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A Non-Harmonized Perspective on Parallel Imports: The Protection of Intellectual Property Rights and the Free Movement of Goods in International Trade

Krithpaka Boonfueng

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**A NON-HARMONIZED PERSPECTIVE ON PARALLEL IMPORTS: THE
PROTECTION OF INTELLECTUAL PROPERTY RIGHTS AND THE
FREE MOVEMENT OF GOODS IN INTERNATIONAL TRADE**

by

Krithpaka Boonfueng

Submitted to the

Faculty of the Washington College of Law

of The American University

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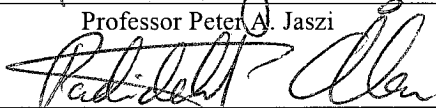
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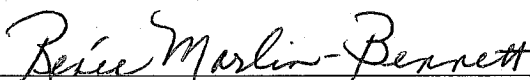
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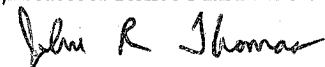
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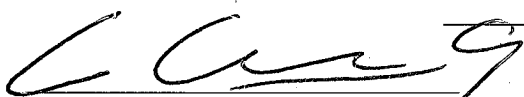
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ABSTRACT

This dissertation aims to define an appropriate international legal standard for the exhaustion doctrine as it pertains to parallel imports, being the importation of genuine goods but without authorization from intellectual property owners. The clarification of this issue is needed because developed and developing countries have different perspectives on the application of the exhaustion doctrine. Under the exhaustion doctrine, once an intellectual property owner deliberately releases or authorizes others to release goods into the stream of commerce, his exclusive right to further control the goods is no longer valid. However, there are three diverse aspects in the application of exhaustion doctrine: national, regional, and international. Developed countries advocate the national exhaustion, whereas developing countries support the international exhaustion and strongly oppose the national exhaustion. Indeed, an exclusive right to exercise control over the first sale should serve as sufficient financial incentive to ensure investment in the creative process. Hence, extending exclusive rights to control goods beyond the first sale

by allowing an intellectual property owner to bar parallel imports is unnecessary to accomplish the incentive function and may unduly interfere with competition and the free movement of goods in the marketplace.

Allowing parallel imports through adoption of an international exhaustion doctrine would support the dissemination of intellectual property works and the free movement of goods and free competition by eliminating a non-tariff barrier, thereby benefiting consumers in terms of lower prices and more selection. With respect to consumers' benefit, as a result of international price differential, parallel imports can play an important role in neutralizing price discrimination by providing beneficial price competition that may lead to lower prices. In addition, parallel imports may help in allocating international resource among nations and reducing the anti-competitive acts of intellectual property owner through price fixing or licensing agreements. In this light, the anti-competitive act via infringement proceedings to block parallel imports should be considered as a misuse of intellectual property rights and a non-tariff barrier. Moreover, parallel imports can prevent or reduce the counterfeit market because they satisfy and fulfill low-end market demand.

Therefore, in this dissertation, the international exhaustion doctrine with some specific exceptions is considered to be the appropriate approach for harmonizing global laws regarding the exhaustion doctrine. This approach could capably balance the concepts of intellectual property rights protection with the free movement of goods principle. The exercise of intellectual property rights should not thwart the notion of free trade and free movement of goods or vice versa.

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INTRODUCTION

The issue of parallel imports represents an important and complex interaction between the free flow of international trade and the protection of intellectual property rights (IPRs). Parallel imports or the so-called gray market is an increasingly significant phenomenon in today's global market place. Unlike counterfeit markets or black markets, gray markets consist of the importation of genuine goods, generally sold under a particular trademark or protected under copyright or patent, into a territory without authorization from the intellectual property owners. The issue is whether this phenomenon can or should be regulated under the intellectual property laws. This is a question that is likely to be prominent in future discussions of international intellectual property norms and international trade and the outcome may have significant consequences for the process of academic development and consumer welfare.

This issue is very important because the legal regulation of parallel imports will determine the degree to which manufactured goods incorporating the intellectual property rights protection can successfully engage in international price discrimination. The multinational manufacturers, who possess intellectual property rights and establish manufacturing around the world, normally charge different prices in each nation creating

arbitrage opportunities.¹ This price differential system set by IPRs owners and/or multinational manufacturers simultaneously creates an opportunity for parallel import activities. Parallel importers can purchase goods from low priced markets in developing countries and sell them to high priced markets in developed countries, generating profit from the price differential. The interests of the IPRs owners to bar parallel imports are divergent from concerns for consumer welfare. In respect of consumer welfare, parallel imports not only increase consumers' choices but also reduce the gap between price differences in each national market by providing lower priced goods for consumers and by forcing domestic manufactures or distributors to reduce the price of domestic goods.

The phenomenon of parallel imports challenges intellectual property law because it presents the unexamined issue of monopoly rights of the owners of intellectual property. It is clear that the IPRs owners have a limited monopoly in so far as the domestic market is concerned. The question is to what extent is such a monopoly compatible with the notion of free trade? This issue also presents the interplay between parallel imports and the scope of exhaustion doctrine. The IPRs owners or domestic exclusive distributors assert their exclusive right of importation and distribution in order to block parallel imports or to control the movement of parallel import goods. The exhaustion doctrine acts to prevent the IPRs owners or local licensees from barring parallel imports. In general, the exhaustion doctrine would teach that once the IPRs owners release or authorize others to release goods, being protected under the intellectual property laws, into the stream of commerce, this exhausts their exclusive right to further

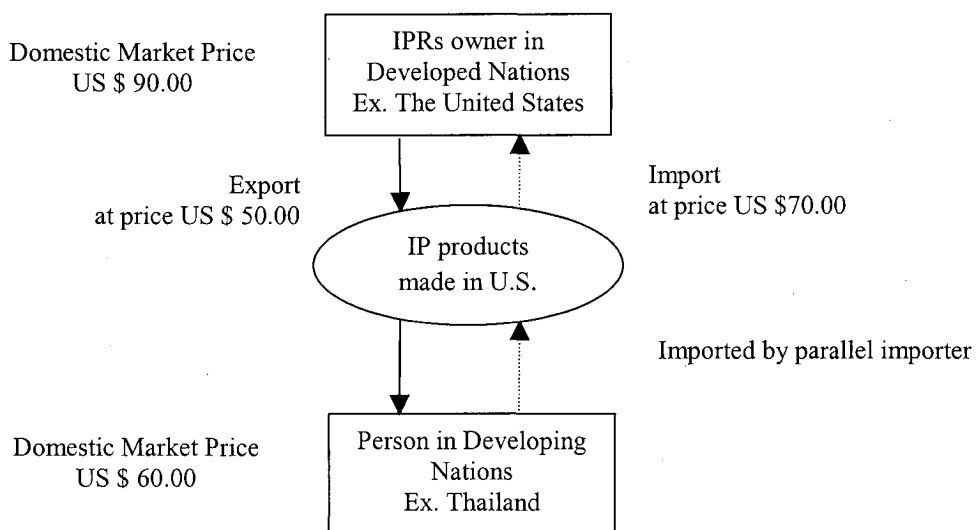
¹ For example, the IPRs owner may charge a different price for the same products in different nations. Generally, the price of products in developed nations is higher than that of products in developing nations.

control. The goods could then be freely resold in other countries without restrictions. This doctrine is also referred to as the “first sale doctrine.” Both of the terms “exhaustion doctrine” and “first sale doctrine” will be used interchangeably throughout this thesis.

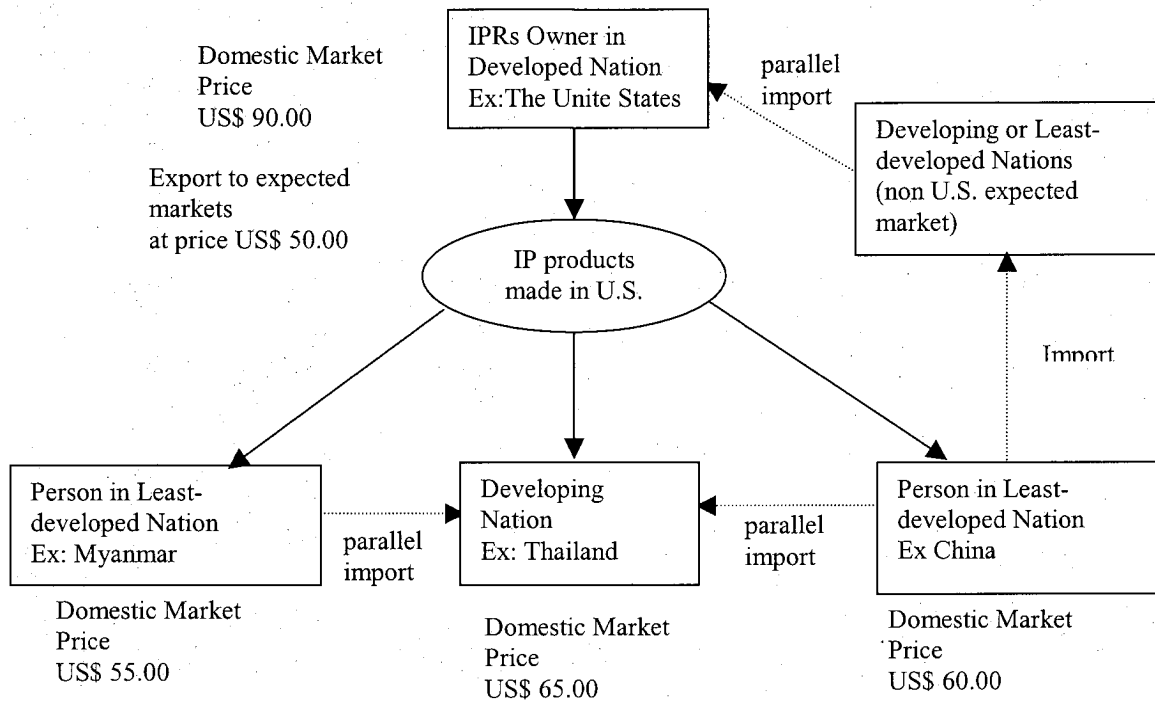
Most commentators have only focused their discussions on the issue of parallel imports between developed countries and developing countries. However, there are many layers of parallel trade in international commerce. This thesis will introduce the phenomenon of parallel imports in a multilateral global setting, not only between developed countries and developing countries but also among developing countries and least-developed countries. Consequently there are two classes of parallel imports: (1) Parallel imports between a developed country and a developing country; and (2) Parallel imports between a developing country and the least-developed country. Two classes of parallel imports can be described in the following models.

