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Why the Reasonable Anticipation Standard Is the Reasonable Way to Assess Contributory Trademark Liability in the Online Marketplace

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¶1 Trafficking in counterfeit and trademark-infringing goods is a widespread and serious problem, particularly in online marketplaces that provide a forum where third parties, with relative anonymity and at limited cost, can ply their trade. Fortunately, the law has long provided a fair, balanced standard for determining when a party can be held liable for contributing to the infringing actions of another. In *Inwood Laboratories, Inc. v. Ives Laboratories, Inc.*, the Supreme Court held that a party can be contributorily liable if it induced the infringement or continued to support conduct that it knew or had reason to know was infringing.¹

¶2 In the nearly thirty years since then, that standard has been fairly applied in a variety of contexts, including with respect to the actions of flea markets,² landlords,³ and credit card processors.⁴ In *Tiffany (NJ) Inc. v. eBay Inc.*,⁵ though, the U.S. Court of Appeals for the Second Circuit took a different approach; it held that the operator of the online marketplace could be found liable only if it had “specific” knowledge of the infringement:

[A] service provider must have more than a general knowledge or reason to know that its service is being used to sell counterfeit goods. Some contemporary knowledge of which

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¹ 456 U.S. 844, 854 (1982).

² *Fonovisa, Inc. v. Cherry Auction, Inc.*, 76 F.3d 259, 264-65 (9th Cir. 1996); *Hard Rock Café Licensing Corp. v. Concession Servs., Inc.*, 955 F.2d 1143, 1148 (7th Cir. 1992).

³ *Polo Ralph Lauren Corp. v. Chinatown Gift Shop*, 855 F. Supp. 648, 650 (S.D.N.Y. 1994).

⁴ *Gucci Am., Inc. v. Frontline Processing Corp.*, 721 F. Supp. 2d 228, 247-48 (S.D.N.Y. 2010).

⁵ 600 F.3d 93 (2d Cir.), *cert. denied*, 131 S. Ct. 647 (2010).

particular listings are infringing or will in the future is necessary.⁶

¶3 Prior to the Second Circuit’s decision in *Tiffany*, the inquiry in other contributory liability cases did not explicitly focus on a particular level of knowledge, either specific or general, that would trigger liability. Rather, courts considered the totality of the circumstances, including the prevalence of infringing activity in the marketplace, and then asked whether that should be sufficient to warrant the imposition of contributory liability. Under this approach, a level of knowledge much closer to generalized knowledge of widespread infringement, rather than specific knowledge of particular instances of infringement, has traditionally been sufficient to support a finding of contributory liability.

¶4 In this respect, *Tiffany* is difficult to square with the line of cases since *Ives*, in which courts have applied the contributory infringement doctrine in analogous “brick-and-mortar” contexts. In *Fonovisa*, for example, the Ninth Circuit found allegations of generalized knowledge of counterfeiting sufficient to state a claim.⁷ The Ninth Circuit upheld the sufficiency of a complaint alleging that the operator of a swap meet—the brick-and-mortar analogue of eBay.com—had knowledge of counterfeiting based on prior seizures followed by law enforcement letters noting continuing, unspecified acts of counterfeiting. On its face, the evidence in *Fonovisa* is the same type of “generalized” knowledge of illegal activity that the Second Circuit found insufficient in *Tiffany*, while purportedly applying the same contributory infringement test.

¶5 This article suggests that, by requiring knowledge of particular infringements, *Tiffany* introduced an artificial threshold into the standard for contributory trademark infringement liability that did not exist before. In doing so, *Tiffany* failed to take adequate account of the common law roots of contributory liability doctrine, which have always taken a more flexible approach and which recognize that “generalized” knowledge of prevalent tortious conduct by third parties, coupled with assistance to the third party, can, under the proper circumstances, be sufficient to trigger a duty to take “reasonable precautions” to prevent that conduct.⁸ The article further suggests that the duty to take reasonable precautions should, as it has in the offline context, be triggered in the online marketplace context when an operator of an online marketplace has sufficient “generalized” knowledge of infringement so that it can “reasonably anticipate” that such conduct will continue to occur in the future.⁹ “Reasonable anticipation,” this article contends, does not require that the online marketplace have knowledge of “which particular listings are infringing,”¹⁰ but rather may be satisfied by demonstrating “generalized” knowledge that infringement is widespread in the marketplace.

¶6 This article further suggests that this more flexible standard is not only consistent with common law traditions, but also is supported by sound policy considerations. By requiring knowledge of specific infringing transactions, the standard espoused by the Second Circuit in *Tiffany* effectively: (a) eliminates the previously well-accepted standard that a party is contributorily liable if it has constructive knowledge of infringement and provides assistance to the infringer; and (b) reduces the test for contributory liability to an actual knowledge test. An actual knowledge requirement, in turn, reduces the incentives for online marketplace operators to ensure the legitimacy of transactions on their sites and results in a higher incidence of infringing and counterfeiting activity.

¶7 In fairness, counterfeit and infringing activity on online marketplaces does raise different issues than trademark violations in the brick-and-mortar context. Online marketplace providers have less knowledge about the identity of sellers, have no physical access to the goods, and process a significantly greater number of transactions. Those differences may well affect the way in which the

⁶ *Id.* at 107 (emphasis added).

⁷ 76 F.3d at 261, 265.

⁸ *See, e.g.*, RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 27 cmt. c (1995).

⁹ RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 27 (1995) (“[Contributory liability attaches when] the actor fails to take reasonable precautions against the occurrence of the third person’s infringing conduct in circumstances in which the infringing conduct can be reasonably anticipated.”).

¹⁰ *Tiffany*, 600 F.3d at 107.

parties' respective rights and obligations should be balanced, but it should not change the underlying test of how contributory liability is assessed. The common law standard is built upon the bedrock principle of reasonableness under all the circumstances. Placing a duty on online marketplaces to take "reasonable precautions" if infringement can be "reasonably anticipated" recognizes and embodies the real-world limitation on the ability of either online marketplaces or brand owners to tackle this issue alone. Rather, the centuries-old common law principles, applied in the modern, online context, envision a joint cooperative effort to ensure the legitimacy of online transactions for the benefit of all—online marketplaces, brand owners and consumers.

¶8 Part I of the article gives background on the growth of online marketplaces and the concomitant rise of counterfeiting and infringing activity. Part II discusses the current state of the law regarding contributory trademark infringement liability, with a particular focus on the *Ives* litigation and the Second Circuit's application of *Ives* in *Tiffany*. Part III analyzes the common law roots of the contributory infringement doctrine. This analysis concludes that the "generalized" knowledge standard is consistent with the common law origins of contributory trademark liability doctrine. Part IV analyzes the "reasonable anticipation" standard in light of the underlying policies trademark law is designed to foster, and concludes that a "reasonable anticipation" standard, paired with a duty to take "reasonable precautions," best furthers those policies.

I.

¶9 Since 1982, when the Supreme Court last addressed contributory trademark liability in *Ives*,¹¹ an entirely new marketplace has arisen and grown enormously. For example, eBay, which was not even founded until 13 years after *Ives* was decided, reported sales of \$57.2 billion in goods and services through its marketplace during 2009 alone.¹² Reflective of this booming growth, the lexicon has even coined a new name for the Monday after Thanksgiving—Cyber Monday—and on November 29, 2010 (last year's Cyber Monday), online sales hit a new one-day high of \$1.028 billion, the first time online sales exceeded \$1 billion in a single day.¹³

¶10 The growth of the Internet and the popularity of web sites like eBay.com have dramatically increased the prevalence of counterfeiting and trademark infringement. Counterfeiting has ballooned into a social and economic menace, creating severe public health and safety hazards, as well as substantial economic harm to legitimate businesses, on a national and global scale. According to estimates by the Federal Bureau of Investigation ("FBI"), in 2002 counterfeiting cost the United States economy more than \$200 billion in lost sales.¹⁴ According to another estimate, counterfeiting accounts for an estimated \$750 billion dollars in global trade each year.¹⁵ The FBI, Interpol, World Customs Organization and International Chamber of Commerce estimate that an astonishing seven to eight percent of world trade every year is in counterfeit goods.¹⁶ It even has been reported that sales of counterfeit goods support terrorist groups throughout the world.¹⁷ The growing scope of

¹¹ 456 U.S. 844 (1982).

¹² eBay Annual Report, 2009 (Form 10-K), at 54 (Feb. 17, 2010), available at <http://viewer.zmags.com/publication/f80680b9?page=1>.

¹³ Allison Enright, *E-retail's First Billion Dollar Day*, INTERNET RETAILER (Dec. 1, 2010), <http://internetretailer.com/2010/12/01/e-retails-first-billion-dollar-day>.

¹⁴ Press Release, U.S. Customs and Border Protection, U.S. Customs, FBI National Intellectual Property Rights Center Holds Industry Outreach Conference (July 17, 2002), available at http://www.cbp.gov/xp/cgov/newsroom/news_releases/archives/legacy/2002/72002/07172002_2.xml.

¹⁵ David S. Wall & Joanna Large, *Jailhouse Frocks: Locating the Public Interest in Policing Counterfeit Luxury Fashion Goods*, 50 BRIT. J. CRIMINOLOGY 1094, 1096 (2010). Indeed, according to United States government estimates, over 750,000 jobs have been lost due to counterfeiting. Press Release, U.S. Customs and Border Protection, U.S. Customs Announces International Counterfeit Case Involving Caterpillar Heavy Equipment (May 29, 2002), available at http://www.cbp.gov/xp/cgov/newsroom/news_releases/archives/legacy/2002/52002/05292002.xml.

¹⁶ StopFakes.gov, *Why Protect Intellectual Property?*, http://www.stopfakes.gov/sf_why.asp (last visited June 14th, 2011).

