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I FOUGHT IT ON eBay

Suing over eBay was big news on both sides of the Atlantic this summer. In the U.S., a Manhattan federal court handed down its long-awaited decision on Tiffany's claims that eBay wasn't doing enough to police and prevent online sales of counterfeits.¹ Tiffany's loss in New York stands in sharp contrast to very similar cases against eBay recently won by LVMH and Hermès in France.

What happened and what does it mean?

Tiffany v. eBay Lawsuit

The Claims

In its 2004 lawsuit, Tiffany made claims against eBay of trademark infringement, unfair competition, false advertising and trademark dilution, under one or both federal and New York State law, all arising out of the sale of counterfeit items by others through eBay. Huge volumes of purported Tiffany silver merchandise were offered on eBay, and eBay actively promoted the development of online jewelry auctions, including by use of the Tiffany name. It was not disputed that a great deal of the purported Tiffany items were counterfeits. Tiffany participated in eBay's VERO (Verified Rights Owner) program, through which a "Notice of Claimed Infringement" (NOCI) can be filed, leading to the shutdown of the auction of the challenged item. Tiffany filed almost 285,000 NOCIs with eBay from mid-2003 through September 30, 2007.

eBay argued it had taken technologically reasonable measures to identify and remove counterfeits. Besides VERO, eBay performed various "fraud engine" searches on items being offered, flagged suspect items for review by eBay staff, and, in numerous cases, removed the items from the site. Over time, other

¹ *Tiffany (NJ) Inc. v. eBay Inc.*, 04 CV 4607 (RJS)(S.D.N.Y.)(July 14, 2008).

changes were made by eBay, including prohibiting “Buy It Now” non-auction sales for purported Tiffany objects (meaning there was more time to detect and review them) and creating a multi-hour hold period before postings referring to Tiffany appeared (for similar reasons).

The Result

The heart of the ruling is its analysis of the contributory infringement claim. The court treated eBay like the owner of a flea market who knows infringing goods might be sold at the market. But it was not proven that eBay knew or had reason to know of the infringement. So while the court accepted eBay had sufficient control over the transactions to have potential liability, and that eBay had a general awareness of the Tiffany counterfeiting problem, the claim failed because Tiffany had not shown that eBay failed to address specific instances of infringement that had been brought to its attention.

The court also rejected a “willful blindness” claim, finding that eBay generally implemented additional anti-fraud measures when it was reasonably and technologically able to do so. Without specific knowledge, Tiffany was not obliged to do more. The court rejected the claim that eBay continued to “supply” its service to known infringers, because in most, if not all cases, where there had been multiple complaints, the poster had been removed. The court found it unreasonable to require removal on the basis merely of an interested party’s one-time “good faith” claim of infringement — some of which claims had turned out to be wrong.

The unfair competition claims failed because there was no evidence of bad faith by eBay. False advertising and dilution (blurring and tarnishment) claims also were rejected. A more novel claim of “contributory infringement” — that eBay invited people to do this — fared no better than the more familiar claims. Joint and several liability for Tiffany (along with the posters of counterfeit items) was rejected by the court because eBay never had possession of nor did it sell the purported Tiffany goods. Finally, the court held that eBay’s use of Tiffany’s trademarks — even in sponsored links on other sites — fell within the “nominative” fair use doctrine; that is, that it used no more of the marks than needed to describe what was being sold and made no suggestion of any affiliation with Tiffany. Tiffany has filed a notice of appeal.

Meanwhile in France

A number of *luxe* product makers, including Dior and Louis Vuitton, prevailed on claims that eBay was selling counterfeit items and had a duty to stop doing so.² LVMH prevailed on its claim although it had never participated in eBay’s VERO system. eBay pointed to the same sorts of safeguards that helped it persuade the U.S. court — VERO, fraud engines, 2006 upgrades to the technology — to no avail.

² La Societe Christian Dior Couture, SA v. La Societe eBay Inc. (Tribunal de Commerce de Paris, jugement prononce 30 June 2008); SA Louis Vuitton Malletier v. eBay Inc. (Tribunal de Commerce de Paris, judgment prononce 30 June 2008).

