



## Don't Let Your Company's Blue Skies Turn Gray: 5 Steps to Protect Your Trademark Rights and Combat Gray Market Sales

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Gray market goods can pose a significant threat to a U.S. company's reputation, customer goodwill, revenues, and, ultimately, profits. The risk is particularly acute for brand owners who sell high-end products, such as industrial and commercial machinery, cars, consumer electronics, jewelry, perfume, and designer clothing. For these and other companies, an awareness of gray goods issues and the best strategies to combat unauthorized resellers is critical to preserving their brand strength and bottom-line.

Unlike stolen or counterfeit (black market) goods, gray market goods are genuine trademarked or brand name products that a manufacturer legally sold abroad through its normal distribution channels, in markets where prices are lower than in the United States. Although these products are not intended for sale or distribution in the United States, the trademarked goods are then imported into the country and resold to U.S. customers at a significant discount relative to competing manufacturer-authorized goods. While U.S. consumers may benefit from initial cost savings, gray goods are usually sold without any original manufacturer warranties. They also may have been built with different specifications and materials, fail to comply with U.S. regulatory standards, be ineligible for service or other support from the original manufacturer, or have other material differences from the U.S.-authorized version of the product. The potential adverse impact of gray goods – both on consumers and manufacturers – is therefore very real. Gray markets threaten to cut into sales of the genuine U.S. version, reduce revenues and profits, damage consumer perceptions of the manufacturer's brand, create confusion in the marketplace, and undermine the manufacturer's relationships with authorized distributors who play by the rules. A manufacturer's losses and reputational harm can be considerable.

The key for a company to avoid or at least significantly mitigate the effect of gray market profiteers is to develop and rigorously implement a strategic plan to police the market for its products and deter unauthorized sales. In this article, we identify five (5) steps that a manufacturer can take to combat gray market sales.

### **Step 1 – Perfect Your Trademark Rights**

Gray goods present a unique challenge. The importation of gray goods and re-sale to U.S. consumers is generally lawful unless, as discussed under Step 2 below, the goods bear a valid and enforceable trademark or brand name, are materially different from the U.S.-authorized version, and such differences are likely to cause consumer confusion regarding, for example, the origin or nature of the products. Thus, for brand owners, the first and most essential step to preventing or limiting the flow of gray market goods is to register their key marks with the U.S. Patent and Trademark Office, or the PTO. Indeed, generally speaking, all of the tools available to a manufacturer to address unauthorized sales of its products that are discussed in this article, including a federal lawsuit under the Lanham Act seeking injunctive relief barring importation of unauthorized goods and an application to U.S. Customs and Border Protection to exclude such goods, are dependent on the existence of a valid and enforceable trademark.

### **Step 2 – Create a Legal Foundation for Enforcement**

A brand owner's legal remedies to stop gray market sales are limited by what is referred to as the "first sale doctrine," which immunizes unauthorized resellers from liability under the Lanham Act for trademark infringement and unfair competition when the gray goods are identical to the authorized U.S. products. Resellers are not immune, however, when they offer foreign-sold goods that are materially different than those sold by the trademark holder in the United States.

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The threshold of materiality is very low – i.e., any difference consumers consider relevant to a decision about whether to purchase a product. Accordingly, a key strategy for a manufacturer to prevent or reduce the importation of gray market goods is to build-in material differences between the products the company offers in different geographic markets, by, for example, introducing differences in:

Appearance of product/packaging	Physical composition of product	Labeling
Product guarantees, warranties, or return policies	Product instructions, manuals, or literature, particularly if written in a non-English language in relevant markets	Service commitments (e.g., repair options, technical trouble-shooting by phone/online)
Add-ons and bonus features	Rebates, reward programs, loyalty programs, or other promotions	Quality control policies and procedures that are different as to products authorized for sale in US and foreign markets

Even if some of these differences may at first seem trivial, they may open up a brand owner's legal options to take the fight to unauthorized resellers, protect its reputation/goodwill, and ensure that its revenues and profits are not undermined by unauthorized gray sales.