¹⁷ ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, THE ECONOMIC IMPACT OF COUNTERFEITING AND PIRACY: EXECUTIVE SUMMARY 15 (2007), available at <http://www.oecd.org/dataoecd/13/12/38707619.pdf>; Press Release, Carratu Int'l, Rise in Counterfeit Market Linked to Terrorist Funding (May 2005), available at <http://www.pressbox.co.uk/Detailed/6073.html>.

this threat to consumers is reflected in Congress's recently-enacted, enhanced criminal penalty provisions for trademark counterfeiting in the Prioritizing Resources and Organization for Intellectual Property Act (PRO-IP Act).¹⁸

¶11 Even before the era of online merchandizing, it had long been recognized that counterfeiting had reached “epidemic” proportions.¹⁹ The rise of the Internet as a commercial forum has only exacerbated this problem. The Organisation for Economic Co-operation & Development (OECD) notes that the Internet has provided counterfeiters with a new and powerful means to sell their products and that a significant share of counterfeit trade is attributable to the Internet.²⁰ Internet auction fraud is the most commonly reported Internet offense, comprising 62.7% of all complaints, according to the Internet Crime Complaint Center's 2005 report.²¹ Indeed, one survey estimated that, during 2006, up to 3 million consumers may have bought a counterfeit item that carried one of the “top ten” luxury brand names, with almost a third (29 percent) of such purchases from online marketplaces such as eBay.²² In 2007 alone, eBay reportedly posted more than 2 million potentially counterfeit listings, and hosted 50,000 sellers attempting to sell fake goods.²³

¶12 This results in two distinct harms that undermine the important policy objectives of trademark law—*viz.*, to lower consumer search costs, foster quality control, and avoid social waste and consumer deception.²⁴ Counterfeit goods obviously tarnish the carefully built reputations of legitimate businesses, undermine their credibility, diminish the good will of their trademarks, and reduce the demand for genuine products. Consumers also suffer enormous harm from the sale of counterfeit goods. Especially when the transactions are completed online, without an opportunity to inspect the goods, consumers are particularly susceptible to unscrupulous counterfeiters who tout their knock-offs as legitimate goods. This risk is heightened in light of the growing sophistication of counterfeiters and their ability to produce knock-offs that, on their surface (and in online listings), appear to be genuine articles.²⁵

II.

¶13 This part of the article examines the current state of the law concerning contributory trademark infringement doctrine. It focuses on the Supreme Court's decision in *Ives* and the lower court decisions that underlie it. In doing so, it closely analyzes the facts of the underlying decisions and the authorities on which *Ives* relied. A proper and careful reading of those decisions reveals that “generalized” knowledge, based on the prevalence of third-party infringing conduct and without knowledge of specific individual infringements, has always been considered a relevant part of the mix of information in determining whether a party has the requisite state of mind to be held contributorily liable for the infringing activity of third parties.

¶14 *Ives* remains the Supreme Court's most recent analysis of contributory trademark infringement liability, so looking closely at the conduct and evidence at issue in that case is a fitting place to start. In *Ives*, the plaintiff manufactured and marketed the patented prescription drug cyclandelate under the trademark CYCLOSPASMOL.²⁶ After the patent expired, the defendant began marketing a generic version of the drug to pharmacists, intentionally copying the appearance of the trademarked

¹⁸ Pub. L. No. 110-403, § 205 (2008) (amending 18 U.S.C. § 2320).

¹⁹ S. Rep. No. 526, at 5 (1984), *reprinted in* 1984 U.S.C.C.A.N. 3627, 3630.

²⁰ ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, *supra* note 17, at 14-15.

²¹ Emily Favre, *Online Auction Houses: How Trademark Owners Protect Brand Integrity Against Counterfeiting*, 15 J.L. & POL'Y 165, 167 n.9 (2007).

²² Wall & Large, *supra* note 15, at 7.

²³ Suze Bragg, *Courts Weigh Online Practices*, CASUAL LIVING, Aug. 1, 2008, at 79.

²⁴ William M. Landes & Richard A. Posner, *Trademark Law: An Economic Perspective*, 30 J. L. & ECON. 265, 275 (1987).

²⁵ *See, e.g.*, Robert Klara, *The Fight Against Fakes*, BRANDWEEK, June 27, 2009 (“[N]ot only is there a lot more phony stuff out there, but it's better made, easier to get, fetching higher prices and taking a bigger chunk out of brands' earnings ...”).

²⁶ *Inwood Labs. v. Ives Labs.*, 456 U.S. 844, 846 (1982).

pills.²⁷ The plaintiff sued and sought a preliminary injunction against the generic manufacturers of cyclandelate and also against the wholesalers of the generic capsules.²⁸ The plaintiff claimed that the defendant's actions induced pharmacists to illegally substitute and mislabel a generic drug for CYCLOSPASMOL, thereby contributing to the infringing activities of the pharmacists.²⁹

¶15 The plaintiff in *Ives* initially moved for a preliminary injunction against the generic manufacturers and wholesalers under three theories: (1) contributory trademark infringement under Section 32 of the Lanham Act; (2) federal unfair competition under Section 43(a) of the Lanham Act; and (3) unfair competition under New York law.³⁰ The plaintiff based its contributory trademark infringement claim on the theory that the pharmacists who mislabeled generic capsules with Ives's trademark were direct infringers and the defendants contributed to that infringement by providing the capsules and through promotional materials describing the generic product as equivalent to the branded product.³¹

¶16 The district court adopted a narrow test for contributory trademark liability. It held that, “[b]efore the passage of the Lanham Act, the doctrine of contributory trademark infringement went no further than to hold one who *actively shared* a retailer's infringement, as in the case, for example, of one who places the infringing label on the articles before delivering them to the retailer” and that “[n]othing in the language or history” of the Lanham Act “intimates that it was intended to expand the doctrine.”³² It limited the scope of contributory liability to instances where the party “*knowing[ly] and deliberate[ly]* instigat[ed]” the druggists to substitute defendant's goods for plaintiffs, acknowledging that such intentional conduct “would justify holding defendants equally with the pharmacists as infringers.”³³ It found, however, that there was “no showing that defendants have *conspired with* the pharmacists or *counseled or suggested* that they disregard the doctors' orders.”³⁴ In doing so, the district court noted evidence that “a number of pharmacies around the country have improperly filled prescriptions for ‘Cyclospasmol’ with generic cyclandelate” and that some “falsely labeled the containers as containing ‘Cyclospasmol,’” but rejected that evidence as insufficient to satisfy a standard requiring “active[] shar[ing]” in the third party's infringing conduct.³⁵

¶17 The Second Circuit affirmed the denial of preliminary injunctive relief. Judge Friendly, however, rejected the district court's standard of contributory trademark infringement as being “unduly narrow.”³⁶ The Second Circuit acknowledged that “knowing and deliberate instigation” where one “actively shared” infringement would constitute contributory infringement, but that that standard did not “mark the limits of the doctrine.”³⁷

¶18 Instead, it stated that a manufacturer would be contributorily liable if it “suggested, even if only by implication, that a retailer fill a bottle with the generic capsules and apply Ives's mark to the label....”³⁸ It went further still, noting that contributory liability could attach if the generic manufacturer “continued to sell capsules” to those it “knew or had *reason to know*” were engaging in that practice.³⁹ The Second Circuit stated that consideration of how “widespread” the generic drug manufacturer's knowledge was of these general infringing activities could be probative of whether

²⁷ *Id.* at 847.

²⁸ *Ives Labs. v. Darby Drug Co.*, 455 F. Supp. 939, 942 (E.D.N.Y. 1978).

²⁹ *Inwood*, 456 U.S. at 850.

³⁰ *Ives*, 455 F. Supp. at 939.

³¹ *Id.* at 942.

³² *Id.*

³³ *Id.* at 945.

³⁴ *Id.* (emphasis added).

³⁵ *Id.* at 944-46.

³⁶ *Ives Labs. v. Darby Drug Co.*, 601 F.2d 631, 636 (2d Cir. 1979).

³⁷ *Id.*

³⁸ *Id.*

³⁹ *Id.*

the defendant acted with the requisite state of mind.⁴⁰ It affirmed the district court, however, on the ground that the plaintiff “failed to adduce the quantum of proof necessary,” in part because it had identified only fifteen instances of illegal substitution.⁴¹

¶19 On remand, the district court once again rejected plaintiff’s contributory infringement claims after a trial on the merits.⁴² The district court, however, did not make reference to or analyze the evidence under the “reason to know” standard articulated by the Second Circuit. Instead, it found that “defendants did not suggest, even by implication, that pharmacists fill bottles with the generic drug cyclandelate and apply the trademark Cyclospasmol.”⁴³ It considered, but rejected, a survey of pharmacists introduced by Ives at trial that showed an additional ten instances of mislabeling as “hardly justifi[ng] an inference that the defendant[s] ... impliedly invited druggists to mislabel.”⁴⁴

¶20 On appeal, the Second Circuit reversed. First, it reconfirmed that awareness of widespread infringement was a form of evidence relevant to the state-of-mind standard.⁴⁵ It concluded that the additional instances of mislabeling provided by Ives at trial constituted a “pattern of illegal substitution and mislabeling in New York” that was “precisely the sort of showing which we held would be probative of plaintiff’s [Section] 32 claim... .”⁴⁶ It further concluded that “[t]he additional evidence introduced by Ives at trial was clearly sufficient to establish a [Section] 32 violation” and that the district court “erred” by “declining to give any weight to [the] additional evidence offered by Ives.”⁴⁷

¶21 The Supreme Court granted *certiorari* to review the Second Circuit’s decision. Although it reversed the Second Circuit on the ground that it failed properly to apply a “clearly erroneous” standard to the review of the district court’s factual findings, it confirmed that liability can extend to third parties who contribute to the trademark infringement, even if they are not directly responsible.⁴⁸ The Supreme Court rearticulated the *Ives* test as a two-prong test for determining whether a party is liable for the trademark-infringing conduct of third parties. It held that such liability will attach:

- (1) “if a manufacturer or distributor *intentionally induces* another to infringe a trademark,” or
- (2) if it continues to supply its product to one whom it *knows* or *has reason to know* is engaging in trademark infringement.”⁴⁹

¶22 Applying this standard, the Court found inappropriate, based on the District Court’s factual findings, the Second Circuit’s conclusion that the “illegal substitution and mislabeling” of a generic drug as CYCLOSPASMOL was “neither *de minimis* nor inadvertent.”⁵⁰ In other words, the Supreme Court found no basis for overturning the district court’s factual finding that the instances of illegal substitution were not widespread such as to justify an inference of knowledge, whether actual or

⁴⁰ *Id.* at 644.

⁴¹ *Id.*

⁴² *Ives Labs. v. Darby Drug Co.*, 488 F. Supp. 394, 398 (E.D.N.Y. 1980).

⁴³ *Id.* at 397.

⁴⁴ *Id.*

⁴⁵ *Ives Labs. v. Darby Drug Co.*, 638 F.2d 538, 543 (2d Cir. 1981) (“Since the governing legal principles have already been set forth in Judge Friendly’s opinion upon the earlier appeal, ... we need not repeat them here.”).

⁴⁶ *Id.*

⁴⁷ *Id.* at 542-43.

