, manufacturing, airline reservations, and high volume financial transaction processing.

Complaint (Del.), *supra* note 2, at 4-5.

26. *Id.*

27. Complaint, *supra* note 4, at 6. These prices reflect IBM's multi-million dollar investment in developing the 3090 equipment and supporting software. *Id.*, at 4. For example, the system software for the 3090 contains more than a million lines of code and required approximately 1,500 person-years of labor to produce. *AMI v. IBM*, 746 F. Supp. 520, 533 n. 10 (E.D. Penn. 1990). IBM 3090 systems are protected by numerous patents and copyrights, and are sold or leased subject to carefully drafted license and restrictive use agreements. Complaint, *supra* note 4, at 4, 13-14.

28. Complaint (Del.), *supra* note 2, at 6.

29. IBM describes this capacity as follows:

Because of the modular design of the 3090, processors, memory and channels can readily be added to or removed from a 3090 processor complex. Thus, the various components of the 3090 processor family can be combined in a large variety of ways to create many different configurations of various speeds, capacities and capabilities. In this way, 3090 processor family can be combined in a large variety of ways to create many different configurations of various speeds, capacities, and capabilities. In this way, 3090 processor complexes can easily be upgraded or downgraded in the field (*i.e.*, without return to the factory) to support tens of thousands of different configuration possibilities. When a processor complex is downgraded, parts are removed and when a processor complex is upgraded, parts are added (and parts are also sometimes removed to accommodate the addition of the various parts that effect the upgrade).

such as memory or information storage, more than 29,000 different 3090 systems can be formed.<sup>30</sup> This enables a 3090 system to be precisely configured, meeting the needs of each user.<sup>31</sup> As users' needs change, 3090 systems can be readily modified to adapt by adding or replacing modular components.<sup>32</sup>

This flexibility has also created the opportunity for a used 3090 market. A 3090 system can often be modified to meet the needs of a new user.<sup>33</sup> Thus, 3090 users who no longer need their systems can usually resell or re-lease them.<sup>34</sup> This fact substantially enhances the value (and price) of a 3090 system.<sup>35</sup> The market for used 3090's has developed as "brokers" buy or lease used 3090's and then resell or re-lease them. IBM itself is such a broker, with a growing market share likely to reach about 80% of the 3090 re-leasing market by 1995.<sup>36</sup> Independent brokers, including Comdisco and Allen-Myland, Inc. ("AMI"), will hold the remaining 20% market share.<sup>37</sup>

The existence of independent brokers depends on protection provided by anti-trust regulation.<sup>38</sup> IBM has had monopolistic control over large segments of the computer marketplace for decades. However, in 1956, IBM agreed to a Consent Decree in *United States v. International Business Machines, Inc.*,<sup>39</sup> which severely restricts its activities. Key provisions of the Consent Decree force IBM to both sell and lease its products.<sup>40</sup> Before the Decree, IBM refused to sell its products.<sup>41</sup> IBM machines were available only by lease.<sup>42</sup> This allowed IBM to keep firm control over its products.<sup>43</sup> Other provisions of the decree require IBM to allow attachments to or experiments with IBM equipment.<sup>44</sup> The 1956 Consent Decree still controls IBM's business activities today and pro-

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Complaint (Del.), *supra* note 2, at 5-6.

30. *Id.*

31. Comdisco Broker Interview, *supra* note 6.

32. Comdisco's White Paper, *supra* note 3, at 10-13.

33. *Id.*, at 11.

34. *Id.*, at 13.

35. The existence of the re-leasing industry itself depends on the long-term value of the 3090 system. If a 3090 system rapidly lost value, it would not be re-leaseable several years into a lease. Comdisco Broker Interview, *supra* note 6. *See also* Comdisco White Paper, *supra* note 3, at 10-13.

36. Lemming, *supra* note 12, at 1. Lemming notes that since IBM itself has 80% of the re-leasing market, it can't afford to damage the market while attacking its competitors. *Id.*

37. *Id.*

38. Comdisco White Paper, *supra* note 3, at 6-7.

39. 72-344 CCH Trade Cas. 68,245 (S.D.N.Y. 1956).

40. *Id.*

41. AMI v. IBM, 746 F. Supp. 520, 542 (E.D. Penn. 1990).

42. *Id.*

43. Comdisco White Paper, *supra* note 3, at 6.

44. *United States v. IBM*, 72-344 CCH Trade Cas. 68, 245 (S.D.N.Y. 1956).

vides for a free market in the computer industry.<sup>45</sup>

The free market for IBM computers both serves consumers and provides many opportunities for independent brokers.<sup>46</sup> For example, in 1989, IBM sold 200E computer systems for \$4,500,000 and 400E systems for \$8,375,000.<sup>47</sup> Roughly the same modular components could be used to configure either one 400E system or two 200E systems.<sup>48</sup> A broker who purchased a 400E system, plus additional hardware costing \$279,000, could create two 200E systems at a cost of about \$8,690,000, \$310,000 less than the price of two IBM 200ES.<sup>49</sup> The broker could then sell the two smaller systems and pass the savings along to his customers.<sup>50</sup>

Many 3090's enter the market through leases rather than sales.<sup>51</sup> IBM sells the systems to its subsidiary IBM Credit Corporation ("ICC"), which then leases the equipment to users.<sup>52</sup> Independents such as Comdisco also lease out 3090 systems which they own.<sup>53</sup> Often, a system which has been leased to one user is later moved to another and re-leased.<sup>54</sup> Whenever a 3090 system is resold or re-leased, it almost always needs to be modified since different users rarely require identical configurations.<sup>55</sup>

When modifying a system, brokers often remove modules no longer needed.<sup>56</sup> These modules are usually incorporated in other systems.<sup>57</sup>

45. Comdisco White Paper, *supra* note 3, at 6.

46. *Id.*

47. *AMI v. IBM*, 746 F. Supp. 520, 528 (E.D. Penn. 1990).

48. *Id.*

49. *Id.*

50. *Id.*

51. Interview with Craig Brown, in-house counsel for Forsythe & McArthur, a Chicago-area independent computer leasing company, in Skokie, Ill. (Sept. 23, 1993). Brown said that the "majority of 3090's reaching the market today arrive through a lease arrangement." *Id.* There are two types of leases: operating lease (lessor retains ownership) or lease-to-own (ownership transfers at lease end). See also Wendy L. Marshall, *Leasing Can Salve Fears of Fast Obsolescence*, BUSINESS GAZETTE COMPUTER ADVERTISING SUPPLEMENT, Feb. 1992, at 1.

52. Marshall, *supra* note 51.

53. *Id.*

54. *Id.*

55. The need for flexibility is demonstrated by the frequency of computer system changes:

[B]usinesses that are growing and expanding, have growing and expanding computer needs. Seventy-seven percent of Comdisco's customers upgrade or replace their equipment within two years; 94 percent of the company's customer [sic] have made changes of enhancements within three years.

Most users are on a growth trend, needing more power, size, and capacity, and leasing gives them the flexibility to do all those things at the least costs.

*Id.*

56. Comdisco's public position statement offers the following example of a typical re-leasing arrangement:

Thus, the individual modules are "scrambled" (i.e., moved from system to system) during resale, re-leasing, or enhancement.<sup>58</sup> Scrambled equipment presents a unique challenge to brokers, since it is difficult to reassemble the original parts when returning it to the owner at the end of the lease.<sup>59</sup> The original parts may have been distributed among many different computer systems.<sup>60</sup>

Comdisco claims that the standard industry practice is to return leased systems with exactly the same kinds of modules, but not necessarily with the exact same individual components, that were leased out.<sup>61</sup> Since most of the computers belong to IBM, this means that IBM is usually the party who receives back the scrambled systems.<sup>62</sup> However, this is not always the case. Specifically, Comdisco alleges that IBM reconfigures 3090 systems owned by independents and scrambles their compo-

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[L]et's say that 24 months into a 60-month ICC lease, Company A upgrades the memory of its 9121-260 from 128 MB to 256 MB with a used alternative from an independent leasing company, whose price is almost \$70,000 better than ICC's new alternative.

