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# Colleges and Universities: Unfair Competition -- Taxation -- Status of Educational Institution Engaged in Profit-Making Enterprise

F. James Kane

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*Colleges and Universities*UNFAIR COMPETITION — TAXATION — STATUS OF EDUCATIONAL INSTITUTION  
ENGAGED IN PROFIT-MAKING ENTERPRISE*Introduction*

The growing concern for higher standards of education in the United States, coupled with the educational demands of the recent flood of eligible applicants to colleges and universities all over the country, has focused public attention on our educational institutions in the past few years. With an eye to heavy and increasing enrollments, many colleges have embarked upon programs of expansion, aimed at enlarging physical plant, administrative staff and faculty. The university today is vastly different from that known to the students of past eras. Many universities are "cities" in themselves, providing the student with goods and services of every manner and description. Indeed, in theory at least, the average student could have every need satisfied during his years of study without ever leaving the campus.

Even among smaller colleges, the marked trend toward "extra-curricular" commercialism can be noted. The "bookstore" has been so drastically altered that even the student wonders if the name still applies. Gigantic "feeder" corporations are wholly owned and controlled by educational institutions and their profits are channeled into the general funds to provide educational facilities over and above those derived through income from student fees, gifts and endowments.<sup>1</sup>

It is the purpose of this Note to analyse such commercialism in the light of the laws of unfair competition and taxation. To what extent will the universities' commercial rights be protected by the courts? Are their rights to provide goods and services limited to the needs of the students, or can they actually compete for public trade with private enterprise? Does private enterprise have a right to compete freely for student business? What property rights may the university exploit and how far do these extend? Does the fact that the destination of business profit is an educational fund entitle that business to preferential tax treatment in the eyes of the law? These are some of the questions that will be considered.

*I. The Power of a University to Engage in a Business for Profit*

At the very outset we are met with the vital question of whether a charitable corporation, specifically a university, has the power to engage in profit-seeking activities. If such a power exists, it must be derived from the statute governing the formation and organization of the institution, and in case of conflict between articles of incorporation and the governing statute, the statute controls.<sup>2</sup> The controlling statutes may expressly grant authority to participate in profit-seeking ventures,<sup>3</sup> or they may leave room for

<sup>1</sup> See, e.g., the discussion of the tax exemption requested for the Mueller Macaroni Co., wholly owned and controlled by the New York University Law School. *C. F. Mueller Co. v. Commissioner*, 190 F.2d 120 (3rd Cir. 1951), reversing 14 T.C. 922 (1950). See also *The Foundation Racket*, NEW REPUBLIC, Jan. 30, 1950, p. 11, which observes the inroads by universities into commercial ownership (radio station by Gonzaga College, Willow Run Airport by the Univ. of Michigan, hydro-electric plant by the Utah State College, and street railway by Morningside College of Sioux City, Iowa) and attributes \$150,000,000 income annually to businesses owned by educational institutions.

<sup>2</sup> *Accord*, State *ex rel.* McElhinney v. All-State Agricultural Ass'n, 242 Iowa 860, 48 N.W.2d 281 (1951); State *ex rel.* v. Southern Publishing Ass'n., 169 Tenn. 257, 84 S.W.2d 580 (1935).

<sup>3</sup> "[N]or shall such corporation be prohibited from engaging in any undertaking for profit so long as such undertaking does not inure to the profit of its members." IND. ANN. STAT. § 25-510(c) (1948).

"Carrying on business at a profit as an incident to the main purposes of the corporation . . . (is) not forbidden to non-profit corporations, but no corporation formed or existing under this part shall distribute any gains, profits or dividends to any of its members as such except on dissolution or winding up." CAL. CORP. CODE § 9200.

such authority by implication.<sup>4</sup> Conversely, the applicable statute may specifically prohibit such undertakings.<sup>5</sup>

Authority by implication may arise from a general non-profit corporation act,<sup>6</sup> or, as in the case of a state university, from the enabling legislation empowering its board of trustees or regents to supervise property and expenses.<sup>7</sup> To remain consistent with these grants, a commercial venture by the university must be reasonably incidental to the educational purposes of the institution to be sustained. Thus, a bookstore maintained on the campus of one state university was held to be incidental to the educational function of the school, and a taxpayer's complaint challenging the constitutional authority of the university to engage in such an enterprise was dismissed.<sup>8</sup> Similarly, a power will be implied from the general supervision grant to apply free from legislative and judicial control profits incidentally derived from a campus business to the building and maintenance of dormitories and other buildings.<sup>9</sup>

Under the prohibitive rule of the Tennessee statute,<sup>10</sup> however, an injunction was granted in a quo warranto proceeding by the state, on application of several commercial printers, to prevent a college printing shop from doing commercial printing in direct competition with them, despite the fact that the printing shop served some educational and financial needs of the student-operators who gained practical experience and received credit on their tuition, and that all profits went into the general funds of the school.<sup>11</sup> Two years later, faced with an almost identical situation, the court again granted the injunction prohibiting the non-profit corporation from doing printing and publishing work in competition with private enterprises, stating: "It is only so long as profits are earned incidentally only in the prosecution of the direct objectives of the association that they may be earned at all."<sup>12</sup> Thus, even though the enterprise was not permitted to continue in this case, the language indicates that the court would allow such activity in future cases if the business venture of the university were intimately connected with its chartered educational aims. There was no suggestion that the statute was an absolute prohibition on such activity.