⁴⁸ *Inwood Labs. v. Ives Labs.*, 456 U.S. 844, 853, 858 (1982) (“As the lower courts correctly discerned, liability for trademark infringement can extend beyond those who actually mislabel goods with the mark of another.”) As the Second Circuit noted, *Ives* addressed contributory liability in the context of a manufacturer providing products to a distributor. 600 F.3d at 105 & n.10. Some courts, including the *Tiffany* court, have applied the *Ives* test where a party contributes *services* to an infringer (including in the Internet context) and has the ability to deny the infringer access to its services. *See, e.g., Fonovisa, Inc. v. Cherry Auction, Inc.*, 76 F.3d 259, 265 (9th Cir. 1996) (*Ives* “laid down no limiting principle that would require defendant to be a manufacturer or distributor”); *Lockheed Martin Corp. v. Network Solutions, Inc.*, 194 F.3d 980, 984 (9th Cir. 1999) (extending *Ives* to service providers who exercise “[d]irect control and monitoring of the instrumentality used by a third party to infringe”). For example, courts have applied *Ives* to landlords, *Polo Ralph Lauren Corp. v. Chinatown Gift Shop*, 855 F. Supp. 648, 650 (S.D.N.Y. 1994), and to flea market operators, *Hard Rock Café Licensing Corp. v. Concession Servs., Inc.*, 955 F.2d 1143 (7th Cir. 1992).

⁴⁹ 456 U.S. at 854.

⁵⁰ *Id.* at 857.

constructive. Had such evidence—*viz.*, widespread “illegal substitution and mislabeling”—been in the record, there is no reason to believe the Supreme Court would have found that evidence irrelevant to the question of whether the contributory liability standard was satisfied. That is why it echoed the Second Circuit in agreeing that “frequent improper substitutions” were relevant in determining whether the manufacturer “implicitly had suggested that pharmacists substitute improperly.”⁵¹

¶23 In *Ives*, Justice White concurred with the majority opinion, but wrote separately on the proper application of the test the majority articulated. He agreed that “a finding of contributory infringement requires proof of either an intent to induce illegal substitution or continued sales to particular customers whom the manufacturer knows or should know are engaged in improper palming off.”⁵² However, he took issue with the Second Circuit’s statement, which he felt the Supreme Court adopted, that liability could attach if the manufacturer “could reasonably anticipate that their generic drug product would by a substantial number of druggists be substituted illegally.”⁵³ Justice White expressed concern that finding contributory liability based on “[t]he mere fact that a generic drug company can anticipate that some illegal substitution will occur” represented a “significant change in the test for contributory infringement” that would “water[] down” the intentional inducement test.⁵⁴

¶24 Justice O’Connor, writing for the majority, responded to Justice White’s criticism in footnote 13 of the majority opinion. The majority noted that, “[i]f the Court of Appeals had relied upon that statement to define the controlling legal standard, the court indeed would have applied a ‘watered down’ and incorrect standard.”⁵⁵ That is not what the Second Circuit, or the Supreme Court by adopting the Second Circuit’s test, did, however. Instead, the Second Circuit considered, under the intentional inducement prong, whether the manufacturer could “reasonably anticipate” direct infringement as relevant to whether the manufacturer had “suggested, even by implication” that the druggists illegally substitute. In other words, such evidence is relevant to state of mind, whether under the intentional inducement prong or under the negligence-based, “reason to know” standard. That is why the majority concluded the standard was not “watered down,” but rather that the evidence was properly considered “merely to buttress the [Second Circuit’s] conclusion that the legal test for contributory infringement . . . had been met.”⁵⁶

¶25 Evidence of generalized knowledge of widespread infringement, therefore, is relevant regardless of the contributory trademark infringement theory (*i.e.*, inducement, actual knowledge or reason to know) because it can either (A) “indicate” circumstantially the contributory tortfeasor’s “intention,” or (B) demonstrate that the contributory infringer acted negligently with respect to the direct infringer’s acts under the “should have known” prong of the test.

¶26 A close analysis of the *Ives* opinions thus makes clear that courts can, and should, consider generalized knowledge, such as awareness of the frequency and volume of infringing conduct in general, in assessing liability for contributory infringement because it is circumstantial evidence of the contributory tortfeasor’s state of mind. As one commentator noted, “all [that *Ives* arguably requires] is that a substantial number of pharmacists commit direct infringement by substituting the generic capsules for plaintiff’s while applying the latter’s trademark.”⁵⁷

⁵¹ *Id.* at 852. See also A. Samuel Oddi, “Contributory Copyright Infringement: The Tort and Technological Tensions,” 64 NOTRE DAME L. REV. 47, 77 (1989) (“[T]he Court seemingly approved the drawing of an inference of ‘suggestion’ on the basis of the quantity of mislabeling proven. . . .”).

⁵² *Ives*, 456 U.S. at 860 (White, J., concurring).

⁵³ *Id.* at 859, 860 (emphasis omitted).

⁵⁴ *Id.* at 859, 861.

⁵⁵ *Id.* at 854 n.13 (majority opinion).

⁵⁶ *Id.*

⁵⁷ Oddi, *supra* note 51, at 77 (noting that *Ives* resembles the Supreme Court’s analysis in *Sony Corp. of America v. Universal City Studios*, 464 U.S. 417 (1984), where contributory copyright liability attaches “provided the copyright owner can prove significant direct infringement”).

¶27 A holding that knowledge of “widespread” but unspecified infringement is relevant to the state-of-mind element of the contributory infringement standard cannot be squared with a requirement like the one stated in *Tiffany* that contributory liability attaches *only* upon specific knowledge of particular infringing transactions. If specific knowledge were the standard for determining whether a party has “reason to know of infringement by third parties” or “implicitly had suggested” illegal substitutions, knowledge of “widespread” but unspecified infringement would be irrelevant.

¶28 It is not surprising, therefore, that other courts applying *Ives* under similar circumstances have considered “generalized knowledge” to be relevant to the contributory liability analysis. In *Ciba-Geigy Corp. v. Bolar Pharm. Co.*,⁵⁸ for example, the Third Circuit addressed claims by a prescription drug manufacturer identical to the claims in *Ives*. Upon the expiration of the patent for the prescription drug APRESAZIDE, the defendant commenced marketing a generic version in the same size, shape and color as the prescription product to wholesalers, who sold the generic product to pharmacists.⁵⁹

¶29 The plaintiff sued the generic drug manufacturer claiming that the defendant manufactured and distributed the generic product with the “reasonable anticipation” that pharmacists would illegally substitute a generic drug for APRESAZIDE, thereby contributing to the infringing activities of the pharmacists.⁶⁰ Among the evidence the Third Circuit found probative of the defendant’s constructive knowledge of infringement by pharmacists were the convictions “of at least 93 pharmacists and pharmacies for passing off in New York in the three years preceding the filing” of the lawsuit.⁶¹ Similarly, in *Mini Maid Servs. Co. v. Maid Brigade Sys., Inc.*,⁶² the Eleventh Circuit held that, “[i]f the infringement is *serious and widespread*, it is more likely that the franchisor knows about and condones the acts of its franchisees.”⁶³

* * *

¶30 In *Tiffany*, both the district court and the Second Circuit purported to apply *Ives* to determine whether eBay could be contributorily liable for infringing activity based on its admitted “generalized” knowledge of infringing activity by its vendors.⁶⁴ *Tiffany* argued that “the only relevant question [was] ‘whether all of the knowledge, when taken together, puts [eBay] on notice that there is a substantial problem of trademark infringement.’”⁶⁵ The Second Circuit rejected this argument:

Tiffany understands the “lesson of *Inwood*” to be that an action for contributory trademark infringement lies where “the evidence [of infringing activity] — direct or circumstantial, taken as a whole — ... provide[s] a basis for finding that the defendant knew or should have known that its product or service was being used to further illegal counterfeiting activity.” ... We think that *Tiffany* reads *Inwood* too broadly

We... do not think that *Inwood* establishes the contours of the “knows or has reason to know” prong. Insofar as it speaks to the issue, though, the particular phrasing that the Court used — that a defendant will be liable if it “continues to supply its product to *one* whom it knows or has reason to know is engaging in trademark infringement,” ... supports the district court’s interpretation of *Inwood*, not *Tiffany*’s.⁶⁶

⁵⁸ 747 F.2d 844 (3d Cir. 1984).

⁵⁹ *Id.* at 849.

⁶⁰ *Id.*

⁶¹ *Id.* at 853 n.4.

⁶² 967 F.2d 1516 (11th Cir.1992).

⁶³ *Id.* at 1522 (emphasis added); see also RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 27 cmt. c.

⁶⁴ *Tiffany* (NJ) v. eBay, 600 F.3d 93, 103-04 (2d Cir. 2010); *Tiffany* (NJ) v. eBay, 576 F. Supp. 2d 463, 508 (S.D.N.Y. 2008).

⁶⁵ 600 F.3d at 107.

⁶⁶ *Id.* at 107-08 (quoting *Inwood Labs. v. Ives Labs.*, 456 U.S. 844, at 854 (1982)). It is certainly up for debate whether the Second Circuit put too much weight on the Supreme Court’s specific language (*i.e.*, “to *one* whom it knows”) by interpreting it to require specific knowledge of identified individual infringers before contributory infringement liability could attach. As is shown by a careful reading of *Ives* and the authorities on which it relies, the specific facts of those cases show that general knowledge of prevalent infringing conduct can satisfy the “reason to know” standard.

¶31 The Second Circuit thus rejected the notion that eBay could be liable if this generalized knowledge of counterfeiting gave rise to a “reasonable anticipation” that particular listings might be counterfeit. Instead, the court held,

For contributory trademark infringement liability to lie, a service provider must have more than a general knowledge or reason to know that its service is being used to sell counterfeit goods. Some contemporary knowledge of which *particular listings* are infringing or will infringe in the future is necessary.⁶⁷

¶32 *Tiffany* is in considerable tension, if not direct conflict, with other decisions in the analogous brick-and-mortar context. In *Fonovisa, Inc. v. Cherry Auction, Inc.*,⁶⁸ the Ninth Circuit applied the *Ives* standard to the brick-and-mortar analogue of an online marketplace—a swap meet where a substantial number of vendors allegedly sold counterfeit and infringing merchandise.⁶⁹ The plaintiff alleged that the flea market operator either knew or was chargeable with constructive knowledge of infringing sales by virtue of three allegations, none of which constitutes the type of “specific” knowledge required by the Second Circuit: (1) the Fresno County Sherriff earlier had seized more than 38,000 counterfeit recordings from the same swap meet; (2) the Sherriff sent a letter a year later notifying the swap meet operators of unspecified, ongoing sales of infringing merchandise; and (3) in the same letter, the Sherriff reminded the swap meet operators that they had agreed to provide the Sherriff with information identifying each vendor.⁷⁰

¶33 Based on these allegations, the Ninth Circuit concluded that there was “no dispute” that the swap meet operators “were aware that vendors ... were selling counterfeit recordings....”⁷¹ The Ninth Circuit accordingly held that the swap meet operators could be held contributorily liable because the operator’s indifference to the pervasive acts of infringement by third parties satisfied the “reason to know” standard of *Ives*.⁷² There were no allegations that the operator knew which specific vendors were selling counterfeits, nor were the trademark owners required to identify which particular items being sold at the swap meet were counterfeit; instead, the Ninth Circuit held that the allegation that the operators continued to provide services with the knowledge that unspecified ongoing acts of infringement were occurring satisfied the test for contributory liability under *Ives*.⁷³

¶34 As the next part of this article demonstrates, the common law roots of contributory infringement doctrine are consistent with *Fonovisa* in recognizing that generalized knowledge of the kind that existed in *Tiffany* and *Fonovisa* can be a sufficient factor in establishing contributory trademark liability.