The Paris Commercial Tribunal found eBay was not a mere site host, which might enjoy statutory immunity, but a broker of the illicit items. While the American court said it was acceptable for eBay not automatically to eject counterfeit sellers after a first instance, the French court reached the opposite conclusion. It awarded the equivalent of over US\$60 million in damages. An early June decision by another French trial court concerning eBay counterfeits had gone in favor of Hermès.

In a decision handed down at the same time, involving four fragrance makers under the LVMH wing³, the same court found eBay liable for taking no steps to prevent sales of items outside manufacturer-authorized distribution channels.

Observations

1. While it acknowledges Tiffany's frustration with the frequent appearance of phony Tiffany goods on eBay, the U.S. court says policing is the rights owner's burden. The court dwelled on the relative efforts made and costs incurred by Tiffany and eBay in dealing with counterfeits. Consider this contrast:

eBay spends \$20 million yearly on tools to promote trust and safety on its web site; that's what a quarter of its 16,000 employees do. Half work as customer service representatives. Some 200 do nothing but hunt for infringing items; another 70 work with law enforcement. eBay spent \$5 million annually to upgrade its fraud search engine, updating it weekly from 2003 to 2006. The fraud engine flags thousands of suspect listings daily. Sometimes eBay reimbursed buyers of items that turned out to be counterfeit. eBay never refused to pull down an auction that was the subject of a Tiffany NOCI.

Tiffany spent \$763,000 to deal with online counterfeiting in 2003, just 0.05% of its net sales. Over five years, it budgeted \$14 million for anti-counterfeiting — three to five million dollars of which was for the Tiffany litigation against eBay. From 2003 to 2006, Tiffany spent the equivalent of just three person days a week (in-house) and between just 1.15 and 1.6 person days a week (outside counsel) monitoring eBay. It only began to monitor eBay on a daily basis in 2006. Tiffany declined to use technological tools proposed by eBay to facilitate VERO reporting. Despite asking for the identities of the sellers of the assertedly phony items, Tiffany never sued one. Tiffany stopped pursuing sellers of counterfeit goods on eBay, either directly through cease and desist demands or by assisting law enforcement authorities, in 2003.

The case thus reminds everyone of an old message: rights owners proceed at their peril by not maintaining an economically reasonable level of trademark/trade dress enforcement activity. It's a good moment for trademark owners to review their anti-counterfeiting programs to make sure their scope and targets reflect a good faith effort to

³ *SA Parfums Christian Dior v. eBay Inc.* (Tribunal de Commerce de Paris jugement prononcé 30 June 2008). In addition to Parfums Christian Dior, the other plaintiffs were Kenzo Parfums, Parfums Givency and Guerlain.

address the problem while also being cost-effective. Perhaps the U.S. court would have been more inclined to Tiffany's view if it had gone after repeat quantity sellers of alleged counterfeits directly, as well as demanding that eBay do so. Distribution channel issues also should be considered to make sure what the rights owner does in one area is consistent with positions it takes in another.

2. Where there is licensing or franchising, who will be responsible for dealing with eBay sale of counterfeits issues, and to what extent, should be addressed in the agreement.
3. Multi-national brands may find there is now more than one way to skin a counterfeiting cat. Careful attention to where suit is brought could pay big returns. If a U.S. brand had a choice of chasing eBay in the U.S. or in France, France might be a better choice right now, particularly if distribution channel violations are involved.⁴ A French court's judgment probably could be enforced in any country in the European Union. Moreover, unlike situations in which pure speech and the First Amendment have been involved, U.S. courts may be more willing to enforce a French court's judgment in this context, where sales of goods are involved.

Internet Advertisers Versus The Tax Collector

It's not that the Internet is all we think about, but a tax law adopted by New York this spring — and now being challenged in court — could have major implications for the issue of who may be held responsible to pay state taxes for on online sales. And when it comes to taxes, surprises are hardly ever good news.

Faced with budgetary shortfalls, states are looking for new approaches to capture the sales tax that has been uncollected through online sales. In the current environment, online retailers generally do not collect sales tax if the purchaser is in a state where the retailer has no retail stores or other operations. If online retailers do not collect sales tax, purchasers often do not pay the use tax (tax imposed when an item is purchased out of state for use in state) that they should pay. And government-enforcement against on-line purchasers for a small amount of sales/use tax will not be cost effective for the states.

