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## Portolano Cavallo Studio Legale

### Italy: Can Luxury Companies Successfully Oppose Sales In Discount Stores?

16 June 2009

Article by Antonella Barbieri and Davide Ajello

What happens when a licensee sells goods to a discount store in disregard of a provision in the licensing agreement?

A balance must be struck between:

- the legitimate interest of the proprietor of the trade mark covered by the licensing agreement in being protected against a discount store which does not form part of the selective distribution network and that uses the trade mark in a manner which could damage the reputation of that mark; and
- the legitimate interest of the discount store in being able to resell the goods in question by using methods which are customary in its sector of trade.

In a recent case (C-59/08) the European Court of Justice (ECJ) pronounced on the extent of protection available to luxury trade marks.

#### Facts

The famous fashion house Christian Dior Couture SA (Dior) and Société Industrielle Lingerie (SIL) were parties to a trade mark licensing agreement for the manufacture and distribution of luxury corsetry goods (the Products).

The agreement stated that:

*"in order to maintain the reputation and prestige of the trade mark [Dior], the licensee agrees not to sell to wholesalers, buyers' collectives, discount stores, mail order companies, door-to-door sales companies or companies selling within private houses without prior written agreement from the licensor, and must make all necessary provision to ensure that that rule is complied with by its distributors or retailers".*

SIL ran into financial difficulties and asked Dior for permission to sell the Products outside Dior's selective distribution network. Dior expressly refused. Despite that refusal and in breach of its contractual obligations, SIL sold the Products to Copad SA (Copad), a company operating in the discount store business. Dior sued SIL and Copad for infringement before the French courts.

The defendants argued that:

- the sale of the Products outside the selective distribution channels did not fall within the scope of the French national provisions on trade mark law that transpose Article 8(2) of EU Directive 89/104/EEC (the Directive); and
- those sales implied exhaustion of Dior's trade mark rights for the purposes of the national legislation transposing Article 7(1) of the Directive.

Following the first and second instance judgments, the *Cour d'appel de Paris* ruled that SIL and Copad had not committed an infringement under the provisions transposing Article 8(2), but that the sales did not imply exhaustion of Dior's trade mark rights for the purposes of the legislation transposing Article 7(1).

Copad appealed to the *Cour de cassation*, insisting that the rights to the Dior trade mark were exhausted as a result of SIL having put the goods at issue on the market.

Dior brought a cross-appeal, alleging that the *Cour d'appel de Paris* had erred in ruling out infringement by SIL and Copad.

#### Provisions of the Directive

The main provisions of the Directive at issue in this case were Articles 7(1), 7(2), 8(1) and 8(2), which read as follows:

*"7(1) The trade mark shall not entitle the proprietor to prohibit [the trade mark's] use in relation to goods which have been put on the market in the European Economic Area (EEA) under that trade mark by the proprietor or with his consent.*

*(2) Paragraph 1 shall not apply where there are legitimate reasons for the proprietor to oppose further commercialisation of the goods, especially where the condition of the goods is changed or impaired after they have been put on the market."*

*"8(1) A trade mark may be licensed for some or all of the goods or services for which it is registered and for all or part of the*

member state concerned. A licence may be exclusive or non-exclusive.

(2) The proprietor of a trade mark may invoke the rights conferred by that trade mark against a licensee who contravenes any provision in [its] licensing contract with regard to [the contract's] duration, the form covered by the registration in which the trade mark may be used, the scope of the goods or services for which the licence is granted, the territory in which the trade mark may be affixed or the quality of the goods manufactured or... services provided by the licensee."

The French *Cour de cassation* referred three questions to the ECJ for a preliminary ruling:

- Must Article 8(2) be interpreted as meaning that the proprietor of a trade mark can invoke the rights conferred by that trade mark against a licensee which contravenes a provision in the licence agreement prohibiting sales to discount stores on the grounds of the trade mark's prestige?
- Must Article 7(1) be interpreted as meaning that a licensee who puts goods bearing a trade mark on the market in the European Economic Area, in disregard of a provision of the licence agreement prohibiting sales to discount stores on the grounds of the trade mark's prestige, does so without the consent of the trade mark proprietor?
- If not, can the proprietor invoke such a provision to oppose further commercialisation of the goods on the basis of Article 7(2)?

### ECJ Ruling

#### First question

The first question concerns, in essence, whether a provision in a licence agreement prohibiting the licensee to sell to discount stores the goods bearing the trade mark covered by the contract on grounds of the trade mark's prestige falls within the scope of Article 8(2).

In order to answer this question, the ECJ's preliminary examination considered whether the list of provisions in Article 8(2) is exhaustive or merely provides guidance. The ECJ concluded that the "provision of Article 8(2) contains no adverb, or expressions such as 'especially' or 'in particular', that would allow for a finding that the list simply provides guidance".

Therefore, contrary to Dior's claim, the ECJ held that the wording of Article 8(2) shows the list to be exhaustive.

After this clarification, the ECJ stated that the violation of a clause in a trade mark licence agreement for luxury goods which provides that in order to safeguard and ensure the repute and prestige of the brand, the licensee undertakes to not sell certain products to wholesalers and discount stores could nevertheless fall within the provision of Article 8(2) to the extent that its infringement could affect the quality of the trade mark.

Previous case law<sup>1</sup> has established that:

*"The essential function of the trade mark is to guarantee the identity of origin of marked goods or services to the consumer or end user by enabling him, without any possibility of confusion, to distinguish the goods or services from others which have another origin."*

For the trade mark to be able to fulfil this essential role, it must guarantee that all goods or services bearing it have been manufactured or supplied under the control of a single undertaking which is responsible for their quality.

