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The Risks Of Online Auctions, Counterfeit Goods

Law360, New York (July 16, 2009) -- The recent string of lawsuits brought by luxury brand manufacturers against eBay have highlighted once again that local laws can affect online business models in unexpected and dramatic ways.

Whereas a common standard can often be discerned from seemingly conflicting court opinions in the United States, the eBay cases outside of the United States appear to simply reflect the different standards by which Internet auction sites will be judged when they are used to auction counterfeit luxury goods.

So far in the United States, courts have largely found in favor of eBay.

For example, when Tiffany & Co. sued eBay for facilitating what Tiffany estimated to be hundreds of thousands of auctions involving counterfeit Tiffany jewelry, the District Court for the Southern District of New York held that "it is the trademark owner's burden to police its mark and companies like eBay cannot be held liable for trademark infringement based solely on their generalized knowledge that trademark infringement might be occurring on their Web sites."^[1]

In the Tiffany & Co. case, Tiffany argued that eBay was liable for both direct trademark infringement as well as contributory infringement.

Tiffany claimed that eBay directly infringed its trademark by (1) advertising the availability of Tiffany jewelry on eBay; (2) by using the Tiffany name on the eBay home page and in eBay documents and publications; (3) by subsequently deriving revenue from the sale of that jewelry on its Web site; (4) by purchasing "sponsored links" on Google and Yahoo advertising eBay listings that offered Tiffany jewelry for sale; and (5) generally by participating in the sale of counterfeit merchandise on the eBay Web site^[2].

The court rejected Tiffany's direct infringement claim and concluded that eBay's use of the marks was protected by the doctrine of nominative fair use.

Variously stated, the doctrine of nominative fair use provides that "[a] defendant may use a plaintiff's trademark to identify the plaintiff's goods so long as there is no likelihood of confusion about the source of defendant's product or the mark-holder's sponsorship or affiliation."^[3]

A defendant asserting the nominative fair use defense must prove that (1) the product or service in question is one not readily identifiable without use of the trademark, (2) only so much of the mark or marks may be used as is reasonably necessary to identify the product or service, and (3) the user must do nothing that would, in conjunction with the mark, suggest sponsorship or endorsement by the trademark holder^[4].

Applying this test, the court found that eBay's use of Tiffany's marks was protected under the nominative fair use doctrine because:

- 1) Tiffany jewelry was not readily identifiable without using the Tiffany trademark;
- 2) by only using the Tiffany name, eBay used only so much of the mark as was reasonably necessary to identify the product; and
- 3) eBay's use of the Tiffany marks did not do anything to suggest that Tiffany endorsed eBay or was affiliated with eBay; rather, at most, the use of the Tiffany marks suggested that individual eBay sellers were selling authentic Tiffany merchandise on Ebay.

The court also emphasized that eBay never takes possession of items sold through its website and does not itself directly sell counterfeit merchandise to buyers.^[5]

The court also found that eBay's practice of purchasing the keyword "Tiffany" as part of sponsored link advertising efforts did not constitute direct infringement.

While the court held that eBay's use of Tiffany's marks in the sponsored links constituted "use" under the Lanham Act because the use went beyond internal use of the trademark, the court held that such use was protected under nominative fair use for the same reasons as outlined above^[6].

Finally, the court held that eBay was not liable for contributory infringement of Tiffany's marks. In arriving at this conclusion, the court applied the Inwood Laboratories test for contributory infringement, which provides that contributory infringement occurs if a party "continues to supply its product to one whom it knows, or has reason to know, is engaging in trademark infringement."^[7]

The court held that the relevant inquiry is not whether eBay could reasonably anticipate possible infringement but rather whether eBay continued to supply its services to sellers when it knew or had reason to know of infringement by those particular sellers.^[8]

Explaining that generalized knowledge of infringing activity is not sufficient to meet the "know or have reason to know" standard set forth in Inwood, the court held that to

support a contributory infringement claim, Tiffany would have to show that eBay knew or had reason to know of specific instances of actual infringement and failed to act in response.[9]

Because the record showed that eBay took down auctions whenever it received an objection notice from Tiffany, the court held that eBay was not liable for contributory infringement for generally allowing the sale of counterfeit Tiffany products on its Web site.[10]

European courts have been less inclined to absolve eBay of responsibility for monitoring the sale of counterfeit products on its website. For example, in 2008, a French court found eBay liable to Paris luxury house, Hermes, for the sale of two fake Hermes handbags posted by sellers on the online auction site.

Hermes argued that eBay was a direct participant in the sale of counterfeit products not only because the site offered counterfeit traders a platform for their fraudulent transactions but also because eBay provides a number of services designed to enable the transactions to take place.

Hermes further argued that eBay directly profits from the counterfeit trade by taking a commission from each sale that takes place on its site, thereby making eBay a participant in the fraudulent transaction and not merely a passive host.

The French court agreed with Hermes and held that "by selling Hermes bags and branded accessories on the eBay.fr site, and by failing to act within their powers to prevent reprehensible use of the site," the user and eBay "committed acts of counterfeiting and imitation of French brand names to the detriment of Hermes international."^[11]

eBay and the seller who posted the counterfeit bags were jointly ordered to pay \$30,000 to Hermes and eBay was ordered to place a notice of the ruling on its French home page for three months.