The prospective effects of such activities on the commercial market is, of course, one factor governing the permissible limits of interpretation of these empowering statutes. The analogous situation of a school board, acting under general statutory authority to do anything which would advance the interests of education, illustrates this influence. In one instance where a school board attempted to sell texts to students at cost, the court, upon the petition of two taxpayers, enjoined such activity, reasoning that although the board could do whatever was necessary to accomplish its purpose, such action could not transform its character as a board of education to that of a trading corporation.<sup>13</sup> Here the complaining taxpayers were also commercial competitors whose market position was protected, at least indirectly, by the decision.

<sup>4</sup> "Each corporation shall have power: . . . (n) To have and exercise all powers necessary or convenient to effect any or all of the purposes for which the corporation is organized." ILL. ANN. STAT. ch. 32, § 163(a)(4) (Smith-Hurd 1954).

<sup>5</sup> "The means, assets, income or other property of the corporation shall not be employed, directly or indirectly, for any purpose whatever than to accomplish the legitimate objects of its creation, and by no implication shall it engage in any kind of trading operation. . . ." TENN. CODE ANN. § 48-1109 (1955).

<sup>6</sup> ILL. ANN. STAT. ch. 32, § 163(a)(4) (Smith-Hurd 1954).

<sup>7</sup> OHIO REV. CODE ANN. § 3335.10 (Page 1954), grants the board of trustees of Ohio State University general supervisory powers subject to the control of the general assembly in the matter of contracting debts.

<sup>8</sup> Long v. Board of Trustees, 24 Ohio App. 261, 157 N.E. 395 (1926).

<sup>9</sup> Fanning v. University of Minnesota, 183 Minn. 222, 236 N.W. 217 (1931).

<sup>10</sup> TENN. CODE ANN. § 48-1109 (1955).

<sup>11</sup> State ex rel. v. Southern Junior College, 166 Tenn. 535, 64 S.W.2d 9 (1933). The words of the charter of the college here being construed are substantially the same as TENN. CODE ANN. § 48-1109, note 5 supra.

<sup>12</sup> State ex rel. v. Southern Publishing Ass'n, 169 Tenn. 257, 84 S.W.2d 580, 582 (1935).

<sup>13</sup> Kuhn ex. rel. Sheehan v. Board of Educ., 175 Mich. 438, 141 N.W. 574 (1913). But see Cook v. Chamberlain, 199 Wis. 42, 225 N.W. 141 (1929), where the court recognized that such a sale of books was intimately connected with educational purposes.

It is in the area of liberally construed statutory powers, pointing towards ever-widening "approved" areas of commercial enterprise, where problems of unfair competition arise. If a university may own and control commercial corporations, operate laundries, sell jewelry, all of which are derivative sources of profit to it, they are operating in direct competition with outside interests. They are selling goods and performing services which otherwise would be sold or performed by purely commercial enterprises for private profit, and this regardless of whether the students alone or the public in general constitute the purchasing element. Admittedly, a distinction must be made between goods and services furnished on campus for the students, and an unqualified entry by the university into the general public market, since the policy considerations differ considerably in each case. Throughout this Note, this distinction between related and unrelated business activity will be used for purposes of discussion and analysis.

## II. *Businesses Related to the Educational Purposes of the University*

It is likely that the Tennessee courts, in construing the applicable statute,<sup>14</sup> would not categorize a campus bookstore as a "trading operation" as long as it (1) sold only books (2) to students (3) at cost. This narrow approach is in almost total judicial disfavor, and the trend has been toward enlarging the scope of related businesses and the corresponding legal protection granted to them, as the following discussion will demonstrate.

It is generally been accepted that the maintenance of dormitories and dining halls for students is directly related to the educational function.<sup>15</sup> Additionally, a university, in the exercise of its discretionary powers, has the right to make and enforce reasonable rules governing its student body, and a student by voluntarily entering a university, may waive legal privileges he might otherwise enjoy.<sup>16</sup> Assume that a college passes a regulation forbidding students to frequent eating places in the area not controlled by the college, and that as a result of this regulation a local restaurateur's business is ruined. Is this unfair competition? A Kentucky court met this problem in *Gott v. Berea College*<sup>17</sup> when asked to pass on a regulation contained in a student manual which stated: "The institution provides for the recreation of its students, and ample accommodation for meals and refreshment, and cannot permit outside parties to solicit student patronage for gain."<sup>18</sup> Dismissal from the school was the penalty for breach of this rule. The court held that this was a reasonable rule, that the college owed the plaintiff-restaurateur no special duty, and therefore he had no remedy against the school.<sup>19</sup> The rationale of the decision was that although there was interference with plaintiff's business relations, it was justified because of the paternal duty the school owed its students and the necessarily wide discretion granted for the exercise of this duty. In essence, the court

<sup>14</sup> TENN. CODE ANN. § 48-1109 (1955).

<sup>15</sup> *Phillips Academy v. Andover*, 175 Mass. 118, 55 N.E. 841 (1900); *Harvard College v. Assessors of Cambridge*, 175 Mass. 145, 55 N.E. 844 (1900); *Yale Univ. v. Town of New Haven*, 71 Conn. 316, 42 Atl. 87 (1899).

