Australian
Intellectual Property Law
Bulletin

Trade marks can make or break a distributor-ship

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Introduction

When an overseas principal sets up an exclusive distributorship in Australia, it will generally do all it can to support its exclusive distributor. However, the principal needs to ensure that its own trade mark rights are fully protected. Set out below are two scenarios which highlight how trade marks can make or break a distributorship.

Take away tips

- Overseas principals should consider conditional assignment of their trade mark to an Australian distributor as a possible means of deterring parallel importation of their goods.
- Principals should clearly specify in distribution agreements their trade mark and intellectual property rights as applicable at the commencement, during the term and at the termination of those agreements.

Scenario 1

An overseas principal has appointed an exclusive Australian distributor who is promoting its products and meeting sales targets. Unfortunately, substantial quantities of the principal's genuine goods are being parallel imported into Australia by third parties. The distributor is deeply concerned at its loss of market share. What can the principal do to protect its distributor?

Scenario 2

The long-term relationship of the principal and its exclusive Australian distributor is falling apart. The principal intends to terminate the distributorship at the end of the current term but it has suspicions that that distributor will then misappropriate the principal's brands. What can the principal do to protect itself?

Scenario 1 — parallel importation

Nature of parallel importation

When an overseas manufacturer exports to Australia, it may choose to set up a distributor in Australia under an exclusive distribution agreement. Unfortunately for the exclusive Australian distributor, unauthorised parties may source and sell in Australia genuine products which may have been originally manufactured and trade marked by the overseas manufacturer. This parallel importation by unauthorised parties strikes at the heart of the exclusive agreement between the overseas manufacturer and its Australian distributor. An important question is whether this type of parallel importation represents an infringement of the trade mark rights of the overseas manufacturer in Australia. The short answer to that question is that such conduct does not usually constitute trade mark infringement. Parallel importation of this nature is generally protected under s 123 of the Trade Marks Act 1995 (Cth) (the Act). Under this section of the Act, no trade mark owner can claim infringement of its trade mark if the sale of the subject goods bears a trade mark which has been applied by the manufacturer or with its consent. Furthermore, the rights of the parallel importer to sell such genuine goods in Australia generally extend to the publicising, advertising and distribution of such genuine goods.

Ownership of the Australian trade mark

The above protection of the parallel importer against a claim of trade mark infringement assumes that the overseas manufacturer owns its trade mark in Australia. However, trade mark registration rights apply only to the jurisdiction in which the mark is registered. As a consequence, if the overseas manufacturer allows its Australian distributor to own the trade mark in Australia then the parallel importer usually cannot claim the protection of s 123 of the Act because the Australian trade mark owner did not apply the subject trade mark to the imported goods.

Conditional assignment agreements

Naturally, most overseas manufacturers are reluctant to allow their Australian distributors to obtain ownership of their trade mark rights in Australia. As a consequence, some overseas manufacturers have set up conditional assignment agreements with their Australian distributors under which the distributor is allowed to become the registered owner of the trade mark in Australia on the condition that the mark will be assigned back to the overseas manufacturer when the distribution agreement terminates. This contrived arrangement has generally proven to be a successful option under the Australian law. Australian courts have been prepared to accept the beneficial ownership of the Australian trade mark by the distributor, declining to look behind this ownership into the contrived assignment agreement between the distributor and the overseas manufacturer.

Nature of distributor relationship

There are certain caveats to the general position on parallel importation outlined above. It is important for the overseas manufacturer to maintain an arms-length relationship with its Australian distributor which owns the trade mark in Australia. If the overseas manufacturer takes a controlling financial interest in the Australian distributor, that distributor's ownership of the trade mark could be deemed to be under the control of the overseas manufacturer. As a consequence, the Australian trade mark owner could be seen to be consenting to the affixing of the trade mark applied by the overseas manufacturer. In those circumstances, the parallel importer could thereby claim the protection of s 123 of the Act.

Trade mark affixed with consent

From the viewpoint of the parallel importer, it is important to first check that the overseas manufacturer is the registered Australian owner of the subject trade mark before it commences parallel importation into Australia. However, this precaution is not foolproof. It is also important for the parallel importer to check that the trade mark on the goods it is importing was affixed with the consent of the overseas manufacturer. In a world of global supply and complex licensing arrangements, it may be difficult to prove that the relevant consent was given to the affixing of the trade mark by the overseas manufacturer. Parallel importers should also be careful that they do not expose themselves to a claim of misleading conduct if they imply that they can provide manufacturer's warranties which may apply to the imported goods.

Principals and their Australian distributors should of course comply with local labelling laws and regulations relating to health, flammability, recyclability, weights and measures etc. However, it is not possible for an overseas principal to claim copyright infringement of its labelling as a means of preventing parallel importation of its goods into Australia. This follows the case of *R A Bailey & Co Ltd v Bocaccio Pty Ltd*[1] (and the subsequent introduction of s 44C of the Copyright Act 1968 (Cth).

Although the general position under Australian trade mark law on parallel importation is fairly settled, there are particular circumstances which make it advisable for Australian distributors and parallel importers to consult their intellectual property lawyers before embarking on major commercial activities which depend on the operation of s 123 of the Act.

Did you want to mention labelling laws that might apply — they can be different here from overseas and in some cases features like composition or taste as well?