Similarly, in 2008, the Commercial Court of Paris ordered eBay to pay the luxury group Moet Hennessy Louis Vuitton SA ("LVMH") approximately \$63.2 million for failing to prevent the sale of counterfeit goods on eBay's Web site. LVMH argued that 90 percent of the Louis Vuitton bags and Dior perfumes sold on eBay's website were fakes.

The French court held that eBay had not done enough to prevent the sale of counterfeit products on its website. The court also ordered eBay to stop allowing diversion sales of perfumes manufactured by Christian Dior, Guerlain, Givenchy and Kenzo, which can be sold only through an agreed-upon network of distributors.

Unlike the U.S. court in Tiffany who viewed eBay as a mere host for the website, the French court found that eBay served as a "broker," or intermediary between sellers and buyers in exchange for commissions.

Based on that, the court held that eBay was not protected by French law that limits a “host’s liability” for infringing material posted by a third party.

While the Hermes and LVMH cases demonstrate that French courts are receptive to suits against eBay, cosmetics giant L’Oreal has received mixed responses to its lawsuits against eBay in five European countries.

L’Oreal’s suits have tracked fact patterns and claims that mirror those of the other cases against eBay. L’Oreal emerged victorious in German court; however the cosmetics company has not fared as well throughout the rest of Europe.

For example, in Belgium, the Brussels Commercial Court held that eBay does not have a “general monitoring obligation” of the items offered on its website and is not required to police its site to prevent counterfeit goods from being sold.

Departing from earlier French decisions rendered on nearly identical facts, a French court held that eBay had “fulfilled its obligation in good faith” by setting up systems to try to detect sales of fake goods and therefore was not liable to L’Oreal.[12]

Just last month, on May 22, 2009, the UK High Court held that eBay was not jointly liable for the sale of counterfeit L’Oreal products on its UK website and is under no legal duty or obligation to prevent infringement of third parties’ registered trademarks.[13]

Furthermore, the UK High Court held “there is nothing in eBay’s systems and policies which favors or encourages the listing or sale of counterfeit goods; rather, on the contrary, eBay takes active steps to prevent or at least minimize such activity.”[14]

Although the court ruled in favor of eBay on whether eBay was jointly liable for infringements committed by sellers posting fake L’Oreal products on its Web site, the court referred the question of whether eBay was liable for the use of L’Oreal’s trademarks in sponsored links to the European Court of Justice (“ECJ”).

The ECJ is currently considering the issue of whether use of a trademark in a sponsored link by a service provider is use of a trademark at all.

Nonetheless, eBay contends that even if the site is liable for use of L’Oreal’s trademark in the sponsored links, they are exempt from liability under, among other things, Article 14 of the E-Commerce Directive.

The eBay cases are difficult to reconcile given that they involve almost identical facts. A number of these cases have been appealed and how they are ultimately decided will set important precedent regarding the responsibilities that online auction sites and manufacturers have in policing the sale of counterfeit products.

The cases demonstrate that the law governing direct infringement for using trademarks in sponsored links to drive traffic to auction postings outside the United States remains largely unsettled.

But on the issue of contributory infringement, the trend seems to signal an increasing reluctance to hold online auction sites liable for trademark infringement arising out of auctions that are hosted on their sites.

Nevertheless, online auction sites cannot play a completely passive role in policing the sale of counterfeit products. In the cases where the court ruled in eBay's favor, the court recognized that eBay operated a take-down program (eBay's VeRO program) under which eBay would remove any items suspected of infringement upon being notified of such infringement by rights holders.

While online auction sites may not have an obligation to pre-screen products before they are listed on their sites, the courts' emphasis on Bay's take-down program is significant.

Failure to have such a program, or failure to respond appropriately to take-down notifications, will strengthen a manufacturer's argument that the operator knowingly allowed the sale of infringing items or "willfully turned a blind eye" to the infringement and might lead to different outcomes.

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[1] Tiffany Inc. v. eBay Inc., 576 F. Supp.2d 463, 527 (S.D.N.Y. 2008).

[2] Id. at 494.

[3] Id. at 496 (citing Merck & Co., 425 F. Supp. 2d 405, 413 (S.D.N.Y. 2006); Nihon Keizai Shimbun Inc. v. Comline Bus. Data Inc., 166 F.3d 65,73 (2d. Cir. 1999)).

[4] Id. (citing New Kids on the Block vs. New America Publ'g Inc., 971 F.2d 302, 308 (9th Cir. 1992)).

[5] Id. at 497-98.

[6] Id. at 500-01.

[7] Inwood Labs v. Ives Labs, 456 U.S. 844, 854 (1982).

[8] Tiffany, 576 F. Supp.2d at 503 (citing Medic Alert Found. United State Inc. v. Corel Corp., 43 F.Supp.2d 933, 940 (N.D. Ill. 1999).

[9] Id. at 510.

[10] Id. at 518.

[11] "French Court Fines eBay Over Counterfeit Goods." AFP Web site, afp.google.com/article/ALeqM5ieVhIM9xNEzcmDtrdw6ToFLtkRAg, June 4, 2008.

[12] L'Oreal reports that it is working with eBay to address its continuing concerns and has since appealed both the French and the Belgian courts' decisions.

[13] L'Oreal SA v. eBay International AG, [2009] EWHC 1094 (Ch).

[14] Id.