Why can't the states just require the online retailers to collect the sales tax on the states' behalf as do the big box retailers like Wal-Mart and Target? The reason is that states cannot impose taxes that unduly burden interstate commerce. In a 1992 decision, the Supreme Court ruled that out-of-state retailers cannot be required to collect sales tax on purchases that are sent to states where the retailers do not have a physical presence. *Quill Corp. v. North Dakota*, 504 U.S. 298, 309 (1992). Online retailers like Amazon.com generally have no real or tangible personal property in states other than the state in which their headquarters are located.

⁴ We are aware of at least one U.S. lawsuit, brought after the French decisions, which tries to apply its breach of selective distribution channels argument to eBay — but it's still too early for there to have been any decision.

Almost all online retailers, however, use a myriad of third party advertisers whose web sites place links directing visitors to the retailers' web site. For example, Amazon.com employs the "Associates Program," whereby advertisers place one or more Amazon advertisements on their own web sites. Amazon.com pays the advertisers a small commission for the referred sales. These referred sales account for approximately nine percent of the retailers' sales.

If advertisers directing Internet traffic to online retailers can be deemed agents or otherwise an extended arm of the retailers, then the retailers may be deemed to have a physical presence in the state where the advertiser is located, and thus be subject to the burden of collecting sales tax for that state.

This precise issue is now ripe for decision in New York. In April 2008, New York passed a new tax law providing that a retailer "shall be presumed to be soliciting business through an independent contractor or other representative if the seller enters into an agreement with a resident of this state under which the resident for a commission or other consideration, directly or indirectly refers potential customers, whether by a link on an internet website or otherwise, to the seller." The new law requires an out-of-state retailer like Amazon.com, which uses advertisers based in New York, to collect sales tax for all tangible goods sold to New Yorkers, even if the purchases have nothing to do with the advertising service provided by the advertisers.

After this new law was passed, Overstock.com severed its ties with approximately 3,400 New York-based advertisers as of June 1, 2008, the date that the new law went into effect. Amazon.com, on the other hand, kept its New York-based advertisers and started charging its New York customers sales tax.

Both Amazon.com and Overstock.com have sued New York for a declaration that the new statute is unconstitutional. Amazon.com claims that it is difficult, if not impossible, to identify whether a third party advertiser is a New York resident in its Associate Program. Even if Amazon can identify whether the third party advertiser is a New York "resident," Amazon.com claims that it would be impossible for Amazon.com to know whether each and every one of the linked third parties "directly or indirectly" engage in solicitation in New York.

That being said, it appears that technological advances, not available ten years ago when the *Quill* decision was rendered, make it easier for online retailers to administer and collect sales tax despite the difficulty of dealing with the variations in tax rates, allowable exemptions, and administrative and recordkeeping requirements. Many commentators have opined that the rules under *Quill* are antiquated, given the rapid development of technology and the Internet that have made sales across borders widespread. Until the Supreme Court rules again or Congress otherwise acts, states will continue to expand their tax bases under the existing system and taxpayers will continue to challenge the expansion. If the constitutional challenge made by Amazon.com and Overstock.com turns out to be unsuccessful, many states will follow New York to expand the sales tax basis.

The Tax Group of Schiff Hardin LLP is closely monitoring the expansion of the states' taxing agenda on out-of-state retailers and keeps its clients and friends informed of further developments. If you are concerned about the impact of these developments, please feel free to contact us.

FOLLOWING UP

Here are quick updates on important developments in matters covered in previous issues of this newsletter.

