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EBAY: A TALE OF TWO DEFENSES

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Friday, August 22, 2008 — To paraphrase Charles Dickens: it was the best of defenses; it was the worst of defenses. There was a retailer of luxury items, which many consumers coveted and desired at less than full price, headquartered in France; there was a retailer of luxury items, which many consumers coveted and desired at less than full price, headquartered in the United States. In both countries, there was an electronic auction broker which offered third parties the opportunity to auction off their secondhand goods to the world at severely discounted prices. Both the French retailer and the U.S. retailer were losing large sums of money because of sales by third-party purveyors of counterfeit items offered on the website of this electronic auction broker.

While these two retailers (LVMH and Tiffany & Co. (“Tiffany”)) were in comparable predicaments, they each went down a different path to address the counterfeit issue arising with this electronic auction broker (eBay), with widely divergent results.

LVMH (the retailer of luxury items headquartered in France), as well as some of its related subsidiaries (e.g., Christian Dior), brought actions against eBay in France (in the Commercial Court of Paris). LVMH asserted that eBay failed to take proper steps to ensure, as is its duty, that its business does not facilitate illicit acts to the detriment of others, like LVMH, and that the sale of counterfeit items at eBay harmed LVMH to the tune of 20 million euros. LVMH sought damages from eBay.

Tiffany (the retailer of luxury items headquartered in the United States) also brought an action against eBay in the United States (in the U.S. District Court for the Southern District of New York). Tiffany asserted that eBay had a duty to police its website for counterfeiters and to take them down. Tiffany asserted that this duty arose once it provided eBay with general knowledge that such counterfeiters were present. Tiffany asserted that sellers on eBay of lots with more than five Tiffany items were likely to be counterfeiters, and eBay should block such sales automatically.

Thus, these two Courts, faced with these very similar (but different) problems, reached very different conclusions, and identified different duties for this same retailer.

Part I summarizes the LVMH Decision by the French Court and the duties found to be owed by eBay to LVMH.

Part II summarizes the Tiffany Decision by the U.S. Court and the duties found to be owed (or not owed as is the case) by eBay to Tiffany.

Part III suggests best practices for rights owners like LVMH and Tiffany with respect to enforcing their rights to prevent counterfeits on sites like eBay in light of these two divergent decisions

Part I: Paris, France: The LVMH Decision

On June 30, 2008, the Commercial Court of Paris in France handed down a decision in favor of LVMH and against e-Bay that shook the retail world. See, e.g., Doreen Carvajal, *EBay Ordered to Pay \$61 Million in Sale of Counterfeit Goods*, NY TIMES, July 1, 2008.

The French Court summarized LVMH's "charges" against eBay as "failing to ensure, as is its duty, that its business does not generate any illicit acts to the detriment of" others such as LVMH. LVMH's charges were supported by "the indulgence with which eBay hosts obviously illicit advertisements on its sites [which] fosters acts of infringement and causes various losses to" LVMH.

Each of eBay's defenses was summarily rejected by the French Court and a large damages award was granted to LVMH.

French Defense 1: The French Court Lacked Jurisdiction (Denied)

eBay's first line of defense was to challenge the French Court's jurisdiction to hear the dispute. Its attack on the French Court's authority was twofold: eBay asserted that since the computer servers hosting its eBay websites which ran the disputed advertisements were all located in the United States, the dispute should only be heard by U.S. Courts.

eBay further asserted, alternatively, that if the Court were to obtain jurisdiction based on the location of the harm being suffered, the dispute would have to be heard, respectively, by each of the foreign courts of the countries at whose public the advertisements were directed.

Although the Court recognized that eBay's arguments regarding its jurisdiction were properly pled, it nonetheless found the merits of the arguments "ill-founded".

The French Court made clear that it had the authority to hear the parties' disputes regarding eBay's activities throughout the world with respect to the LVMH items. The French Court's reasoning was that under international statute, the French Court has jurisdiction over tort actions based on where the damage occurred. In this case, since LVMH is located in France, and eBay's Internet site is accessible to the French public, the French Courts have jurisdiction to award damages caused in France. This jurisdiction extended not only to advertisements directed to France, but to counterfeit sales throughout all of eBay's worldwide operations.