<sup>16</sup> *Anthony v. Syracuse Univ.*, 224 App. Div. 487, 231 N.Y. Supp. 435 (1928), reversing 130 Misc. 249, 223 N.Y. Supp. 796 (Sup. Ct. 1927); *People ex rel. Pratt v. Wheaton College*, 40 Ill. 186 (1866). *But see State ex rel. Stallard v. White*, 82 Ind. 278 (1882), and dictum in *People ex rel. Tinkoff v. Northwestern Univ.*, 333 Ill. App. 224, 77 N.E.2d 345 (1947), to the effect that students stand in a different position in relation to a public school than to a private one, at least as far as admission requirements are concerned.

<sup>17</sup> 156 Ky. 376, 161 S.W. 204 (1913). See generally 1 NIMS, UNFAIR COMPETITION AND TRADE MARKS § 171 (4th ed. 1947).

<sup>18</sup> 156 Ky. 376, 161 S.W. 204, 205 (1913).

<sup>19</sup> What is a reasonable rule under the circumstances is a question of fact. *Gott v. Berea College*, 156 Ky. 376, 161 S.W. 204 (1913). However, the courts seem most reluctant to interfere with the discretionary right of university officials to prescribe and enforce rules governing their student body. See *Anthony v. Syracuse Univ.*, 224 App. Div. 487, 231 N.Y. Supp. 435 (1928), reversing 130 Misc. 249, 223 N.Y. Supp. 716 (Sup. Ct. 1927). Despite the fact that a state university may, because of its character as a public institution, be hindered in prescribing rules of admission, this does not affect its right to prescribe rules governing the enrolled student body. See *State ex rel. Stallard v. White*, 82 Ind. 278 (1882).

denied any analogy between the school and a trading corporation. And yet, as will be illustrated in the *Notre Dame Ring* case,<sup>20</sup> *infra*, this is the precise analogy relied upon to restrict competition where the university's commercial rights are threatened by an outside interest.

A second interesting point raised in the *Gott* case in the form of a supplemental holding is that even if the rule were unreasonable, Gott was in no position to complain of it for he was not a student, nor did he have any children who were students. What Gott actually was attempting to do was protect his business, and not attack the rule as such. By way of contrast, the usual suit involving interference with business relations produces a different result. For example, a recent New Jersey case<sup>21</sup> involved a suit by a monument maker against a cemetery association to restrain the association from exercising its influence over "captive" lot owners which resulted in interference with plaintiff's prospective business. It was held that although the lot owners themselves were the only ones who could contest the rules set out by the cemetery association, plaintiff certainly had standing to sue on the business tort of interference with his prospective contracts. But however reasonable such a holding might be in the general area of business interference, it does not dim the lustre of the *Gott* holding, for the university stands in loco parentis to the students, and this relationship normally justifies interference with outside business. This was clearly enunciated in *Davison-Nicholson Co. v. Pound*:

. . . the right to protect a public educational institution and its student body is equal to or superior to the right of one, as a merchant, desiring to deal with such institution, or its students, and a wide discretion is necessarily vested in its governing board to determine the conditions on which such person may deal with the institution or student body; and if this discretion is exercised in good faith, there will, in general, . . . be no liability to one with whom the students have been forbidden to deal.<sup>22</sup>

Although this line of reasoning would seem to dispose of questions involving essential services performed for the students, several other problems arise when the university goes further and provides non-essential goods, such as articles of clothing and jewelry in its bookstore, or expands services performed for the students to cover faculty members, employees and their families — in short, those persons living in the surrounding area who normally would be customers of outside businesses. For instance, could the university limit sales of certain commercial clothing and jewelry to the campus bookstore and thus restrict outside competition, and still satisfy the good faith requirement of the *Davison-Nicholson Co.* case by showing that the profits derived from the sales went into general funds to improve facilities and lower tuition rates? The question can be skirted if some commercial property right can be discovered which the university has exclusive power to exploit, and which exploitation creates a special demand for such merchandise. The recognition of such a property right would grant the university a virtual monopoly on profit-making goods sold, and leave private enterprise powerless to compete, for its competition would result in a usurpation of this exclusive right. This would give the university still another commercial power not heretofore recognized at law.

### III. *The Notre Dame Ring Case: The Recognition of Commercial Property Rights*

The seeds of such a doctrine were sown in the recent case of *John Roberts Mfg. Co. v. University of Notre Dame Du Lac*.<sup>23</sup> Plaintiff was a jewelry manufacturer who manufactured and sold, through a South Bend, Indiana (the location of the University) outlet, a "Chinese copy"<sup>24</sup> of defendant's official class ring which bore the school name, seal,

<sup>20</sup> *John Roberts Mfg. Co. v. University of Notre Dame Du Lac*, 258 F.2d 256 (7th Cir. 1958), affirming 152 F. Supp. 269 (N.D. Ind. 1957).

<sup>21</sup> *Di Cristofaro v. Laurel Grove Memorial Park*, 43 N.J. Super. 244, 128 A.2d 281 (App. Div. 1957). See generally 1 NIMS, *op. cit. supra* note 17, § 176.

<sup>22</sup> 147 Ga. 447, 94 S.E. 560 (1917) (syllabus by the court).

<sup>23</sup> 258 F.2d 256 (7th Cir. 1958), affirming 152 F. Supp. 269 (N.D. Ind. 1957).