Model 1: Product Produced in the Developed Nations

A. Between Developed Nations and Developing Nations

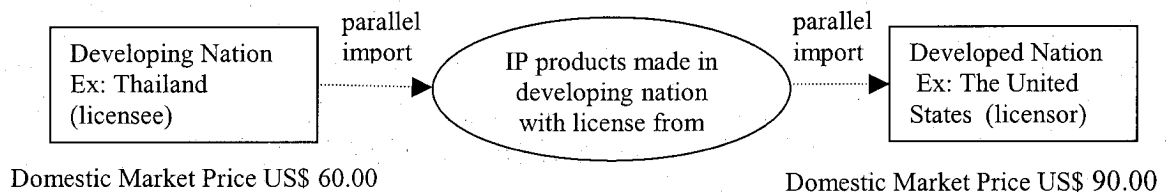


B. Among Developing Nations and Least-developed Nations

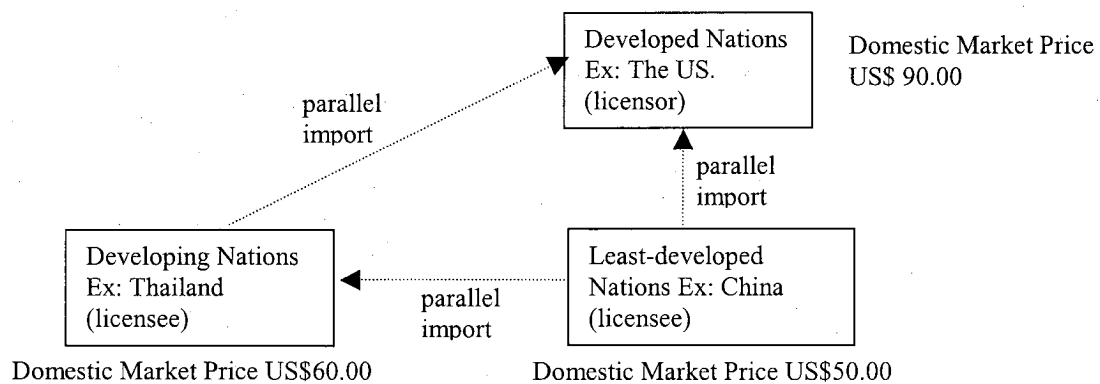


Model 2: Product Produced in Developing Nation under a License Agreement

A. Between Developed Nations and Developing Nations



B. Among Developing Nations and Least-developed Nations



The existing exhaustion doctrine asserts that every nation accepts the notion of an exhaustion doctrine, but can differ in the scope of application of an exhaustion doctrine. There is a conflict between developed countries and developing countries in the scope of application of the exhaustion doctrine. Developed countries utilize a principle of national exhaustion in an attempt to curb parallel imports. Parallel imports are seen as harmful to the IPRs owners since the benefit of receiving a royalty from the import licensing fee is lost, and it also affects domestic sales revenues and the control of the movement of intellectual property products. On the other hand, the developing and least-developed countries favor allowing parallel imports in order to provide low-price items to consumers by applying an international exhaustion doctrine. The controversy over the scope of exhaustion doctrine is a result of the different IPRs protection and political, cultural, and economic perspectives between developed and developing countries.²

The Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) serves as a bible of international IPRs protection. However, the TRIPs Agreement chose not to address or answer the sensitive issues on the scope of exhaustion doctrine. Under Article 6, the TRIPs Agreement does not require a member to reject or accept parallel imports but leaves it open for members to make their own choice.³ The issue of parallel imports is not settled because it is the last stand of developing countries to protect their

²For example, developed nations as producers of intellectual property (IP) products tend to provide a broad variety of high protection and extend the scope of IPRs in favor of their creators by combating against the international exhaustion doctrine. On the contrary, developing and nations as consumers of IP products tend to allow free access to intellectual property and provide a narrower protection by relying on the international exhaustion doctrine. Nevertheless, based on national policy and social and consumer benefits, some developed nations with strong IPRs protection such as Australia and Japan, may adopt the international exhaustion doctrine. It is worth studying to determine why those developed nations apply an international exhaustion because their experiences and reasons could be used to persuade other developed nations to adopt an international exhaustion doctrine. See further discussion in Chapter Two and Three.

³ See The Agreement on Trade-Related Aspects of Intellectual Property Rights, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1C, Legal Instruments-Results of the Uruguay Round, 33 I.L.M. 81 (1994) [hereinafter TRIPs].

Article 6 of the TRIPs Agreement provides: Exhaustion

“ For the purposes of dispute settlement under this Agreement, subject to the provisions of Articles 3 and 4 nothing in this Agreement shall be used to address the issue of intellectual property rights.”

benefits from parallel imports. Additionally, the 1999 WTO-Seattle Ministerial meeting failed to even discuss the exhaustion doctrine issue in relation to parallel imports. However, later the 2000 WTO-Doha Ministerial conference only confirmed that developing countries could allow parallel imports for public health reason. Therefore, there is no clear answer as to whether nations should adopt the international exhaustion or national exhaustion.

Probably, in the near future, this issue will be discussed in further TRIPs negotiations. There are two possible solutions to this issue. The first would be the recent TRIPs approach of "Status Quo," which allows nations to adopt its own national law regime by prohibiting parallel imports for the benefit of the national intellectual property industry, or allowing parallel imports for the benefit of their consumers. The other alternative is a harmonized approach based on adoption of the international exhaustion subject to some specific exceptions.

The division over parallel imports is not new. For many decades, scholars in the area of intellectual property law, antitrust law or competition law, social welfare, economics, and international trade have debated these issues. But recently, on the economic globalization scale, the issues over parallel imports have become more urgent as a result of consumers' movement and new technology such as Internet dissemination and electronic commerce, which have reduced transportation and communication costs. The increased freedom in the movement of goods and increased market integration has reduced impediments to international trade. The development of international trade has pushed the issue of parallel imports to the forefront of intellectual property concerns.

Due to the current paradox, a realistic approach to solve the issue of parallel imports should be to seek the harmonization in principle and the scope of exhaustion doctrine. Harmonization in the exhaustion doctrine is necessary because today the

volume of world trade is dramatically increasing and the issue of parallel imports is more complex and subject to argument than before. Without an international standard of exhaustion doctrine, the international trade and the movement of products will be impeded by inconsistent regulations in each nation that can potentially cause a non-tariff barrier. This harmonization should strive for equilibrium between the maximization of free trade and the IPRs protection. It should concern not only intellectual property law, but also competition law, and international trade policy in order to deal with balancing interests between the IPRs owner and consumers, and also balancing interests among developed, developing and least-developed countries.

In summary, this thesis aims to define the appropriate international legal standards for exhaustion doctrine to clarify the issue of parallel imports that would provide benefits to all nations by taking into account the perspectives of developed countries and those of developing and least-developed countries. This thesis also affirms that parallel imports support the global market or free movement of goods.⁴ There are many conflicts between developed and developing countries in the scope of exhaustion doctrine whether it should be international or national. Due to currently no answer to this question, therefore, this thesis will propose the international exhaustion with some specific exemptions as the most effective legal standard for global harmonization on this matter.

⁴ The principle of free movement of goods is a significant component of the WTO conference. The main purpose of the General Agreement on Tariffs and Trade (GATT) is to eliminate both tariff and non-tariff barriers in order to stimulate the global market and the free movement of goods. In the Uruguay Round, IPRs protection was a significant issue because intellectual property has become the driving force behind many commercial and financial activities in the developed world. To maximize IPRs protection globally, the TRIPs Agreement was established to deal with the tension between international trade and intellectual property rights. TRIPs promotes the balance between the undistorted and unimpeded free trade of intellectual products and the protection of IPRs owners' interests in intellectual products. The high variance among national IPRs rights has become increasingly incompatible with market globalization. TRIPs establishes a minimum standard of IPRs protection that WTO members have to abide by. See INTERNATIONAL TRADE AND INTELLECTUAL PROPERTY: THE SEARCH FOR A BALANCED SYSTEM (George R. Stewart et al. 1994); and also see John G. Byne, Comment, *Changes on the Frontier of Intellectual Property Law: An Overview of the Changes Required by GATT*, 34 DUQ. L. REV. 121, section II and III (1995)(explaining the GATT history and the impact of GATT on intellectual property law).

CHAPTER ONE

INTELLECTUAL PROPERTY AND FREE TRADE POLICY

I. INTRODUCTION

In the trade of intellectual property goods, there is an intrinsic tension between the concept of free trade and the protection of intellectual property rights. Based on the idea that international trade could be maximized by liberalization of trade, the World Trade Organization (WTO) and the General Agreement on Tariffs and Trade (GATT)⁵ were principally created to promote international trade and free movement of goods in international forum. The primary purpose of GATT is to eliminate both tariff and non-tariff barriers in order to stimulate the global market and the free movement of goods. As a matter of self-interest or national benefit, every country focuses on its own benefit by limiting importation to protect domestic businesses. Import restrictions such as quotas or import regulations are considered tariff barriers to international trade, which are prohibited under GATT. Similarly, intellectual property laws may be used as an instrument for prohibiting importation. Although not traditionally considered a non-tariff barrier, the excessive protection of intellectual property rights limiting or prohibiting

⁵ General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. A-3, T.I.A.S. No. 1700, 55 U.N.T.S. 187 [hereinafter GATT]

importation may be considered a non-tariff barrier under the idea of national protectionism.⁶

The national law allowing IPRs owners to exercise their right to prohibit parallel imports could be considered a non-tariff barrier, particularly when the IPRs owner's purpose for impeding parallel imports is to prevent the free movement of goods, protect his own benefit, or maintain the monopoly power in the domestic market. Such conduct not only obliterates the concept of free trade and free movement of goods, but also is a form of unfair trade. The prohibition of parallel imports by IPRs owners is one example of how the exercise of IPRs conflicts with the principle of free movement of goods and causes a non-tariff barrier.⁷

On the other hand, the inadequate IPRs protection constitutes trade distortions and undermines the goal of free trade.⁸ The IPRs protections are premised upon a theory of

⁶ See *id.* at Preamble para. 3 (stating "Being desirous of contributing to these objectives by entering into reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade and to the elimination of discriminatory treatment in international trade."); art. III, P1, P2, P4. (stating national regulations governing non-tariff barriers to trade.); art. XI (general elimination of quantitative restrictions such as quotas, import or export licenses or other measures); art. XX (d)(providing general exceptions for members to use a non-tariff barrier in case of necessary to the IPRs protection.); see Padideh Ala'i, *Free Trade or Sustainable Development?: An Analysis of the WTO Appellate Body's Shift to a More Balanced Approach of Trade Liberalization*, 14 AM. U. INT'L L. REV. 1129 (1999) (analyzing the concept and application of Article XX, including case studies); see JOHN H. JACKSON ET AL., *LEGAL PROBLEMS OF INTERNATIONAL ECONOMIC RELATIONS* 383 (3rd ed., 1995) (explaining that Uruguay Round results in a reduction of worldwide tariff.); see Jeffrey Garten, *American Trade Law in a Changing World Economy*, 29 INT'L LAW. 15, 17 and 30-31 (1995) (explaining and discussing the elimination of tariff and non-tariff barriers and regarding the importance of IPRs in NAFTA and GATT/TRIPS); and also see Hilary A. Kremen, *Caveat Venditor: International Application of the First Sale Doctrine*, 23 SYRACUSE J. INT'L L. & COM. 161, 161-163 (1997)(mentioning that although the application of national exhaustion doctrine is not a tariff, it has a negative effect on importation.)

⁷ See Frederick M. Abbott, *Nature and Scope of the Agreement: Commentary: The International Intellectual Property Order Enters the 21st Century*, 29 VAND. J. TRANSNAT'L L. 471, 479 (1996).