French Defense 2: eBay As A Site Host Was Immune From Liability For Its Site Users' Infringements (Denied)

French law, like the law in other jurisdictions, recognizes that when a party merely hosts another's website, the liability of the host for illicit acts performed by others on that website is limited: Article 6.1.2 of the Act dated June 21, 2004 on confidence in the digital economy. eBay argued that the protection of this French Act should extend to eBay as the operator of the eBay websites since the alleged illicit activity was being committed by its users, not eBay itself. The French Court did not agree.

The French Court found that eBay's role in the illicit activities occurring on eBay websites was far more extensive than eBay merely acting as a storage site of advertisements by others. While eBay clearly provided such storage services, those services were incident to what the French Court understood to be eBay's real business as a broker of services. The French Court understood eBay's main business was to act as an intermediary, for a profit, between sellers and buyers. The French Court found significant the extensive steps eBay took to promote and develop sales on its sites, such as offering sellers "sales managers", the creation of on-line "stores", and the possibility of becoming a "Power Seller". The French Court found eBay's role to be that of "a mandatory player in sales taking place on its sites", a role by which eBay profited through commissions it made on each sale.

Thus, the French Court concluded that eBay's "hosting and brokering services are indivisible, since eBay offers an advertisement storage service for the sole purpose of acting as a broker" and the statute's immunity for a mere host of Internet sites for the wrongdoing of the sites' users did not apply.

French Defense 3: eBay Acted Responsibly In Setting Up The VeRO Program And Taking Down Illicit Advertisements When Notified By The Rights Owner (Denied)

LVMH charged eBay with taking part in the marketing of infringing goods. The French Court found that "eBay's sites fostered and amplified the marketing on a very large scale of infringing products through electronic selling" and that eBay was an essential participant in this activity.

The French Court found eBay to have defaulted on its duties, including:

"its obligation to ensure that its business does not generate any illicit actions, in this case acts of infringement, to the detriment of an economic player such as [LVMH]";

"its obligation of verifying that the sellers who habitually carry out numerous transactions on its sites are duly registered with the competent authorities"; and

its duty "to set up effective and appropriate measures in order to combat infringement".

Significantly, the French Court found that eBay failed to exercise its duty of supervision in light of eBay's acknowledgment that there were infringing products sold on its websites. The Court found particularly disturbing that eBay did not ***on its own initiative*** take down advertisements and sales of obviously counterfeit items on its website, which were touted with captions such as "a fine imitation of famous Louis Vuitton design", or were obviously counterfeits "simply on the basis of the prices asked and of the quantities offered." The Court also found the subsequent remedial measures that eBay took to combat counterfeits as evidence that eBay acknowledged its own wrongdoing prior to that time in not making such efforts.

Among the measures that the Court faulted eBay for not taking included:

failing to require sellers to supply, upon request, the purchase invoice or a certificate of authenticity of the products offered for sale;

failing to sanction any guilty vendor by terminating his or her account when a breach was found; and

failing to take down illicit advertisements when notified by LVMH.

The French Court also found that eBay's request that "companies who are victims of infringement on its sites contribute financially to the struggle against illicit acts committed on its sites" was "not well-founded."

In sum, the French Court found eBay liable for its acts of abstention and negligence in allowing the sale of counterfeit items on its website, and so held eBay responsible.

Remedy Requested By LVMH: Damages And Publication By eBay Of The Results (Granted)

LVMH asserted it was damaged in three ways:

tortious injuries caused by the sale of counterfeit items;

damage to the company's image; and

moral damage.

Based on LVMH's assertion, the French Court found eBay liable for each of the categories of damages in the amount of:

Euro 7,920,000 for damage from counterfeit sales;

Euro 10,260,000 for damage to the Company's image by illicit sales in the years 2001 through 2006; and

Euro 1,000,000 for moral damage using the Court's "sovereign power of assessment" because damages were not otherwise proven.

Finally, the Court also ordered eBay to publicize this adverse verdict.