III.

¶35 This part of this article traces the common law roots of contributory infringement doctrine, specifically with respect to the quantum and type of knowledge courts consider in determining whether a party should be contributorily liable for the tortious conduct of third parties. It concludes that common law tort principles, as articulated in the *Restatements of Tort and Unfair Competition*, recognize both that (i) constructive knowledge is a sufficient trigger for contributory liability, and (ii)

⁶⁷ *Id.* at 107 (emphasis added).

⁶⁸ 76 F.3d 259 (9th Cir. 1996).

⁶⁹ *Id.* at 261.

⁷⁰ *Id.*

⁷¹ *Id.*

⁷² *Id.* at 265.

⁷³ *Id.* at 265; *Hard Rock Café Licensing Corp. v. Concession Servs., Inc.*, 955 F.2d 1143, 1149 (7th Cir. 1992) (finding evidence that the swap meet operator “did not ask vendors whether their goods were counterfeit because they were sure to lie to him” probative of knowledge of third-party infringement under *Ives*). Of course, the operators of “brick and mortar” flea markets and the like have the opportunity to physically inspect the goods being sold there, a luxury online marketplaces lack. This article suggests that this should not affect the analysis of what type of knowledge should suffice to trigger a duty under the common law principles applicable to contributory trademark infringement. Rather, consideration of the circumstances unique to online marketplaces should shape the contours of what “precautions” against infringing conduct are “reasonable” under the circumstances. *See* pp. 46-50, *infra*.

constructive knowledge can be evidenced by proof of prevalent direct infringement by third parties, regardless of whether the contributory infringer has knowledge of specific infringing transactions.

¶36 Neither the Copyright Act nor the Lanham Act (with a limited exception)⁷⁴ contains express contributory liability provisions.⁷⁵ Rather, the imposition of contributory infringement liability, under either area of the law, has been derived from common law tort theories.⁷⁶ In the Patent Act, by contrast, direct and contributory infringement are defined in the statute.⁷⁷ Although formulated slightly differently by courts depending on whether the underlying infringement is of a trademark,⁷⁸ or a copyrighted work,⁷⁹ the doctrinal foundation for both is the common law of tort.⁸⁰

¶37 The two-prong test set forth in *Ives*⁸¹ reflects the two primary bases in the common law for the imposition of contributory liability: (1) active inducement (as the Supreme Court in *Ives* puts it, “if a manufacturer or distributor intentionally induces” another to infringe); and (2) assistance to the direct tortfeasor where the contributory tortfeasor knows or has reason to know that the other “is acting or will act tortiously”⁸² (in *Ives*, “continues to supply ... to one whom it knows or has reason to know” is a direct infringer).

⁷⁴ 15 U.S.C. § 1114(1) (2005) (providing for contributory infringement liability if a party supplied counterfeit or imitation labels with “knowledge that such imitation is intended to be used to cause confusion, or to cause mistake, or to deceive”).

⁷⁵ The Lanham Act expressly covers a specific type of contributory trademark infringement relating to the reproduction of a trademark on labels or wrappers intended to be used in commerce. 15 U.S.C. § 1114(1)(b) (2005) (imposing liability where any person “reproduce[s], counterfeit[s], cop[ies], or colorably imitate[s] a registered trademark and appl[ies] such reproduction ... to labels, signs, prints, packages, wrappers, receptacles or advertisements intended to be used in commerce upon or in connection with the sale, offering for sale, distribution, or advertising of goods or services on or in connection with which such use is likely to cause confusion, or to cause mistake, or to deceive”).

⁷⁶ *Hard Rock Café*, 955 F.2d at 1148 (trademark infringement is “species of tort” and “appropriate boundaries” of contributory infringement liability are “guide[d]” by “common law”); see also *Metro-Goldwyn-Mayer Studios, Inc. v. Grokster*, 545 U.S. 913, 930-31 (2005) (noting that secondary liability under Copyright Act “emerged from common law principles and are well established in the law”); 4 J. Thomas McCarthy, MCCARTHY ON TRADEMARKS AND UNFAIR COMPETITION § 25:17 (4th ed.) (contributory trademark infringement is “a judicially created doctrine that derives from the common law of torts”) (quoting *Tiffany (NJ) v. eBay*, 600 F.3d 93, 103-04 (2d Cir. 2010)); John T. Cross, “Contributory Infringement and Related Theories of Secondary Liability for Trademark Infringement,” 80 IOWA L. REV. 101, 109-129 (1994); Mark Bartholomew & John Tehranian, “The Secret Life of Legal Doctrine,” 21 BERKELEY TECH. L. J. 1363, 1368 (2006); John T. Cross, *Contributory Infringement and Related Theories of Secondary Liability for Trademark Infringement*, 80 Iowa L. Rev. 101, 109-29 (1994).

⁷⁷ 35 U.S.C. § 271 (2010) (defining liability for those who directly infringe, “actively induce[] infringement,” and who sell components “knowing” them to be adapted for use to infringe); see also *Sony Corp. of Am. v. Universal City Studios*, 464 U.S. 417, 440 n.20 (1984).

⁷⁸ See *Inwood Labs. v. Ives Labs.*, 456 U.S. 844, 854 (1982) (contributory liability attaches if defendant “intentionally induces” infringement or “continues to supply” goods or services to one it “knows or has reason to know is engaging in trademark infringement”) (emphasis added).

⁷⁹ *Gershwin Pub. Corp. v. Columbia Artists Mgmt., Inc.*, 443 F.2d 1159, 1162 (2d Cir. 1971) (contributory liability attaches if defendant has “knowledge or reason to know” of infringement and “materially contributes” to it) (emphasis added).

⁸⁰ Although the Digital Millennium Copyright Act (“DMCA”), 17 U.S.C. § 512 (2010), is distinct to copyright law, it too echoes common law principles by limiting its “safe harbor” provisions to situations where the Internet Service Provider lacks either “actual knowledge” or “in the absence of such actual knowledge is not aware of facts or circumstances from which infringing activity is apparent.” 17 U.S.C. § 512(c) (emphasis added). Echoing *Tiffany*, the court in *Viacom Int’l Inc. v. YouTube, Inc.*, concluded that “knowledge of specific and identifiable infringements of particular individual items” is required before an ISP falls outside of the DMCA safe harbor. 718 F. Supp. 2d 514, 523 (S.D.N.Y. 2010). That decision is on appeal to the Second Circuit. Similar issues concerning the requisite level of knowledge for contributory patent infringement are being reviewed by the Supreme Court. *Global-Tech Appliances, Inc. v. SEB S.A.*, 131 S. Ct. 458 (2010) (granting *certiorari* on whether inducing patent infringement claim requires “deliberate indifference of a known risk” or “purposeful, culpable expression and conduct”).

⁸¹ (1) “if a manufacturer or distributor intentionally induces another to infringe a trademark,” or (2) “if it continues to supply its product to one whom it knows or has reason to know is engaging in trademark infringement.” *Ives*, 456 U.S. at 854.

⁸² RESTATEMENT (SECOND) OF TORTS § 877(c) (1979) (Directing or Permitting Conduct of Another). The full text of Section 877(c) provides:

For harm resulting to a third person from the tortuous conduct of another, one is subject to liability if he

- (a) orders or induces the conduct, if he knows or should know of circumstances that would make the conduct tortuous if it were his own, or
- (b) conducts an activity with the aid of the other and is negligent in employing him, or
- (c) permits the other to act upon his premises or with his instrumentalities, knowing or having reason to know that the other is acting tortiously, or
- (d) controls, or has a duty to use care to control, the conduct of the other, who is likely to do harm if not controlled, and fails to exercise care in the control, or
- (e) has a duty to provide protection for, or to have care used for the protection, third persons or their property and confides the performance of the duty to the other, who causes or fails to avert the harm by

¶38 As with any tort, liability for contributory infringement can attach only if the defendant owes a duty to the plaintiff and acts tortiously (*i.e.*, with intent, recklessness, negligence or, in the case of strict liability, without any fault), resulting in harm.⁸³

¶39 With respect to inducement, the contributory trademark infringement tort has typically required intent.⁸⁴ In *De Kuyper v. Witteman*, for example, the court denied a motion to dismiss on plaintiff's allegation that defendant was "actively engaged" by supplying infringing labels "with the obvious purpose of enabling others by the use of the labels to palm off their goods."⁸⁵ Similarly, in *Von Mumm v. Witteman*, the court drew an inference of intent to induce where the defendant supplied champagne labels with plaintiff's trademark printed on it; actual knowledge that the labels would be used to infringe was inferred.⁸⁶ At least one early decision, however, appears to have applied a negligence standard to an inducement claim.⁸⁷ Actual knowledge, including willful blindness, can also equate with intent.⁸⁸

¶40 The "reason to know" prong, however, is the prototypical expression of a negligence standard.⁸⁹ As the Seventh Circuit put it:

[T]he Restatement of Torts tells us that [a landlord or licensor of property] is responsible for the torts of those it permits on its premises "knowing or having reason to know that the other is acting or will act tortiously...." The common law, then, imposes the same duty on landlords and licensors that the Supreme Court [in *Ives*] has imposed on manufacturers and distributors.⁹⁰

¶41 Whether generalized knowledge of direct infringement satisfies any of these types of contributory liability turns on what level of fault (*i.e.*, intent or negligence) meets the tort requirements. Requiring specific knowledge of infringing transactions effectively means actual knowledge which equals an intentional tort. Premising liability on generalized knowledge of infringing conduct that suggests a foreseeable risk of future infringing conduct, by contrast, constitutes a negligence standard. The scope of protection afforded brand owners (and the scope of any concomitant duty owed by online marketplaces) is directly tied to the applicable fault standard. That is:

If strict liability is applied to contributory infringers, as it is for direct infringers, this would provide a broad scope of protection. Conversely, if contributory infringement were limited to intentional conduct on the part of the alleged contributory infringement, this would result in a significant narrowing of the tort compared to strict liability. An intermediate scope of protection for contributory infringement would result if premised upon a finding of negligent conduct by the contributor.⁹¹

failing to perform the duty.