⁸ See Marshall A. Leaffer, *Protecting United States Intellectual Property Abroad: Toward a New Multilateralism*, 76 IOWA L. REV. 273, 277 (1991), citing in Intellectual Property and Trade: Hearings Before the Subcomm. on Courts, Civil Liberties and the Administration of Justice of the House Comm. on the Judiciary, 99th Cong., 2d Sess. 51-53 (1986)(statement of Harvey E. Bale Jr., Asst. U.S. Trade Representative for Trade Policy and Analysis.)

natural law and on national policy.⁹ The variation in IPRs protections among nations is a result of the difference in developed and developing nations' policy opposing or supporting the natural law theory.¹⁰ Developed countries provide a strong IPRs protection. Conversely, developing countries are reluctant to strengthen their intellectual property laws. Their concerns are over the question whether providing the IPRs protection creates a favorable trade-off between the short-term cost to consumers through higher prices and the long-term benefit to consumers through increased innovation.¹¹ In the past the issue of inadequate IPRs protection was discussed in multilateral trade negotiations but no agreement was reached. Since 1994, IPRs protection has been successfully negotiated in the Uruguay Round¹² by standardizing and strengthening IPRs

⁹ See Frederick M. Abbott, *Protecting First World Assets in the Third World: Intellectual Property Negotiations in the GATT Multilateral Framework*, 22 VAND. J. TRANSNAT'L L. 689 (1989) (explaining that the theory of natural law is based on a concept that a person naturally owns intellectual property she or he creates and that misappropriation from that person without compensation is wrongful. The national policies on the scope of legitimized IPRs vary widely depending on the results of a cost/benefit analysis balancing the immediate public welfare against long-term interests in private capital formation.)

¹⁰ Thus the national regulations for providing IPRs protection that would maximize global welfare may not necessarily maximize national welfare because it raises the price of goods such as pharmaceuticals or software in domestic market. See Carsten Fink, *Entering the Jungle of Intellectual Property Rights Exhaustion and Parallel Imports*, Apr. 1999 at 12, available at http://www1.worldbank.org/wbiep/trade/c_papers/fink-parallel.pdf. (visited Mar. 6, 2002) (explaining that with parallel imports, consumers in countries that would have lower prices under uniform pricing would benefit from restrictions on parallel trade, whereas consumers in countries that would have higher prices under price discrimination would be worse off from such restrictions.)

¹¹ See John H. Barton, *Symposium: Global Trade Issues in the New Millennium: The Economics of TRIPS: International Trade in Information-Intensive Products*, 33 GEO. WASH. INT'L L. REV. 473, 487-89 (2001). (explaining that the answer of this question depends on social evaluations and perspectives of each nation.)

¹² See J.H. Reichman, *The TRIPS Component of The GATT's Uruguay Round: Competitive Prospects For Intellectual Property Owners In An Integrated World Market*, 4 FORDHAM INTELL. PROP. MEDIA & ENT.L.J. 171, 176 (1993) (pointing out that there are two recent developments that lead directly to the successful multilateral trade negotiations in the area of intellectual property: the rise of information-based technologies and The increase of manufacturers' capacity to produce IP goods in developing countries.); J.H. Reichman, *Computer Programs as Applied Scientific Know-How: Implications of Copyright Protection for Commercialized University Research*, 42 VAND. L. REV. 639, 656-92 (1989); Paulo Roberto de Almeida, *The "New" Intellectual Property Regime and Its Economic Impact on Development Countries*, in *LIBERALIZATION OF SERVICES AND INTELLECTUAL PROPERTY IN THE URUGUAY ROUND OF GATT* 74-76 (Giorgio Sacerdoti ed., 1990); and also see David Hartridge & Arvind Subramanian, *Intellectual Property Rights: The Issues in GATT*, 22 VAND. J. TRANSNAT'L L. 893, 895-96 (1989).

protection in Member States. This negotiation was successful because of the serious concern of many developed countries on the global prevalence of IPRs infringements.¹³

Consequently, in this thesis, Chapter One, Part II explains the relationship between IPRs protection and international trade. The connection between parallel imports and free trade policy is addressed in Part III, which includes the basic arguments of opponents and proponents of parallel imports.

II. THE RELATIONSHIP BETWEEN INTELLECTUAL PROPERTY RIGHTS PROTECTION AND INTERNATIONAL TRADE

The strengthening of IPRs protection has become an important part of international trade deliberation that encourages the expansion of international trade on a global scale. Nevertheless, at the same time, the excessive IPRs protection such as the prohibition of parallel imports has occasionally impeded the international trade. For a better understanding, this section will begin with the basic principles of intellectual property and then describe the concept of the global market and free movement of goods.

A. Basic Principles of Intellectual Property

Intellectual property is considered an intangible product of human activity.¹⁴ Although it is intangible, its expression or visible form may be fixed in something

¹³ The IPRs infringements cost manufacturers and firms losing billions of dollars in income per year. For example, in China, the value of pirated goods was almost \$2.3 billion in 1996 and \$ 2.8 billion in 1997. See Steven Mufson, *Piracy Still Runs Rampant in China; Yet Industries Oppose Asking for Sanctions*, WASH. POST., Mar. 27, 1998, at E3.

tangible. Intellectual property laws provide a set of exclusive rights to IPRs owners to authorize or prevent others from commercially profiting from the intellectual property.¹⁵

With regard to parallel imports, there are three relevant fundamental principles of IPRs: a principle of territoriality, a principle of universality and a principle of exhaustion. The first and second principles focus on the scope of exclusive rights of the IPRs owner. The last principle concentrates on the limitation of the IPRs. Understanding these principles is useful in discussing the legal issues relating to parallel imports because these issues are relevant to the exclusive rights of intellectual property owner.

1. Principle of Territoriality

The IPRs protection is territorial, depending upon the national intellectual property laws of each nation. This results in separate rights for the IPRs owner within each geographical area.¹⁶ Thus, infringement of IPRs outside a particular jurisdiction may not be considered infringement by the domestic intellectual property law.¹⁷ The principle

¹⁴ See Edwin C. Hettinger, *Justifying Intellectual Property*, in *INTELLECTUAL PROPERTY: MORAL, LEGAL, AND INTERNATIONAL DILEMMAS* 24 (Adam D. Moore ed., 1997) (explaining that under the Lockean Proviso, a laborer has a prima facie natural right to possess and personally use the fruits of his or her labor. Although one cannot physically possess or occupy ideas, property in ideas is justified for having a right to enjoy their fruits of their labor.); Justine Hughes, *The Philosophy of Intellectual Property*, in *INTELLECTUAL PROPERTY: MORAL, LEGAL, AND INTERNATIONAL DILEMMAS* 117 (Adam D. Moore ed., 1997); and also see Baird, *Common Law Intellectual Property and the Legacy of International News Service v. Associated Press*, 50 U. CHI. L. REV. 411, 413 (1983).

¹⁵ See Fink, *supra* note 10, at 8-9. (explaining that IPRs are of limited or unlimited duration and ubiquitous. Some of various rights are of limited duration such as patents, design, and copyright and others may provide an entitlement for unlimited duration such as moral right, trade secret. The various types of IPRs can be categorized into two groups. The first is the IPRs that motivate incentive and creative such as patent, copyright and the second is the IPRs that determine "information asymmetries" such as trademark.)

¹⁶ See Barbara A. Curry, Comment, *Grey Market Imports: A Genuine Problem for the United States Trademark Owner, Customs Service, and Court*, 7 J. INT'L. L. BUS. 762, 776 (1986) (explaining that the territoriality principle identifies creation of trademark rights as "to maintain and protect a trademark owner's established goodwill.")

¹⁷ For example, the U.S. Supreme Court in *Brown v. Duchesne* ruled that "the patent act do not, and were not intend to, operate beyond the limits of the United States; and as the patentee's right of property and

of territoriality is expressed in Article 4 bis of the Paris Convention and is considered an important element of the Paris Convention. It means that national laws on the creation, existence and lapse or expiration of a patent only have a legal effect within the territory of the individual nation involved, and do not affect an equivalent patent elsewhere.¹⁸ Trademark rights are also territorial, meaning that a trademark is valid only in a country where the mark is registered. The trademark in different territory is independent from other.¹⁹ Unlike patent and trademark, copyright is not quite territorial. Under the Berne Convention, a copyright is automatically protected and valid without registration. However, the scope of exclusive rights and protection depends on the copyright law of each country. Thus copyrights in different countries are independent from one another.

The principle of territoriality applied to the exhaustion doctrine recognizes that the first sale of intellectual property products abroad should not exhaust the rights of an IPRs holder to exclude parallel imports of the products.²⁰ Therefore, the scope of exhaustion doctrine should be a “national exhaustion doctrine” at a national or domestic, not international, scale.

exclusive use is derived from them, they cannot extend beyond the limits to which the law itself is codified. And the use of it outside of the jurisdiction of the United States is not an infringement of his rights.” See *Brown v. Duchesne*, 60 U.S. 193, 195-96 (1856); and also see *Dowagiac Manufacturing Co. v. Minnesota Moline Plow, co*, 235 U.S. 641 (1915).

¹⁸ See W R CORNISH, *INTELLECTUAL PROPERTY : PATENTS, COPYRIGHT, TRADEMARKS AND ALLIED RIGHTS* 247 (4th ed, 1999); and also see Friedrich Karl Beire, *Territoriality of Trademark Law and International Trade*, 1 IIC 48 (1970).

¹⁹ Alongside the principle of the territoriality, the principle of the independence also deals with trademarks and patents. The principle of the independence of trademarks is expressed in Article 6(3) of the Paris Union Convention for the Protection of Industrial Property of 20 March 1883, as last revised at Stockholm on 14 July 1967 which provides: “A mark duly registered in a country of the Union shall be regarded as independent of marks registered in other countries of the Union...” The possibility of independent assignments is first of all implicit in article 6quater of the Paris Union Convention. See c-9/93, *IHT Internationale Heiztechnik GmbH and Another v. Ideal-Standard GmbH*, [1994] 3 CMLR 857 (1994).

²⁰ See *Boesch v. Graff* 133 U.S. 697 (1890).

2.Principle of Universality

The principle of universality is generally discussed in conjunction with trademark rights. This principle provides that a trademark right is entitled to universal protection beyond the boundaries of the originating country.²¹ If the trademark is legally affixed on a product, whether domestic or foreign, the trademark product's legality should be universal and not viewed as infringing on the rights of other trademark owners in the country of importation.²² The doctrine of universality recognizes a trademark as an indication of product origin (a badge of origin).²³ An IPRs owner should not use his right to bar imports of products first released to a foreign market by himself or with his authorization.²⁴ Although this principle is typically seen in trademark, rationally it should be applied to patent and copyright as well.²⁵

Hence, under the principle of universality, IPRs are recognized on a worldwide basis. Goods, produced legally either domestically or overseas, would always be considered as genuine and legitimate goods. Thus after goods are first released into the market either by the IPRs owner or with his consent; the IPRs owner would lose any control over the goods. Then the importation of the goods into other territories would not

²¹ See Curry, *supra* note 16, at 777.

²² See *Osawa & Co. v. B&H Photo*, 589 F. Supp. 1163, 1171-72 (S.D.N.Y. 1984); and also see Curry, *supra* note 16, at 777.

²³ See *Appolinaris Co. Ltd. v. Scherer*, 27 F. 18, 20 (C.C.S.D.N.Y. 1886); *A. Bourjois & Co. v. Katzel*, 275 F. 539(2nd Cir. 1921), rev'd, 260 U.S. 689 (1923). The U.S. court in *Appolinaris* case applied the principle of universality to allow parallel imports. However, the principle of universality was replaced by the principle of territoriality and no "universal" trademark survives after the court decision in *Katzel* case. The court decided in favor of domestic distributor and trademark owner. See *A. Bourjois & Co. v. Katzel*, 275 F. 539(2nd Cir. 1921), rev'd, 260 U.S. 689 (1923).