Part II: New York, NY, USA: The Tiffany Decision

On July 14, 2008, the United States District Court for the Southern District of New York handed down a decision against Tiffany and in favor of eBay that shook the retailing world just as much as the earlier LVMH Decision. See, e.g., Holly Pekowsky and Anthony F. Lo Cicero, *Tiffany V. eBay: Trademark Owners Beware*, IP Law 360, Portfolio Media, New York (July 16, 2008) (available at www.arelaw.com); Charles R. Macedo, *Holly Pekowsky and Anthony F. Lo Cicero, Tiffany (NJ) Inc. v. eBay Inc.: Guidelines for Online Retailers to Police the Sale by Third Parties of Counterfeit Goods*, Common Law Journal (July 24, 2008) (available at www.arelaw.com).

Tiffany, in the New York action, sought to hold eBay liable for direct and contributory infringement, unfair competition, false advertising, and direct and contributory trademark dilution on the grounds that eBay facilitated and allowed counterfeit items to be sold on its website.

Tiffany argued that eBay had the obligation to investigate and control the illegal activities of sellers on its website, and in particular should have refused to post any listing offering five or more Tiffany items since such listings were likely to be counterfeits.

While the New York Court sympathized with Tiffany's plight, it found Tiffany's case unavailing.

NY Defense 1: eBay Acted Responsibly In Setting Up The VeRO Program, And It Is Tiffany's Duty To Identify Counterfeits (Granted)

eBay's main defense to Tiffany's infringement assertions rested on its assertion that through its Verified Rights Owners ("VeRO") Program, a "notice-and-takedown" system "whereby rights owners could report to eBay any listings offering potentially infringing items, so that eBay could remove such reported listings", eBay acted responsibly to address counterfeit issues and should not be expected to do more. For example, the New York Court explained, "[h]ere, when Tiffany put eBay on notice of specific items that Tiffany believed to be infringing, eBay immediately removed

those listings.” (Slip op. at 2; see also id. at 11-12, 51 (“However, for the reasons described above, the Court finds that eBay responded appropriately to notice of specific infringing items, and that evidence of eBay’s general knowledge of infringement is insufficient to impute knowledge to eBay of specific infringing listings.”)). (This is the same program which the French Court found to be evidence of eBay’s guilt for not doing more prior to instituting the program).

Fundamental to eBay’s defense was the New York Court’s recognition that while there were eBay users who sold counterfeit Tiffany items, there were also eBay users who sold authentic secondhand Tiffany items. The New York Court emphasized that Tiffany had no legal grounds to object to the sale of authentic secondhand Tiffany items. With respect to the counterfeit Tiffany items, the New York Court examined in detail the steps that eBay took to prevent counterfeit items from being sold and the steps that Tiffany took to police eBay users from selling counterfeit marks.

The Court, in making the comparison, found that eBay acted responsibly; as between eBay and Tiffany, found that the duty to identify counterfeiters lay in the first instance with Tiffany, as the rights owner, and in the second instance with eBay, as the website operator, to take down counterfeits upon receiving specific notices of infringement.

With respect to the respective duties of eBay and Tiffany to police the sale of counterfeit Tiffany items on eBay’s website, the Court found as follows:

Here, when Tiffany put eBay on notice of specific items that Tiffany believed to be infringing, eBay immediately removed those listings. eBay refused, however, to monitor its website and preemptively remove listings of Tiffany jewelry before the listings became public. The law does not impose liability for contributory trademark infringement on eBay for its refusal to take such preemptive steps in light of eBay’s “reasonable anticipation” or generalized knowledge that counterfeit goods might be sold on its website. Quite simply, the law demands more specific knowledge as to which items are infringing and which seller is listing those items before requiring eBay to take action.

(Slip op. at 2).

NY Defense 2: eBay’s Use Of The Tiffany Mark Was Protected Under The Nominative Fair Use Doctrine (Granted)

A significant aspect of Tiffany’s complaint in the New York Action was that eBay promotes the sale of Tiffany items, including the counterfeit items, by using Tiffany’s marks in advertisements on eBay websites and other websites and publications. Tiffany objected to eBay’s actions, contending, in essence, that eBay caused a market for the counterfeiters in the first instance, and then profited from the market that it created.