<sup>24</sup> See generally 1 CALLMAN, UNFAIR COMPETITION AND TRADE MARKS § 16.2(d) (2d ed. 1950).

and several other symbols peculiar to the university. Plaintiff copied the ring from one procured from the Notre Dame bookstore (the official outlet for the ring) by misstatements of purpose (to use as a gift), and, despite lip-service to the acknowledged policy of the school to sell the rings only to juniors, seniors and alumni of Notre Dame, sold a great number of them to sophomores in direct contravention of such policy. The court affirmed an injunction against the plaintiff who had brought a declaratory judgment action against the school, adopting that trial court's judgment and decree:

That the Plaintiff be, and is hereby perpetually enjoined from using the words "University of Notre Dame" and the official seal and identifying symbols of the defendant in connection therewith, on any ring manufactured by the plaintiff and from the sale and disposition thereof.<sup>25</sup>

The gravamen of the counter-claim upon which the university prevailed was unfair competition. The name of an educational institution is now analogized to a trade name and the appropriation of this name, or the seal or symbols of the university, for use on commercial products in direct competition with the school is unfair competition, regardless of the fact that neither the name nor seal is registered as a trade mark or collective mark under the applicable laws.<sup>26</sup> This is even more than could be had by a trading corporation in that it grants an exclusive right at common law, the permanency of which is not available under trade mark or design patent registration acts.

Although there was a definite fraud practiced by Roberts Co. on the university in the procurement of the ring which, of itself, would have grounded an injunction in the instant case,<sup>27</sup> the court apparently did not rely on this element in reaching its decision regarding unfair competition. Nor did it rely on the fact that Roberts Co. had violated the school's longstanding policy of selling the class rings solely to upperclassmen and alumni. Thus the holding is significant even if we assume that the plaintiff had obtained the ring in a legitimate manner and furthermore had adhered to the policy of the school in selling the rings only to the authorized purchasers, thereby competing directly and fairly with the school for limited business.

It is significant because, under this assumption, the court extends judicial protection of the corporate name beyond its usual scope, *i.e.*, where the corporate name had attained a "secondary meaning" and a subsequent use of the name by another company would probably deceive or confuse the public, and where the value of the name of the first user might be "diluted" by any subsequent, though not competitive, use on a commercial product.<sup>28</sup>

In the first place, there is no public deception here, for the public is not involved, and those who are involved certainly must be taken to know that the ring bought from

<sup>25</sup> 258 F.2d 256, 257 (7th Cir. 1958).

<sup>26</sup> The fact that Notre Dame had registered the seal under the Indiana trademark law, IND. ANN. STAT. § 66-130 (Supp. 1957) before the trial had no bearing on the issue. Also, whether or not the mark was registerable under the Lanham Act, 60 Stat. 427 (1946), 15 U.S.C. §§ 1051-1127 (1952) — a question involving a decision as to whether or not the mark was used in interstate commerce — was held not necessary to a decision under the facts before the court. For a discussion of this question, see Derenberg, *One Year of Experience Under the Lanham Act in the Patent Office*, in 1948 ABA PATENT, TRADE-MARK AND COPYRIGHT LAW PROCEEDINGS 32, at 38-39; Derenberg, *The Eleventh Year of Administration of the Lanham Trademark Act of 1946*, 48 TRADEMARK REP. 1037, at 1053-55 (1958).

<sup>27</sup> The copying of a design which otherwise might have been used or copied is rendered unfair competition by fraud or unfairness in the procurement of the design from its originator or franchised user. *Dior v. Milton*, 9 Misc. 2d 425, 155 N.Y.S.2d 443 (Sup. Ct. 1956). See also RESTATEMENT, TORTS § 741(a) (1938).

<sup>28</sup> The cases mainly relied on by the Seventh Circuit in determining that the appropriation of the university's name was, of itself, unfair competition involved circumstances where there was evidence of either purchaser confusion or dilution of the corporate name. See *American Steel Foundaries v. Robertson*, 269 U.S. 372 (1926); *S.C. Johnson & Son v. Johnson*, 116 F.2d 427 (10th Cir. 1940); *Standard Oil Co. of N.M., Inc. v. Standard Oil Co. of Cal.*, 56 F.2d 973 (10th Cir. 1932); *Cornell Univ. v. Messing Bakeries, Inc.*, 285 App. Div. 490, 138 N.Y.S.2d 280, *aff'd*, 309 N.Y. 722, 128 N.E.2d 421 (1955).

a commercial jeweler is not the ring sold by the Notre Dame bookstore. A classic statement of this "secondary meaning" doctrine is found in *Crescent Tool Co. v. Kilborn & Bishop Co.*, where Judge Learned Hand stated:

The cases of so-called "non-functional" unfair competition . . . are only instances of the doctrine of "secondary" meaning. All of them presuppose that the appearance of the article, like its descriptive title in true cases of "secondary" meaning, has become associated in the public mind with the first comer as manufacturer or source, and, if a second comer imitates the article exactly, that the public will believe his goods have come from the first, and will buy, in part, at least, because of that deception. . . . The critical question of fact at the outset always is whether the public is moved in any degree to buy the article because of its source. . . .<sup>29</sup>

The "public" as referred to above encompasses nothing more than the particular purchasing element which, in the ring case, consisted of the student body and alumni of the university. This buying element knew that the rings were not sold by the Notre Dame bookstore and was not actually deceived in any way as to their source. It would seem unreasonable to assume that the school had enfranchised a commercial jeweler in the same area, especially since the bookstore had been the exclusive outlet for many years. To determine whether there is deception, the test to be applied is that of the ordinarily intelligent purchaser.<sup>30</sup> Also, the purchasers are interested only in obtaining a Notre Dame ring, and this whether made by Roberts Co. and sold by a commercial jeweler, or made by any other manufacturer and sold by the Notre Dame bookstore. To believe otherwise would impute philanthropy where the facts of the case contradict such a notion.<sup>31</sup>