⁸³ W. PROSSER, THE LAW OF TORTS § 44 (4th ed. 1971).

⁸⁴ See RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 27(a) (liability attaches if the "actor intentionally induces the third person to engage in the infringing conduct"); A. Samuel Oddi, *Product Simulation and Contributory Trademark Infringement: A Right Suggests A Wrong*, 25 ARIZ. L. REV. 601, 620-21 (1983).

⁸⁵ *De Kuyper v. Witteman*, 23 F. 871, 871-72 (S.D.N.Y. 1885).

⁸⁶ *Von Mumm v. Witteman*, 85 F. 966 (C.C.N.Y. 1898).

⁸⁷ *Reid, Murdoch & Co. v. H.P. Coffee Co.*, 48 F.2d 817, 819-20 (8th Cir. 1931) (finding liability where defendant supplied product with plaintiff's mark under circumstances where third party passing off "might well have been anticipated by the defendant").

⁸⁸ *Hard Rock Café Licensing Corp. v. Concession Servs., Inc.*, 955 F.2d 1143, 1149 (7th Cir. 1992) ("We have held that willful blindness is equivalent to actual knowledge for purposes of the Lanham Act."); see also *United States v. Khorozian*, 333 F.3d 498, 504 (3d Cir. 2003) (holding, in a federal bank fraud case, that "willful blindness constitutes sufficient fraudulent intent"); *State St. Trust Co. v. Ernst*, 15 N.E.2d 416, 419 (N.Y. 1938) (finding that "blindness to the obvious" including "heedlessness and reckless disregard of consequence may take the place of deliberate intention").

⁸⁹ RESTATEMENT (SECOND) OF TORTS § 877(c) (1979) (citation omitted) (landlord liable under negligence standard if it permits a tort, "knowing or having reason to know that the other is acting or will act tortiously").

⁹⁰ *Hard Rock Café*, 955 F.2d at 1149.

⁹¹ Oddi, *supra* note 51, at 64 n.130.

¶42 The common law roots of contributory liability suggest that the “intermediate scope” afforded by a negligence standard (“reason to know”) is the historical norm and the standard articulated by *Ives*. Generalized knowledge of widespread tortious conduct by third parties has long been recognized as a basis for common law contributory liability. Oliver Wendell Holmes observed in 1881 that a person would have sufficient knowledge to make them “liable for the consequences of [their] act” as long as they had knowledge “as would have led a prudent man to perceive danger, although not necessarily to foresee the specific harm.”⁹² Applying this negligence principle to contributory liability doctrine, the *Restatement (First) of Torts* states that an actor would be liable for the negligence of a third party if the actor “creates a situation which involves an unreasonable risk to another because of the *expectable action* of ... a third person.”⁹³ An action of a third person is “expectable” to an actor, in turn, when the actor “creates a situation or does an act, which affords a temptation to, or an opportunity for, intermeddling by a person or *class of persons* whom he knows or *should know* to be peculiarly *likely* to do so.”⁹⁴ The *Restatement* did not find contributory liability to be limited to situations where the direct tortfeasor is *specifically* known.

¶43 The same concept also is set forth in the *Restatement (Second) of Torts* § 877(c). That section provides that contributory liability attaches if one permits another “to act upon his premises or with his instrumentalities, knowing or having *reason to know* that the other is acting or *will act* tortiously.”⁹⁵ The *Restatement* expressly defines “reason to know” as “knowledge of facts from which a reasonable man ... would either infer the existence of the fact in question or *would regard its existence as so highly probable* that his conduct would be predicated on the assumption that the fact did exist.”⁹⁶

¶44 The “reasonable anticipation” test in the *Restatement (Third) of Unfair Competition* echoes these common law principles. Under that test, contributory liability attaches if “(a) the actor *intentionally induces* the third person to engage in the infringing conduct; or (b) the actor fails to take *reasonable precautions* against the occurrence of the third person’s infringing conduct in circumstances in which the infringing conduct can be *reasonably anticipated*.”⁹⁷

¶45 Although the inducement standard requires intent, the *Restatement* makes clear that the “inducement may consist of an express suggestion that the third person market the goods or services under another’s trademark” or “may also be implicit in the actor’s conduct.”⁹⁸ With respect to the latter, it states that “[a] failure to take reasonable precautions where there is a known *risk of substantial infringement* may indicate an intention to induce the infringing conduct, thus subjecting the manufacturer or distributor to liability under clause (a) of this Section.”⁹⁹ Thus, even under an intentional inducement standard, generalized knowledge can be relevant to determining the contributory tortfeasor’s state of mind. This position is consistent with *Ives*, as demonstrated by the colloquy between Justice White’s concurrence and the majority, which is discussed earlier.¹⁰⁰

¶46 The *Ives* decision, although setting forth the “reason to know” standard, analyzed the issue under the “intentional inducement” prong. For further insight into the roots and meaning of the “reason to know” standard, it is useful to examine more closely the authority upon which *Ives* relied. Running through both the Second Circuit and Supreme Court decisions in *Ives*, as well as the articulation of the contributory liability standard in the *Restatement (Third) of Unfair Competition*, is the seminal decision in *Coca-Cola Co. v. Snow Crest Beverages, Inc.*¹⁰¹ In *Ives*, the Supreme Court cited and relied upon *Snow*

⁹² OLIVER WENDELL HOLMES, JR., THE COMMON LAW 147 (1881).

⁹³ RESTATEMENT (FIRST) OF TORTS § 302(b) (1934).

⁹⁴ *Id.* at § 302(b) cmt. m (emphasis added).

⁹⁵ RESTATEMENT (FIRST) OF TORTS § 877(c) (1979).

⁹⁶ *Id.* § 12(1) cmt. a (emphasis added).

⁹⁷ RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 27 (1995) (emphasis added).

⁹⁸ *Id.* at § 27 cmt. b.

⁹⁹ *Id.* at § 27 cmt. c (emphasis added).

¹⁰⁰ See *supra* text accompanying notes 52-56.

¹⁰¹ 64 F. Supp. 980 (D. Mass. 1946), *aff’d* 162 F.2d 280 (1st Cir. 1947), *cert. denied*, 332 U.S. 809 (1947).

Crest as good authority and implicitly adopted the *Snow Crest* standard for contributory infringement liability by upholding the *Snow Crest* test articulated by Judge Friendly in the first *Ives* opinion.¹⁰²

¶47 *Snow Crest* expressly considered as probative the type of generalized knowledge found insufficient in *Tiffany*. In *Snow Crest*, Coca-Cola alleged that, “when bars received orders for rum (or whiskey) and Coca-Cola, bars frequently substituted defendant’s product, ‘Polar Cola.’”¹⁰³ Echoing the common law roots of the contributory infringement doctrine, the court framed the issue as whether the defendant—the manufacturer and distributor of Polar Cola—was “under a duty to investigate such passing off, or to take steps to safeguard against such passing off, or to eliminate or curtail sales of its product” after “it had notice that *some unnamed bars*” had substituted its product for Coca-Cola.¹⁰⁴

¶48 The *Snow Crest* district court held that such a duty arises in two distinct circumstances, based on upon the relative prevalence of infringing third-party conduct in the marketplace. The district court noted that “it is, of course, defendant’s duty to avoid intentionally inducing bars to market defendant’s products as products of plaintiff’s ... [and] to avoid knowingly aiding bars which purchase defendant’s products from marketing those products in such a manner as to infringe plaintiff’s trade-mark.”¹⁰⁵ These statements parallel the “intentional inducement” and “actual knowledge” parts of the *Ives* standard.

¶49 *Snow Crest* did not stop there; instead, it made clear that intentional inducement and continued supply with actual knowledge do not define the outer scope of a defendant’s duty. It identified two other circumstances under which the defendant would have a “reason to know” of infringing activity and therefore a duty to take reasonable measures to prevent infringing acts of its customers.

¶50 Under the first, the defendant would owe a duty to the plaintiff if the defendant “had known or a normal bottler would have known that *most* bar customers specifically ordered Coca-Cola and that consequently a normal bottler would infer from defendant’s large volume of sales that many bars” were substituting defendant’s cola for Coca-Cola.¹⁰⁶ This formulation—which expressly premises a duty on the prevalence of general infringing activity—confirms that generalized knowledge can establish contributory liability under well-settled common law principles.

¶51 Under the second circumstance, a defendant would have a duty if it had “known that *many* bar customers specifically ordered Coca-Cola and had also known that *some particular bars* were in fact” substituting defendant’s product.¹⁰⁷ Under this formulation, when the directly infringing activity is less prevalent (“many” vs. “most”), a duty is triggered only with knowledge of “particular bars” “in fact” committing infringement—or as *Tiffany* put it sixty-four years later, “some contemporary knowledge of which particular listings are infringing.”¹⁰⁸

¶52 Thus, under *Snow Crest* (which both the Second Circuit and Supreme Court cited as setting forth the proper criteria for contributory infringement liability), where infringement by third parties is prevalent (knowledge that “most” transactions are infringing), a duty is imposed even in the absence of knowledge of specific infringing acts. Where the infringement is less prevalent (knowledge that “many” transactions are infringing), the court will not impose a duty unless the defendant had knowledge that at least “some particular” transactions infringed.¹⁰⁹

¹⁰² Judge Friendly held that *Snow Crest* stated the “proper criteria” for a contributory infringement claim, *Ives Labs., Inc. v. Darby Drug Co., Inc.*, 601 F.2d 631, 636 (2d Cir. 1979), and the Supreme Court agreed. See *Inwood Labs v. Ives Labs.*, 454 U.S. 844, 854 n.13 (1982).

¹⁰³ *Snow Crest*, 64 F. Supp. at 988.

¹⁰⁴ *Id.* (emphasis added).

¹⁰⁵ *Id.* at 989.

¹⁰⁶ *Id.* (emphasis added).

¹⁰⁷ *Id.* (emphasis added).

¹⁰⁸ 600 F.3d at 107.

¹⁰⁹ Oddi, *supra* note 84, at 643 (“Under Judge Wyzanski’s analysis, a duty of reasonable care would be imposed upon the seller of the imitation product to protect the trademark owner from direct trademark infringement only when ‘most’ purchasers of the product from the imitator’s customers order the product by trademark and the high volume of sales by the imitator inferred trademark infringement by its customers. However, if there were only ‘many’ sales by trademark, this would necessitate that the defendant have actual knowledge of particular customers who were engaged in such tortious conduct.”).

