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## **Trademark Rights at a Discount - Is Trademark Law Still Effective?**

The two decisions of the Federal Supreme Court Chanel No. 5 and Camel Tours reprinted *infra* in this issue, 1) together with a couple of others in recent years, may come as a surprise to those who regarded Germany as a country where the enforcement of industrial property rights has a good chance of success. One had assumed that the principle is still valid that trademark proprietors need not tolerate the use of their marks where such use endangers future enforcement or at least limits the uniqueness and thus the protective scope of the mark.

The result of the two decisions, where in both cases owners of famous or at least well-known trademarks were dismissed with their claims, could certainly not have been predicted on the basis of prevailing case law in Germany. And even if one tries to understand the reasoning of the Court in these two cases, a deep uncertainty remains whether it will still be possible in the future to defend effectively valuable marks and trade names if the present trend remains.

1) In the Camel Tours decision the two lower instances had issued injunctions in favor of the owner of the cigarette mark "Camel" on the basis of well-established case law that famous trademarks enjoy protection also for products and services which are not similar or related to the protected goods. As we may see later, perhaps the lower instances granted too much protection which might therefore have caused the Supreme Court to interfere.

a) The Supreme Court does not question that "Camel" is a well-known mark and therefore normally entitled to broad protection in Germany. However such protection should not be granted automatically and against any use by third parties if the proprietor cannot demonstrate that by that use damage might occur to his mark. The argument which the Court of Appeals had used in its reasoning, namely that consumers "associate" the third party's use with the famous mark, is not considered sufficient.

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Even without knowing details of plaintiff's assertions in this respect and in spite of the legal restrictions for cigarette manufacturers in regard to advertising, it is nevertheless general knowledge of a vast majority of consumers that the typical advertisement of "Camel" maintains that it is worthwhile walking miles for this cigarette. Thus "making tours" is at least very closely associated with this mark and the licensing of "Camel" to a tour organizer would not come as a surprise. In fact, this is what the trademark proprietor actually did. If now a third party - here a tour organizer from Turkey doing business in Germany - uses the mark for the same services, whether prior to the authorized licensee or not, one assumes that he has authorization from the trademark owner as well. Furthermore, the activities of such third-party user would certainly diminish the business of the authorized licensee.

Such factual circumstances were sufficient in the past to enjoin the use of famous marks for non-similar products 2) for the sole reason that licensing by the trademark owner would be affected or simply that the third party would have saved expenses by introducing his own product on the market through the use of an already existing and well-accepted mark. In view of the requirements of protection for a well-known mark in the Dimple decision, 3) it is difficult to see how the Supreme Court could have dismissed the claim had the Court of Appeals based its decision on Sec. 1 of the Act Against Unfair Competition as in the Dimple case, instead of applying the more general rules developed for famous marks, according to Sec. 823 Civil Code. 4)

b) But another point is more surprising and even disappointing; namely that the Supreme Court accepted the explanation of the defendant that he had used "Camel" as a descriptive term for the kind of tours he was offering in Turkey. The Supreme Court appears to believe in the good faith of defendants in cases where normal business men would have been suspicious on the basis of the circumstances of the case. The assumption that the tour organizer had chosen a "typical animal from his home country" is certainly a good story from "1001 Nights" but difficult to believe in real life. First of all, I did not find one camel excursion offered in travel agent brochures for Turkey, while there are of course many in the countries of North Africa. Presumably Germany has more camels (in the zoos) than Turkey (in the streets). Also, why did the defendant use an English word if he was offering "Kamel-Touren" to German customers? This author is therefore inclined to believe that the defendant chose "Camel Tours" intentionally, thereby using the image of a hiker with a sense of adventure.

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Besides that, even if the designation in question as used by a defendant is descriptive, it constitutes an infringement according to well-established case law if it is used "as a mark" and not in a descriptive way ("We offer camel c) There remains one point which might in fact be the main reason why the Supreme Court hesitated to affirm potential damage for the "Camel" trademark. It points out in the decision that the endangering of a famous mark can practically be excluded should the activities of the alleged infringer be so unimportant that in fact nobody realizes the use on the market. The defendant had neither a subsidiary nor an establishment in Germany. His contacts were made through travel agents only, and in principle he organized group tours for altogether circa 10,000 customers per year. Therefore the general public has never been aware of his activities. In view of the fact that service companies have generally a rather limited appearance in public anyway which is especially true for a foreign company, according to the Federal Supreme Court the plaintiff lacks legal interest in enjoining this particular use.

Although this argument could be regarded as the most convincing one, 5) there are slight reservations about continuing future use by an unauthorized party. Under German law, if business activities, even of very limited scope can be proven by a foreign company, this company enjoys protection for its firm name right from the beginning. 6) If, therefore, the "infringer" is the first on the market, even with very limited activities, and "Camel" licensed a third company in the travel branch afterwards or if the trademark owner itself starts such a business in Germany, the defendant, based on its own activities, can enjoin the original trademark owner from doing business in this field, in spite of its very limited business activities there. And in fact, the defendant in this case had raised a counterclaim against the plaintiffs based on these very allegations. This part of the case was remanded to the Court of Appeals for further decision. Can one really hold that the defendant's activities as such were insufficient to constitute an infringement, and at the same time conclude that he was successful in acquiring a non-registered prior "common law right" for his trade name? Even for a non-smoker such a result is unacceptable! 7)

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2) The second decision, Chanel No. 5, is in many respects even more surprising. Its facts can be summarized in a few sentences.