²⁴ See WARWICK A. ROTHNIE, *PARALLEL IMPORTS* 4 (1993). (mentioning that the sale abroad is just to imply consent of IPRs owner to domestic marketing.)

²⁵ The rationale is that the substance of patent and copyright in goods has not been changed during the transfer of those goods. Moreover, the reputation of patent or copyright owner could not be damaged from

constitute infringement of the IPRs. Such an approach requires that the scope of the exhaustion doctrine be international, not national.

3.Principle of Exhaustion or First Sale Doctrine

3.1 Overview

The exhaustion doctrine or the first sale doctrine is one of the basic principles to limit the exclusive rights of an intellectual property owner. Under the exhaustion doctrine, once the IPRs owner exercised his exclusive right either by marketing the products or giving the consent to others to market those products, the right to control or to capture further commercial benefit over the products is exhausted. A person buying a legally release product is free to use or resell the product without infringing the IPRs.

Historically, since 1873 the United States court had consistently held that intellectual property products were free for further distribution after the authorized first sale. This principle was called “the first sale doctrine.”²⁶ This concept was later introduced into Europe by German judges under the terminology “exhaustion of intellectual property rights.”²⁷

the further transportation of goods. The consent of IPRs owner for the first sale should allow the purchaser to use the goods universal and free to further distribution it without constituting any infringement.

²⁶ See *Adams v. Bruke*, 84 U.S. (17 Wall) 453 (1873); *Keeler v. Standard Folding-Bed Co.* 157 US. 659 (1895); *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339 (1908); *Curtiss Aeroplane & Motor Corp. v. United Aircraft Eng'g Corp.*, 266 F. 71 (2nd Cir. 1920); and *Quality King Distributors, Inc. v. L'anza Research International Inc.*, 118 S.Ct. 1125 (1998).

²⁷ See Abdulquwi A. Yusuf & Andres Moncayo von Hase, *Intellectual Property Protection and International Trade: Exhaustion of Rights Revisited*, 16 WORLD COMPET. L. & ECON. REV., 117 (1992), cited in The German Supreme Court defining the concept of exhaustion in early 1902. (stating “The effect of the patent resides in the fact that domestically no one except the patentee -and persons authorized by him- may produce the produce or place it in the market. Thereby, however, the effect of the patent is exhausted. If the patentee produces the product and place it in the market within his right to preclude the competition of others, he has already enjoyed the advantages which the patent grants him and has thus

The aim of first sale doctrine or exhaustion doctrine is to limit the exclusive rights of an intellectual property owner and to balance two colliding properties, namely the intellectual property right of the intellectual property owner and the common proprietary right of the owner of a copied product.²⁸ As the result of different legal systems the first sale doctrine or exhaustion doctrine has developed in two different ways. Most common-law countries such as the United Kingdom, Australia, and New Zealand use the implied license theory in the context of exhaustion doctrine. They believe that in the absence of any restriction on the sale contract, the purchasers should be able to freely dispose of the goods incorporating intellectual property. Thus if there is a restriction clause on resale or importation, the rights of IPRs owners do not become exhausted and they can bar such importation. In contrast, continental Europe such as Germany and the United States use the principle of exhaustion doctrine.²⁹ They consider that the exclusive right of the intellectual property owner is automatically exhausted after the first distribution of the goods either by himself or with his consent. This difference in application of the exhaustion doctrine makes for the disparate treatment of parallel imports throughout the world, which will be further explained and discussed in Chapter Two.

expended his rights. A patent does not grant to its holder the right to prescribe the conditions under which trade with its producers is to take place.”)

²⁸ See Herman Cohen Jehoram, *International Exhaustion Versus Importation Right: a Murky Area of Intellectual Property Law*, available at http://www.ivir.nl/publications/cohen_jehoram/cohen2.doc. (visited Mar. 15, 2002). (pointing out that the owner of a copy of an IP product should “remain free to enjoy the specific privileges of traditional ownership” and “free to resell or otherwise dispose of his property.”).

²⁹ See Yusuf & Hase, *supra* note 27, at 117; see ROTHNIE, *supra* note 24. (analyzing both the common law approach and the United States approach.); see Richard H. Stern, *Some Reflections on Parallel Importation of Copyrighted Products into the United States and the Relation of the Exhaustion Doctrine to the Doctrine of Implied Licence*, [1989] EIPR 119, 123-24; and also see Abraham van Melle, *Parallel Importing in New Zealand: Historical Origins, Recent Developments, and Future Directions*, [1999] EIPR 63.

3.2 The Requirements for Triggering the Exhaustion doctrine

In general, it seems that there are four characteristics of goods that are required to trigger the first sale or exhaustion doctrine. First, the goods have to be lawfully produced in order to claim for the exhaustion doctrine.³⁰ Second, the goods in question have to be initially sold either by the intellectual property owner himself or with his consent. Third, the title of goods has to transfer to the purchaser in order to implicate the first sale doctrine.³¹ Finally, the IPRs owner should receive a benefit to offset his investment before his right was exhausted. It is important that the IPRs owner receives some benefits in order to provide incentive for the production or invention of new works.

However, the purpose of the first sale doctrine or exhaustion doctrine is to limit the right of intellectual property owner so that double benefit is not reaped. The exhaustion doctrine is set to balance the intellectual property owners' interest and the public's interest. Although receiving a benefit is a requirement for implication of the exhaustion doctrine, it still must be considered whether the IPRs owner receives an adequate benefit from his first sale to exhaust his exclusive right to control over the products. Each nation has a different standard to decide whether the benefit is enough for

³⁰ See 17 U.S.C. § 109(a); and see MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT, § 8.12 [B][4]. [hereinafter NIMMER ON COPYRIGHT]; The problem is whether the scope of the exhaustion doctrine should be national or international in scope. In other words, should "lawfully produced goods" be only those legally produced in the domestic market, or inclusive of goods legally produced overseas. A more detailed discussion is presented in Chapter Two in the context of the United States.

³¹ In order to assert a first sale defense, the person must be the owner of that copy. The owner's right may be acquired by virtue of a sale, gift, bequest or other transfer of title. Therefore, leasing, lending or licensing does not trigger the first sale doctrine. See NIMMER ON COPYRIGHT, *supra* note 30, at § 8.12 [B][1], citing in *Microsoft Corp. v. Harmony Computer & Electronic, Inc.*, in which the court held that Section 109(a) is inapplicable because "Microsoft only licenses and does not sell its products." There is a comment that "[I]f by 'Products' the court meant to refer to tangible diskettes, and if by 'licenses,' the intent was to convey that such physical items are merely leased or lent, then that conclusion was correct. On the other hand, if the court inferred from the fact that the copyright to the software was licensed to end-

triggering an exhaustion doctrine.³² Moreover, it is difficult to judge whether the IPRs owner has given his consent to the sale or importation. Differences arise among nations regarding whether consent can be implied or must be specifically expressed, and each nation approaches this determination of consent differently.³³ This subject matter will be further explained and analyzed in Chapter Two.

3.3 Variation in the Scope of the Exhaustion Doctrine

The scope of the exhaustion doctrine can be applied nationally, regionally or internationally. Under a national exhaustion doctrine, once goods are initially put on the domestic market, the IPRs owner is not allowed to further control the commercial exploitation of goods. However, the IPRs owner could still oppose the importation of original goods marketed abroad because the initial sale overseas does not exhaust his

users that section 109(a) was therefore inapplicable, then it entirely misunderstood the first sale doctrine.” *See Microsoft Corp. v. Harmony Computer & Electronic, Inc.*, 846 F. Supp. 208 (E.D.N.Y. 1994).

³² The issue whether such sale triggers the exhaustion doctrine is a controversial and complex issue because the court of each nation has different perspective, which should be perceived in Chapter Two. In my opinion, there is a difference between an adequate benefit standard and a full benefit standard and it is important to study how to harmonize this issue at international level. The suitable international standard should be “reasonably adequate benefit” because it would best forward the goal of intellectual property law to balance between a creators’ benefit and a society’s benefit. If the word “full benefit” reduces the right of consumers and unreasonably increases the ability of IPRs owners to control products, it abuses the fundamental concept of IPRs protection. Moreover, the benefits should be either money benefits (such as royalty) or non-money benefits (such as pleasure or honor). For example, when IPRs owner donates his work such as one painting for charity purpose, he has not received a money benefit, but he has received a non-money benefit. Therefore, his right to control the painting is exhausted under the first sale doctrine.

³³ For example, a Japanese court ruled that if the IPRs gave proper notice of the limitation on importation or resale to all resellers, the right of intellectual property owner was not exhausted upon first sale. In instances of no clear notice, it could be found that intellectual property owner give his implied consent to parallel importation and that no infringement had occurred. *see BBS Kraftfahrzeugtechnik AG v. Racimex Japan KK.*; *Jap Auto Products KK.* The English translation of this Japanese Supreme Court decision has been published in 29 IIC 331 (1998) [hereinafter BBS case]; The United Kingdom considers it is unnecessary to have a clear notice. Sufficient circumstances to show that intellectual property owner does not intend to prohibit further sale or importation is enough to exhaust the right of intellectual property owner. *see Zino Davidoff SA v. A&G Imports Ltd.*, [1999] 2 CMLR 1056; and *see* further discussion in Chapter Two in the context of Japan and European Union.

exclusive right. The concept of a national exhaustion doctrine is based upon the principle of territoriality and independence of intellectual property. The United States has led in the adoption of this approach.³⁴

The regional exhaustion doctrine is a combination of national and international exhaustion principle. The first sale by the IPRs owner or with his consent exhausts any IPRs over the products not only domestically, but within the whole region, and parallel imports within the region can no longer be opposed based on the intellectual property right. However, the IPRs owner can still prohibit parallel importation from outside the region because his right does not become exhausted. The European Union has adopted this approach known as a Community-wide exhaustion doctrine.³⁵

Finally, under the international exhaustion doctrine, the intellectual property rights are exhausted once the product has been sold by the intellectual property owner or with his consent in any part of the world. After the first sale, the IPRs owner loses his exclusive right and no longer has right to prohibit parallel imports from abroad. The international exhaustion doctrine promotes the principle of free movement of goods and free trade. Developed nations such as Japan, Australia, and New Zealand have adopted this approach. Developing nations such as Thailand, Singapore, Argentina, Hong Kong, and Chile have also utilized the international exhaustion doctrine.³⁶

³⁴ See further discussion in relation to the United States in Chapter Two.

³⁵ See further discussion in Chapter Two regarding the European Union.

³⁶ See Thai Patent Act 1999 Article 36(7); Khaw Lake Tee, *The 1990 Amendments to the Malaysian Copyright Act 1987*, [1991] EIPR 132; George Wei, *Parallel Imports and the Law of Copyright in Singapore*, [1992] EIPR 139; and see BBS Case, *supra* note 33.; see Section 24 of the Hong Kong Copyright Ordinance (Cap 528) and Section 20 of the Hong Kong Trademark Ordinance (Cap 559, available at <http://www.justice.gov.hk> (visited Apr. 8, 2002); see Fink, *supra* note 8, at 7 (mentioning that Argentina and Chile adopt the international exhaustion doctrine.)