¶53 This article suggests that this articulation accurately reflects the scope of contributory infringement liability under the “reason to know” prong of *Ives* and that the standard set forth in the *Restatement (Third) of Unfair Competition* is an apt restatement of those principles.

IV.

¶54 This section of the article examines the standards for contributory trademark liability discussed above in light of the policy goals of trademark law. It concludes that, in addition to being the traditional common law standard and the one adopted in *Snow Crest* and *Ives*, a constructive knowledge standard of contributory liability flexible enough to be satisfied in some circumstances by general knowledge best advances those policies.

¶55 Trademark law promotes three distinct policies: (1) to prevent consumer confusion, (2) to protect the goodwill of businesses, and (3) to promote competition within the market.¹¹⁰ From an economic perspective, trademark law’s furtherance of these policies contributes to efficiency by reducing consumer search costs.¹¹¹ Instead of inquiring into the provenance and qualities of every potential purchase, consumers can avoid confusion by looking to trademarks as shorthand signals of quality and source.¹¹² In this way, trademarks make obtaining information about products less costly. Consumers will demand more of these signals and will arguably become better informed, leading to a more competitive market.¹¹³ Thus, one way to express “[t]he value of a trademark is the saving in search costs made possible by the information or reputation that the trademark conveys or embodies about the brand.”¹¹⁴

¶56 These benefits depend on the continued ability of trademarks to function as a reliable shorthand indicator for consumers. For this to be the case, a consumer’s past experience with a product or service must be a good predictor of their future experiences with the same brand.¹¹⁵ This gives trademark owners an incentive to maintain consistent quality of their goods so that the shorthand information conveyed by the trademark is consistent with consumer expectations.¹¹⁶

¶57 Underlying this economic framework is the tenet that consumers must be able to trust that trademarks accurately convey information about the products or services they brand.¹¹⁷ It should almost go without saying, then, that the economic benefits of trademarks depend critically upon the proper legal protection of trademark rights. Trademark law plays an essential role in upholding a trademark’s ability to signal quality because otherwise, free-riding competitors copying a reputable trademark will capture profits that should have gone to the trademark owner if consumers believe the products come from the same source.¹¹⁸ If such free-riding is allowed to continue, and consumers realize through experience that products bearing the same mark may be offered by different businesses with different standards, the information embodied in trademarks will be destroyed.¹¹⁹

¶58 There is no doubt that free-riding conduct is rife on internet auction sites like eBay, where counterfeit trademarks are used to sell products. Therefore, this is not a situation like the one that

¹¹⁰ Fara S. Sunderji, *Protecting Online Auction Sites from the Contributory Trademark Liability Storm: A Legislative Solution to the Tiffany Inc. v. eBay Inc. Problem*, 74 *FORDHAM L. REV.* 909, 917-18 (2005).

¹¹¹ Stacey L. Dogan & Mark A. Lemley, *Trademarks and Consumer Search Costs on the Internet*, 41 *HOUSTON L. REV.* 777, 786 (2004).

¹¹² *Id.* at 786-87.

¹¹³ *Id.*

¹¹⁴ Landes & Posner, *supra* note 24, at 270.

¹¹⁵ *Id.* at 269.

¹¹⁶ *Id.*; see also RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 4 cmt. A (1995) (policy of trademark law is to “protect[] and encourag[e] investments in good will,” and to protect purchasers’ ability “to distinguish among the goods and services of competing sellers.”).

¹¹⁷ Dogan & Lemley, *supra* note 111, at 787.

¹¹⁸ Landes & Posner, *supra* note 24, at 270; see also *Inwood Labs. v. Ives Labs.*, 456 U.S. 844, 854 n.14 (1982) (noting that infringement “subverts” goals of protecting “goodwill” and hurts consumers by “depriv[ing]” them of the “ability to distinguish among goods”).

¹¹⁹ *Id.*

may exist when, for example, search engines, advertising firms, and others use trademarks to “help competitors reach their audiences through nontraditional ‘uses’ of established marks.”¹²⁰ Such uses may well be consistent with the economic rationale of trademark law by reducing a consumer’s overall search costs.¹²¹ The relevant question, as the *Tiffany* court recognized, is: “[W]ho should bear the burden of policing” against confusing and economically inefficient uses of trademark owners’ brands?¹²²

¶59 To answer this question from an efficiency perspective, the cost of avoiding a harm should be borne by the party who can do so most cheaply—*i.e.*, the cheapest cost avoider.¹²³ In the context of counterfeit goods sold in online marketplaces, answering the question of who is the “cheapest cost avoider” is not straightforward.

¶60 There are significant arguments for why online marketplaces can bear the cost of combating infringement most cheaply. The marketplace has supervision and control over access to its service.¹²⁴ It arguably is in the best position, as *Tiffany* alleged in its complaint against eBay, to implement anti-infringement measures such as, for example, automated programs that will screen new listings for counterfeit goods as they are being posted and scan existing listings regularly for evidence of infringement.¹²⁵ eBay, for example, already employs a “fraud engine” that uses “rules and complex models that automatically search for activity that violates eBay policies.”¹²⁶ Furthermore, the online marketplace may have the best access to information that may reveal infringements. eBay’s “Verified Rights Owner (‘VeRO’) Program” allows mark owners to submit notices of infringing listings directly to eBay, while Yahoo! Auctions created a Neighborhood Watch Program that allows users to “review” and report questionable auctions.¹²⁷ This could suggest that the marketplace itself already serves as a centralized portal that receives notices of infringement from multiple sources.

¹²⁰ Dogan & Lemley, *supra* note 111, at 802.

¹²¹ *Id.* at 831 (“Holding search engines liable for giving consumers what they are looking for—content targeted in response to their queries—would be perverse in a legal system devoted to helping consumers conduct efficient searches.”).

¹²² *Tiffany (NJ) Inc. v. eBay, Inc.*, 576 F. Supp. 2d 463, 469 (S.D.N.Y. 2008).

¹²³ See generally Guido Calabresi, THE COSTS OF ACCIDENTS: A LEGAL AND ECONOMIC ANALYSIS, 131-198 (1960) (explaining the concept and discussing three guidelines for identifying the cheapest cost avoider); Robert Cooter & Thomas Ulen, LAW AND ECONOMICS 320-31 (4th ed. 2003) (discussing how a legal standard allocates the burden of precautions places the burden of harm on either the injurer or the victim, and that standard should be set to place the burden on the party who can avoid that cost most cheaply).

¹²⁴ Online marketplaces thus differ from the typical classified page, which, under appropriate circumstances, could avail itself of the safe harbor of 15 U.S.C. § 1114(2)(B). See *Tiffany*, 576 F. Supp. 2d at 507 n.33 (finding eBay to be an “online action house or flea market” and not an electronic “classified advertiser” entitled to 15 U.S.C. § 1114(2)(B) protection, despite the fact that eBay never physically takes possession of the goods); *but cf.* *Hendrickson v. eBay*, 165 F. Supp. 2d 1082, 1095 (C.D. Cal. 2001) (suggesting that eBay is entitled to protection under 15 U.S.C. § 1114(2)(B)). Section 1114(B)(2) provides that “[w]here the infringement or violation complained of is contained in or is part of paid advertising matter in a newspaper, magazine, or other similar periodical or in an electronic communication,” the remedy available against that advertiser in a Section 43(a) false designation of origin action is limited to an injunction against future publications of the infringing advertisement, provided the advertiser is an innocent infringer or innocent violator. Even if Section 1114(2)(B) applied to an online marketplace that exercises a significant degree of control, Section 1114(2)(B) makes clear that the safe harbor only applies to “innocent” infringers. Under the reasonably anticipate/reasonable precautions standard discussed *infra*, an online marketplace must be at least negligent in order for liability to attach, taking it outside the Section 1114(2)(B) safe harbor to the extent it applies. A traditional newspaper with actual or constructive knowledge of infringing transactions, similarly, would not be “innocent” and would be liable under the same reasoning. *Dial One of the Mid-South, Inc. v. BellSouth Telecomm., Inc.*, 269 F.3d 523, 527 (5th Cir. 2001) (holding that innocent infringement is determined based on a standard of “objective reasonableness”); *but see* *World Wrestling Fed’n, Inc. v. Posters, Inc.*, 2000 WL 1409831, at *3 (N.D. Ill. Sept. 20, 2000) (requiring actual knowledge or reckless disregard before infringement is considered not innocent).

¹²⁵ First Amended Complaint, *Tiffany (NJ) Inc. v. eBay Inc.*, No. 04 CV 4607, 2004 WL 1413904, at ¶ 35 (S.D.N.Y. Jul 14, 2004) (No. 04 CV 4607) (alleging that because “eBay asserts that it currently reviews all listings for goods that are offered through its website,” it is “able automatically to screen out and remove from its database all listings by sellers of five or more pieces of Tiffany jewelry”); see also Virginia Welch, Comment, *Contributory Trademark Infringement: Who Bears the Burden of Policing Online Counterfeiting Activity?*, 13 SMU SCI. & TECH. L. REV. 361, 372 (2010) (noting that “internet companies are more likely to be equipped with the necessary technology to implement antifraud programs”).

¹²⁶ *Tiffany (NJ) Inc. v. eBay, Inc.*, 600 F.3d 93, 98-99 (2d Cir. 2010), *cert denied*, 131 S. Ct. 647 (2010).

¹²⁷ TRADEMARKS AND UNFAIR COMPETITION COMM. OF THE N.Y.C. BAR ASS’N, ONLINE AUCTION SITES AND CONTRIBUTORY TRADEMARK LIABILITY 3 (2003), available at <http://www.abcny.org/pdf/report/Online%20Auction%20Sites%20Final%20Report.pdf> [hereinafter COMMITTEE REPORT]; see also *Tiffany*, 600 F.3d at 99 (VeRO is a “notice-and-takedown system allowing owners of intellectual property rights, including Tiffany, to report to eBay any listing offering potentially infringing items, so that eBay could remove such reported listings.”) (internal quotation marks omitted).