Lead

In April 2007, we provided a report on safety and liability issues raised by the use of lead in jewelry and other consumer products. Impatient states have moved into the field. California and other states have laws already in effect; Massachusetts has rules that take effect in October; other states have requirements in the works — and they won't be consistent. Nor is it just an issue for the jewelry or toy industries, as a case pending in Illinois federal court points up. In July a Chicago judge refused to dismiss a purported class suit over lead claimed to be in Christian Dior "Addict Positive Red" lipstick.⁵

As this issue went to press, Congress passed and President Bush signed H.R. 4040, the Consumer Protection Reform Act, which became law on August 14, 2008. Because this is an issue that won't go away, the Accessories Council, the Fashion Jewelry Trade Association and Schiff Hardin are sponsoring a program September 11 on legal and regulatory issues related to lead in jewelry and other accessories. Watch for further details by e-mail.

Dooney & Bourke Wins Claim Over Claimed Infringement of Monogram Multicolore Bag

Way back in the first issue of this newsletter in November 2006, we reported on a decision by the federal appellate court for New York reviving claims by LVMH that Dooney & Bourke's "It Bag" had infringed on the fabulously successful Murikami-designed Monogram Multicolore bag. The appeals court held the Multicolore bag's "design plus color trademark" was a "strong" (albeit unregistered) mark, and sent the matter back to the trial court for further proceedings.

Those proceedings have ended with a victory for Dooney & Bourke. In a May 30 decision,⁶ District Judge Shira Scheindlin found there was no evidence to establish consumer confusion between the bags, whether at point of initial interest, point of initial sale or after sale, and granted summary judgment to Dooney & Bourke. The court also dismissed LVMH's trademark dilution claims. Between the two bags, sales have reached not quite a quarter of a billion dollars. LVMH said it would appeal the decision.

⁵ *Stella v. LVMH Perfumes and Cosmetics USA, Inc.*, 07 C 6509 (N.D.Ill.)(Bucklo, U.S.D.J.).

⁶ *Louis Vuitton Malletier v. Dooney & Bourke, Inc.*, ___ F.Supp.2d ___, 2008 WL 2245814 (S.D.N.Y.)(May 30, 2008).

Leegin Fallout

We reported last September on the U.S. Supreme Court's decision in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, which reversed almost a century of federal antitrust law to reject claims that retail price maintenance is automatically illegal. As we noted then, the decision did not change similar laws prohibiting such behavior in a number of states. However, it has had an effect at the federal level. The Federal Trade Commission decided this spring that, in light of *Leegin*, it should modify a 2000 consent order on resale price maintenance made with Nine West Group (now owned by Jones Apparel Group). Under the modified order, 9 West will have to report periodically on its RPM activities to the FTC. Various consent orders made with state attorneys general are unchanged.

FACTA

We reported this March on litigation against retailers and others for not handling credit card transactions in accordance with the federal Fair and Accurate Credit Transactions Act ("FACTA"). In particular, we noted the penalty (from \$100 to \$1,000 per transaction) for printing out on a receipt given to the customer more than the last five digits of the account number or the card expiration date. A new law signed by President Bush on June 3, 2008 changes the rule with respect to expiration dates and now provides that printing of the expiration dates on a receipt is not a separate willful violation if the receipt is otherwise compliant.

Additionally, some courts have held the law does not apply to electronic displays not printed out by the consumer (such as e-mailed receipts) — although other courts have held it does.

Schiff Hardin's Women's Networking Group

Schiff Hardin's Women's Networking Group hosted its latest event "Fabulous Fashion: Updating the Basics" at Nordstrom. Guests were treated to a fantastic fashion show, great ideas for fall looks, and a gift card to enjoy Nordstrom's Anniversary Sale.

Our Networking Group will host fashion-related events in New York and Chicago later this year — stay tuned for more details in the coming months.

Schiff Hardin Lawyers Urge Greater Design Protection

In the lead article in the July issue of an international law journal dealing with intellectual property and communications issues, Schiff Hardin Fashion Group members **David Jacoby** and **Judith S. Roth** argue that fashion design needs broader and readier protection than it currently receives in the United States, and also needs a coordinated international approach. Entitled "Fashion and Design: Imitation Is Not The Sincerest Form of Flattery," the article in *Convergence* responds to a University of Virginia Law Review article arguing that knock-offs help, not hurt, sales by fashion designers. Contact us for more information.



eFashion

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The Accessories Council is a not-for-profit, national trade association that was established in 1995 with the mission of increasing consumer use and awareness of accessories.