A discount store had purchased and sold luxury perfume (Chanel No. 5) at bargain prices which did not come through the manufacturer's normal trade channels. The store had not been appointed an authorized dealer by the manufacturer, and thus was violating the latter's selective distribution system. When attacked by the trademark proprietor, it turned out to be not a case of dealing in gray-market goods but of perfume that was a cheap copy of the original product.

The Supreme Court confirmed the injunction but refused full compensation (which would have been due in a case of violation of a selective distribution system), and only granted a

moderate license fee because it accepted the defense of good faith with respect to the falsification.

Since it is at least surprising that a store offering counterfeit products of famous makes should be treated more favorably than somebody offering genuine goods as an outsider of a selective distribution system, a closer examination of the reasoning of the Court is of interest.

a) From the established facts of the case, the Supreme Court was convinced that the discount store had purchased the copy of the Chanel No. 5 from a dealer who was known to him as a reliable and "normal" source of merchandise. That the price was considerably cheap (20% below the normal dealer price) and the store of the supplier amounted to only 30 sq. m., according to the court should not have been a reason to suspect that the goods were not genuine.

Plaintiff had alleged that in the case of original goods whose packages no longer bear the usual identification number, defendant would nevertheless have committed a violation of Sec. 1 of the Act Against Unfair Competition, since the goods which normally are distributed through a selective distribution system could only have been obtained through breach of contractual obligations of unfaithful dealers. Such a situation is regarded by the courts as contrary to honest trade practices and gives rise to an injunction and damages. 8) According to the plaintiff, the defendant could therefore be regarded as having acted in bad faith, at least in regard to this fact pattern. If one assumes that it was in fact impossible to recognize the fraudulent character of the perfume, the defendant still could not ignore circumstances proving the

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product's dubious origin. He should have known that, according to prevailing case law, the removal of the identification number used by the manufacturer to control his selective distribution network violates Sec. 1 of the Act Against Unfair Competition.

the Supreme Court, however, came to a simple and therefore most surprising conclusion: Since the case law on selective distribution concerns the unauthorized sale of genuine goods, and the defendant had offered copies there can be no dealer's breach of contract and the defendant cannot have taken advantage of such breach of contract! Therefore, it is not an act of unfair competition. 9) However, since good faith must be assumed with respect to the fraudulent character, the defendant is not liable for damages at all, since a claim for damages requires fault, which means at least negligence. The reasoning of the Court as to the last point is certainly correct. However, since the Court knew that the defendant was aware of committing an act of unfair competition, albeit a different kind, its denial of the existence of an unfair advantage with respect to authorized dealers, seems not to be totally satisfactory. In view of the fact that offering this perfume, had it been a genuine product, would have created market confusion and would have given the defendant an unfair advantage over the faithful dealers, reasons which are normally used to justify claims against an outsider, the Court could have concluded that these very same facts also are present - and even more so in the case of copied products. Is there not even more confusion on the market if the product is offered by a non-authorized dealer and at a cheaper price and in addition is a falsification?

b) Those familiar with German law would expect that if damages are excluded the Court would at least grant a generous claim for unjust enrichment under Sec. 812 of the Civil Code which is the fall-back provision in case of unintentional infringement of industrial property rights.

The fundamental decision in this context in a utility model case was issued by the Patent Chamber of the Federal Supreme Court in 1976. 10) The principles laid down there were very favorable to the proprietors of industrial property rights who could use the instrument of unjust enrichment not only in the case of impossibility of proving fault of the infringer, but also in cases where the period of limitation for patent and trademark infringement (3 years) had expired, since the claim for unjust enrichment has a period of limitation of

30 years. If one considers the wording of that decision, it is indeed not surprising that in the present case the plaintiff was optimistic as to the amount of compensation he would be entitled to claim. The Supreme Court held in the Plastic Hollow Section decision as follows:

It is incompatible with law and equity that the infringer should with impunity

retain what he has gained by an unlawful act of infringement. The Patent and Utility Model Acts confer the commercial use solely upon the proprietor of the industrial property right. Anyone who uses an industrial property right, without the consent of its proprietor, commits an illicit act and is obliged to refund the enrichment gained by the infringing act under Secs. 812 et seq.

