

Technology Law Analysis

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DELHI HIGH COURT: INTERMEDIARIES MAY LOSE SAFE HARBOR PROTECTION IN CASE OF NON-COMPLIANCE WITH THEIR OWN POLICIES; CLARIFIES THE SCOPE OF THE FIRST SALE DOCTRINE UNDER TRADEMARK LAW

In a recent judgment, the Delhi High Court held:

- *Intermediaries must abide by their own terms and conditions/policies or risk losing protection under Section 79 of the Information Technology Act, 2000.*
- *E-Commerce platforms may be held liable for tortious interference by allowing sellers to operate on the platform upon receipt of actual knowledge that sale by such sellers is in breach of third party agreements.*
- *Owner of a trademark can object to unauthorized resale of products bearing their registered trademark in cases of impairment of the products. "Impairment" may include change in warranties, return policies, selling prices of the product.*

BACKGROUND:

Direct selling businesses (such as Amway, Oriflame, etc.) were concerned about their products being sold on the e-commerce platforms due to several reasons such as sale without authorization. Hence, suits were filed by Amway India Enterprises Pvt. Ltd. and Modicare Ltd. and Oriflame India Pvt. Ltd. (collectively "**Plaintiffs**") against e-commerce platforms Amazon Seller Services Pvt. Ltd, 1MG Technologies Pvt. Ltd., Flipkart Internet Pvt. Ltd., Jasper Infotech Pvt. Ltd. ("**E-commerce Platforms(s)/Platform(s)**") and independent sellers enlisted on the said e-commerce platforms ("**Independent Sellers**") (E-commerce Platforms and Sellers collectively referred as "**Defendants**").

The judgment¹ is an interim order passed by the Delhi High Court ("**DHC/Court**"), inter alia, directing e-commerce platforms to prevent all sales of the Plaintiffs' products on their platforms without first obtaining prior written consent from the Plaintiffs. The Defendants have recently filed appeals against the judgment which remain pending before the Division Bench of the DHC.²

Business of Plaintiffs

The Plaintiffs are in the business of direct selling i.e. the products of the Plaintiffs can only be sold through individuals (known as direct sellers) engaged by each Plaintiff. Sale through such direct sellers is regulated by way of agreements between the respective Plaintiff and its sellers and each Plaintiff's code of ethics/conduct. Direct sellers of the Plaintiffs are prohibited from selling the products in retail stores and e-commerce websites under the code of ethics/conduct formulated by each Plaintiff. Direct selling businesses are regulated by way of the Direct Selling Guidelines, 2016 ("**DSG**") issued by the Government of India.³

The DSG:

- Provides that sale of products of direct selling entities (i.e. the Plaintiffs in this case) can only be made by direct sellers.⁴
- Imposes certain obligations upon the direct sellers such as carrying their identity cards when engaging with a customer, not using misleading, deceptive and unfair trade practices, etc.⁵
- Provides that sale of products of a direct selling entity on an e-commerce platform can only be made upon receiving prior written consent from the entity.⁶

PLAINTIFFS' CONTENTIONS:

In each of the seven cases filed, the contentions of the respective Plaintiffs are similar. The Plaintiffs became aware of their products being sold on the E-commerce Platform by several sellers without their consent. The Plaintiffs separately wrote to the E-commerce Platforms stating that:

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2020, 2019, 2018, 2017, 2016, 2015

IFLR1000: Tier 1 for Private Equity and Project Development: Telecommunications Networks.
2020, 2019, 2018, 2017, 2014

AsiaLaw Asia-Pacific Guide 2020: Tier 1 (Outstanding) for TMT, Labour & Employment, Private Equity, Regulatory and Tax

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- a. the sale of respective Plaintiff's products on the platform without the Plaintiff's consent was in violation of the DSG.
- b. their products sold on these platforms are in fact tampered products where the Plaintiff's unique QR code is removed, return/ refund policies and/or warranties are changed.
- c. the proper details including name and contact details of the sellers are not available on some of the platform.
- d. In some cases, the products were being sold at a price different from the selling price set by the respective Plaintiff.