Again assuming that Roberts Co. had sold rings only to alumni and upperclassmen and again considering the class of purchasers in such a case, the modern unfair competition theory of dilution also fails to provide substantive bases for protection of the university's profit-making ventures. This theory is increasingly popular in cases of this type and has been codified in Illinois, Massachusetts and New York.<sup>32</sup> Essentially, the dilution theory does away with the requirement of actual competition and affords a basis for relief where use of a name or mark by a competitor is likely to injure the trade name or business reputation of the other. If, in the ring case, the buyers had consisted of the same authorized group, and the rings were of comparable quality no matter which source sold them, there would be no likelihood of injury to the reputation or the distinctive quality of the name of the University of Notre Dame. On the other hand, a sale of the ring by the competing commercial jeweler to the general public would undoubtedly dilute the distinctive feature of the ring and afford the university legal grounds for complaint.

The rule of general application which may be derived from the *Notre Dame Ring* case and which may establish precedent for future cases of this type is stated in the lower court opinion and repeated with approval on appeal:

The effect of assuming a name by a corporation under the law of its creation is to exclusively appropriate it as an element of the corporation's existence and the use of the name of a corporation on merchandise manufactured by another for sale in competition with the same type of merchandise of the corporation would not only be actual deception and create actual confusion but would of *itself* constitute a passing or palming off of its merchandise for that of the corporation, the name of which it is wrongfully using, and would be a most flagrant violation of the law of unfair competition. (Emphasis supplied.)<sup>33</sup>

<sup>29</sup> 247 Fed. 299, 300 (2d Cir. 1917).

<sup>30</sup> *Compare* Yale and Towne Mfg. Co. v. Adler, 149 Fed. 783 (E.D.N.Y. 1906), with decision on appeal, 154 Fed. 37 (2d Cir. 1907). The factual situation is distinguishable from the *Notre Dame* case in that the sales were being made to the general public through numerous commercial outlets.

<sup>31</sup> The record shows that 479 of the rings were sold by Roberts Co. While 50% of these were sold to sophomores who could not buy a ring at the bookstore, a number of sales undoubtedly were attributable to the fact that the commercially sold rings, while substantially the same in quality as the school-sold rings, were lower in price.

<sup>32</sup> ILL. ANN. STAT. ch. 140, § 22 (Smith-Hurd Supp. 1957); MASS. ANN. LAW ch. 110, § 7A (1954); N.Y. GEN. BUS. LAW § 368-c(3).

What the court has granted to the university is the right to exploit its own name commercially as a common law trade-mark or trade name<sup>34</sup> and to bring an action for unfair competition against anyone who attempts to infringe upon the property right thus granted, regardless of whether there is any other element of actual unfairness in the appropriation. It is true that protection of a university's name has been afforded by the courts where another in competition with it as an *educational institution* has attempted to appropriate its name.<sup>35</sup> It is also true, as in *Cornell Univ. v. Messing Bakeries, Inc.*,<sup>36</sup> that a university which releases a formula (for making bread) to the general public for commercial exploitation may condition the use of its name in connection therewith and enjoin violations of such conditions which suggest connection of the product with the school (placing Cornell's name on commercially-sold bread). The *Notre Dame* case, however, goes further still by protecting a commercial venture of the university against outside competition. Although dilution of a university's name and destruction of its good will present a sound basis for seeking relief when its name is used on a loaf of bread sold to the general public by a commercial interest, it is not such if the university itself also were to sell bread with its name on it to the public. Thus where the *Cornell* case emphasized protection against commercial *exploitation*, the *Notre Dame* case emphasizes protection against commercial *competition*. Cornell objected to the use of its name to help sell a commercial product with which it had no connection. Notre Dame objected to the use of its name in the sale of a product in direct competition with its own sales of the product.

There can be no doubt that the analogy of a university to a trading corporation is clearly drawn, and indeed there may be "no sound or salutary reason why a charity should not be entitled to the same protection as a business corporation, namely the protection of its name, symbols, labels, reputation, membership, credit and activities."<sup>37</sup> It is also suggested that a "fraternal" society is as much entitled to be protected in its "trade name" as is an ordinary trading, mercantile or manufacturing concern.<sup>38</sup> This is the same analogy denied in the *loco parentis* cases,<sup>39</sup> and although

<sup>33</sup> 152 F. Supp. 269, 271 (N.D.Ind. 1957); 258 F.2d 256, 258-59 (7th Cir. 1958). Although the court again alluded to the old stand-bys of "deception" and "confusion," it is significant that the word "purchaser" was not included. The deception arising here would seem to be solely connected with the sale of rings to underclassmen which gives them indicia of an academic standing which they had not yet attained. The important recognition here is that the use of the corporate name of the university is *of itself*, and exclusive of any element of deception, unfair competition. This is the property right to be protected by the injunction.

Also, equity not only will enjoin the appropriation and use of a trade-mark or trade name when it is completely identical with the name of the corporation, but will also enjoin such appropriation and use where the resemblance is so close as likely to produce confusion as to identity, to the injury of the corporation to whom the name belongs. *Cape May Yacht Club v. Cape May Yacht & Country Club*, 81 N.J. Eq. 454, 86 Atl. 972 (1913). Thus, it is arguable that any use of the words "Notre Dame" on a commercial product will be enjoined.