Because the original 128 MB memory segment isn't due back to ICC for another three years, the independent leasing company remarkets the off-coming item to another customer and immediately allocates from its inventory an identical IBM memory segment, which will be installed on the machine prior to its return to ICC. At the end of the lease, to restore Company A's equipment back to its original configuration, the independent leasing company removes the 256 MB board it installed and replaces it with a 128 MB board made by the same manufacturer and identical to that which was originally removed. It has the same part number, but, obviously, a different serial number.

Comdisco White Paper, *supra* note 3, at 11.

57. *Id.*

58. Such "scrambled" parts are not unique to the computer industry. Lemming, *supra* note 12, at 6. It is common for leased airplanes or aircraft equipment to be rebuilt with parts of the same make and model as the original, but with different actual parts (and part numbers). *Id.* There is some question, however, whether the industries are directly analogous:

Aircraft parts, we are told, must meet strict federal standards, so the original lessor knows the part it gets back is satisfactory. This, some say, is not the case with computers, since the original lessor can't rely on government standards. But this argument ignores the fact that IBM must certify that the boxes ICC gets back after a modification satisfy its standards and qualify for maintenance.

*Id.*

59. Comdisco's White Paper, *supra* note 3, at 11.

60. *Id.*

61. This practice apparently originated with earlier IBM computer systems. Lemming, *supra* note 12, at 6. It is, however, possible (at least sometimes) to "unscramble" a computer system's parts. Comdisco managed to return the 3090 computer at issue in the Delaware suit with all the original parts exactly the way they were leased out. *Comdisco Returned The 3090 At The Heart of ICC's Suit*, TECHNOLOGY NEWS OF AMERICA CO., INC., Mar. 1992 at 7.

62. Comdisco returned the 3090, *supra* note 61, at 7.

nents when it brokers the leases on these systems.<sup>63</sup>

IBM 3090 modification sometimes means merely slipping modular memory boards in or out of the computer.<sup>64</sup> But more extreme modification occurs as well: module capacity is sometimes increased by "remanufacturing": soldering on additional memory chips.<sup>65</sup> These chips may have been "stripped" from other 3090 modules and thus were originally created by IBM.<sup>66</sup> The additional chips may also have been manufactured by other companies.<sup>67</sup> It appears, however, that the remanufactured boards involved in the IBM-Comdisco dispute may be confined to those rebuilt from parts originally created by IBM.<sup>68</sup>

IBM claimed that remanufactured boards are inferior to original memory cards, primarily because they fail more frequently.<sup>69</sup> Comdisco denied this allegation.<sup>70</sup> The issue is confused somewhat because IBM itself remanufactures 3090 memory and has never denied the authenticity of the resulting boards.<sup>71</sup> When 3090 systems were re-leased and

63. In the European market, IBM actually endorses the position that 3090 parts are fungible:

[I]n a letter to the European Leasers and Traders Association outlining its policy in Europe. . . IBM said that. . . when the machine is restored to its original specification before being returned to IBM, it can be reconfigured with the original parts, or with equivalent IBM parts.

*In the News*, BACON'S SERVICE INDUSTRY NEWSLETTER, Dec. 1991.

These computers reconfigured in Europe are sometimes shipped back to the U.S. market. *Id.*

64. See *supra* notes 4 and 5 and accompanying text for discussion of the processes of reconfiguration and remanufacturing.

65. *Id.*

66. According to industry sources, the memory which IBM alleges is counterfeit: was fabricated by combining IBM components from boards of low capacity (and low value) to make boards of high capacity (and high value). The resultant boards, according to IBM, were labeled to look like authentic products made at an IBM plant, which they are not.

*IBM Files Its First Multinational Suits in Memory Disputes*, TECHNOLOGY NEWS OF AMERICA Co., Inc., July 1992, at 10.

67. See *supra* note 17 (indicating that BSM, but not Comdisco, engages in remanufacturing).

68. *Id.*

69. Answer, *supra* note 2, at 3, 10-16.

70. *Id.*

71. It is not clear whether IBM's manufacturing processes are any better or worse than those used by 3rd parties:

The procedure used [by third-party technicians for IBM] to replace memory components may be even more likely to yield unreliable boards than the techniques used by the firms IBM has sued. Specifically, during repair memory chips (mounted on subassemblies) were individually desoldered and new subassemblies resoldered on boards. During remanufacturing, whole low-density memory boards were stripped of components and whole boards were resoldered using industrial flow soldering techniques. The industrial processes are specifically designed to subject components to the smallest risk of overheating and other stresses that can easily occur when individual components are replaced by hand.

scrambled, memory boards which had been remanufactured by third parties were sometimes presented to IBM for warranty service.<sup>72</sup>

### B. CURRENT LITIGATION

The crux of IBM's trademark claim<sup>73</sup> was that reconfiguring or remanufacturing 3090's makes them "counterfeit."<sup>74</sup> Since leasing counterfeit equipment violates the Lanham Act, IBM claimed that leasing altered equipment violates IBM's rights under trademark law.<sup>75</sup> If such modification inevitably transforms authentic IBM computers into counterfeits, IBM's claims were almost irrefutable. Without the ability to modify 3090's, neither Comdisco nor any other IBM competitor would be able to accommodate the needs of 3090 users, and the competitive re-leasing market for 3090 equipment would collapse.<sup>76</sup> But if IBM boards retain their genuine<sup>77</sup> character despite reconfiguration, then IBM's claims could have been resolved by minor changes in the re-leasing industry, such as requiring disclaimers on modified equipment.<sup>78</sup> It ap-

*IBM Files*, *supra* note 66, at 11.

72. Complaint, *supra* note 4, at 5-7.

73. *Id.*

74. *Id.*

75. IBM also makes claims (not discussed in this Comment) based on property, patent, and copyright law. *Id.*

76. An executive at a large corporate lessee says:

ICC has won a lot of leases solely on price. Now we're faced with the possibility of losing out down the line if third-party subleasing at favorable prices dries up or is shut down. That prospect converts ICC's dramatic up-front price breaks into loans rather than bargains.

COMPUTERWORLD, Feb. 4, 1991.

Comdisco states this view as follows:

IBM already controls the majority of new computer systems presently on lease. If it wins the suit, it will also control the bulk of used systems and parts. Without healthy competition from used equipment vendors, IBM will be free to decide if it will remarket equipment, to whom, under what circumstances, and at what price.

Comdisco's White Paper, *supra* note 3, at 2.

77. The term "genuine" as employed in this Comment refers to the application of the word under the Lanham Act. Lanham Act, *supra* note 19. The Act allows those other than the trademark holder to use the mark for genuine goods, but prohibits such use if the goods are not genuine. *Id.* It is the conclusion of this Comment that the term "genuine" does not imply that the goods are unaltered or "as new."