¶61 It therefore may be more costly for trademark owners to take such measures, because each mark owner would usually be capable of policing only their own brands, and hundreds or thousands of mark owners would replicate the same measures. If trademark owners find infringing items offered for sale on an online marketplace, they would have to contact the marketplace in an effort to get the infringing listings removed, or sue thousands of sellers individually in a piecemeal attempt to solve the problem.¹²⁸ Placing the responsibility of policing trademarks in the hands of a single enforcer who has control over the forum hosting the infringement is tempting based on these considerations, and may partly explain why this has been done in other jurisdictions outside the U.S.¹²⁹

¶62 Furthermore, as Tiffany itself suggested in its complaint against eBay, online marketplaces stand to profit from the sale of infringing goods through the charging of listing fees (which means they profit even from the mere offer to sell) as well as, in some cases, a percentage of the final sale price.¹³⁰ It could be argued that if the burden of trademark enforcement is not placed on online marketplaces, they would be “[w]ithout a financial reason to prevent counterfeiting.”¹³¹ By contrast, trademark owners have strong financial incentives to develop and maintain the goodwill associated with their brands.¹³²

¶63 The counterarguments that counsel for placing the burden on trademark owners do not lack in persuasive power, however. Trademark owners, as the designers or manufacturers of their goods, have particular expertise in the specific characteristics unique to their brands and are therefore arguably “in the best position to determine if a given listing infringes their rights.”¹³³ This includes not only familiarity with a brand’s distinguishing features and qualities, but also an understanding of which products in a brand line are particularly susceptible to counterfeiting or which products or ranges of products do not exist in the brand owner’s product line but have been specifically developed by counterfeiters.¹³⁴ A 2003 report of the Trademarks and Unfair Competition Committee of the New York City Bar Association on online auction sites and trademark infringement liability (“Committee Report”) observed that before an online marketplace’s employees could become experts in detecting counterfeits of various trademarked goods, they would require “special training” to learn these brand characteristics that a brand’s owners are already intimately familiar with.¹³⁵ Without this expertise, the report noted, online marketplaces may also be forced to require proof of trademark rights or authenticity before a listing can be posted, and such measures would detract from the “convenience and ease of the online marketplace.”¹³⁶

¶64 Moreover, if the legal standard forced online marketplaces to bear the extra costs associated with training employees or slowing down the listing process, it may result in “undue chilling of

¹²⁸ *Louis Vuitton S.A. v. Lee*, 875 F.2d 584, 588 (7th Cir. 1989); *cf.* *In re Aimster Copyright Litig.*, 334 F.3d 643, 645-46 (7th Cir. 2003) (recognizing that suing individual infringers would be futile).

¹²⁹ *See SA Louis Vuitton Malletier v. eBay Inc., & eBay Int’l A.G.*, Cour d’appel [CA] [regional court of appeal], Paris, Pole 5 – Div. 2, Docket No. 08/12820 (Sept. 3, 2010) (Fr.) (finding that eBay not merely a host, but instead actively assisted infringers by promoting sales and collecting commission; no showing of particularized knowledge necessary), *available at* http://www.juritel.com/Ldj_html-1533.html; *see also S.A. Christian Dior Couture v. eBay, Inc. & eBay Int’l A.G.*, Cour d’appel [CA] [regional court of appeal], Paris, Pole 5 – Div. 2, Docket No. 08/12821 (Sept. 3, 2010) (Fr.) (same), *available at* http://legalis.net/spip.php?page=jurisprudence-imprimer&id_article=2970; *eBay France v. Hermès Int’l*, Cour d’appel [CA] [regional court of appeal] Reims, 1ère, (July 20, 2010) (Fr.) (eBay liable because it suggests purchases based on visitors’ previous purchases and enables sellers to employ cross-merchandising), *available at* http://legalis.net/spip.php?page=jurisprudence-decision&id_article=2960; *Hermès Int’l v. eBay*, No. Tribunal de grande instance [T.G.I.] [ordinary court of original jurisdiction] Troyes, Civil Chamber, Docket No. 06/02604 (June 4, 2008) (Fr.), *translated at* <http://www.law.pace.edu/files/pilr/AllCasesTranslated.pdf>.

¹³⁰ First Amended Complaint, *Tiffany (NJ) Inc., v. eBay, Inc.*, 2004 WL 1413904 ¶ 35 (accusing eBay of neglecting trademark enforcement for its own “convenience and profit”).

¹³¹ Sunderji, *supra* note 110, at 938.

¹³² Dogan & Lemley, *supra* note 111, at 787 n.30.

¹³³ COMMITTEE REPORT, *supra* note 127, at 13; *see also* Sunderji, *supra* note 110, at 936 (recognizing that counterfeits based on the “unique characteristics of trademarked goods” is “a task better suited to those who actually make the goods”).

¹³⁴ Memorandum of Understanding between Internet Platforms and Rights Owners, European Commission (May 4, 2011), *available at* http://ec.europa.eu/internal_market/iprenforcement/docs/memorandum_04052011_en.pdf (recognizing the duty of brand owners to provide online marketplaces with such information).

¹³⁵ COMMITTEE REPORT, *supra* note 127, at 13.

¹³⁶ *Id.*

unquestionably legitimate behavior.”¹³⁷ Online marketplaces like eBay have made it significantly easier for consumers to locate and purchase authentic brand name items they seek. Although one source reported two million potentially counterfeit listings on eBay in 2007, this represented less than 0.86% percent of the 2.34 billion listings eBay hosted that year.¹³⁸ To continue operating, some online marketplaces may pass the increased costs on to consumers through heightened service fees, which would make the services less accessible to consumers. If these costs are sufficiently high, some online marketplaces “might need to stop selling trademarked goods” entirely.¹³⁹ Indeed, the Committee Report concluded that, in some cases, enforcement by the online marketplace could be so “expensive and impractical” that “smaller online auction sites, unable to afford the risks of infringement liability, may be forced out of business” altogether.¹⁴⁰ In other words, if the liability regime placed the costs of preventing trademark infringement solely on online marketplaces, consumers may be deprived of these forums for legitimate goods that have become fixtures of modern commerce.¹⁴¹ This has been called a “perverse” result that would undercut the role of trademarks to “help[] consumers conduct efficient searches” for goods they desire.¹⁴²

¶65 Further complicating this analysis of the competing considerations is the fact that even if particular measures can be taken more cheaply by one party in some circumstances it is unclear whether that will still be the case if other variables change. In addition, enforcing trademarks in online marketplaces is a complex effort that will involve many different measures, and the cheapest cost avoider for each measure may differ. This suggests, at the very least, that a bright line rule that rigidly places the burden on either online marketplaces or trademark owners would be inappropriate.¹⁴³ One commentator has noted that given the “valid arguments on both sides,” the focus should be on “burden-sharing rather than burden-shifting because it would be a much more efficient, genial, and definite way to prevent consumer fraud.”¹⁴⁴

¶66 Accordingly, a liability rule in this context should recognize that it is most efficient to allocate the burden of policing online marketplaces to both brand owners and online marketplaces. Both have a shared interest in ensuring legitimate transactions, and both are, in their own way, uniquely situated to avoid the costs of infringing and counterfeit goods in the most efficient manner. The cheapest cost avoiding principle is best furthered by a flexible rule that recognizes a joint burden. As the Ninth Circuit has observed, “[w]e must be acutely aware of excessive rigidity when applying the law in the Internet context; emerging technologies require a flexible approach.”¹⁴⁵ Similarly, the European Court of Justice has held that precautions demanded of online marketplaces must not only be “effective” but also “proportionate,” and “strike a fair balance between the various rights and interests” of the parties involved.¹⁴⁶

¶67 The common law principles discussed above are based on the bedrock concept of reasonableness under the circumstances. Properly applied, these principles contemplate precisely the paradigm of joint cooperation that best furthers trademark policies. With that in mind, an appropriate standard for contributory liability in the online marketplace should contain the following

¹³⁷ Dogan & Lemley, *supra* note 111, at 832.

¹³⁸ See Bragg, *supra* note 23, at 79; eBay Annual Report, 2007 (Form 10-K), at 51 (Feb. 28, 2008), available at <http://investor.ebayinc.com/annuals.cfm> (follow “2007 Annual Report / Form 10-K” hyperlink).

¹³⁹ Sunderji, *supra* note 110, at 939.

¹⁴⁰ COMMITTEE REPORT, *supra* note 127, at 13; see also Virginia Welch, *Contributory Trademark Infringement: Who Bears the Burden of Policing Online Counterfeiting Activity?*, 13 SMU SCI. & TECH. L. REV. 361, 372 (2010) (“[S]maller companies that are not able to afford the extensive policing efforts necessary to satisfy the court’s burden will be forced to close down.”).

¹⁴¹ Sunderji, *supra* note 110, at 913.

¹⁴² Dogan & Lemley, *supra* note 111, at 831.

¹⁴³ See Todd Evan Lerner, *Playing the Blame Game, Online: Who is Liable When Counterfeit Goods are Sold Through Online Auction Houses?*, 22 PACE INT’L L. REV. 241, 265 (2010) (noting that “the online counterfeiting problem is simply too massive to place responsibility solely on either the auction site or the brand owner, so the logical conclusion is to have them both share the responsibility of policing online auction houses”).

¹⁴⁴ Welch, *supra* note 140, at 372.

¹⁴⁵ *Brookfield Commc’ns Inc. v. West Coast Entm’t Corp.*, 174 F.3d 1036, 1054 (9th Cir. 1999).

¹⁴⁶ Case C-324/09, *L’Oreal SA v. eBay International AG*, 2011 E.C.R. I-____, ¶¶ 143-44.

features. First, it should provide for liability based on actual knowledge of infringing conduct by third parties, coupled with a failure by the online marketplace to remove the infringing listings. Such a test would cover the active inducement and actual knowledge standards recognized in *Ives*. Such a provision should also include an explicit recognition that actual knowledge may be satisfied with willful blindness, which has long been recognized as being equivalent to knowledge, even in trademark cases.¹⁴⁷

¶68 Second, the proper standard should provide for liability through constructive knowledge, which can be established where the online marketplace fails to take reasonable precautions in circumstances in which the infringing conduct can be reasonably anticipated. This prong is based on the common law standards embodied in the language of the *Restatement (Third) of Unfair Competition* § 27. As discussed in Part III, the “reasonably anticipated” language is based on the “has reason to know” standard in tort law. Thus, under this test, trademark-infringing activity can be “reasonably anticipated” when a reasonable marketplace operator under like circumstances would have reason to know of infringing third-party conduct. As discussed in Part III above, a consideration in determining whether infringing third-party activity can be “reasonably anticipated” is the prevalence of third-party infringing activity in the marketplace. As in *Snow Crest* and *Ives*, the plaintiff would bear the burden of demonstrating prevalence sufficient to trigger reasonable anticipation.