<sup>34</sup> The distinction between trade-mark and trade name is not entirely clear. Generally, however, the former refers to a mark or sign as affixed to a vendible commodity while the latter embodies a business and its good will. *American Steel Foundries v. Robertson*, 269 U.S. 372 (1926). From the standpoint of effect, protection given the exclusive right to use a trade name places a heavier burden on a competitor than does the exclusive use of a trade mark. I NIMS, UNFAIR COMPETITION AND TRADE MARKS § 45 (4th ed. 1947).

<sup>35</sup> *Trustees of Columbia Univ. v. Axenfeld*, 136 Misc. 831, 241 N.Y. Supp. 4 (Sup. Ct. 1930); *Columbia Grammar School v. Clawson*, 120 Misc. 841, 200 N.Y. Supp. 768 (Sup. Ct. 1923).

<sup>36</sup> 285 App. Div. 490, 138 N.Y.S.2d 280, *affirmed*, 309 N.Y. 722, 128 N.E.2d 421 (1955).

<sup>37</sup> *Golden Slipper Square Club v. Golden Slipper Restaurant & Catering, Inc.*, 371 Pa. 92, 88 A.2d 734, 736 (1952). *Cf.*, *Cape May Yacht Club v. Cape May Yacht & Country Club*, 81 N.J. Eq. 454, 86 Atl. 972 (1913). See generally 1 NIMS, *op. cit. supra* note 17, § 86.

<sup>38</sup> *Liberty Life Assur. Soc'y v. Herald of Liberty*, 15 Del. Ch. 369, 138 Atl. 634, 637 (1927). The case suggests that there may be competition with plaintiff even extending to plaintiff's own members as long as the name defendant uses does not produce confusion and he indulges in no other unfair practice. As applied to a university, such a holding would be superseded by the *loco parentis* privilege of a university to restrict those seeking to deal with its students. See notes 17 & 18 *supra*.

<sup>39</sup> See text at notes 17 & 18 *supra*.

this denial is undoubtedly appropriate because of the school's primary character as an educational institution when it prescribes reasonable regulations for the students which interfere with outside interests, one might wonder why this primary character has been so completely ignored when a university's own commercial rights are involved.<sup>40</sup>

#### IV. *Commercial Competition with Educational Advantage: The Villyard Case*

The extreme in judicial protection of university commerce has been reached in *Villyard v. Regents of the Univ. System of Georgia*.<sup>41</sup> Plaintiffs operated commercial laundry and dry cleaning establishments in the area of the Georgia State College for Women. Defendants originally operated a laundry and dry cleaning service on campus for the benefit of students, and, over the warranted protests of the plaintiffs, expanded the service to include the families of anyone in any way connected with the operation of the educational institution. Defendants had never paid license fees or taxes, nor had they registered the business name in the clerk's office as required by law, and their prices were less than current commercial rates. Plaintiffs sought to enjoin the service provided residents of the area who otherwise would have patronized the plaintiffs' businesses. The substantive basis of the action was unfair competition. The question of the regents' power to maintain such a laundry was quickly disposed of on the ground that there was no express or "necessarily implied" prohibition against such an operation in the sections of the Georgia code empowering the board of regents.<sup>42</sup> The court held that the plaintiff had failed to state a cause of action:

. . . if the operation of the laundry and drycleaning service, at a price less than the commercial rate for the benefit of those connected with the school, is lawful, it matters not that such enterprise is competitive with the plaintiff's business.<sup>43</sup>

Such a decision completely ignores the fact that the competitive advantage secured here was due at least in some measure to the tax-free status of the educational institution. Plaintiffs fully recognized the right of the Georgia college to engage in its related activity of providing student services and contested only its right to engage in the unrelated activity of supplying such services to prospective patrons of outside businesses. The competitive advantage secured by a tax-free status in any business is obvious, and whether a university extends student services to the general public or enters an entirely unrelated field, there are problems of unfair competition constantly arising.

#### V. *Businesses Unrelated to the Educational Function: A Problem of Taxation*

The essential error in the *Villyard* decision was the court's failure to recognize that the purpose of the statutory grant of power was not to secure tax-free status for a competitive business. This points to the problem to be faced when the university, either by means of its own corporate structure or through a separately organized corporation wholly owned and controlled by it, undertakes to deal with the general public in direct competition with commercial enterprises, *i.e.*, the problem of taxation and its relation to competitive status.

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<sup>40</sup> The university operates in areas of the law of unfair competition as both a trading corporation and as an educational institution. The *loco parentis* cases indicate that little or no restriction will be placed upon its discretionary powers as an educational institution. The *Notre Dame Ring* case reflects the proposition that the university's commercial rights are not affected or diminished by the educational purposes of its formation and operation. The overall picture suggests that a school may either claim or deny the analogy to a pure trading corporation as the situation demands, and be fairly sure of winning its lawsuit. It may be through a type of "judicial paternalism" that the courts have seen fit to extend legal protection to such commercial ventures on an equal level with others, or it may be through an implicit recognition that university commerce needs protection and encouragement rather than limitation and competition. The fact of the matter is that the courts are dealing with primarily educational institutions, and the increasing scope of protection afforded university commerce is due to a fundamental commitment that the education of youth is an essential means of obtaining desired cultural goals.