78. Even if reconfigured or remanufactured 3090 computers are authentic, IBM's trademark and copyright claims based on the "counterfeit" parts number labels would remain. Complaint, *supra* note 4, at 4, 8, 11. However, redesigning the labels so that they would put users and maintenance personnel on notice that the parts had been altered would almost certainly resolve this claim, since the claim depends on the argument that the labels are misleading. *Id.*

In *Intel Corp. v. Terabyte International, Inc.*, 1993 WL 375176 (9th Cir. (Cal.), 1993) (Nos. 92-55207, 92-55424) the defendant sold Intel 287-6 math coprocessors as though they were model 287-10's. *Id.* at 1. Intel's original designation, "287-6" had been removed, and replaced with the designation "287-10." *Id.* The Intel Logo was not removed. *Id.* Though

pears that the terms of the settlement require just such minor changes.<sup>79</sup>

The just-settled phase of the dispute<sup>80</sup> between IBM and its independent competitors<sup>81</sup> is part of a group of cases<sup>82</sup> consolidated as *In-*

the 287-6's and 287-10's are similar and can be used for some of the same applications, 287-10's are designed to run faster. *Id.* When 287-6's are used for applications designed for 287-10's, they have a high failure rate. *Id.* at 5. The court held that though the coprocessors were actually produced by Intel, they were not authentic Intel 287-10's and it was a violation of trademark right for the defendant to sell them as 287-10's. *Id.* It would seem that attempts to label remanufactured 3090 IBM computer equipment to mimic original products would be likewise misleading and thus violate trademark rights.

Comdisco conceded that neither it nor any other vendor should sell or lease altered IBM equipment without notice that the equipment had been so altered. Stipulation, *supra* note 7. Comdisco claimed that it was never its policy to release altered IBM equipment without notice, but conceded that in some cases it did so inadvertently. *Id.* at 2-3. IBM itself has also sold or leased altered 3090 equipment, though IBM denies that it has ever done so knowingly. *IBM Forgets Its Own Rules In Memory Card Muddle*, TECHNOLOGY NEWS OF AMERICA, Co., Inc., July 1992, at 13.

Such oversights, both on IBM's part and on the part of IBM's competitors, can be resolved by more careful industry practice. In cases where Comdisco released altered equipment without notice, it has already agreed to either replace the equipment with IBM parts which are not altered (or with non-IBM parts) or to maintain the equipment (since IBM refuses to do so) if the customer so desires. Stipulation, *supra* note 8, at 2-3.

79. The settlement allows Comdisco to both reconfigure and remanufacture IBM 3090 systems and thus to provide viable services to consumers. Settlement, *supra* note 1, at 3-4. Comdisco has thus not been driven from the field. *Id.* It is merely required to be honest and forthcoming about the status of its parts. *Id.* Systems which have been reconfigured as IBM planned them to be remain fully IBM parts. *Id.* Those which have been soldered together in ways IBM never intended are not fully IBM parts, but must be sold as "Altered IBM." *Id.*

80. Preliminary Pretrial Scheduling Order, *IBM v. Comdisco*, No. 92 C 6777 (N.D. Ill. filed Dec. 7, 1992).

81. Litigation between IBM and independent 3090 brokers began in 1988, with *AMI v. IBM* 693 F. Supp. 262 (E.D. Penn. 1988), *supplemental claims* 746 F. Supp. 520 (E.D. Penn. 1990). This case originated as a failed anti-trust action against IBM. *Id.* IBM alleged that copying the 3090 system software to reconfigure 3090s which AMI owned violated IBM's copyright and rights under the licensing agreement. *Id.* at 529-31.

IBM 3090 computers require specific system software in order to function. *Id.* at 526-27. Whenever a 3090 system is reconfigured, the system software must be modified to reflect the new configuration. *Id.* at 528. Non-IBM technicians can modify the code by "splicing" software. *Id.* at 528-29. They copy different parts of the software from the various systems from which the reconfigured parts came. *Id.*

The IBM license agreement for this software prohibits any copying other than for archival purposes. *Id.* at 527. The court agreed that such copying violated the license agreement, but this victory was hollow, since the court refused to enforce the agreement. *Id.* at 541. The court held that IBM's 1956 antitrust consent decree estopped IBM from enforcing the license or any other legal right which would prevent copying. *Id.* The court reasoned that to prevent the splicing would effectively prevent competition. *Id.* at 542.

82. This branch of the dispute originated in 1991 when IBM filed a suit against Comdisco, for "misappropriation of computers and parts owned by" IBM. Complaint (Del.), *supra* note 2, at 3. IBM sought injunctive relief from the parts scrambling resulting from re-leasing 3090 systems. *Id.* The Court dismissed the case for lack of jurisdiction. Dismis-

*ternational Business Machines Corp. v. Comdisco, Inc.*<sup>83</sup> In August 1991, IBM sought a preliminary injunction to prevent Comdisco from representing the reconfigured memory boards as IBM equipment "unless Comdisco believes its equipment" qualifies for IBM maintenance under the original lease.<sup>84</sup> In November, the parties stipulated to an order to this effect.<sup>85</sup> The order also required that Comdisco inform past customers so as to mitigate the effect of past statements which would have violated the order.<sup>86</sup>

In effect, Comdisco conceded that it cannot lease altered IBM parts without so informing its customers, or claim that its equipment is eligible for IBM maintenance unless the equipment actually is eligible.<sup>87</sup> Comdisco claims that it was never policy to do so.<sup>88</sup> Comdisco has conceded that in the few cases where it may have accidentally leased altered parts without notifying its customers, it has a duty to rectify the situation.<sup>89</sup>

Most of IBM's original counts, such as that for conversion, were dismissed or dropped.<sup>90</sup> IBM filed an amended complaint containing the still-viable counts in March, 1992.<sup>91</sup> In these counts, IBM alleged that soldering and otherwise altering 3090 equipment makes the equipment unauthentic,<sup>92</sup> so that the lease of altered equipment constitutes

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sal Order, *supra* note 10. Moreover, Comdisco actually replaced the one 3090 computer system which was actually in dispute in the Delaware case with the exact same parts that it had originally possessed, with the exception of a few which had failed and been replaced during the course of maintenance. *Comdisco Returned the 3090 at the Heart of ICC's Suit*, *supra* note 61, at 7.

83. See *supra* note 81 (for discussion of anti-trust issues). IBM also seeks to join as a fifth defendant the party which ships Comdisco's equipment to its foreign subsidiaries. Motion of Plaintiff, *IBM v. Comdisco*, No. 92 C 6777 (N.D. Ill. filed June 1, 1992).

The only portion of the case which has been published to date is the Court's holding that all stipulations, orders, and discovery requests apply to Comdisco's foreign subsidiaries as well as U.S. transactions. *IBM v. Comdisco*, 1993 WL 155511 (N.D. Ill. 1993)(No. 92 C 9777).

84. Stipulation, *supra* note 8, at 2-3.

85. *Id.*

86. Comdisco agreed to offer such parties three options: replacement of the altered memory with that which has not been altered, replacement of the altered memory with like non-IBM memory, or continuation of the existing memory with Comdisco maintenance. *Id.*

87. *Id.*

88. Answer, *supra* note 2, at 2-4, 10-15.

89. Stipulation, *supra* note 8, at 2-3.

90. Order Dismissing Count, *supra* note 18, and Amended Complaint, *IBM v. Comdisco*, No. 92 C 6777 (N.D. Ill. filed Mar. 17, 1992) [hereinafter Amended Complaint].

91. *Id.*

92. *Id.*



trademark infringement under the Lanham Act.<sup>93</sup> Comdisco conceded most of IBM's factual allegations.<sup>94</sup> However, Comdisco denied IBM's claim that Comdisco did not follow equivalent quality control procedures as does IBM when soldering 3090 memory cards,<sup>95</sup> or that the soldered boards were inferior to IBM's.<sup>96</sup>

Thus, the issue appears to have narrowed, in part, to whether Comdisco could continue to use the IBM trademark when it leased IBM parts identified as having been altered by third parties, which Comdisco did not claim as eligible for IBM maintenance except where it actually was eligible.<sup>97</sup> The settlement agreement appears to contain no new limitations on Comdisco's business practices.<sup>98</sup> Comdisco can continue to reconfigure 3090 systems without destroying their genuine nature, as they have in the past, and can even remanufacture 3090 parts so long as Comdisco labels the parts as "altered."<sup>99</sup>

During litigation, Comdisco denied that identifying the origin of parts originally made by IBM was improper,<sup>100</sup> and offered numerous affirmative defenses.<sup>101</sup> The basis of Comdisco's position was that its

93. 15 U.S.C. § 1114, 1125(a) (1988). Additional counts (not discussed in this Comment) charge unfair competition and interference with business relations. Amended Complaint, *supra*, note 90.