¶69 It should be emphasized that an online marketplace that can reasonably anticipate subsequent infringing activities by others “is required to take only those precautions that are reasonable under the circumstances.”¹⁴⁸ An online marketplace that has taken “reasonable precautions” would not be liable even if third parties continue to engage in infringing or counterfeit transactions.¹⁴⁹

¶70 A similar two-prong test providing for liability based either on actual knowledge or on constructive knowledge measured by a reasonableness standard has been adopted in the European Union. The European Court of Justice held that an online marketplace may be found liable where it has “actual knowledge of illegal activity” by its users and has not “acted expeditiously to remove or disable access to, the information.”¹⁵⁰ Under this prong, actual knowledge can be inferred where the online marketplace has “provided assistance” to third-party infringers (e.g., by “optimising the presentation of the offers for sale ... or promoting those offers”).¹⁵¹ Even if the online marketplace has no actual knowledge of infringing activity, it may nonetheless be held liable if it is “aware of facts or circumstances on the basis of which a diligent economic operator should have identified the illegality in question and acted.”¹⁵² Awareness of facts or circumstances that trigger this duty to act may arise from, for example, the online marketplace’s own investigation or notifications from brand owners or other users.¹⁵³

¶71 In addition to remaining consistent with common law traditions and cases such as *Snow Crest*, a standard featuring these two prongs would be flexible enough to advance the policy considerations discussed above. In particular, the “circumstances in which the counterfeiting or trademark infringing activity could be reasonably anticipated” will vary based on the practical and technological considerations that apply to a particular marketplace, and the corresponding “reasonable precautions” will also depend on the circumstances. In this way, the standard does not set a bright

¹⁴⁷ See, e.g., *Hard Rock Café Licensing Corp. v. Concession Servs., Inc.*, 955 F.2d 1143, 1149 (7th Cir. 1992) (“We have held that willful blindness is equivalent to actual knowledge for purposes of the Lanham Act.”); *Mattingly v. United States*, 924 F.2d 785, 792 (8th Cir. 1991) (finding, in a civil tax fraud case, that “the element of knowledge may be inferred from deliberate acts amounting to willful blindness to the existence of fact or acts constituting conscious purpose to avoid enlightenment”); *Gucci Am., Inc. v. Frontline Processing Corp.*, 721 F. Supp. 2d 228, 249 (S.D.N.Y. 2010) (noting that even under the Second Circuit’s decision in *Tiffany*, willful blindness is sufficient for a showing of actual knowledge).

¹⁴⁸ RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 8 cmt. C (1995).

¹⁴⁹ *Id.* (“An actor who has taken reasonable precautions is not subject to liability despite the fact that others continue [to infringe].”).

¹⁵⁰ Case C-324/09, *L’Oreal SA v. eBay International AG*, 2011 E.C.R. I-____, ¶¶ 119.

¹⁵¹ *Id.* ¶116.

¹⁵² *Id.* ¶120.

¹⁵³ *Id.* ¶121.

line rule that always places most of the burden on a particular party, but rather allows that burden to be properly shared. The standard does this by triggering a duty on the marketplace only to take precautions that are commensurate with the scope of the infringement problem.

¶72 For example, in the case of an online marketplace where virtually all Tiffany goods sold are counterfeit, the only “reasonable precaution” may be for the online marketplace to place a blanket prohibition on all Tiffany goods unless their authenticity is established. In such a case, the legal standard set out above would place most, if not all, of the burden to prevent infringement on the marketplace owners. In the words of *Snow Crest*, where “most” of the transactions infringe, the general knowledge of that prevalent activity triggers the reasonable precaution duty.¹⁵⁴

¶73 In other circumstances, where counterfeiting does not post as stark or obvious a risk, a more even sharing of the burden would be appropriate. For example, where many articles are non-infringing, it may make more sense (as *Snow Crest* recognizes) to require specific knowledge on the part of the online marketplace.¹⁵⁵ The “notice and take-down procedures”¹⁵⁶ employed by online marketplaces like eBay, therefore, may be a “reasonable precaution” that would counsel against liability where there are many perfectly legitimate transactions involving a particular brand. This recognizes that trademark owners, working cooperatively with online marketplace providers, are the most efficient cost avoider. Another example of this type of burden-sharing “reasonable precaution” would be online marketplaces providing space for trademark owners to publish a page educating buyers about their products with instructions on how to detect fakes.

¶74 At the same time, the standard must be flexible enough to evolve with changes in technology. For example, if new technologies provide ways to determine the authenticity of an item by reviewing a scan of a photograph of the item, that might impose a duty on the online marketplace to adopt such technologies. Such a standard might also provide an incentive for brand owners to invest in the development of such technologies, or to include secret markings on their goods to facilitate such scanning and identification of authenticity.

¶75 The central point is not that courts should develop a rigid checklist of what precautions are reasonable, but that an appropriate standard must allow for a fact-intensive inquiry that does not limit liability to the knowledge of specific instances of infringing conduct. The trier of fact must be able to consider whether, under all the circumstances, general knowledge of widespread infringing conduct is sufficient to impose a duty to take further reasonable measures. If circumstances triggering a duty to take reasonable precautions are found to exist, the marketplace owners may discharge their duty by taking anti-counterfeiting measures commensurate with the scope of the problem. These may include electronic measures to filter out new listings or identify existing listings that are offering infringing goods, or other systems for identifying, suspending, and banning infringing users by IP address. The European Court of Justice has also identified the suspension of third-party infringers and the use of measures that make it easier to identify an online marketplace’s customer-sellers as two examples of precautions that a court might, under appropriate circumstances, require an online marketplace to adopt.¹⁵⁷

¶76 Applying such a standard to the dispute between eBay and Tiffany, it would be up to a trier of fact to determine (1) whether 75% of Tiffany items sold on eBay in 2004 and 2005 were indeed counterfeit, as Tiffany argued;¹⁵⁸ (2) whether eBay knew of this fact; (3) whether this knowledge,

¹⁵⁴ *Coca-Cola Co. v. Snow Crest Beverages*, 64 F. Supp. 980, 990 (D. Mass. 1946).

¹⁵⁵ *Id.* at 990.

¹⁵⁶ A Memorandum of Understanding between major rights owners including Nike and Burberry and online marketplaces including eBay and Amazon, spearheaded by the European Commission, defines “notice and take-down procedures” as any procedure taken by an online marketplace that enables a brand owner to notify the marketplace of any allegedly infringing use of the marketplace, in order to allow the marketplace to take appropriate action. *See*, Memorandum of Understanding between Internet Platforms and Rights Owners, *supra* note 134, at ¶ 5. Recognizing the need for both the brand owner’s expertise and the marketplace’s action, the memorandum calls notice and take-down procedures “indispensable” in the fight against counterfeiting online. However, the nature of such measures, and whether they will be sufficient to avoid liability, should depend on the nature of the marketplace and the circumstances it faces.

¹⁵⁷ *Id.* ¶¶ 142-43.

¹⁵⁸ *Tiffany (NJ) Inc. v. eBay Inc.*, 600 F.3d 93, 97 (2d Cir. 2010).

though general, was sufficient to trigger “reasonable anticipation;” and (4) whether eBay’s precautions like its “fraud engine”¹⁵⁹ and VeRO Program,¹⁶⁰ constitute reasonable precautions in light of the totality of the circumstances. The standard should be flexible and should appropriately focus a trier of fact on these issues, not whether eBay had specific knowledge of particular infringing listings. Based on Judge Sullivan’s ruling, it appears that the court would have found that eBay was not contributory liable. Had the court applied this more nuanced, balanced standard, it would have created more efficient incentives, more fully supported the policies underlying trademark and tort law and promoted more equitable results in future cases.

¶77 Although the standard proposed in this paper is put forth specifically with the online marketplace in mind, it bears emphasis that the standard is derived from, and remains equally applicable to, the brick-and-mortar context. Indeed, the fact that the proposed standard has its origins in the common law emphasizes its implicit position that there is nothing unique about the Internet that justifies a different standard. In *Lockheed Martin Corp. v. Network Solutions, Inc.*, the court, after considering contributory trademark infringement in the flea market context, held that the application of the *Ives* standard does not turn on whether the service provider is online or in brick-and-mortar.¹⁶¹ Rather, “[d]irect control and monitoring of the instrumentality used by a third party to infringe the plaintiff’s mark permits the expansion of *Ives*’s ‘supplies a product’ requirement for contributory infringement” to a service provider.¹⁶² The district court in *Tiffany* applied the *Lockheed Martin* analysis and determined that “eBay exercises sufficient control and monitoring over its website such that it fits squarely within the *Fonovisa* and *Hard Rock Café* line of [flea market] cases,” and therefore the same standards should apply.¹⁶³

¶78 Certainly, online marketplaces differ in significant ways from brick-and-mortar ones. Courts considering contributory liability and reasonable precautions in an online context should consider those different facts. Reasonable precautions in the case of eBay may quite possibly be satisfied by its existing measures such as its fraud engine and VeRO program, whereas a reasonable precaution in the brick-and-mortar flea market context may involve the market owner walking up and down the aisles of the market looking for counterfeit goods. In addition, it is certainly possible that different business models within a single online marketplace system would cause courts to conclude that different reasonable precautions are necessary. This is no different from how the courts apply the common law standard differently in the brick-and-mortar context to a single retail location as compared with a multi-acre swap meet.

CONCLUSION

¶79 As e-commerce continues to explode and online marketplaces come to play a larger and more prominent role in global trade, the opportunities for trademark counterfeiters to leverage the Internet’s anonymity to free-ride off the goodwill of strong and reputable marks will also expand. The resulting erosion of the source-identifying capacity of trademarks will result in an increase in consumer search costs and economic harm to brand owners and to online marketplaces. The prevalence of counterfeiting and infringement will also diminish consumer confidence in online marketplaces as trustworthy alternatives to traditional brick-and-mortar markets.

¶80 The Second Circuit’s decision in *Tiffany*, by effectively reading the “reason to know” standard out of *Ives* and imposing a rigid “specific knowledge test,” robs the common law doctrine of its essential flexibility. The *Tiffany* rule effectively places the entire burden of trademark enforcement on the owners of marks and will under-deter the incident of trademark infringement and counterfeiting.

¹⁵⁹ *Id.* at 98-99.

¹⁶⁰ *Id.*

¹⁶¹ *Lockheed Martin Corp. v. Network Solutions, Inc.*, 194 F.3d 980, 984 (9th Cir. 1999).

¹⁶² *Id.*

¹⁶³ *Tiffany (NJ) v. eBay*, 576 F. Supp. 2d 463, 506 (S.D.N.Y. 2008).

¶81

An appropriate legal standard should recognize that generalized knowledge is, as it always has been, probative of whether the online marketplace has “reason to know” of the direct infringement and therefore may have a duty to the brand owner to take reasonable precautions. Whether this duty is triggered, as *Snow Crest* recognizes, is a fact-sensitive inquiry that, at bottom, depends on how prevalent the underlying tortious activity is. This kind of standard acknowledges that both online marketplaces and trademark owners have a role to play in the protection of trademark rights online. Recognizing this type of standard would restore uniformity to this “ill-defined” area of law and provide clear guidance to brand owners and online marketplaces alike to ensure the legitimacy of transactions in this increasingly vital sector of the national and global economy.