<sup>41</sup> 204 Ga. 517, 50 S.E.2d 313 (1948).

<sup>42</sup> GA. CODE ANN. § 32-101 (1952); *State v. Regents*, 179 Ga. 210, 175 S.E. 567 (1934), cited approvingly in *Villyard v. Regents*, *supra* note 41, at 315.

<sup>43</sup> 50 S.E.2d 313, 316 (1948).

Under the Internal Revenue Code of 1928,<sup>44</sup> exemption from federal taxation was granted to corporations organized and operated exclusively for religious, charitable or educational purposes, no part of the net earnings of which inured to the benefit of any private individual or share holder. Under this law, a strict ruling denied exemption to an association formed to operate the Stanford University bookstore on the ground that it was not a division or part of the university in contemplation of law and that the "mere business of selling books or other 'general merchandise' on a college campus does not connote an 'educational' purpose."<sup>45</sup> The harshness of this ruling is apparent from the facts that this was a separate association in name only; that it made 99% of its sales to students, and that all proceeds over and above costs of operation were returned to the students in proportion to their purchases. The dissenting opinion pointed out these facts and urged a more liberal trend towards a doctrine of reasonable relation to educational purposes. Such a position was accepted in *Squire v. Students Book Corp.*<sup>46</sup> where exemption was granted to a student-operated bookstore association because it bore a close and intimate relationship to the functioning of the college itself.

But regardless of isolated cases which treated the universities harshly, a doctrine of liberal exemption from taxation had evolved in the period between 1924 and 1950, which was ultimately to move Congress to recognize the commercial inequities inherent in the tax-free status of unrelated businesses. This doctrine involved the "ultimate destination" test which placed the emphasis on the destination of profits gained rather than the source of the income. If the profits were used in furthering the religious, charitable or educational purposes of the organization it was of no consequence that their source was a commercial enterprise and they remained tax exempt.<sup>47</sup>

State court decisions did not so readily embrace this doctrine, however, and authority is found for the proposition that if the primary purpose of an activity or use of property is to make a profit, there will be no tax exemption for this particular activity, regardless of the fact that all profits are devoted to the general purposes of the organization. The courts of Idaho, Missouri, and New York have interpreted state property tax exemption statutes in this manner.<sup>48</sup>

The line of cases setting forth the ultimate destination doctrine undoubtedly gave rise to "the alleged abuses which existed prior to 1950, the common denominator of each being its characterization as an 'unfair method of competition.'"<sup>49</sup> The tax free status in the *Villyard* case allowed operation at a lower cost, hence a reduction in price; in the case of a "feeder" corporation it allows expansion of operations by reinvestment of all profits, whereas a competing commercial corporation must first satisfy its tax burden.

In 1950, Congress enacted Sections 421-24 of the Internal Revenue Code, imposing a tax on the "unrelated business income" of educational, charitable and other exempt organizations, and the competitive advantage previously secured by the tax-free status of these businesses came to an end.<sup>50</sup> These sections are embodied substantially unaltered in Sections 511-15 of the 1954 Internal Revenue Code. Essentially, these provisions were aimed at putting commercial ventures of an exempt organization, which

<sup>44</sup> Int. Rev. Code of 1928, § 103(6), 45 Stat. 813 (1928).

<sup>45</sup> *Stanford Univ. Bookstore v. Helvering*, 83 F.2d 710, 712 (D.C. Cir. 1936).

<sup>46</sup> 191 F.2d 1018 (9th Cir. 1951).

<sup>47</sup> *Trinidad v. Sagrada Orden*, 263 U.S. 578 (1924); *Roche's Beach, Inc., v. Commissioner*, 96 F.2d 776 (2d Cir. 1938); *C.F. Mueller Co. v. Commissioner*, 190 F.2d 120 (3d Cir. 1951), *reversing* 14 T.C. 922 (1950), which had attempted to break away from the ultimate-destination precedent.

<sup>48</sup> *In re Gem State Academy Bakery*, 70 Idaho 531, 244 P.2d 529 (1950); *Evangelical Lutheran Synod v. Hoehn*, 335 Mo. 257, 196 S.W.2d 134 (1946); *Y.W.C.A. v. City of New York*, 217 App. Div. 406, 216 N.Y. Supp. 248, *aff'd per curiam*, 245 N.Y. 562, 157 N.E. 858 (1927).

<sup>49</sup> Webster, *Federal Taxation of Business Activities by Charitable Foundations*, in 2 N.Y.U. CONFERENCE ON CHARITABLE FOUNDATIONS PROCEEDINGS 79, at 80 (1955).

<sup>50</sup> Int. Rev. Code of 1939, § 421-24, added by Revenue Act of 1950, § 301, 64 Stat. 947. (now INT. REV. CODE OF 1954, § 511-15).

were regularly carried on for a profit, on an equal footing with private competition when dealing with the purchasing public. Section 513(a) of the Code defines "unrelated trade or business" as:

[A]ny trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption. . . .<sup>51</sup>

The parenthetical clause in the above provision put an end to the ultimate destination test. Now the business itself must be related to the charitable purpose to gain an exemption, and neither the need for funds to carry on the purpose, nor the fact that the funds are used for that purpose will of itself establish the requisite relationship for exemption.