94. Stipulation, *supra* note 8.

95. Answer, *supra* note 2, at 2-3, 14-15.

96. *Id.* Industry sources tend to confirm Comdisco's position on this issue. See *supra* note 71 and accompanying text for a discussion of comparative quality of remanufacturing techniques.

97. Since the record in the case is under protective order, it is impossible to determine whether these issues remained the focus of the IBM-Comdisco dispute at the time it was settled. However, for the purposes of this Comment it is assumed that these issues remained unresolved at that time, as it appears from that part of the record which is public.

98. See *supra* notes 14, 15, and 79 discussing the details of the settlement terms and their impact on Comdisco's business.

99. Settlement, *supra* note 1, at 3-4.

100. Answer, *supra* note 2, at 14.

101. The first defense is that which succeeded for AMI in *AMI v. IBM*, the 1956 consent decree. Answer, *supra* note 2, at 4-5. See *supra* note 81 for discussion of the grounds of the AMI decision. Other defenses are: violations of the 1956 Consent Decree under the Sherman Anti-Trust Act, laches, acquiescence, estoppel and waiver, that the IBM mark was not false more likely to confuse, fair use, and the incapacity of 3090 software and equipment to sustain patent or copyright protection. Answer, *supra* note 2, at 23-26.

The last of Comdisco's defenses is that the design of the 3090 is functional, and therefore incapable of trademark protection. Answer, *supra* note 2, at 14. However, since it is the IBM mark, not the 3090 equipment itself, which is in dispute the author is unable to see the relevance of this defense.

It is true that designs which are functional cannot be protected by trademark; only "communicative" designs can support trademark protection. *Sno-Wizard Mfg., Inc. v. Eisemann Prods. Co.*, 791 F.2d 423, 427 (5th Cir. 1986). "Under the utilitarian functionality test, the ultimate inquiry is whether the configuration as protected will hinder competition." *Id.* "To achieve the status of 'functional,' a design or feature must be superior or

3090 modules are not counterfeit and that it was thus not passing off fake goods as genuine. Moreover, Comdisco claimed that 3090 modules are "fungible,"<sup>102</sup> so that it is unreasonable for IBM to demand its lessees to return each module with the exact original serial number.<sup>103</sup> Comdisco contended that the equipment was returned to IBM in the exact same configuration in which it was delivered except that the serial numbers on some of the component parts were different.<sup>104</sup> Comdisco declined to countersue IBM for reconfiguring Comdisco-owned IBM 3090's.<sup>105</sup> Instead, it sought to prove that the practices of modifying and subleasing 3090 systems is a legitimate practice and an industry standard.<sup>106</sup> The settlement appears to have largely vindicated this claim, except in cases where Comdisco misled customers.<sup>107</sup>

Finally, Comdisco alleged that IBM had a hidden motive beyond simply protecting its "assets and customers."<sup>108</sup> that IBM was trying to force customers to do business with IBM only, so that IBM could dictate prices by eliminating competition.<sup>109</sup> Comdisco claimed that in foreign markets where IBM has no competition, 3090 equipment was considerably more expensive than it was in the United States.<sup>110</sup>

### III. ANALYSIS

The sale of modified goods does not infringe trademark rights unless "the reconditioning or repair [is] so extensive or so basic that it would be a misnomer to call the article by its original name, even though the words 'used' or 'repaired' were added."<sup>111</sup> This is true even if the goods are degraded "so long as the manufacturer is not identified with the in-

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optimal in terms of engineering, economy of manufacture, or accommodation of utilitarian function or performance." *Sicilia Di R. Biebow & Co. v Cox*, 732 F.2d 417, 429 (5th Cir. 1984).

102. Comdisco's White Paper, *supra* note 3, at 8.

103. *Id.* at 8-11.

104. *Id.*

105. *Id.* at 13-15.

106. *Id.*

107. Nothing in the settlement agreement appears to restrict releasing per se. Settlement, *supra* note 1. Wall Street's positive reaction to the settlement shows that industry analysts do not perceive the agreement as a fundamental threat to Comdisco's business practice. *Comdisco Settles Suit*, *supra* note 14.

108. Comdisco's White Paper, *supra* note 3, at 13-15.

109. *Id.*

110. Comdisco brought this matter to IBM's attention nearly 10 months before IBM sued. *Id.* at 13-15. Why did not IBM seek a business resolution of the issue? Memory modification began two decades and three "computer generations" before 3090 systems were introduced. *Id.*

111. *Champion Spark Plug Co. v. Sanders et al.*, 331 U.S. 125, 129 (1947).

ferior qualities of the [modified] product."<sup>112</sup> Specifically, the U.S. Supreme Court, in *Champion Spark Plugs v. Sanders*,<sup>113</sup> addressed the truthfulness of information which reaches the consumer, stating "[f]ull disclosure gives the manufacturer all the protection to which he is entitled."<sup>114</sup>

The court in *Champion* relied on *Prestonettes, Inc. v. Coty*,<sup>115</sup> which also focussed on truthfulness: "When the mark is used in a way which does not deceive the public we see no such sanctity in the [trademark] word as to prevent its being used to tell the truth. It is not taboo."<sup>116</sup> Justice Holmes wrote that "[i]f a man bought . . . a demijohn of Old Crow whiskey, he certainly could sell . . . the whiskey in bottles, and tell what it was, if he stated that he did . . . the bottling."<sup>117</sup>

Given the rules of *Champion* and *Prestonettes*, even 3090's remanufactured with some non-IBM parts are genuine.<sup>118</sup> Remanufacturing equipment which began as IBM memory, to function like IBM

112. In *Champion*, the defendants reconditioned used spark plugs and sold them without removing the trademark. *Id.* at 126-27. The reconditioned plugs were inferior to new plugs. *Id.* The trademark holder sued, claiming that the rebuilt plugs were not authentic, so that their sale violated its trademark rights. *Id.* The court approved an order which required the defendants to clearly identify the plugs as used but allowed the defendants to indicate that the plugs were originally made by Champion. *Id.* at 127-28. The court reasoned that "inferiority is immaterial so long as the article is clearly and distinctively sold as repaired or reconditioned." *Id.* at 128.

113. *Id.*

114. *Id.* It may be noted that truthfulness is exactly what IBM got from Comdisco under the terms of the agreement—which does limit Comdisco's business practices so long as Comdisco is truthful and forthcoming. Settlement, *supra* note 1, at 2-4.

115. 264 U.S. 359 (1924).

116. In *Prestonettes*, the U.S. Supreme Court held that trademark rights do not prevent a manufacturer from buying powder and perfume in quantity, mixing it with a "binder," and selling it in different containers which contained the original product's trademark, so long as the label clearly indicated how and by whom the goods had been altered. *Id.* at 367-68. The fact that the product may have been degraded by the alteration was not relevant: "If the defendant's rebottling the plaintiff's perfume deteriorates it and the public is adequately informed who does the rebottling, the public . . . is likely to find it out." *Id.* at 351.

117. *Id.* The terms of the settlement follow Holmes' view almost to the letter. Comdisco is allowed to alter or even degrade the goods, but it must inform consumers of what they do. Settlement, *supra* note 1, at 2-4.

118. Nobody would claim that it was a "misnomer" for a used car dealer to sell a used Ford which had been repaired with a few non-Ford parts as a "Ford." Similarly, it's hard to imagine why it would be a "misnomer" to use the name IBM for a complex computer system built almost entirely by IBM but with a few non-IBM parts. See *Champion*, 331 U.S. 125, 128-29.