Based on these facts, the Plaintiffs contended in their respective suits that:

1. Defendants are acting in violation of the DSG according to which consent of the Plaintiffs is required to sell their products on an E-commerce Platform;
2. The E-commerce Platforms cannot seek safe harbor protection under Section 79⁷ of the Information Technology Act, 2000 ("IT Act") since even after being aware of unlawful acts of the Independent Sellers, such sellers have been allowed to continue to sell on the platforms and therefore no due diligence has been observed by the E-commerce Platforms as required under the Information Technology (Intermediary Guidelines) Rules, 2011 ("Intermediary Guidelines"); and
3. Due to the active involvement of E-commerce Platforms in facilitating unauthorised sale through the platform, E-commerce Platforms are liable for tortious interference in the contractual relationship of the Plaintiffs with their direct sellers.

CONTENTIONS OF THE E-COMMERCE PLATFORMS:

1. The E-commerce Platforms relied on the safe harbor provided under Section 79 of the IT Act to contend that as an intermediary, the only requirement is to take down content upon receiving actual knowledge in the form of a court order as held in *Shreya Singhal v. Union of India*⁸.
2. The E-commerce Platforms also contended that DSG is not law but advisory in nature and hence not binding upon them especially since no contractual relationship existed between the E-commerce Platforms and the Plaintiffs.
3. Under the first sale doctrine recognized under Section 30(3)⁹ of the Trademarks Act, 1999 ("TMA"), the Plaintiffs' rights have exhausted upon the first sale of the products being made by the Plaintiffs to the Independent Sellers therefore the Plaintiffs cannot prevent subsequent sale of genuine products on the E-commerce Platforms.

JUDGMENT OF THE DHC:

I. The DSG are law and not merely advisory in nature.

The DHC held that the DSG have the force of law and are binding upon direct selling businesses. The DHC also clarified that the DSG apply to 'any person who sells or offers for sale'¹⁰ the products of direct selling entities (such as the Plaintiffs) and therefore the E-commerce Platforms and all sellers of the Plaintiffs' goods on E-commerce Platforms are bound by the DSG. The DHC noted that government authorities including the Food Safety and Standards Authority of India have informed the E-commerce Platforms of the applicability of the DSG upon such E-commerce Platforms.

II. Owner of a trademark may object to subsequent sale of products bearing their trademark in cases of "impairment" of the product

The Plaintiffs' alleged that under Section 29(6) of the TMA, use of the Plaintiffs' trademarks by the Defendants for advertising, sale of products, etc. without prior authorization from the Plaintiffs amounts to infringement. In response to this, the Defendants argued that the Plaintiffs have already made the first sale of their products to the Independent Sellers and therefore, as per Section 30(3), the Plaintiffs now do not have a right to object to resale or prevent the E-Commerce Platforms from otherwise dealing in their products.

However, the DHC held that Defendants cannot seek protection under the first sale doctrine when there is substantial impairment in the condition of the goods, as provided under Section 30(4)¹¹. The DHC noted that impairment of goods does not have to be physical impairment but can also include differences in services, warranties, packaging, pricing, quality control etc.

To determine if there was "impairment" in the facts of the cases at hand, the DHC considered the reports prepared by Local Commissioners appointed to visit the warehouses and storage facilities of the Defendants ("LC Reports"). The LC Reports stated that:

- a. products of the Plaintiffs' were being re-packed and re-labelled at the premises visited.
- b. There was evidence of tampering of products in the form of removal of QR codes, removal of seals on products and resealing of products at almost all the Defendants' premises visited including the warehouses of the E-Commerce Platforms.

It was further noted by the DHC that when the Plaintiffs' products are listed on the E-Commerce Platforms, the return policies of the E-Commerce Platforms become applicable which are different from

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the return policies offered by the Plaintiffs. Further, some of the Plaintiffs produced evidence that on some platforms the products were being sold at a price higher than the selling price set by the respective Plaintiff.

The Delhi HC therefore noted that the E-commerce Platforms are changing the warranties/ return/ refund policies/ prices of the products which amounts to "impairment" of the goods and therefore, protection under Section 30(3) of the TMA cannot be sought.

III. Intermediaries must comply with the due diligence requirement provided under the Intermediary Guidelines or risk losing safe harbor protection

The DHC noted that for intermediaries, including the E-commerce Platforms, to continue to enjoy the status of intermediaries, the due diligence requirements provided under the Intermediary Guidelines need to be complied with.¹² These due diligence requirements include formulating terms and conditions for users informing them not to host, display, upload, modify, publish, transmit, update or share any information which, *inter alia*, infringes upon a third party's intellectual property rights or is unlawful in any manner.