B. Encouraging the Global Market and Free Movement of Goods Through the Strengthening of Intellectual Property Rights Protection

1. Overview

Recently, the phenomenon of global integration created by the expansion of free trade policy and new digital and Internet technology has created an unlimited global market,³⁷ which has accelerated the global economy.³⁸ The value from sales of intellectual property products such as pharmaceuticals, software, music and movies has increased through the internationalization of markets.³⁹ However, many countries especially developing countries do not provide IPRs protection and even if IPRs protection is provided, it is very weak and usually unenforceable. The absence of IPRs protection functions as a trade barrier.⁴⁰

³⁷ For example, the new digital technology can change all form of information such as text, sound, and image into binary code that can be transmitted on the Internet. International institutions rapidly issue the regulations of intellectual property rights to cover the new change.

³⁸ See Robert Solow, *Technological Change and the Aggregate Production Function*, 39 REV. ECON. & STAT. 312 (1957); see KEITH E. MASKUS, *INTELLECTUAL PROPERTY RIGHTS IN THE GLOBAL ECONOMY* 2 (2000); and also see Robert Burrell, *The Information Society: Change and Challenges*, in *INTELLECTUAL PROPERTY IN THE DIGITAL AGE: CHALLENGES FOR ASIA* 12-15 (Christopher Heath & Anselm Kamperman Sanders eds., 2001).

³⁹ U.S. Pharmaceutical firm annually sell products abroad totaling over \$40 billion. The U.S. trade surplus in software is over \$ 20 billion for the year 2000 and movie exports around \$ 6.5 billion. See Barton, *supra* note 11, at 473, citing in the PhaRMA Annual Survey, Table 12, available at [http://www.phrma.org/publications/industry/profile00/phrma Tables.pdf](http://www.phrma.org/publications/industry/profile00/phrma%20Tables.pdf). (visited Apr. 15, 2002); Business Software Alliance, *U.S.-Owned Software Industry Produces Trade Surpluses*, available at <http://www.bsa.org/statistics/index99.html>. (visited Mar. 6, 2002); and Compare U.S. Dep't of Commerce, *Cross-Border Trade in 1998 and Sales Through Affiliates in 1997*, 79 Surv. Current Bus. 28, 48 and 64-65, tbl 1, available at <http://www.ita.doc.gov/td/sif/USSTH-05.htm>. (visited Mar. 6, 2002)

⁴⁰ See Barton, *supra* note 11, at 486.; and also see FREDERICK ABBOTT, THOMAS COTTIER, & FRANCIS GURRY, *THE INTERNATIONAL INTELLECTUAL PROPERTY SYSTEM: COMMENTARY AND MATERIALS: PART ONE*, 2 (1999). (stating "As goods and service move more freely and quickly throughout an increasingly integrated global economy, producers and distributors need to assure that the creative or innovative elements of these goods and services, and the elements that give these goods and service and the elements that give these goods and services their unique character and, thus, their competitive advantage, are protected against misappropriation. The absence of effective protection of intellectual property in many parts of the world in essence amounts to new types of trade barriers.")

As a result of globally increasing infringement on intellectual property rights,⁴¹ developed countries, particularly the United States, have attempted to strengthen IPRs protection on a global scale because the developing countries' IPRs laws have been ineffective in combating the IPRs infringement or piracy.⁴² Consequently, in the early 1980s, demands increased by developed countries for improving the level of IPRs protection. This led to the international negotiation in the General Agreement on Tariffs and Trade (GATT) to create a major international IPRs protection initiative. The protection of international IPRs was created in the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs). The TRIPs Agreement was a major step forward for a harmonized and integrated global system for IPRs protection.⁴³

2. General Agreement on Tariffs and Trade (GATT) as the Main Multinational Agreement Supporting the Free Trade and Free Movement of Goods

Historically, the tariff negotiation began with the first draft at Church House, Westminster from October 15 to November 26, 1946. The negotiation of the second draft took place in New York from April 10 to August 22, 1947. The second draft negotiation generated the "Final Act Adopted at the conclusion of the Second Session." This included

⁴¹ See Hettinger, *supra* note 14, at 20. (pointing out that besides modern information technologies making unauthorized taking of intellectual property works easier than before, one more reason for the widespread piracy of intellectual property is that many people think it is unjustified to exclude others from obtaining copies of the goods.)

⁴² See PETER NANYENYA-TAKIRAMBUDDE, TECHNOLOGY TRANSFER AND INTERNATIONAL LAW 71-72 (1980).

⁴³ *Id.*

the text of the General Agreement on Tariffs and Trade (GATT).⁴⁴ After this successful event, many further multinational trade negotiations were undertaken, such as Tokyo Round, and Uruguay Round. The Uruguay Round was considered the most important trade negotiation since it was the first time that GATT successfully incorporated trade in intellectual property rights⁴⁵ and trade in services into the multinational trade negotiation.

The GATT has had a significant role in encouraging free trade⁴⁶ and reducing tariff and non-tariff barriers in the world trading system. Every country has used tariff and non-tariff barriers to protect their own interests.⁴⁷ Hence, an important purpose of GATT was to eliminate both tariff and non-tariff barriers among members and to ensure that Contracting Parties⁴⁸ did not violate GATT obligations in order to protect their own interests. Under GATT, a new World Trade Organization (WTO) was established to supervise and enforce the GATT provisions. The WTO is the global supremacy body dealing with the rules of trade between nations. The three main purposes of the WTO are to help trade flow as freely as possible, to serve as a forum for trade negotiations, and to

⁴⁴ See DENIEL GERVAIS, *THE TRIPS AGREEMENT: DRAFTING HISTORY AND ANALYSIS* 4 (1998). (explaining the drafting history and analysis the TRIPs Agreement. This agreement was signed at Geneva on October 30, 1947 by representatives of 25 governments.)

⁴⁵ See Yusuf & Hase, *supra* note 27, at 115. (mentioning that a primary focus for GATT regarding intellectual property rights was to ensure that measures taken by governments to protect IPRs did not constitute barrier to legitimate trade among contracting parties. In respect to GATT, the contracting parties may adopt or enforce domestic legislative IPRs protection measures that are not arbitrary or discriminatory, or a disguised restriction on international trade.)

⁴⁶ See GATT, *supra* note 5.

⁴⁷ See MARC WILLIAMS, *INTERNATIONAL ECONOMIC ORGANIZATIONS AND THE THIRD WORLD* 154 (1994). (For example, the US trade law have been updated to threaten to undertake retaliatory action against unfair trade practices if an agreement suitable to US interest is not concludes. As domestic interest groups in the major capitalist states promoted their sectional interests. The US demand for a liberal regime for IPRs in effect seeks to grant protection to American transnational corporations. In addition, rising of new protectionism mainly practiced by the US, EC, and Japan, the use measure differ from the old protectionism through a greater reliance on non-tariff barriers include quotas, voluntary export restraints, customs valuation procedures, administrative authorizations to import, subsidies and health standards.)

⁴⁸ Due to GATT basically a contact, the signatories are called "contracting parties" rather than "members."

provide a forum for the dispute settlement.⁴⁹ The powerful enforcement and dispute settlement system under the WTO is regarded as the strong point of GATT.

3. From GATT to Agreement on Trade-Related Aspects of Intellectual Property (TRIPs)

As the result of widespread IPRs piracy, developed nations (such as the United State, the European Union, and Japan) mainly export intellectual property products and lose their benefit. Due to the serious loss of benefit to U.S. industries from piracy abroad,⁵⁰ the U.S., as the world's leading technological innovator with strong IPRs protection, needed other nations to also strengthen their own IPRs protection laws. This objective is to prevent intellectual property piracy in foreign countries and to open foreign markets to American industries.⁵¹ Therefore, the U.S. played a leading role in pushing to incorporate intellectual property concerns into the trade issues.

The United States, the European Community and Japan attempted to include international protection of intellectual property rights at the GATT forum in the Tokyo Round, but no agreement was reached.⁵² However, the proposal by these industrial countries was later successful with the inclusion of trade-related intellectual property rights protections in the Uruguay Round. At the 1994 Uruguay Round of the General

⁴⁹ See World Trade Organization, What Is the WTO?, available at

http://www.wto.org/english/thewto_e/thewto_e.htm. (visited Feb. 15, 2002)

⁵⁰ The U.S. industries roughly loss more than U.S.\$ 60 billion annually from piracy and other forms of IPRs infringement. See Report to the United States Trade Representative, Foreign Protection of Intellectual Property Rights and the Effects on U.S. Industry and Trade, USITC Pub. 2065 (1988).

⁵¹ See Jame M. Cooper, *Sprints in the Material World: A Post-modern Approach to United States Trade Policy*, 14 AM. U. J. INT'L L. REV., 954, 967-68 (1999); and also see ROBERT GILPIN, *THE POLITICAL ECONOMY OF INTERNATIONAL RELATIONS* 199-200 (1987).

⁵² See Abdulquwi A. Yusuf, *TRIPs: Background, Principles and General Provisions*, in *INTELLECTUAL PROPERTY AND INTERNATIONAL TRADE: THE TRIPs AGREEMENT* 6-7 (Carlos M. Correa & Abdulquwi A. Yusuf, eds., 1998)(stating that the U.S. and the EU introduced a draft agreement on measures to discourage

Agreement on Tariffs and Trade (GATT),⁵³ the United States, the European Community and Japan proposed more than the traditional reduction of tariff rates. These countries asserted that inadequate IPRs protection led to trade distortion and created a non-tariff barrier.⁵⁴ As the result of the strong pressure to strengthen IPRs protection around the world, the protection of intellectual property rights was included in GATT.⁵⁵

The Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) under the Uruguay Round, effective on January 1, 1995, provides the minimal standard for the IPRs protection.⁵⁶ Its aim is to bring various developing countries such as China, Thailand, India, and Taiwan in compliance with the minimum standard.⁵⁷ The TRIPs Agreement is significantly linked to trade regulation and to dispute resolution under GATT. The WTO is responsible for enforcement of the new IPRs protection under the

the importation of counterfeit goods at the GATT Tokyo Round of Multilateral Trade Negotiations. Unfortunately, the US-EEC proposed agreement on counterfeit goods was never adopted in this Round.)

⁵³ See GATT, *supra* note 5.

⁵⁴ See U.S. Framework Proposal To GATT Concerning Intellectual Property Rights, 4 INT'L TRADE REP. (BNA) 1371 (Nov. 4, 1987).

⁵⁵ The main reason why developed nations desire to incorporate IPRs protection into GATT is because the system of GATT provides an efficient enforcement mechanism when a member violates GATT obligations. Prior multinational agreement such as the Bern Convention and WIPO Treaties only create a protection standard, but did not provide an enforcement mechanism.; One scholar commend that integrating trade law and intellectual property law creates problems because the economic of information-intensive products (IIPs) can be significant different from that of the products traditionally the subject of international trade law. IIPs may be defined "as products whose content or development requires a substantial intellectual expenditure in development or creation but can thereafter be reproduced at relatively low cost." See Barton, *supra* note 11, at 474 -76.(stating "In general economic trade theory, we think of trade as equalizing prices near the world's lowest available marginal cost, which benefits the world's consumers in the form of lower prices. For IIPs, however, market prices are necessarily significant exists precisely to maintain that difference, as an incentive for innovation and creativity."); The World Trade Organization (WTO) considers the intellectual property products as information-intensive products (IIPs), through the Uruguay Round's General Agreement on Trade in Services. See TRIPs, *supra* note 3, art.31.