This viewpoint was apparently shared by the parties in *IBM v. Comdisco*, who agreed to allow (in fact, to require) Comdisco to call altered IBM 3090 computers "IBM" but only with the caveat that the parts are "altered IBM", not *fully* IBM and not eligible for IBM maintenance. Settlement, *supra* note 1, at 3-4.

memory, cannot make the use of the name IBM a "misnomer."<sup>119</sup> These cases allow for a certain inferiority in reconditioned goods, so that even if IBM's claim that remanufacturing degrades the 3090 memory is true, the computers remain authentic.<sup>120</sup> Both cases demand truth. Comdisco and other brokers could truthfully claim that the computers they lease out are "modified IBM" equipment, just as the defendants in *Champion* said that their plugs were modified Champion plugs.<sup>121</sup>

However, both *Champion* and *Prestonettes* arose in the context of sales, not leases.<sup>122</sup> This Comment contends that the well-established rule that resellers of altered genuine goods may use the original trademark should be extended to lessors as well. There is no direct precedent determining whether leasing modified trademarked goods violates the Lanham Act even though sales do not.<sup>123</sup> This Comment approaches the issue of the disavowability of trademark in three ways. First, this Comment considers whether traditional or modern policies supporting trademark protection justify a trademark owner's disavowal of altered goods. Second, it considers the necessary balance between the policies supporting trademark protection and those supporting free trade. Third, it considers the analogous case of the "gray market", in which manufacturers of trademarked goods intended for foreign markets disavow their authenticity when imported into the United States. This Comment concludes that given any of these three approaches, manufacturers should never be allowed to disclaim their own re-leased goods unless the modification is hidden from consumers.

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119. See *Champion*, 331 U.S. 125, 128-29.

120. *Id.* at 126-128.

121. *Id.*

122. See *supra* notes 112 and 116 and accompanying text for discussions of the facts in *Prestonettes* and *Champion*.

123. The author has been unable to find any cases which directly address the ability of a trademark holder to disclaim his own goods for the purpose of sustaining trademark violations against those who lease them after they have been altered. This is surprising since the lease of used trademarked goods often involves the sale of altered goods. For example, used cars rarely if ever contain the exact same parts with which they were originally manufactured, and are typically repaired with some parts which were not produced by the original manufacturer. See *Champion*, 331 U.S. 125, 128-29 for a discussion of practices in the auto industry.

This lack of precedent is most likely attributable to the fact that manufacturers rarely have any reason to disavow the authenticity of their products on resale, even if altered. The reverse is typically true: the fact that the product has a resale value merely enhances the trademark's value. Manufacturers rarely put themselves in the embarrassing position of claiming that products which they themselves originally produced are no longer authentic. "[O]ne is immediately struck by the obvious incongruity of the argument that the sale of genuine trademarked goods can constitute trademark infringement . . . [It is a] seemingly implausible proposition." Laufer, *supra* note 20, at 169.

## A. POLICIES SUPPORTING TRADEMARK PROTECTION

1. *Traditional "Source" View*

Three policies are often cited to support trademark protection: identification of product source, assurance of product quality, and protection of good will.<sup>124</sup> The traditional "source" view was that trademark law was primarily designed to assure that buyers would know who produced items offered for sale.<sup>125</sup> This was thought to benefit both trademark holders and consumers. Trademark holders benefit because reputation and repeat buyers drive sales.<sup>126</sup> Consumers benefit from the ability to rely on trademarks to determine the nature and quality of goods and services.<sup>127</sup>

This Comment contends that the traditional "source" view of trademark offers little support for the notion that a trademark holder should have the power to disavow his own products when they are altered. The source of a product does not change merely because the product is modified. To permit a trademark holder to disclaim products which it has released into the marketplace would confuse consumers as to their origin. If products are completely stripped of their trademark, buyers would be led to believe that the goods did not derive from the trademark holder when in fact they did.<sup>128</sup>

The best method of indicating the source of the equipment involved in the IBM-Comdisco dispute would be full disclosure — to allow independents to call the computers "modified IBM" or "rebuilt IBM" — or,

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124. "Trademarks serve three basic purposes: 1) to indicate origin; 2) to guarantee equal quality of all goods under that mark; and 3) as an embodiment of good will." Laufer, *supra* note 20, at 169.

125. *Id.*

126. *Id.* at 174-75.

127. *Id.*

128. For example, if Comdisco were to strip the IBM logo from the 3090 computers which it re-releases or resells and use its own trademark, consumers would naturally assume that Comdisco had created the computer rather than IBM. This would not only be untrue, but would actually deprive IBM of goodwill. Used IBM Computers rarely fail. Complaint, *supra* note 4, at 8. If such high-quality goods were labelled "Comdisco" rather than "IBM", Comdisco would gain goodwill, not IBM. It is difficult to imagine why IBM would want to force Comdisco to do so.

If so, and if IBM prevails in the current litigation and so can prevent the release of altered goods under its own trademark, alteration itself would become impossible. Comdisco would be "between a rock and a hard place": unable to release an altered product under its original IBM label (for violation of trademark) and unable to release the product under any other label either (as deceptive).

In effect, such a position would mean that trademark protection provides an invisible "string" of continuing control between a trademark owner and its products even if they have been sold or leased to others. The trademark owner could effectively prevent possessors from altering the product in any way, or force them to remove the product from commerce if they did alter it.

as the settlement chose to do, "altered IBM."<sup>129</sup> To exclude the use of the IBM mark entirely would leave independent lessors with no way to inform consumers of the nature or origin of their equipment. Such a restriction would impede, not promote, the spread of useful consumer information. There is no more reason in leases than in sales to make trademarks "taboo."

This Comment contends that in light of the "source" view, only IBM equipment which has been remanufactured using parts originally manufactured by non-IBM firms might arguably lose its authentic character. Even such equipment<sup>130</sup> is at least "partly" IBM. Dramatically altered equipment could, without confusion, be called "modified IBM using non-IBM parts." The consumer will be less informed and more confused by stripping the IBM name entirely from equipment which it originally manufactured than if the trademark remains, together with an explanation.<sup>131</sup>

## 2. *The Modern "Quality" View*

Over the last few decades, commentators have focused on the role trademarks play in assuring quality products and competitive prices in the marketplace,<sup>132</sup> thereby increasing the efficiency of the economy as a whole.<sup>133</sup> Trademark holders are encouraged to produce goods which offer good quality for the price.<sup>134</sup> Good products build reputation and tend to induce previous buyers to buy again.<sup>135</sup> Trademarks also provide a mechanism to hold merchants responsible in the marketplace for poor-quality goods. A merchant who attempts to promote sales by foisting shoddy goods into the market using trademarks, risks devaluing the trademarks by associating them with undesirable products.<sup>136</sup>

If altering 3090 equipment degrades it (as IBM claimed but Comdisco denied), then this "quality" view of trademark might seem to offer limited support for IBM's original position.<sup>137</sup> IBM's mark would be associated in the marketplace with shoddy goods whose poor quality did not result from IBM's actions.

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129. Settlement, *supra* note 1, at 4.

130. See *supra* note 5. (Comdisco denies ever having leased equipment containing parts not originally manufactured by IBM.) The terms of the settlement would seem to allow Comdisco to mix fully IBM parts, altered IBM parts, and non-IBM parts in the same system so long as all of these parts were truthfully labelled. Settlement, *supra* note 1, at 2-4.