The profit gained by the infringer was exactly what the plaintiff in the present case was asking for. The First Chamber of the Federal Supreme Court, competent for unfair competition and trademark matters, perhaps impressed by its own "good faith arguments" with respect to the counterfeit issue, comes to another surprising conclusion. The Court went back to the eighty-year old theories of what "enrichment" really means in the sense of Sec. 812 Civil Code, and repeats the usual formula that the defendant must give back what he has "received." For the straightforward thinking plaintiff that was exactly what he expected. However, for the Supreme Court, "received" should not be understood as the money gained in the transaction but "received" is the use of the trademark. Since this use cannot be given back to the trademark proprietor, as the Court correctly explains, the defendant must reimburse the value of such use. And while one could at this point argue again that this value is represented by the defendant's profit, the Court makes the case again more surprising by indicating that the normal value of a trademark is what a licensee would pay for it, i. e. a reasonable and usual royalty. And although the Court, which was only asked to give a declaratory judgment in this respect, did not expressly indicate the percentage, it referred to former case law according to which a trademark royalty amounts to 2% maximum of the turnover of the defendant if claimed against an infringer.

From the facts of the decision the neutral observer can now calculate: The defendant's sales price of the perfume was DM 80 per bottle, so that the royalty amounts to DM 1.60. Since the defendant had also indicated what he had paid for the bottle, namely DM 56.38, he leaves the courtroom with a profit of DM 22 per bottle, whereas the trademark proprietor is left with DM 1.60.

c) Unfortunately it cannot be expected that this decision will remain unnoticed by professional counterfeiters who arrived at turnovers of \$ 70 billion last year, according to a recent newspaper article. 11) With respect to the

perfume dealt with in the present case, Chanel No. 5, the article referred to losses of 10% of its turnover due to counterfeits. Other trademarked goods lose up to 40%.

It should therefore be examined briefly as to whether the legal basis, namely the doctrine of unjust enrichment, did not give the Court an alternative. For a neutral observer there would have been a number of conclusive arguments for a more favorable outcome. The Court could first of all have concluded that in particular with respect to such luxury products as perfume, the use value of a trademark depends nearly 100% on the trademark and not on any sales efforts of the dealer. No one, including the defendant in the present case, would have contradicted the fact that a "no name" perfume would have been sold at not even 10% of the price of the counterfeit. A royalty rate of normal trademark license contracts is therefore far from reality. Who, by the way, as an owner of a famous trademark, would be willing to grant a license to a counterfeiter in the first place? An unrealistic idea! The "objective value" which the Court wants to take as an estimate basis is therefore not a royalty of 2% which a licensee might be

willing to pay under usual circumstances for the sale of commodities where neither prestige nor notoriety on the market nor exclusiveness is an issue.

In fact, any perfume producer, not only someone selling counterfeit products, would be willing to pay much, much more for the authorization to use "Chanel No. 5" for one of his products. If therefore the Supreme Court wants to make a distinction between the profit gained by the sale of the product (which allegedly belongs to the defendant) and the profit gained from the use of the mark (which is due to the trademark proprietor) it should have come to the opposite conclusion: profit for a "no-name" counterfeit perfume: 0%; profit due to the use of "Chanel No. 5": 100%.

The Supreme Court seems to overlook the fact that former decisions had granted at least an additional damage claim in cases where the use of the trademark went beyond a normal license situation and constituted damaging confusion on the market. 12) Since one cannot deny that the sale of a counterfeit luxury product constitutes a typical case of damaging use, the Court should either have increased the royalty to the actual value of the trademark or it should have granted additional damages based on the former decisions cited.

Trademark proprietors and practitioners are puzzled by these decisions, and trademark counterfeiters will see enormous chances in growing markets which are already flooded with counterfeit goods. If such low standards of negligence are applied and no substantial damages awarded, the chances to cut down counterfeiting in practice prove to be illusory. Of course, the same supplier cannot come to the same dealer with the same cheap Chanel No. 5 perfume for a second time. However, there are many suppliers and many more dealers, and many more trademarks - "and the cheat goes on! "

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1) See this issue, Chanel No. 5, at 688 and Camel Tours at 695

2) See Federal Supreme Court decision, GRUR 1966 623 -Kupferberg, with comment by BEIER.

3) See Federal Supreme Court decision, 17 IIC 271 (1986) - Dimple.

4) See the presentation of German case law by SCHRICKER. 11 IIC 166 et seq. (1980).

5) See, however, BEIER. GRUR 1966 627, who correctly points out that protection against further dilution should be the primary goal because the advertising power of the famous mark is at stake.

6) See Federal Supreme Court decision, 11 IIC 526 (1980) - Concordia.

7) See also the criticism concerning this decision by OLESH. 1988 WRP 347, who points out that the former principle of protection for famous trademarks is practically dead.

8) For the most recent decisions, see Hamburg Court of Appeals, GRUR 1987 387- Davidoff-Kosmetika; Frankfurt Court of Appeals, GRUR 1987 642 -Kodierung; contra, Karlsruhe Court of Appeals, GRUR 1988 463 - Lancôme.

9) KNAAK, this issue, at 581, with reference to SCHRICKER, 1987 EWir 723, seems to share this view. Whether he also agrees with the Supreme Court outcome concerning the amount of damages remains unclear.

10) See 9 IIC 156 (1978) - Plastic Hollow Section.

11) See also the article by KNAAK with respect to international efforts against counterfeiting.

12) See 44 BGHZ 372, 383 - Meßmer Tee.