⁵⁶ Besides the TRIPs Agreement, there are other various conventions administered by the World Intellectual Property Organization (WIPO) and the World Trade Organization (WTO) that provide a broad multilateral framework for IPRs rule for the international community. For instance, the European Union and the European Patent Organization increasingly provide a IPRs protection framework for Europe. Other regional arrangement such as NAFTA and Mercosur set out the minimum standard of IPRs protection.

⁵⁷ See Ruth L. Gana, *Prospects for Developing Countries Under the TRIPS Agreement*, 29 VAND. J. TRANSNAT'L L. 735, 740 (1996).

TRIPs Agreement and for monitoring whether members completely comply with TRIPs obligations.⁵⁸

The TRIPs Agreement also adopted and linked to provisions from the Paris Convention of Industrial Property (1883) and the Berne Convention for the Protection of Literary and Artistic Works (1886).⁵⁹ Members have to satisfy the minimum protection standards and prevent infringement of intellectual property rights through their own domestic law enforcement. Members of TRIPs Agreement must implement the minimum required provisions within a one-year period. However, the developing countries and least-developed countries have periods of five years and ten years respectively for compliance.⁶⁰

III. THE PHENOMENON OF PARALLEL IMPORTS AND INTERESTING CONCERNS PERTAINING TO PARALLEL IMPORTS

The issue of parallel imports is a controversial subject with a number of concerns. To better understand the phenomenon of parallel imports, Part A will describe the meaning of parallel imports. Part B then will explain the factors that encourage parallel imports and make the parallel imports issue worthy of more consideration. Finally, Part C will discuss whether parallel imports should be prohibited or allowed in light of the concerns for consumer welfare, free riding and free trade.

⁵⁸ See Adrian Otten & Hannu Wager, *Compliance with TRIPS: The Emerging World View*, 29 VAND. J. TRANSNAT'L L. 391, 392 and 411-12 (1996).

⁵⁹ See TRIPs, *supra* note 3, art. 1(3) and 2(1)(adopting Article 1 through 21 and 19 of the Paris Convention), and art. 9(1) (adopting Article 1 through 21 of the Bern Convention)

⁶⁰ *Id.* art. 65 and 66.

A. The Meaning of Parallel Imports or Gray Market

Parallel imports or gray market goods are genuine goods and should not be confused with counterfeit goods.⁶¹ Parallel imports consist of genuine goods with IPRs protection that are transported from one market to another market without the authorization of the IPRs owner.⁶² In other words, parallel imports involve the importation of genuine goods outside the authorized distribution channel.⁶³ Parallel imported goods would be sold in competition with goods that the IPRs owner has authorized for sale in the domestic market.⁶⁴ Parallel imports have become a serious issue for IPRs owners, manufacturers, local licensees, and local authorized distributors,⁶⁵ particularly in the United States.⁶⁶

There are two forms of parallel imports. The first involves domestically produced goods legitimately sold to international markets which are then imported back into the

⁶¹ See *id.* art. 51, n14(a). (providing the meaning of "Counterfeit trademark goods") and art. 51, n14(b). (providing the meaning of "Pirated copyright goods"); In general, parallel import or gray market has the same meaning. Therefore, parallel import is used in this dissertation.

⁶² See Keith E. Maskus, *Parallel Import*, 23 WORLD ECON. 1269 (2000).

⁶³ See James Cross, James Stephans, & Robert E. Benjamin, *Gray Markets: A Legal Review and Public Policy Perspective*, 9 J. PUB. POL'Y & MARKET. 183 (1990)(explaining that the importation of genuine goods from a foreign source bypasses the authorized U.S. distributor and trademark licensee, allowing for the sale of genuine goods directly to U.S. retailers or consumers.)

⁶⁴ See Michael S. Knoll, *Gray-market Imports: Causes, Consequences and Responses*, 18 LAW & POL'Y INT'L BUS. 145, 146 (1986); and also see DEVID BENDER, DAVID GERBER, GRAY MARKET AND PARALLEL IMPORT PROTECTIONISM VS. FREE TRADE 11 (1986); and also see Richard A. Fogel, *Grey Market Goods and Modern International Commerce: A Question of Free Trade*, 10 FORDHAM INT'L L.J. 308 (1987). For instance, parallel import goods are produced and legitimately sold abroad under a particular trademark and imported into the United States and sold in competition with goods of the U.S. trademark owner of the identical mark.

⁶⁵ See Stuart Jackson & Richard Kempner, *Parallel Imports into and within the European Union*, in INTELLECTUAL PROPERTY IN THE GLOBAL MARKETPLACE: VOLUME I: ELECTRONIC COMMERCE, VALUATION, AND PROTECTION §14.1, 1-2 (Melvin Simensky et al. eds., 2d ed. 1999). (explaining that vast differences in wealth and costs of production among developed, developing and least-developed countries have encouraged a significant increase in parallel imports.)

⁶⁶ See Knoll, *supra* note 64, at 146. (pointing out that the presence of these parallel imports in the U.S. domestic market has a negative impact on the IPRs owner. The U.S. market is a major target for parallel imports because of its encouragement of free trade and generally higher domestic product prices.)

domestic market and sold in competition with the domestic goods without authorization by the IPRs owner or local licensee. The second involves commodities that are legitimately produced under a license authorizing sales in one particular market, which are then imported into other markets but without authorization.⁶⁷

B. The Factors that Motivate Parallel Imports

In general, there are three essential conditions for parallel imports: (1) a supply of goods that are readily available in other markets; (2) barriers to trade (such as transportation costs, duties, tariffs and legal restrictions) are minimal; and (3) price differentials (including foreign exchange rates) are sufficiently large to make a profit.⁶⁸ This paper will separate the elements of parallel imports into four parts: price differentials, transportation costs, emergence of free trade and global market policy, and currency fluctuation.

1. Price Differentials

Due to cost differences, the IPRs owner benefits from lower production costs in developing countries by setting up a subsidiary or by granting a license for its goods to be manufactured locally. By exporting these foreign produced goods back to the home country a profit is made.⁶⁹ In order to maximize their profit in each national market,

⁶⁷ See Knoll, *supra* note 64, at 146.

⁶⁸ See Dale F. Duhan & Mary Jane Sheffett, *Gray Markets and the Legal Status of Parallel Importation*, 52 J. MARKET. 75-83 (1988).

⁶⁹ For example, the cost of product in the United States is \$ 60 and the U.S. selling price is US \$ 120. Whereas, the cost of production is \$ 30 in Mexico and the Mexico selling price is US\$ 80. Consequently, if

intellectual property owners charge different prices for the same goods in different market based on the consumer's wealth. The parallel imports are essentially "an arbitrage response to international price discrimination that a supplier tries to sustain via exclusive distribution territories over different national markets."⁷⁰ The price difference or price discrimination is considered as the main reason for the emergence of parallel imports.

2. Transportation Cost

When importing products, the importer must consider the cost of importation (such as shipping cost and import transaction cost) in determining whether a profit can be made from those goods placed in competition with locally produced goods. In general, parallel imports emerge when the price of the domestically produced goods is higher than the price of the foreign produced goods by a large enough margin that the importer can both cover the costs of importation and receive a rational profit.⁷¹

3. Emergence of Free trade and Global Market Policy

Theoretically, in a single international marketplace, products in the global market should be transportable from one nation to another without restriction. Parallel imports

the US. intellectual property owner sets up his subsidiary in Mexico and imports its goods back into the U.S., a greater profit is made than if he just sold domestically manufactured goods in his home country.; see Jackson & Kemper, *supra* note 66, at 2.(mentioning that practically, to sell products in a foreign market, an exclusive distributor is almost chosen as the distribution strategy. The exclusive distributor imports products and sells them for profit. For increasing the number of sale, the exclusive distributor has to build goodwill of imported products by advertising, having a marketing plan, and providing a product warranty.)

⁷⁰See David A. Malueg & Marius Schwartz, Parallel Imports, Demand Dispersion, and International Price Discrimination, Economic Analysis Group Antitrust Division, U.S. Department of Justice (August 25, 1993) at 4.

⁷¹ See Knoll, *supra* note 64, at 146.

have arisen through this free flow of goods in the international marketplace. Recently, there has been a dramatic increase in the amount of the parallel imports.⁷² Typically, a tariff raises the price of imported goods by adding to the costs of supplying the product. However, recently the developed countries promoted international trade by reducing tariffs and eliminating non-tariff barriers, which have created a situation where imported goods prices are actually lower than the price of domestic goods. Importers have an incentive to take advantage of price differences by supplying parallel import goods.

4. Currency Fluctuation

Parallel importers can also profit from the exchange rate differential by purchasing identical goods from a country with a weak currency and importing them into a country with a strong currency.⁷³ Due to foreign exchange fluctuations, a new pricing system for global distribution networks adjusts distributors' price lists on quarterly basis to reflect these fluctuations.⁷⁴ During the economic crisis in Asia, the majority of currencies in Asia suffered from severe depreciation and fluctuation.⁷⁵ However, one positive effect of this currency crisis has been the increased exports from the Asian countries as the result of Asian currencies' lower product cost compared with that of the

⁷² *Id.* at 145; According to one estimate, sales of gray-market goods totaled \$6 billion in 1984. *see* Boyer, *The Assault on the Right to Buy Cheap Imports*, FORTUNE, Jan 7, 1985, at 89.

⁷³ *See* Malueg & Schwartz, *supra* note 70, at 1.; and also *see* John S. Chard & C.J. Mellor, *Intellectual Property Rights and Parallel Imports*, 12 WORLD ECON. 69-83 (1989) (explaining that initially in the early 1980s, the large differences in exchange rates between the U.S. dollar and other currencies resulted in price differentials that highly motivated importers to import parallel goods into the U.S.)

⁷⁴ *See* TIMOTHY H. HIEBERT, PARALLEL IMPORTATION IN U.S. TRADEMARK LAW 3 (1994) (pointing out that the exchange fluctuations also affect the price of product. Currency fluctuation is a sensitive issue. Thus a price list should be updated or reviewed quarterly. The quarterly new price list in each distribution zone can deal with the exchange fluctuation problem.)

dollar.⁷⁶ As a result of Asia's crisis, Asian countries reduced their importation of foreign goods and increased the exportation of cheaply priced goods into developed countries, widening the trade gap in their favor.⁷⁷ A further consequence, being the increase in parallel imports is a direct result of these currency fluctuations and economic crisis. This benefits U.S. consumers in terms of low price⁷⁸ because in order to compete with parallel imports domestic companies have to hold down their prices and have less ability to raise prices of their domestic goods, making obtaining a profit more difficult⁷⁹

C. Basic Arguments by Proponents and Opponents of Parallel Imports

1. Consumer Welfare

1.1 Proponents of Parallel Imports

There are two basic arguments that favor parallel imports based on consumer welfare interests. One focuses on price and the other on selection. The basic argument is that parallel imports reduce anti-competitive practices by intellectual property owners, which in turn benefits consumer by providing better prices and greater selection. Parallel imports offer consumers alternative choices in products and pricing.