131. See Justice Holmes' discussion in *Prestonettes*, *supra* note 116.

132. *Id.*

133. Laufer, *supra* note 20, at 173-75.

134. *Id.*

135. *Id.*

136. *Id.*

137. See *Parfums Stern, Inc. v. United States*, 575 F. Supp. 416 (S.D. Fla. 1983).

However, in *Prestonettes*<sup>138</sup> Justice Holmes dismissed this exact kind of concern. In *Prestonettes*, the reconditioned goods were clearly inferior to new ones. Yet Holmes noted that so long as the person who degrades the goods is known to the public, it is his reputation—not that of the mark holder—which will suffer when goods are modified.<sup>139</sup> Consequently, so long as the public knows that someone other than IBM is responsible for altering the 3090's leased by independents (as the settlement in *IBM v. Comdisco* requires<sup>140</sup>), it is the independents (not IBM) whose reputations are at stake. If the quality of the products leased by Comdisco is lower than that of the products leased by IBM, the market will observe the difference and put the blame—and competitive disadvantage—where it belongs, on Comdisco.<sup>141</sup>

### 3. Recent "Good Will" View

A firm's trademark functions as a legal embodiment of its good will, and protecting good will is a third policy often cited in recent trademark cases.<sup>142</sup> Unlike the traditional "source" view, which balanced benefits to buyer and seller, and unlike the "quality" view, which focuses on benefits for the economy in general, the more recent "good will" view looks only to the benefit of the trademark holder. Given the "good will" viewpoint, trademarks are treated like other property rights,<sup>143</sup> and thus,

138. 264 U. S. 359, 368.

139. *Id.*

140. Settlement, *supra* note 1, at 2-4.

141. See *supra*, note 117, for a discussion of *Prestonettes*.

142. Laufer, *supra* note 123, at 172. This theory of trademark protection is conspicuous by its absence from U.S. Supreme Court cases. C. Dustin Tillman, *Lever Brothers Corp. v. United States: An Expansion of Trademark Protection Beyond the Limits of K-Mart Corp. v. Cartier, Inc.*, 18 N.C.J. INT'L L. & COM. REG. 685, 717 (1993). The K-Mart court failed to address trademark theories at all. *Id.* Older cases also omit goodwill as an underpinning of trademark law. A. *Bourjois & Co. v. Katzel*, 260 U.S. 689 (1923), refers only to the "source" theory, and *Prestonettes* mentions goodwill, but only the context of the "quality" theory. *Craig v. Harney*, 331 U.S. 367, 370-71 (1947).

143. *Osawa & Co. v. B. H. Photo* demonstrates this "propertarian" view of trademark rights well. 589 F. Supp. 1163 (S.D.N.Y. 1984). In that case, the court granted an injunction barring grey market imports. *Id.* at 1170. The court held that mere money damages would not be sufficient to protect the trademark (as would likely be the case in protecting real estate). *Id.*

The court recognized a "separate legal existence" in a trademark right. *Id.* at 1172. The court repudiated both the "source" and "quality" policies, favoring only the theory the trademarks protect goodwill, whose "proper lawful function is not necessarily to specify the origin or manufacture of a good (although it may incidentally do that), but rather to symbolize the goodwill of the domestic markholder so . . . [he] . . . may be confident that his goodwill and reputation (the value of the mark) will not be injured." *Id.*

The court noted that because the grey goods were much less expensive than those authorized for U.S. sale, "many [consumers] will no doubt assume. . . that plaintiff is gouging, which will engender hostility to the mark." *Id.* at 1169. The court seemed unconcerned as

may be more vigorously defended than under other theories.<sup>144</sup>

If trademark holders are allowed to unilaterally disavow their products merely because the goods are modified, they are likely to simply use such modification as a pretext for claiming high-quality used goods as authentic and disclaiming shoddy ones, since nearly all used products are altered in some way.<sup>145</sup> Even if altering 3090 systems degrades them, as IBM contends,<sup>146</sup> it is hard to see how IBM's good will is injured, so long as consumers are aware that somebody else has altered the computers.<sup>147</sup> Why would consumers blame the original producer for harmful alterations? The reputation which will suffer is that of the firm which performs the modifications.<sup>148</sup>

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to whether or not the markholder was actually gouging, rejecting economic arguments. *Id.* Such concerns were unable to "undercut the essential persuasiveness of plaintiff's case"—that the markholder was entitled to the court's support in its efforts to maintain the value of its trademark and goodwill. *Id.*

However, there is good reason to suspect that the *Osawa* court's rationale was wrong. "[T]he [K-Mart] Court's failure to address. . . trademark theories suggest[s] that Lever and its supporting cases have taken the wrong approach." Tillman, *supra* note 141, at 720. *Osawa* is one of the cases supporting Lever. *Id.* Moreover, though *K-Mart* did not explicitly over-rule *Osawa*, it did allow grey market imports on very similar facts. *Id.* *Osawa* is probably bad law, and the rationale underlying it—a vigorous "propertarian" view of trademark rights—is probably bad law too.

144. *Id.*

145. This would enable a manufacturer to promote an image of quality based not on truth but on selective dissemination of information. For example, take the hypothetical case of a manufacturer, WidgetCo which generally produces top-quality widgets and has a good reputation as a result, but which has poor quality control and so occasionally sells defective widgets which wear out prematurely.

Sellers of used WidgetCo products would naturally seek to present their goods as WidgetCo widgets to gain the full value of the product, including its trademark. If they were allowed to do so, the prematurely worn widgets would be associated with the WidgetCo name and tend to degrade WidgetCo's reputation.

But, if sellers of used WidgetCo were not allowed to use the WidgetCo name without consent from WidgetCo, this would permit WidgetCo to selectively decide which widgets would continue to be associated with its trademark. Worn-out, defective goods could be disclaimed, and only full-quality used widgets associated in the marketplace with the WidgetCo mark. Thus consumers would never know that WidgetCo had poor quality control, and the strong reputation of WidgetCo would be partly based on that ignorance.

If trademarks embody the good will of a company, logically they ought to embody bad will as well. They cannot do so if a mark holder can use the excuse of minor modifications to disassociate itself from low-quality goods and the bad will they generate.

146. See *supra* note 5 for discussion of the issues in the IBM-comdisco litigation.

147. *Prestonettes*, 264 U.S. at 367.

148. *Champion*, 331 U.S. at 128.



#### 4. Trademark Rights & Aftermarket Control

Part of the value of a product is its trademark.<sup>149</sup> Otherwise identical goods will command a higher price if they bear a trademark.<sup>150</sup> Having paid for it, the possessor, not the mark holder, owns this added value.<sup>151</sup> To permit a mark owner to revoke its trademark would, in effect, allow the mark owner to unilaterally destroy this added value. The threat of doing so would provide the trademark holder with leverage over the current possessor of the goods.<sup>152</sup> Allowing a trademark holder to unilaterally revoke his mark would permit the trademark holder to exert indirect control over the goods he manufactured after he releases them into trade.<sup>153</sup> Such control would create an invisible "string" connecting a mark holder to the goods he produces even after they have entered the market.<sup>154</sup>

Trademarks are limited by the doctrine of exhaustion,<sup>155</sup> under which trademark rights can be exercised only once.<sup>156</sup> The policies which underlie this doctrine strongly suggest that trademarks are not intended to allow a trademark holder to maintain control over products

149. This concept underlies the doctrine of exhaustion. See *infra* note 155 for a discussion of this doctrine.

150. *Id.*

151. The mark holder owns the mark itself, of course, but not the added value which the mark gives to the goods. The mark holder has sold, and the possessor has paid for, this additional value.

152. The mark owner could use this leverage to force the possessor to deal only with the mark owner, or to refrain from using or disposing of the goods in certain ways. For example, consider WidgetCo. See *supra* note 145. If owners of used WidgetCo widgets could not sell them as WidgetCo products (and thus could not gain the full value of their goods) without WidgetCo's consent, their investment in WidgetCo widgets would be at the mercy of WidgetCo. WidgetCo might refuse to grant consent to sell the goods as WidgetCo unless they agreed to buy only WidgetCo products in the future, or unless they agreed to refrain from using the widgets in machines built by WidgetCo's main competitor. Owners of used WidgetCo widgets could avoid such strictures only by taking a loss and selling good-quality WidgetCo widgets without the benefit of their full market value as WidgetCo products.