In addition to formulating such policies, the Court noted that all intermediaries have to strictly adhere to their own policies failing which intermediaries may lose protection under Section 79 of the IT Act.

The DHC noted that the policies of the E-commerce Platforms provided, *inter alia*, that sellers must be authorized sellers and sellers must not act in violation of intellectual property rights of third parties. It was noted that the Plaintiffs had intimated the Platforms of unlawful acts of several sellers on their platforms and therefore, the Platforms had actual knowledge that:

- a. some of the sellers are not authorized sellers of the Plaintiffs and therefore do not have any right to sell the Plaintiffs' products and use the trademarks of the Plaintiffs;
- b. sale of the Plaintiffs' products on the internet is prohibited under the DSG and also under the Plaintiffs' agreements with their sellers and still such sales are being carried out on the E-Commerce Platforms.

The Court held that since the Platforms had knowledge of violation of their policies by certain sellers on account of the aforementioned acts, they were required to follow their policies and prevent further sales from such sellers to be in compliance with the due diligence requirement and continue to stay protected as intermediaries.

IV. E-commerce platforms may be held guilty of tortious interference with the contractual relationship of the Plaintiffs with their distributors/direct sellers

Under the tort of inducement/tortious interference, when a third party acts in a manner which may induce a party to a contract to breach the contract, the non-breaching party can sue the third party for tortious interference. The Court noted that inducement may be indirect and it is enough for a Plaintiff to establish that the defendant had knowledge that their acts caused a breach of contract.¹³ It is not required to show that the defendant had an intent to cause the breach.¹⁴

The DHC noted that E-commerce Platforms carry out substantial sale of products through their platforms and do not act merely as passive players but actively provide several value added services to their sellers. Further, the manner in which Platforms function (details of sellers not shared with consumers, no verification of authenticity of products, etc.) makes it easy for Independent Sellers to breach contracts or sell unlawfully. The Court held that on account of the magnitude of the operations of the Platforms, they had a duty to ensure that their actions do not interfere with the businesses of the Plaintiffs. The DHC noted that the Platforms had knowledge of existing contracts between the Plaintiffs and their sellers and violation of the same on their platforms. The Plaintiffs had even informed the E-commerce Platforms that unauthorized sales and sales of tampered products could result in the consumers losing confidence in the Plaintiffs' brands.

Despite receiving notices from the Plaintiffs, the Platforms did not take any action to remove the products of the Plaintiffs from their websites or had any discussion with the Plaintiffs to ensure that the contracts of the Plaintiffs with their distributors/ sellers are fulfilled. The Court therefore held that continued sale of the Plaintiffs' products on the Platforms would result in tortious interference.

JUDGEMENT:

The DHC granted interim relief to the Plaintiffs and held that:

1. Independent Sellers cannot advertise, display, offer for sale any products of the Plaintiffs on the E-commerce Platforms.
2. The E-Commerce platforms cannot display, advertise, offer for sale, sell, facilitate repackage any product of the Plaintiffs unless the Independent Sellers can give written consent of the Plaintiffs to the E-commerce Platforms.
3. During the pendency of the suit, the E-commerce Platforms should take down any products within 36 hours of Plaintiff notifying them of such listing by the sellers who don't have consent.