⁷⁵ In case of Thailand, the Government had encountered a currency crisis by attempting to maintain an exchange rate pegged to the U.S. dollar. However, it did not succeed and the Government had to change its strategy by using the floating currency system, which caused the severe depreciation in the currency.

⁷⁶ The foreigner can purchase a larger quantity of goods at the same amount of money. In almost all Asian nations after the economic crisis, governments tried to increase exportation, reduce importation, and give incentive to foreign investors.

⁷⁷ See Louis Uchitelle, *International Business: On Asian Crisis Balance Sheet, Credits and Debits for the U.S.*, N.Y. TIMES, Jan. 30, 1998, at A1.

⁷⁸ For example, as a result of lower prices, the U.S. Consumer might prefer to buy gray market goods, such as Sony camcorders from Japan, Hyundai automobiles from South Korea, sneakers from Malaysia and other Asian goods.

⁷⁹ See Richard W. Stevenson & David E. Sanger, *U.S. Braces for Wider Trade Gaps and New Confrontations*, NY TIMES, Dec. 20, 1997, at D1.

Proponents for parallel imports argue that restrictions on parallel imports benefit only the intellectual property owners and contribute nothing to society's economic welfare.⁸⁰ Restrictions on parallel imports facilitate the charging of different prices for the same goods in different markets. The different pricing provides for maximizing profit in each national market.⁸¹ The developing nations assert that parallel imports benefit consumers both in developing and developed nations by enhancing competition, decreasing prices and increasing options for consumers. Parallel imports provide beneficial price competition that may lead to lower prices for consumer. In other words, parallel imports can play an important role in neutralizing price discrimination by providing beneficial price competition.⁸²

⁸⁰ See Feli Martinez, Competition Policy and TRIPs: Background Note, Sept. 2001, at 2, available at <http://www.ceps.be/Pubs/2001/Trips.pdf>. (visited Mar. 19, 2002 (explaining that under Adam Smith's tenet, "the pursuit of self-interest results in the maximization of society's economic welfare provided it is tempered by a competitive market."))

⁸¹ See Robert J. Staaf, *The International Gray Market: The Nexus of Vertical Restraints, Discrimination and Foreign Law*, 19 U. MIAMI INTER-AM. L. REV. 37, 71-78 (1987) (pointing out that the international price difference takes place when manufacturers' ability to control markets price and output differ in each nation's market. The demand elasticity in each nations market is different. From economic perspective, the manufactures create price differences when they have the ability to fully control both a product's quantity and a product' price in a market with less demand elasticity, and few choices for substitute goods are available. Under the law of demand, the consumers will respond to an increase in a product's price by buying less of that product and will respond to a decline in a product's price by buying more of that product. In some products, if consumers are quite unresponsive to price change or to a higher price, demand in such products is said to be inelastic. On the other hand, if consumers are highly responsive to price changes, demand in such products is elastic. If demand is highly inelastic or less elastic, it means that the producers in such products have monopoly power in the market.)

⁸² See Darren E. Donnelly, *Parallel Trade and International Harmonization of the Exhaustion of the Rights Doctrine*, 13 SANTA CLARA COMPUTER & HIGH TECH. L.J. 445, 501-03 (1997) (explaining that because of monopolistic price discrimination, the price of products will be different among markets. Parallel imports serve to keep the competition healthy and prevent discriminatory or monopolistic pricing. For example, in comparison with Spain, product demand in the United States is insensitive to price change. Monopoly pricing implies that the price of products would be higher in the U.S., creating the opportunity for parallel trade and parallel imports.); and also see Tom G. Palmer, *Intellectual Property: A Non-Posnerian Law and Economics Approach*, in INTELLECTUAL PROPERTY: MORAL, LEGAL, AND INTERNATIONAL DILEMMAS 180 (Adam D. Moore ed., 1997) (pointing out that in order to reach utilitarian result, the legal regime should maximize net utility by balancing off the welfare gain from innovations induced by intellectual property rights against the welfare losses resulting from the restrictions on the dissemination of such innovations.); According to the norm of utility maximization, Judge Richard Posner offers "wealth maximization" and "[t]he basic function of law in an economic or wealth-maximization perspective is to alter incentives." In

Furthermore, consumers also benefit from a greater selection of products and in turn the greater product competition leads to greater price competition.⁸³ Consumers in every country can benefit from parallel imports. When there is an insufficient product supply such as pharmaceutical products, the availability of parallel imports offers consumers a greater variety of choices. The free trade restrictions prohibiting parallel imports harm consumers because it limits the purchasing options of the consumers.

1.2 Opponents of Parallel Imports

Opponents of parallel imports, however, argue that the benefit to consumers that this phenomenon can produce is limited to consumers only in certain markets. Although consumers in markets where relatively high prices are charged for goods containing intellectual property may benefit from parallel imports, consumers in other developing countries may not realize such benefits.⁸⁴

area of copyright, Judge Posner explains “to what extent the principal features of copyright law can be explained as devices for promoting an efficient allocation of resources” and show that “the principle legal doctrines are reasonable efforts to maximize the benefits from creating additional works minus both the losses from limiting access and the costs of administering and enforcing copyright protection.” *See id.*, citing in Posner, *Economics of Justice*, 75, and in W.M. Landes & R. Posner, *An Economic Analysis of Copyright Law*, J. LEGAL STUD. 17 (1989).

⁸³See Fogel, *supra* note 64, at 333 and 335. (explaining that the consumer benefits from a greater selection of products, because the consumer is able to buy the product that more closely fulfills his material needs, and greater product competition leads to greater price competition.); see Megeed A. Ragab & G. Andrew Gostlow, *When Business Strategy and the Law are in Conflict: The Case of Parallel Importation in Canadian Border Communities*, in *INTERNATIONAL TRADE AND INTELLECTUAL PROPERTY: THE RESEARCH FOR A BALANCED SYSTEM* 9-13 (George R. Stewart et al. eds., 1994) (mentioning that gray market impacts on business and financial performance -impact on sales, profitability, and cost- and on business practices -impact on buying, product quality, product line scope, pricing policies and price levels, employment, and on bankruptcies); and also see Frederick M. Abbott, *First Report (Final) to the Committee on International Trade Law of the International Law Association on the Subject of Parallel Importation*, 1 J.INT’L ECON.L.607, 612-613 (1998). [hereinafter Abbott, *First Report*]

⁸⁴See Donnelly, *supra* note 82, at 502-5. (pointing out that consumers in poor countries may be harmed if parallel trade is allowed and producers’ response results in the closing of market.); see Malueg & Schwartz, *supra* note 70, at 17-20. (proposing that the intellectual property owners should be permitted to engaging in international price discrimination. Allowing parallel imports may adversely affect developing countries as a

Developed nations contend that price disparity and international market segmentation cause positive economic effects to consumers because manufacturers adjust prices according to consumers' ability to pay. Consumers in developing countries can purchase products with lower and more affordable prices than those in developed countries. So the price disparity and market segmentation not only maximizes profit for the owner of IPRs, but also maximizes benefit for the consumers. A maximum return from intellectual property in each national market is necessary to offset investment costs so that continued creation and innovation is encouraged. This is especially true in the pharmaceutical industry.

Moreover, allowing parallel imports may lead to an overall increase in the price of intellectual property product.⁸⁵ Intellectual property owners in developed countries may choose not to market their products in developing countries or sell it with higher price. Firms from developed countries may not license to manufactures in some developing

result of manufacturers or licensors in developed countries enable to establish price differential. They may raise the price in developing countries or decide not to sell in such countries.); and also see Abbott, *First Report*, *supra* note 83, at 620. (critiquing on the study of Malueg and Schwartz and concluding that this study is incorrect. This study neglects the broader effects of international price discrimination on the international allocation of resources. This study focuses only on the assumption that a monopolist such as the producers of a patented pharmaceutical contributes to the welfare of developing countries in terms of lower prices and does not consider the impact of an international price discrimination on developing countries and consumers acting outside the field of the monopolist's product.)

⁸⁵ See INGE GOVAERE, *THE USE AND ABUSE OF INTELLECTUAL PROPERTY RIGHTS IN E.C. LAW* 80 (1996) (pointing out that although setting the prices based on supply and demand in different markets encourages parallel imports, the IPRs owner could maintain the revenue from his work by "setting higher prices on the first sale, and/or by charging higher license royalties, to make up for the potential losses due to parallel importations, or to prevent parallel importation from being at all beneficial."); and also see V. Korah, *The Limitations of Copyright and patent by the Rules for the Free Movement of Goods in the European Common Market*, 7 CASE W. RES. J. INT'L L. 18 (1982).; and also see Donnelly, *supra* note 82, at 502-5. (explaining that if the IPRs owners choose not to take risks from parallel import by selling only in developed nations with high price, consumers in developing nations will lose their opportunity to access intellectual property goods and have limited choices for selecting goods.)

countries for fear of parallel imports, which will deprive developing countries of foreign direct investment as a means of technology transfer.⁸⁶

The opponent also asserts that allowing parallel imports may eliminate or damage adequate quality control and availability of local maintenance service and support, causing consumer dissatisfaction.⁸⁷ Parallel importers may not provide or indeed be able to provide local service and maintenance after the sale. When compared with domestic goods, parallel import goods may have lower than expected quality that may cause confusion for the consumers. Due to the low quality and the lack of local support and service for parallel imports, consumers may not have a good impression of the products and the owner of the IPRs, the domestic manufacturer and the local distributor may have their reputation damaged.

1.3 Evaluation

In my opinion, consumers would benefit from both lower prices and greater product availability by allowing parallel imports. Parallel imports protect local consumers against artificially high prices through increased domestic competition that can force manufactures to price products reasonably. The intellectual property owners already

⁸⁶ See S.K. Verma, *TRIPS-Development and Transfer of Technology*, 27 IIC 31, 353 (1996) (commenting that this idea is wrong because the decision for licensing technology are based on the production costs, currency margin, import restrictions or duties, technical infrastructure, investment climate, economic, political and other considerations rather than concerning on parallel imports.)

⁸⁷ See Knoll, *supra* note 64, at 168-69. (explaining that an inferior-quality product cause consumer confusion and diminish the reputation of IPRs owner and manufactures. There are two ways in which low quality gray market goods emerge: (1) improper care during importation results in a low quality goods; or (2) the quality of foreign goods differs from the domestic goods. The parallel importer does not have the same incentive to incur the cost associated with proper handling as the trademark owner and authorized distributor. Consumer confusion reduces the value of trademark, which is seen as an indication of the

obtain a profit from pricing their products differently in each market. Therefore, there is no reason to curb parallel imports.

Under the maximizing of profit rule, if the IPRs owners decide not to sell in some developing countries, they will lose out on profits from markets such as China, or India with huge numbers of potential consumers. Moreover, if such goods are really necessary to the developing country, a middleman or a parallel importer will certainly try to import such goods into that market to make a profit. In such instances, the intellectual property owner in a developed country loses all potential profits in that market.

Indeed, the argument regarding the low quality of parallel imports is weak if all intellectual property products in every nation are produced and controlled under the same standard. In addition, under an antitrust perspective, hampering parallel imports allows the intellectual property owners to engage in monopolistic price discrimination. There is a comment that the price difference also results from local goodwill. In my opinion, the price difference results mainly from monopolistic market power rather than the local goodwill since most goods that are sold internationally conform generally to the same standard along with its international goodwill.