153. See *supra* note 152 for a discussion of WidgetCo.

154. See *supra* note 145 for a discussion of a trademark holder's continued control over its products.

155. The doctrine of exhaustion does not apply directly to leases. See Daniel M. McClure, *Trademark and Unfair Competition: A Critical History of Legal Thought*, 69 TRADE-MARK REP. 316-26 (1979). Nonetheless, it is hard to see why the policies which underlie this doctrine would differ between leases and sales. The power that a trademark gives to the trademark holder is to decide when and under what conditions—especially, at what price—the trademarked good is released into the marketplace. *Id.* Once this power has been exercised, it is "exhausted." *Id.* No control exists after the sale. *Id.* Thus, the theory of exhaustion views products more or less like children. Once emancipated, children may bring pride or disgrace to their parents. But either way, they have left their parents' control.

156. *Id.*

bearing its mark after they are released into trade.<sup>157</sup> After a trademark holder has sold its product, its trademark rights are exhausted and it has no further power to control the goods.<sup>158</sup>

After-market control is not furthered by any trademark policy. No policy suggests that trademarks create some "invisible string" tying a manufacturer to goods bearing its trademark. In order for trademarks to serve their legitimate functions, the goods they mark must be free to move freely in the marketplace unhindered by their producers. A string by which a trademark holder could control which of its products are associated with its mark can only serve to allow the trademark holder to manipulate the market perception of the trademark.

IBM's 1956 Consent Decree would make it especially inappropriate for the courts to recognize a "string" between IBM and 3090 systems which it leases. The purpose of the decree was to break, not further, IBM's control over its goods.<sup>159</sup> To allow IBM to establish control over the market for 3090 systems through trademark would directly threaten the open marketplace assured by the consent decree.

#### B. BALANCING FREE TRADE AND TRADEMARK PROTECTION

The doctrine of patent abuse<sup>160</sup> reflects judicial awareness of the danger which intellectual property rights can pose to a free market-

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157. *Id.*

158. *Id.*

159. *AMI*, 767 F. Supp. at 542.

160. The modern status of the doctrine of patent abuse is somewhat unclear. Kevin J. Arquit, *Patent Abuse and the Antitrust Laws*, 59 *ANTITRUST L. J.*, 735, 740-42 (1991). At one extreme, it has been suggested that the doctrine has been simply absorbed into the rule of reason in anti-trust cases; at the other extreme, some courts seem to recognize it as a broad limit on patent rights. Robert J. Hoerner, 59 *Patent Misuse: Portents for the 1990s*, *ANTITRUST L. J.*, 687, 689-92, Vol. 59 (1991). The essence of the doctrine is that where a patent is used to unreasonably restrain trade, it cannot be enforced until a "purge" has been effected. *Id.* The patent abuse doctrine derives from the observation that patents are "an exception to the general rule against monopolies," and thus cannot be unlimited. *Precision Instrument Mfg. Co. v. Automotive Maintenance Mach. Co.*, 324 U.S. 806, 846 (1945). "An often-neglected point, though critical, is that a patent monopoly does not invariably translate into a monopoly in [a] relevant market." Arquit, *supra* note 122, at 740. The patent provides no "market power" if similar goods using non-patented technology can create a competitive marketplace. *Id.* A finding of patent abuse is only possible where such "substitutes" fail to establish a competitive market. *Id.* See also *BSM Corp. v. SPS Technologies, Inc.*, 694 F.2d 505 (7th Cir. 1982).

Thus the doctrine of patent abuse is born of the need to balance policies supporting patents against those supporting free trade. Though the author has found no U.S. reference to a corresponding theory of "trademark abuse", the need to balance policies is no less crucial for trademark law than it is for patent law and has been recognized in Europe.

In *IBM v. Phoenix Co.*, decided under the rules of the European Economic Community, the Commission noted that a rule against "trademark abuse" does exist but (on factual grounds) denied Phoenix's claim that IBM's trademark infringement suit in the United

place.<sup>161</sup> The use of trademark rights to establish a permanent string of control between a trademark holder and its products would threaten policies supporting free trade.<sup>162</sup>

The IBM-Comdisco dispute arose in a market monopolized by IBM and subject to close antitrust scrutiny under the 1954 Consent Decree.<sup>163</sup> Had it gone to trial, it is possible that *IBM v. Comdisco* would have been resolved, at least in part, with reference to the decree. An earlier suit between IBM and independent brokers, *AMI v. IBM*,<sup>164</sup> was resolved in this manner.

At first glance, it might seem odd to apply anti-trust regulation to the market for a single brand of goods (for example, surely the Sherman Act does not prevent General Motors from exploiting its complete monopoly on the market for new Chevrolets). However, the U.S. Supreme Court held that in some cases the market for a single product brand does fall within the power of anti-trust legislation.<sup>165</sup> The Court held that a manufacturer's attempt to create a "safe harbor" in its own aftermarket—to monopolize trade in its own used goods—violates the

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Kingdom rose to the level of "abusive use of trademark." IV/34.349 (European Economic Commission, 1992).

161. Intellectual property rights invariably restrain trade in some ways, but this restraint is accepted in order to promote creativity and investment in research and product development. Where such restraint of trade fails to promote these goals, and is used for illegitimate purposes, however, the balance between free trade policies and trademark rights theories must heavily favor the open market. Arquit, *supra*, note 160, at 740.

162. *Id.*

163. See *supra* note 81 for discussion of the earlier litigation between AMI and IBM.

164. *Id.*

165. In *Kodak*, a group of independent copy-machine repair companies sued Kodak after Kodak refused to sell them replacement parts, making it almost impossible for them to remain in business. *Kodak*, 112 S. Ct. at . . . Within a few years, Kodak had driven most competition from the market and gained almost complete control over maintenance of copying machines which it had manufactured. *Id.* The court refused to sustain Kodak's motion for summary judgement. *Id.*

Section 1 of the Sherman Antitrust Act states, in part:

Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, is declared to be illegal.

15 U.S.C. § 1 (1988).

This Act has been interpreted to invalidate a "tying arrangement" (an arrangement by which a seller refuses to sell one product unless another is also purchased) if the seller exploits "its control over the tying product to force the buyer into the purchase of a tied product that they buyer either did not want at all, or might have preferred to purchase elsewhere." *Jefferson Parish Hospital Dist. No. 2 v. Hyde*, 466 U.S. 2, 12 (1984).

The court held that "tying demands" violate section 1 of the Sherman Act if the seller has sufficient economic power to force a purchaser to act in ways it would not have acted in a competitive market. *Kodak*, 112 S. Ct. at 2079-2081. The court recognized that a single manufacturer's products can form a market in which that manufacturer might exercise unreasonable monopoly control. *Id.* at 2092.

Sherman Anti-trust Act.<sup>166</sup> If IBM were allowed to use the Lanham Act to cripple its competitors in the used 3090 marketplace, it would create just such a forbidden "safe harbor" in which market constraints have little or no power to limit IBM's actions.<sup>167</sup>

The Court declined to accept "Chicago School" economic theories which accepted the creation of "market-share based 'safe harbors,'" such as that Kodak formed in its own aftermarket.<sup>168</sup> The court noted that only "imperfect information" in the market could facilitate Kodak's "safe harbor."<sup>169</sup> The court refused to enforce the "Chicago School" view that such imperfect information is rare and less harmful to the economy than are efforts to alleviate its consequences.<sup>170</sup>

Permitting a manufacturer to disclaim the authenticity of its own goods, and thereby creating a "string of control" whereby a manufacturer maintains economic power over its products after they are sold or leased, would tend to create aftermarket "safe harbors" of the kind limited in *Kodak*.<sup>171</sup> Allowing trademark holders like IBM to disclaim their products would go beyond mere acceptance of "imperfect information" in the market which the *Kodak* court rejected. To permit trademark holders to disassociate themselves from their own product actually encourages misinformation and confusion in the market.