### **Step 3 – Compile Information About Resellers and Sources of Gray Goods**

To stop unauthorized resellers, an important step is to uncover their identities. In today's interconnected world, gray market goods are often sold to U.S. consumers through online marketplaces, such as Amazon and eBay. A central component of an effective anti-gray market goods strategy must focus on active, ongoing monitoring of these channels, potentially using an automated software solution that ranks unauthorized sellers. At a minimum, a manufacturer should compile e-contact information for unauthorized sellers, such as Amazon seller account name or storefront. Depending on their level of gray market activity and whether they are non-compliant with initial electronic cease-and-desist letters, a deeper investigation of select resellers may be merited to learn their true identities, locations/addresses, and other information, which may assist with enforcement efforts.

Once offending resellers have been identified, a manufacturer should conduct test buys of infringing products from unauthorized resellers. The purpose of test buys is to assist the brand owner in identifying the ways in which the infringing product differs from the US-authorized product, which, as discussed above, is critical to overcoming the general legal immunity of resellers. Also, if the manufacturer has applied SKUs, serial numbers, or other tags that allow it to trace its products, the company may be able to better identify leaks in its distribution channels and terminate or re-train problem distributors.

### **Step 4 – Strengthen Control Over and Monitoring of Distribution Channels**

Gray markets goods often result from leaks from a manufacturer's authorized distribution channels in foreign markets. By taking action to plug those leaks, the manufacturer may reduce the volume of gray goods imported into the United States and sold to U.S. consumers. A manufacturer has several options to strengthen its control over its distribution network abroad to deter and prevent leaks to the gray market. For example, a manufacturer might consider terminating distribution agreements with problem distributors, limiting the number of authorized distributors, enlisting an online marketplace reseller to assist with channel management, ensuring audit rights are included in distribution contracts, revisiting distribution agreements to generally strengthen weak language, enhancing vetting of distributors to limit product leakage, and tracing sales volumes.

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## **Step 5 – Implement Enforcement Strategies As to Unauthorized Resellers**

The reality is that many gray market resellers offer a wide-variety of products on online marketplaces. If a brand owner makes an unauthorized reseller's life difficult by sending a specific and targeted electronic cease-and-desist letter asserting trademark infringement and other legal claims (e.g., via Amazon or eBay messaging or e-mail address, if found), or sends a paper cease-and-desist letter if a reseller's physical address can be identified, the reseller may comply and move on to sell another manufacturer's goods. The real challenge, however, is the reseller who altogether fails to comply with a manufacturer's cease-and-desist letter or who appears compliant but shifts between seller accounts and e-storefronts, presenting a constantly moving target.

Under such circumstances, a brand owner has several options to more proactively combat unauthorized resellers and exclude gray goods from the U.S. marketplace:

- Report the reseller to Amazon or other online marketplace for trademark infringement and unfair competition – This may result in the suspension or termination of the reseller's account; however, Amazon does not have a strong track record of acting on gray market sales issues and, thus, legal action will likely be more effective
- File a trademark infringement and unfair competition action in U.S. federal court under the Lanham Act against unauthorized resellers – Through a Lanham Act action against multiple named and unnamed resellers, a manufacturer can potentially obtain an exclusion order barring the importation of gray goods; damages also may be awarded
- Institute a Section 337 proceeding at the International Trade Commission – While no damages are available, the ITC has the authority to issue a general exclusion order barring the importation of gray goods
- Record the trademark with U.S. Customs and Border Protection and apply for Lever Rule protection, which may be available if the brand owner can identify physical and material differences between authorized goods and the gray goods – If Lever Rule protection is granted, customs will interdict gray goods at the border, but there are significant exceptions

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For many companies, gray goods threaten to undermine their hard-earned reputation and customer goodwill in the marketplace and siphon off a significant volume of U.S. sales, reducing revenues and eroding profits. A proactive, thoughtfully planned, and vigilant approach to combating gray market sales is therefore essential. Experienced legal counsel can help develop and implement an enforcement strategy to minimize the effects of gray market resellers and preserve your company's competitive advantage.



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