The doctrine of primary purpose applied to colleges and universities is recognized in section 513(a)(2) which excepts from the definition of unrelated business "any trade or business . . . carried on . . . by the organization primarily for the convenience of its members, students, patients, officers, or employees."<sup>52</sup> The regulations promulgated under this section provide that:

The operation of a wheat farm is substantially related to the exempt activity of an agricultural college if (it) is operated as a part of the educational program of the college, and is not operated on a scale disproportionately large when compared with the educational program of the college. Similarly, a university radio station or press is considered a related trade or business if operated primarily as an integral part of the educational program of the university, but is considered an unrelated trade or business if operated in substantially the same manner as a commercial radio station or publishing house. . . . [M]anufacture and sale of a product by an exempt college would not become substantially related merely because students as part of their educational program perform clerical or bookkeeping functions in the business.<sup>53</sup>

As an example of the exception granted colleges under section 513(a)(2), the regulations cite "a laundry operated by the college for the purpose of laundering dormitory linens and the clothing of students."<sup>54</sup>

Facing again the problem of the *Villyard* case and emphasizing the word "primarily" in section 513(a)(2), it is apparent that a favorable tax position may still exist to some extent, in that a service offered primarily for student benefit may still do outside work in competition with commercial enterprises while retaining its tax-free status. (This is not necessarily true if the laundry were to be organized as a separate feeder organization, however.)<sup>55</sup>

The classification of an activity as related or unrelated admits of a great degree of discretionary interpretation. An activity which at first blush seems to be purely a profit-making enterprise may in reality be intimately connected with the purpose for which the institution seeking the exemption was organized. Such was the situation in *Mobile Arts and Sports Ass'n v. United States*.<sup>56</sup> Claimant was a community non-profit organization organized to operate a football bowl game and to sponsor and operate other activities of an artistic and educational nature that would be of benefit to the community. In holding against the government's contention that the game was operated to make profit like any other business venture, the court allowed exemption, relying on the fact that the corporation itself was properly organized for exemption and that this was not unrelated business income. The latter holding was based on the fact that "the conducting of the Bowl game was and is an integral part of MASA's civic and educational program and bears a close and intimate relationship to the civic and educational objects for which MASA was organized."<sup>57</sup>

<sup>51</sup> Int. Rev. Code of 1954, § 513(a).

<sup>52</sup> Int. Rev. Code of 1954, § 513(a)(2).

<sup>53</sup> Treas. Reg. § 1.513-1(a)(4).

<sup>54</sup> Treas. Reg. § 1.513-1(b).

<sup>55</sup> For a good discussion of the possibility of variance in the tests to be applied to an unrelated business which is part of the educational corporation itself and one which is organized as a separate entity, see 60 *YALE L. J.* 851, 864 (1951).

<sup>56</sup> 148 F. Supp. 311 (S.D. Ala. 1957).

Although the taxation amendment of 1950 has effectively prevented the unfair-competition abuses in the case of an obviously unrelated business enterprise,<sup>57</sup> there still remain areas to be questioned, a good example of which is the *Villyard* situation. Perhaps further legislation is needed to delimit more precisely the scope and meaning of the concept "related business," in order to protect competing private ventures.

### Conclusion

With few exceptions, the power of an educational institution to engage in almost any type of commercial enterprise either directly or indirectly is well-established. As colleges and universities have expanded, their collateral powers have been extended to accommodate the process of growth. As has been demonstrated in the preceding cases the college or university occupies a unique and, in some respects, privileged position in the law of unfair competition because it stands in loco parentis to its student and has the discretionary power to enforce reasonable rules governing them, regardless of the adverse effects on local businesses seeking student patronage. The institution's own commercial rights, however, are given no less protection by reason of its status as a non-profit organization, and the commercial competitor is bound to respect these rights. For example, the property right of a university in its name, seals and symbols, as illustrated in the *Notre Dame Ring* case, gives the university the exclusive right to exploit these items. Affixing the university name or seal to a product in effect gives the university an exclusive and privileged market position protected for all time against all commercial interference.

The sole commercial limitation placed upon such institutions to date is the justified exception to the general trend expanding commercial rights and powers, and consists of the 1950 amendment to the Internal Revenue Code imposing taxation on the unrelated business income of a college or university. Even in this area, however, efforts to negate the competitive advantage of the non-profit organization are overcome by the application of the primary-purpose doctrine to situations like that presented in the *Villyard* case. There is need for further limitation and definition in this area, for despite the fact that the primary purpose of a campus business is to service the student needs, some control should be placed on the non-student trade if the activity is to retain a tax-free status. A claim that the primary purpose is to serve the students may be effectively refuted if it is found that there is a substantial margin of profit taken from all transactions and a large volume of outside business being done. This situation strongly suggests that the quest for profit is more than a secondary or incidental purpose, and invites limitations to the present liberal interpretations of the primary purpose doctrine. Before any further expansion or curtailment of educational commercial enterprising is undertaken, an extensive study should be made to ascertain the effects of such action on the university's function in a society devoted to free enterprise and public education.

F. James Kane

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<sup>57</sup> *Id.* at 316. The factual situation discloses benefit to the community over and above the profit gained, and an intention to run the game whether or not it was profitable. Furthermore, there were no other bowl games in the country on the same day with which this one would compete.

<sup>58</sup> A more completely detailed analysis of the effect of the 1950 amendments may be found in *Colleges, Charities and the Revenue Act of 1950*, 60 YALE L.J. 851 (1951); Dane, *Taxation of Charities Under Revenue Act of 1950*, 9 N.Y.U. INSTITUTE ON FEDERAL TAXATION 895 (1951).