### C. TRADEMARK HOLDER'S DISCLAIMERS OF AUTHENTICITY OF GRAY MARKET GOODS

Most recent cases in which the courts have been presented with the question of whether a trademark holder can sustain a disavowal of the authenticity of goods arise from the "gray market."<sup>172</sup> Gray market goods are defined as originally authentic trademarked items imported into the United States without the consent of the trademark owner.<sup>173</sup> Under section 133.21 of Customs Regulations,<sup>174</sup> gray market goods may

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166. *Kodak*, 112 S. Ct. atb 2092

167. *Id.*

168. Robert H. Lande, *Chicago Takes It On The Chin: Imperfect Information Could Play A Crucial Role in the Post-Kodak World*. 62 ANTITRUST L. J. 193, 195 (1993).

169. Had Kodak customers known that they would later be forced to deal with Kodak in a non-competitive market for parts and repairs, they might have looked elsewhere to purchase equipment. *Id.*

170. *Id.*

171. *Kodak*, 112 S. Ct. 2079-81.

172. *See supra* note 18 for discussion of the gray market.

173. *Id.*

174. 19 C.F.R. 133.21 (1985). The regulations state, in part:

(a) Copying of simulating marks or names. Articles of foreign manufacture bearing a mark or name copying or simulating a recorded trademark or trade name shall be denied entry and are subject to forfeiture. . . A "copying or simulating" mark or name is an actual counterfeit of the recorded mark or name or is one

be legally imported when the foreign manufacturer is the same as,<sup>175</sup> or subject to common control with,<sup>176</sup> the U.S. trademark holder. However, where the foreign manufacturer and U.S. trademark holder are independent of one another, gray market trademarks are regarded as "counterfeit" and gray market imports are not allowed.<sup>177</sup>

In *K-Mart Corp. v. Cartier*,<sup>178</sup> the U.S. Supreme Court upheld these regulations.<sup>179</sup> The Court focused on the relationship between the foreign and domestic trademark holders, rather than on questions of authenticity or trademark theories.<sup>180</sup> Thus, the case does not directly resolve the question of whether originally authentic goods can become "counterfeit".<sup>181</sup>

The *K-Mart* court declined to resolve the gray market issue on economic or policy grounds, and chose instead a "very technical analysis in interpreting the plain meaning of" the Tariff Act of 1930.<sup>182</sup> However, the reasoning in *K-Mart* reflects the Court's recognition that a manufacturer which disavows its own products has taken a rather awkward posi-

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which so resembles it as to be likely to cause the public to associate the copying or simulating mark with the recorded mark or name.

(b) Identical trademark. Foreign-made articles bearing a trademark identical with one owned by a citizen of the United States. . . are subject to seizure and forfeiture. . .

(c) Restrictions not applicable. The restrictions of (a) and (b) of this section do not apply to imported articles when:

(1) Both the foreign and U.S. trademark or trade name are owned by the same person or business entity;

(2) The foreign and domestic trademark or trade name owners are parent and subsidiary companies or otherwise subject to common ownership or control. . .

(3) The articles of foreign manufacture bear a recorded trademark or trade name applied under authorization of the U.S. owner.

*Id.*

175. 19 C.F.R. 133.21(c)(1) (1985).

176. 19 C.F.R. 133.21(c)(2) (1985).

177. *A. Bourjois & Co. v. Katzel*, 260 U.S. 689, 691 (1923).

178. 486 U.S. 281 (1988).

179. In *K-Mart*, various trademark holders challenged sections 133.21(c)(1) and 133.21(c)(2), which allow gray market imports when the foreign manufacturer and U.S. trademark holder are the same or subject to common control. *Id.* The basis of the challenge was that the regulations violated section 526(a) of the Tariff Act of 1930, which reads (in part): "[I]t shall be unlawful to import. . . merchandise of foreign manufacture if. . . [it]. . . bears a trademark owned by a citizen of . . . the United States . . . unless written consent of the owner of such trademark is produced." 15 U.S.C. § 526(a) (1988).

Though section 42 of the Lanham Act was not at issue in *K-Mart*, it appears that the case could be readily extended to sustain the same regulations from attack based on the Lanham Act. *Tillman*, *supra* note 141, 687 n 17. *But see Lever Brothers Corp. v. United States*, 981 F.2d 1330 (D.C. Cir. 1993).

180. *Tillman*, *supra* note 141, at 721.

181. *Id.*

182. *Id.* at 720.

tion.<sup>183</sup> When IBM denies the authenticity of modified 3090's, it takes the same awkward position which trademark holders are forced to adopt in trying to block gray market imports.<sup>184</sup>

#### IV. CONCLUSION

Clearly, the law cannot approve the lease of modified goods as though they were not altered.<sup>185</sup> But, neither should the law recognize a manufacturer's attempt to disclaim the authenticity of its own products merely because the products have been modified. Consumers are capable of comprehending the difference between new goods and those which are used or which have been altered, and will not be confused as to either their source or quality.<sup>186</sup>

Allowing manufacturers to disavow their own products is contrary to the policies underlying both trademark protection and to those favoring free trade.<sup>187</sup> The main theories for the protection of trademarks are to assure that consumers are not confused as to the origin or quality of products in the marketplace.<sup>188</sup> When a manufacturer disavows its products, consumers are led to believe that the goods derived from a source other than the true manufacturer.<sup>189</sup> Consumers are led to think that the goods do not represent the quality of the producer's goods when they do.<sup>190</sup>

Trademark protection is not intended to create an "invisible string" whereby the trademark owner retains some degree of control over the goods which he has produced.<sup>191</sup> Such control would serve only to allow a trademark holder to prevent weaknesses in its products from becoming apparent, or to allow the trademark holder to disavow poor-quality goods and deceive consumers. Trademarks are protected so that consumers can reliably associate tradenames with product quality—both good and

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183. *Id.*

184. The court protected trademark holders who were separate from foreign manufacturers. *K-Mart*, 486 U.S. at 305. Since they were independent, the goods which they allege to be false are not their own. *Id.* But the court refused to protect trademark holders who were unified with the foreign manufacturers. *Id.* In order to gain trademark protection from gray market imports, such unified trademark holders are forced to claim that the gray market products—which they themselves produced and sell elsewhere—are counterfeits. Tillman, *supra* note 124, at 721.

185. See *supra* notes 112 and 116 for discussion of the policies in *Prestonettes* and *Champion* requiring disclosure.

186. *Champion*, 331 U.S. 128.

187. See the discussion in the text, pp. 19-21.

188. McClure, *supra* note 155, at 317.

189. See the discussion in the text, pp. 17-18.

190. McClure, *supra* note 155, at 322.

191. See *supra* note 129, explaining why trademark rights do not create a "string of control" over a markholder's products.

bad. Consumers need both the opportunity to seek products with tradenames they desire, and to avoid products with tradenames they do not desire.<sup>192</sup>

Though the dispute between IBM and Comdisco has now been settled, the threat which IBM was able to direct against its independent competitors shows how dangerous it can be to allow trademark holders to disavow their own products. Such disavowal gives the mark holder an opportunity to control not only its own goods, but the marketplace itself in which they are traded.<sup>193</sup>

Thus, courts should recognize that so long as modified trademarked goods are so identified, they retain their genuine character under the Lanham Act and similar trademark laws. Sale or lease of trademarked goods which have been altered but which are so identified cannot, as a matter of law, violate trademark rights.

*Amy Jacqueline Grason*

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192. *Id.*

193. McClure, *supra* note 155, at 318.