KEY TAKEAWAYS

1. *Standard of due diligence to be observed by Intermediaries*—The judgment of *Shreya Singhal v Union of India* holds that an intermediary is mandated to take down content under Section 79(3) only upon receiving actual knowledge by way of a court order or an order of an appropriate government or its agency. In addition to such court mandated takedowns, intermediaries must also take steps to take down any content upon receipt of knowledge that such content violates their terms of use/policies set up in accordance with the Intermediary Guidelines. Such take downs need not be court mandated and are a part of the due diligence requirement under section 79(2)(c), as noted by the DHC above.
2. *Quality control in warehouses/storage facilities managed by e-commerce platforms* – The visits of the Local Commissioners appointed by the Court in this case revealed the mishandling/tampering of products carried on in the warehouses/storage facilities of several e-commerce platforms. Although at this interim stage the Court has not made any adverse finding against the e-commerce platforms on account of such mishandling, e-commerce platforms must conduct regular checks of their facilities to ensure that no unlawful acts are being carried out at such premises to avoid liability.
3. *A trademark owner can object to resale of their products if the condition of the goods is impaired* - Impairment of the condition of goods has been clarified to include not only physical impairment but also differences in services, warranties, packaging, quality control, advertising, pricing and presentation of the products. In case of such impairment by a reseller or on an e-commerce platform, the owner of a trademark has a right to object to resale. E-commerce platforms must also note that apart from sale of counterfeit products, the owner of a trademark has a right to object to resale of genuine products when the condition of such products is “impaired”.
4. *Liability under tort for e-commerce platforms*- The DHC has noted that on account of the magnitude of operations of e-commerce platforms, they have a duty to conduct proper due diligence and ensure that the platforms do not provide an easy medium for sellers to breach their agreements with the manufacturer/owner of a product. Upon receipt of actual knowledge that sale on their platform is in violation of a contract between the seller and a third party, it is the platform’s duty to prevent further sales.

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You can direct your queries or comments to the authors

¹ CS (OS) 410/2018; CS(OS) 453/2018; CS(OS) 480/2018; CS(OS) 531/2018; CS(OS) 550/2018; CS(OS) 75/2019; CS(OS) 91/2019

² FAO(OS) 135/2019; FAO(OS) 134/2019; FAO(OS) 133/2019; FAO(OS) 142/2019; FAO(OS) 141/2019

³ https://consumeraffairs.nic.in/sites/default/files/file-uploads/direct-selling/Direct%20Selling%20Guidelines%20Final%20_0.pdf

⁴ See Clause 4, DSG

⁵ See Clause 5, DSG

⁶ Clause 7(6), DSG

⁷ 79. Exemption from liability of intermediary in certain cases.—(1) Notwithstanding anything contained in any law for the time being in force but subject to the provisions of sub-sections (2) and (3), an intermediary shall not be liable for any third party information, data, or communication link made available or hosted by him.

(2) The provisions of sub-section (1) shall apply if—

(a) the function of the intermediary is limited to providing access to a communication system over which information made available by third parties is transmitted or temporarily stored or hosted; or

(b) the intermediary does not—

(i) initiate the transmission,

(ii) select the receiver of the transmission, and

(iii) select or modify the information contained in the transmission;

(c) the intermediary observes due diligence while discharging his duties under this Act and also observes such other guidelines as the Central Government may prescribe in this behalf.

(3) The provisions of sub-section (1) shall not apply if—

(a) the intermediary has conspired or abetted or aided or induced, whether by threats or promise or otherwise in the commission of the unlawful act;

(b) upon receiving actual knowledge, or on being notified by the appropriate Government or its agency that any information, data or communication link residing in or connected to a computer resource

controlled by the intermediary is being used to commit the unlawful act, the intermediary fails to expeditiously remove or disable access to that material on that resource without vitiating the evidence in any manner.

Explanation.—For the purposes of this section, the expression —third party information means any information dealt with by an intermediary in his capacity as an intermediary.

⁸ (2015) 5 SCC 1. Please see the NDA Hotline here

http://www.nishithdesai.com/fileadmin/user_upload/pdfs/NDA%20Hotline/IT_Act_Hotline_March_26_2015.pdf

⁹ Section 30(3) provides:

Where the goods bearing a registered trade mark are lawfully acquired by a person, the sale of the goods in the market or otherwise dealing in those goods by that person or by a person claiming under or through him is not infringement of a trade by reason only of—

(a) the registered trade mark having been assigned by the registered proprietor to some other person, after the acquisition of those goods; or

(b) the goods having been put on the market under the registered trade mark by the proprietor or with his consent.

¹⁰ Clause 7(6) of the DSG

¹¹ Section 30(4) provides:

Sub-section (3) shall not apply where there exists legitimate reasons for the proprietor to oppose further dealings in the goods in particular, where the condition of the goods, has been changed or impaired after they have been put on the market

¹² Section 79(2)(c) of the IT Act

¹³ The court placed reliance on *Aasia Industrial Technologies Ltd. v. Ambience Space Sellers Ltd.* 1998 PTC (18) (DB)

¹⁴ *ibid*

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