Scenario 2 — naming rights

Brands and commercial names

When an exclusive distributorship between an overseas principal and an Australian distributor ends, the issue of the ownership of intellectual property generated or used during the distribution period should logically be addressed in the distribution agreement. Unfortunately, this issue is often not addressed adequately and disputes can arise between the principal and its ex-distributor with respect to the ownership and use of brands and names. The main heads of such disputes can include trade marks, reputation, domain names and contractual issues.

Trade mark rights

It is usual practice for the trade marks of imported goods to be registered in the name of the overseas principal. However, if these trade marks have not been registered in Australia by the principal, the Australian distributor may be tempted to register these marks itself. Such a practice by the distributor usually proves to be unsuccessful. The principal, by virtue of its export of the labelled goods to Australia is generally the "first user" and therefore the "true owner" of the trade marks in Australia under s 58 of the Act. As a consequence, the overseas principal would be expected to succeed in an opposition or cancellation of marks which its distributor has purported to register.

Sometimes a distributor may trade under the principal's name in Australia as a retailer or wholesaler and subsequently the distributor may seek to register the principal's name as a trade mark for retailing and wholesaling services in class 35 of the register. This practice is also unlikely to be successful. As the "true owner" of the trade mark for the imported goods, the principal might well be seen to also be the "true owner" of that mark for distribution services on the basis that these services are "integral" to the commercial sale of the imported goods.[2]

Reputation

Unless there is a provision imposing a post-contractual restraint on a distributor, the ex-distributor may decide to continue to sell "genuine goods" bearing a principal's trade mark after the distribution agreement has ended. The distributor might obtain such genuine goods from its existing stock or from overseas sources. If the principal owns the subject registered trade marks in Australia, the ex-distributor would be entitled to sell these "genuine goods" in Australia. However, even though the ex-distributor may offer such goods for sale, it should be careful to trade under its own name rather than that of the principal. The right to sell branded products does not provide the distributor with the right to sell under that branded name. Such activities could constitute misleading and deceptive conduct under s 18 of the Australian Consumer Law (Law).[3] These activities could also constitute false representation as to sponsorship, approval or affiliation under s 29(1)(h) of the Law. Such misappropriation of the principal's reputation can easily occur where the ex-distributor is attempting to retain its original customer base in competition with the principal or its new distributor.

Domain names

Some ex-distributors may decide to include the name of their ex-principal in a domain name and even electronically link this domain name to the distributor's own website. Such behaviour is likely to constitute trade mark infringement and misleading conduct. In addition, it may be difficult for a distributor to continue to maintain registration of a domain name which is not based on a registered trade mark. It is important to note that the registration of a company name, business name or domain name does not provide legal proprietorship in a name. Such legal proprietorship can only be acquired by trade mark registration. As a consequence, the principal may succeed in an action under UDRP provisions to have the ex-distributor's domain name cancelled or assigned to the principal.

Bad faith

Principals and distributors should attempt to avoid potential IP disputes at the outset by addressing the relevant issues discussed above. Distributors who attempt to circumvent the IP rights of principals by clandestine trade mark registration may also fall foul of s 62A of the Act which prohibits trade mark applications being filed in "bad faith". The test of "bad faith" has been defined as "conduct falling short of acceptable commercial standards". This test is quite broad and is being more frequently employed to prevent parties such as distributors from engaging in conduct which might deprive principals of their legitimate trade mark rights.

Contractual issues

Nearly all of the above issues can be addressed in a suitably drafted distribution agreement under which the intellectual property of the principal can be defined and the distributor makes undertakings that it holds no rights in the intellectual property of the principal. However, the distributor may justifiably claim that it has its own intellectual property in its function as a distributor. The rights of the distributor in its own name need to be defined and protected in the agreement, particularly where the distributor is entitled to sell complementary third party or house-branded goods. The distribution agreement should be drafted so that the principal retains all rights in its branded names and reputation in relation to its goods while the distributor retains respective rights in its distribution activities under its own name. The ownership of any future intellectual property generated by the parties during the course of the distribution agreement might also be split along such functional lines. Do you think that we also need to say that there needs to be a clause in the distribution agreement that the distributor cannot use the trade mark as part of its own name? Where does quality control fit into all of this?

For the avoidance of doubt, it would be good practice for principals to include in the distribution agreement a specific provision that the distributor cannot use the principal's name or brand as part of its own name. It is important to emphasise a fundamental difference between distribution agreements and trade mark licence agreements. In a distribution agreement, distributors are often required to promote and present the principal's trade mark in a certain prescribed manner. However, the issue of quality control of the relevant products will not arise unless the distributor is also a trade mark licensee who affixes the principal's trade mark to products manufactured or acquired by the licensee under the quality control of the principal.

Conclusion

Trade marks can be a critical element in distributorship arrangements. The principal can make use of its trade mark rights in order to protect its distributor against third parties or as a means of ensuring that its own trade mark rights are protected against the actions of its distributor. In any event, for a distributorship to operate effectively, there needs to be some element of trust between the principal and its distributor. If the parties become excessively suspicious of each other's motives, it will be difficult for them to develop a mutually beneficial relationship.

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Footnotes

1. *R A Bailey & Co Ltd v Bocaccio Pty Ltd* (1986) 84 FLR 32.
2. *South African Airways Pty Ltd v Virtuoso Ltd* (2012) 93 IPR 494; [2011] ATMO 30.
3. Competition and Consumer Act 2010, Sch 2.