In the *Dior Case* the essential qualities guaranteed by the trade mark, as it relates to luxury and exclusive goods, concern not only material characteristics, but also the allure and prestigious image which bestows an aura of luxury<sup>2</sup> on such goods.

Since Dior goods are high-end luxury goods, the aura of luxury associated with them is essential because it enables consumers to distinguish them from similar goods.

In this respect, the ECJ stated that "an impairment to that aura of luxury is likely to affect the actual quality of those goods" and that the sale of luxury goods by the licensee to third parties which were not part of the selective distribution network might affect the quality of the goods.

Thus, a contractual provision expressly prohibiting such sales because they imply that an impairment of the trade mark quality must be considered to fall within the scope of Article 8(2), giving the trade mark proprietor the right to invoke the rights granted to it by Article 8(2).

Therefore, the ECJ's answer to the first question is that Article 8(2) must be interpreted to mean that the proprietor of a trade mark can invoke the rights conferred by that trade mark against a licensee which contravenes a provision in a licence agreement prohibiting sales to discount stores on grounds of the trade mark's prestige, provided that it has been established that such a violation "damages the allure and prestige which bestows on [the goods] an aura of luxury".

#### Second question

The second question seeks to specify the circumstances in which a licensee that puts goods bearing a trade mark on the market in contravention of a provision in a licence agreement prohibiting the sale of goods bearing that trade mark to discount stores must be considered to have done so without the consent of the proprietor for the purposes of Article 7(1).

Copad submitted that the consent of the proprietor can be deemed not to have been given only if the contravention occurs in respect of one of the provisions in a licence agreement listed in Article 8(2).

Dior considered that any contravention of the licence agreement by the licensee precludes exhaustion of the rights conferred by a trade mark on its proprietor.

According to the ECJ, where a licensee puts goods bearing the trade mark on the market, it must, as a rule, be considered to be doing so with the consent of the proprietor of the trade mark for the purposes of Article 7(1),<sup>3</sup> considering the provision that "exhaustion of that exclusive right occurs when the goods are put on the market by a person with economic links to the proprietor" and that "[t]his is particularly the case where that person is a licensee".

It follows that in such circumstances the proprietor of the trade mark cannot plead that the contract was wrongly implemented in order to invoke, in respect of the licensee, the rights conferred on it by the trade mark. Nonetheless, and contrary to Copad's submission, the licence agreement does not constitute absolute and unconditional consent on the part of the trade mark proprietor to the licensee putting goods on the market that bear the trade mark.

Article 8(2) expressly allows the proprietor to invoke the rights that the trade mark confers on it against a licensee where the latter contravenes certain provisions in the licence agreement, enabling the licensor to control the quality of the licensee's goods through specific requirements with which the licensee undertakes to comply. Therefore, the licensee's contravention of such a clause precludes exhaustion of the rights conferred by the trade mark on its proprietor for the purposes of Article 7(1).

The ECJ stated that Article 7(1) should be interpreted as meaning that a licensee that puts goods bearing a trade mark on the market in disregard of a provision in a licence agreement does so without the consent of the trade mark proprietor if it can be established that the provision in question is listed in Article 8(2).

### Third question

In its third question the referring French Court asked whether, in the event that a licensee puts luxury goods on the market in contravention of a clause in a licence agreement and is deemed to have done so with the consent of the proprietor, the proprietor can nevertheless rely on the clause in a licence agreement to oppose further commercialisation of the goods on the basis of Article 7(2).

Dior submitted that the sale of goods bearing the CHRISTIAN DIOR trade mark to a discount store outside the exclusive distribution network constituted damage to the trade mark's reputation that justified the application of Article 7(2). Copad claimed that the sale of such goods to discount stores did not damage the trade mark's reputation.

According to previous ECJ practice, the damage done to the reputation of a trade mark may, in principle, be a legitimate reason (within the meaning of Article 7(2)) to allow the proprietor to oppose further commercialisation of luxury goods which have been put on the market in the EEA by it or with its consent.<sup>4</sup> The ECJ ruled that where a licensee puts luxury goods on the market in contravention of a provision in the licence agreement, but must nevertheless be considered to have done so with the consent of the proprietor of the trade mark, the proprietor can rely on a contractual clause to oppose the resale of those goods on the basis of Article 7(2), provided that it can show - in the specific circumstances of the case - that such resale damages the reputation of the trade mark.

In this respect, the ECJ indicates the importance of considering factors such as:

- the nature of the luxury goods bearing the trade mark;
- the volumes sold;
- whether the licensee sells the goods to discount stores outside the selective distribution network regularly or only occasionally;
- the nature of the goods normally marketed by such discount stores; and
- the marketing methods normally used in that sector of activity.

### Comment

Case C-59/08 confirms that in order both to prevent unwanted commercial behaviour by licensees and to be successful in the event of disputes, luxury companies wishing to maintain the value of their trade marks must draft detailed and specific contractual clauses, while stressing that such specific provisions are expressly intended to prevent the trade mark's loss of quality and dilution of value.

### Footnote

1. See, for example, *Hoffmann-La Roche*, C-102/77; *Philips*, C-299/99 and *Gillette Company and Gillette Group Finland*, C-228/03.

2. See *Parfums Christian Dior*, C-337/95.

3. See, for example, *Zino Davidoff and Levi Strauss*, C-416/99; *Van Doren + Q*, C-244/00; *Peak Holding*, C-16/03; and *IHT Internationale Heiztechnik and Danzinger*, C-9/93.

4. See, for example, *BMW*, C-63/97.

*The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.*

Specific Questions relating to this article should be addressed directly to the author.