The problem with Tiffany’s argument from the New York Court’s perspective was that as long as at least some of the eBay users sold authentic secondhand Tiffany items, and not all sales were of counterfeit items, eBay was entitled to use the Tiffany marks to promote those legitimate sales in the limited manner that eBay used those marks, under the nominative fair use doctrine.

Remedy Requested By Tiffany: eBay Should Restrict The Sale Of Large Lots of Tiffany Items On Its Own (Rejected)

For the most part, the New York Court found that eBay would react reasonably and responsibly to each specific request that Tiffany made about specific suspected counterfeit activity. However, Tiffany wanted eBay to act on its own based on the general advice from Tiffany that there are a lot of counterfeit Tiffany items being sold. Tiffany did not want to have to bear the responsibility for policing those items on its own. Tiffany sought to have eBay restrict the sale of lots of over five Tiffany items on the grounds that such lots were generally counterfeits. The New York Court

did not accept Tiffany's premise. The problem the New York Court identified with the remedy that Tiffany proposed and sought was that there were lots of over five Tiffany items that were not counterfeit. Thus Tiffany's proposal, from the New York Court's perspective, was not nuanced accurate enough to warrant imposing on eBay. The New York Court denied this requested relief.

Part III: Best Practices: What Should A Rights Owner Do To Police Its Mark?

On their face, the two decisions seem to be at odds.

The French Court found that eBay should know that certain items were counterfeit and should be taken down "simply on the basis of the prices asked and of the quantities offered." The New York Court, on the other hand, found that eBay did not have a duty to automatically take down offers to sell more than five Tiffany items because they were likely to be counterfeit.

The French Court found "not well-founded" eBay's request that "companies who are victims of infringement on its sites contribute financially to the struggle against illicit acts committed on its sites." The New York Court found "the law is clear: 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 website."

The French Court found eBay's VeRO Program to be evidence that its prior efforts to combat counterfeits were insufficient. The New York Court found eBay's VeRO Program to be evidence that eBay acted responsibly.

The French Court was not bothered by LVMH's decision to limit its participation in eBay's VeRO Program. The New York Court found that although Tiffany spent several hundred thousand dollars in participating in the VeRO program, it was not enough.

In light of these apparently divergent duties, what is a retailer to do when faced with large scale sale of counterfeits on a website like e-Bay by third parties, or in other similar venues?

We believe that these decisions suggest the following best practices:

make sure your organization's trademarks, copyrights and other intellectual property rights are properly registered and maintained so that when required, such rights are ready to be enforced;

if there are significant issues of counterfeit sales on eBay-type websites, participate in a significant manner in the notice-and-take-down procedures offered;

go after direct infringers, not just the conduits of their infringement;

consider and coordinate international anti-counterfeiting programs; and

request relief the Court is more likely to award.

Both of these decisions are now the subject of appeals. A series of action facing similar issues are winding their way through the court systems around the world. So far, rights owners have prevailed, not only in the LVMH cases discussed herein, but also in France (in a case by Hermès) and in Germany (in a case brought by Rolex). eBay has prevailed in not only the Tiffany case discussed herein, but also in Belgium (in a case brought by L'Oreal). While the LVMH and Tiffany cases are but two of the recent spat of decisions that have issued regarding eBay's duty to protect rights holders from illicit activity by eBay users, they lay out the theoretical framework for the theories of

imposing or refusing to impose a duty to identify the illicit activity in the first instance on the rights' holder. These two alternative frame works are not only likely to be considered by other courts in the U.S., but by other courts throughout the world and Europe. Only time will tell whether the world's courts will be able to harmonize the law on this point and establish clear guidelines for rights' holders.

Conclusion

A retailer's brand is one of its most important assets. It should be treasured and protected. Many organizations, especially in hard times, tend to forget this important point. While anti-counterfeiting efforts may appear to be necessary evils, they can provide, at their heart, great opportunities, especially for luxury brand owners, to prevent lost opportunities and to maintain the value of their crown jewel assets.

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