



Three Steps Businesses Can Take to Overcome the Impact of Online Product Diversion

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Businesses in various industries want to control the distribution of their product and they do not want their products sold by third parties on the internet, especially below retail prices. Yet many businesses are finding their goods online at reduced prices, sometimes on popular websites like eBay.

The sale of diverted products on third-party websites divests a business of its ability to control the quality of its products. It also can interfere with a company's ability to acquire distributors. Many distributors do not want to sell products that customers can purchase on the internet, often for a cheaper price. Some distributors have implemented policies that require employees to ask companies if their products are sold on the internet (for less) before agreeing to distribute their products. These policies are being implemented because distributors do not want to sell products at retail price and later face unhappy customers who found a better deal online.

When businesses owners find themselves in this situation, they often feel without recourse. Many lawyers advise business owners that the first sale doctrine universally applies to unauthorized internet sales, indicating that their rights as trademark owners do not extend past the first sale of a good.

In many situations, however, this is not the case. This document includes three strategies businesses can use to greatly reduce the unauthorized sale of their products online and, at the same time, ensure their products are distributed safely and in accordance with company policies.

1. Establish Warranties and Service Commitments

Courts have held that selling materially different versions of another company's otherwise genuine products is a violation of that company's trademark(s). Therefore, it is in a business' best interest to establish procedures that differentiate their genuine products (that are sold in the traditional marketplace) from those products wrongfully sold online. The policy should state that the products wrongfully sold online are "materially different" from the genuine products.

One way to practically implement this is to provide warranties and service commitments for products only sold in the authorized chain of distribution. The policy should clearly state that these warranties and service commitments do not apply to products sold unlawfully online.

Businesses should do this because courts have held the absence of manufacturer warranties or services commitments for a resold product can constitute a material difference. And, if an unauthorized reseller fails to fully disclose their absence, he or she may be liable for trademark infringement. See, e.g., *Beltronics USA v. Midwest Inventory Distrib.*, 562 F.3d 1067 at 1073 (10th Cir. 2009). The court in *Societe Des Produits Nestle, S.A. v. Casa Helvetia, Inc.*, 982 F.2d 633, 639 n.7 (1st Cir. 1992), said "[T]he appropriate test [for materiality] should not be strictly limited to physical differences," but should include other differences such as "warranty protection or service commitments [that] may well render products non-identical in the relevant Lanham Trade-Mark Act sense."

2. Establish Quality Controls

Companies should also analyze their product and distribution procedures and adjust them to make it impossible or very difficult for online sellers to replicate. This is also important because it will allow the company to bring trademark claims against the online re-sellers.

Courts have repeatedly recognized that a product re-seller violates the manufacturer's trademarks if the re-seller does not distribute the products in accordance with the same quality control standards applied by the manufacturer. *See Shell Oil Co. v. Commercial Petroleum, Inc.*, 928 F.2d 104 (4th Cir. 1991). This is because “[t]he Lanham Trademark Act affords the trademark holder the right to control the quality of the goods manufactured and sold under its trademark.”

In *Shell Oil*, for example, a wholesaler of bulk oil bought Shell-brand oil from an authorized distributor and then resold it under the “Shell” trademark. *928 F.2d at 106*. The wholesaler argued it was entitled to do so because the Lanham Act does not apply to the sale of genuine goods bearing genuine marks. *Id.* at 107. The court disagreed, holding that “a trademarked good is only ‘genuine’ if it is manufactured and distributed under quality controls established by that good’s manufacturer.” The court also held that because the product was not delivered in accordance with Shell’s quality control standards, consumer confusion was likely, and the Lanham Act was violated.

Third parties selling a company’s products online do not have a vested interest in the quality and appearance of those products. Thus, they frequently do not make the effort to distribute the products in accordance with the standards of quality and often are infringing on trademarks.

3. Take Steps to Remove Unauthorized Items For Sale Online

Once a company can establish the products sold online are “materially different” than the company’s genuine products, the company can explore the possibility of pursuing trademark infringement claims. The easiest way to identify trademark infringement is through monitoring and policing systems. These systems will allow cyber investigators to effectively monitor the internet and send the trademark owners reports of the unauthorized online product sales.

Once these items are identified, the company can work with its legal counsel to send cease and desist letters to offending websites, which oftentimes results in removal. If the offenders refuse to remove the products, the attorney can pursue trademark infringement claims in court to remove them.

Additionally, many websites used to facilitate unauthorized sales do offer help to trademark holders by allowing them to file requests to remove infringing or counterfeit material. For instance, under eBay’s “VeRo program,” a trademark holder can file a “Notice of Claimed Infringement,” which details the nature of the claimed trademark infringement and requests immediate product removal. eBay then evaluates the request and oftentimes removes products for trademark violations.

These third-party websites have a strong interest in removing infringing products because the sites run the risk of being held liable for contributory trademark infringement if they turn a blind eye.

For example, in *Louis Vuitton Malletier, S.A. v. Akanoc Solutions Inc. et al.*, 658 F.3d 936 (9th Cir. 2011), Louis Vuitton discovered several websites it believed were selling products in violation of its trademarks. Louis Vuitton sent notices of infringement to the hosts and providers of the websites documenting the trademark infringement and demanding removal of the content. Because the defendants failed to remove the offending sellers from their websites following Louis Vuitton’s notices, the court found the defendants liable for contributory trademark

infringement. *Id.* at 943; see also, *Inwood Labs. v. Ives Labs.*, 456 U.S. 844, 854 (1982); *Perfect 10, Inc. v. Visa Intl Serv. Ass'n*, 494 F.3d 788, 807 (9th Cir. 2007).

Conclusion: Be Proactive about Unauthorized Product Sales

It is imperative that companies stay proactive when it comes to the unauthorized sale of products online. It is equally important to develop measures to distinguish the business' genuine products from those being sold elsewhere and to attempt to prevent future product diversion. If a business can provide these quality controls and a well-crafted warranty policy, for instance, it can then submit much stronger infringement claims to third-party websites, explaining why the products sold on the website are infringing trademarks.

While these strategies do not guarantee results online or in the courtroom, they are helpful for businesses facing problems related to online product diversion.

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