2.Free Riding

2.1 Opponents of parallel Imports

From an economic approach, the IPRs protection system has been constituted as the result of public goods and non-exclusive characteristic of idea and intellectual

source and/or quality of the goods.); and also see *Osawa & Co. v. B & H Photo*, 589 F. Supp. 1163, 1172-73 (S.D.N.Y. 1984)

property products.⁸⁸ Owners of intellectual property invest a great deal of time, effort, and money to create a new product. However, the cost of copying the work may be low. If everyone was allowed to copy freely, there would be very few original works since the author or inventors would have no financial incentive to invest. There is a trade-off between consumer interest and the need for intellectual property.⁸⁹ Free riding takes place when an individual enjoys benefits of intellectual property product without paying.⁹⁰ The parallel importers arbitrage and take advantage on price differentials by importing goods from low-priced markets to high-priced markets.⁹¹

Arguably it is unfair for parallel importers to derive free benefit from the creators' investments. The intellectual property owners invest tremendous time, money and effort to create the new intellectual property works. Society as a whole is better off when an intellectual property work is created, exploited and distributed.⁹² Opponents of parallel imports assert that parallel imports are free riding and increase the risk on creator's investment return and diminish the attractiveness of investment. This argument is based

⁸⁸ See Martinez, *supra* note 80, at 1.

⁸⁹ *Id.* at 2. (pointing out that there are two possible ways to solve this conflict of interest. Firstly, the state should directly finance the production of intellectual property works, allowing the consumer to pay only the marginal cost of physical reproduction. Secondly, the state should legislate intellectual property laws to grant the exclusive rights to intellectual property owners in order to prevent unauthorized copy or use.)

⁹⁰ See JACK HIRSHLEIFER, PRICE THEORY AND APPLICATIONS 561-65 (2d ed., 1980) (explaining and discussing the free-rider problem)

⁹¹ *Id.* (pointing out that with free riding the price differential is a result of different levels of investment, whereas with arbitrage the price difference is result of price discrimination.); see Knoll, *supra* note 64, at 159.; and also see Martinez, *supra* note 80, at 3. (considering parallel imports as a market failure in production and not distribution. There should be free distribution of intellectual property products without restrictions unless a specific failure arises.)

⁹² See Janet H. MacLaughlin, Timothy J. Richards, & Leigh A. Kenny, The Economic Significance of Piracy, in INTELLECTUAL PROPERTY RIGHTS, GLOBAL CONSENSUS, GLOBAL CONFLICT? 101 (R. Michael Gadbaw & Timothy J. Richards eds., 1988)(mentioning that IPRs protection provides investors with an economic incentive to finance innovative activity and eliminates some investment risk for investors.)

on the economic concept of free riding.⁹³ In the area of trademarks, parallel imports are free riding on the trademark owner's reputation. The goodwill associated with a trademark will depend on the amount of the investment and effectiveness of that investment. Therefore, the level of goodwill in two separate markets is not the same.⁹⁴

Intellectual property owners make investment that creates the premium for an intellectual property product, whereas the parallel importer captures the premium without making any investment.⁹⁵ The intellectual property owners intend to arbitrage for investment return in order to offset expenditures, but the phenomenon of free riding may jeopardize the return on investment.

⁹³ See James Boyle, *Taking Stock: The Law and Economics of Intellectual Property Rights: Cruel, Mean, or Lavish? Economic Analysis, Price Discrimination and Digital Intellectual Property*, 53 VAND.L.REV. 2007, 2012-2015 (2000) (explaining that information or knowledge are public goods when no current user possesses any less or greater right than consumption by any other user. Public goods are characterized by admitting more than one user, with no user's consumption requiring any less consumption by any other user. In particular, public goods suffer from free riders, or non-paying consumers who attempt to gain access to public goods provided at some cost by others. But when intangible information or knowledge is protected by intellectual property law, it is no longer public goods. However, the extension of the intellectual property system such as new media (Internet) bring intellectual property content even closer to the image of the perfect public goods, because costless copying and global distribution.)

⁹⁴ See Knoll, *supra* note 64, at 160-61 and 64. (explaining that the likewise trademark will be associated with the same level of goodwill in other countries to convince the public that the product maintains a constant level of quality. In addition, parallel imports are free riding on services. The domestic distributors, wholesalers, or retailers provide services incur the associated costs, but parallel importers do not provide the same service. If the former cannot possibly exclude consumers who do not purchase from them, a discounter can undercut the authorized dealers while benefiting from the services they provide. Such discounters certainly take a free ride on the service of the authorized dealers.)

⁹⁵ For example, in case of trademark, the trademark protection provides incentives to develop new products by preserving the trademark owner's ability to obtain economic rewards for his investment in developing the product and in establishing the goodwill of his trademark. These investment costs can be substantial and consist of the costs of developing the product, providing warranty services, and promoting the product, including brand advertising. See J. THOMAS MCCARTHY, TRADEMARKS AND UNFAIR COMPETITION § 2:1 (2d ed. Supp. 1989) and also see Knoll, *supra* note 64, at 157-58 and 162-63; see Staff, *supra* note 81, at 37. (stating "a price premium over and above the costs of production, including a normal profit, can create incentives for firms to produce high quality products. This price premise represents the return to brand name (trademark) capital investments... Special capital investment simultaneously serve to insure market performance of quality assurance claim... The price premium or specific quality assuring capital investments for any goods depends on a number of factors. The more frequently a product is purchased, the less quality assurance capital required, because consumers can discipline a deceptive seller more quickly. Once decision is made, trademark capital is subject to risk of changing market conditions. Finally, prices of trademark goods and, therefore, the quality assurance premise, are limited by competition.")

There is no guarantee that investment in an intellectual property product will ensure market success or that it will be profitable. However, if the product is successful in a market, then it becomes a target for piracy and parallel imports. Such free riding adds to the risk of investment and diminishes the attractiveness of investment. As a result of free riding, future product development is diminished because the manufacturer declines to develop new lines of the product. Allowing parallel imports reduce the benefit and incentive for intellectual property innovation, especially in the pharmaceutical industry because of the very high research and development costs.⁹⁶

2.2 Proponents of Parallel Imports

Proponents of parallel imports argue that unlike piracy, parallel importation does not constitute free riding because a price has been paid for the goods. There is no empirical evidence to conclude that the initial purchase price is insufficient to encourage continued investment. In addition, parallel importation decreases piracy. Indeed, allowing parallel import may actually discourage true free riding in the form of piracy by giving consumers a legal option to gain access to products that they desire.

In fact, parallel imports do not represent classic free riding because importers have already paid a full price for the gray market goods. The intellectual property owners receive their royalty fee and profit from the first sale. Allowing intellectual property

⁹⁶ This is especially true in patent products such as pharmaceuticals, where significant investment is put into the initial material costs associated with the experimentation and development of a new product. To get intellectual protection, they have to hire the lawyer to register the copyright, patent, and trademark. Finally, after successfully inventing a new product, the product has to be approved by a government agent before the product is distributed in marketplace. All stages of this process are time consuming and very costly.

owners to bar parallel imports gives a double monopoly to owners of IPRs, which is not in the public interest and conflicts with the concept of the protection of IPRs. The exclusive right over the production and first distribution of the intellectual property product should be enough to reward intellectual property investment. It is not necessary to extend an exclusive right to the further distribution of products. Extending the right over further distribution is inconsistent with the concept of competitive markets and constitutes an inefficient allocation of resources.⁹⁷

In addition, the proponents argue that free riding in piracy and in parallel importation is different. Piracy involves counterfeit goods, whereas parallel imports are legitimate goods where the intellectual property owner has already received a royalty. Indeed, gray market may actually discourage the more extreme and damaging form of pirate free riding. Parallel imports can also serve to prevent or reduce the counterfeit market or black market by fulfilling the demand of low-income markets. Therefore, the free riding effects of parallel imports are not as tremendous as piracy.

Some scholars commented that “parallel imports are driven not so much by free riding on promotional efforts of authorized distributors, but by international price discrimination.”⁹⁸ Although free riding is an important issue of parallel imports in some upscale industries such as perfumes, price discrimination was an essential factor in many

⁹⁷ See Martinez, *supra* note 80, at 2

⁹⁸ See Malueg & Schwartz, *supra* note 70, at 2; “The assumption that, if legally permitted, parallel imports would mandate a uniform price across all market embodies two ingredients. First, consumers view parallel imports as perfect substitutes for authorized goods. Second, the supply of parallel imports would be perfectly elastic.” *Id.* at 3.

industries such as automobiles, camera, or ski equipment.⁹⁹ On the whole, parallel imports occur because of international price discrimination, rather than free riding.¹⁰⁰

2.3 Evaluation

In my opinion, parallel imports do not represent a classical form of free riding and the negative effects are less than those of piracy. Parallel imports reduce the volume of piracy because the gray market goods fulfill the demand of low-income markets. Moreover, free riding in parallel importation has a less dramatic effect among developing and least-developed countries than among developed and developing countries. For example, the free ride on the price differences between the United States' market and Thailand's market differs from those between Thailand's market and India's market because the price difference between Thailand's price and India's price is much smaller than price difference between Thailand's price and the United States' price.

Moreover, parallel imports primarily result from international price differences and not free riding. If there was no price discrimination and all products were priced uniformly, parallel importers would not have enough incentive to purchase the products from lower price markets for importation and sale into higher price markets. It is not necessary to completely maximize the economic return for owners of IPRs in order to maintain a reasonable incentive for further intellectual property development.¹⁰¹

⁹⁹ *Id.* at 5-6; and also see David G. Tarr, An Economic Analysis of Gray Market Imports, Federal Trade Commission, September 25, 1985.

¹⁰⁰ See Martinez, *supra* note 80, at 3. (pointing out that parallel imports are actually a market failure in production not distribution; thus the assumption should be allowing the free distribution of intellectual property products without restrictions unless arising of a specific failure.)

¹⁰¹ It is important to concern whether the maintaining of reasonable incentive for producers on intellectual property based products really requires the maximization of their economic return to achieve through the

3. Free trade

3.1 Proponents of Parallel Imports

In general, free trade or trade liberalization is advantageous to all nations, producers, and consumers.¹⁰² A neo-classicism perceptive considers trade a “source of enrichment” and that international exchange can be a source of enrichment rather than impoverishment.¹⁰³ Welfare gains are maximized through the flow of goods across boundaries. Free trade enhances national welfare by encouraging specialization. Free movement of goods produced efficiency in the allocation and distribution of resources and goods.¹⁰⁴ Parallel imports play an important role in manipulating international resource allocation among nations.

effective system of price discrimination and prohibiting parallel import. It is necessary for assumption that prohibiting parallel import and squeezing the last dollar from customers' pocket do not ensure the incentive and support investment. Moreover, excluding free rider from access to public goods like intellectual property products by means of a legal mechanism is extremely costly and of doubtful social value because the free rider does not impose a direct cost on either creators or consumers.

¹⁰² See Malueg & Schwartz, *supra* note 70, at 20. (explaining the free trade and concluding that “the world welfare would be improved by “encouraging unrestricted parallel import in order to undermine price discrimination.” Free trade bestows many benefits to the average person. Those countries that lower trade barriers and open their markets enjoy higher economic standards of living. Consumers have access to a wider range of higher quality products at prices lower than they would otherwise pay. The average person also benefits in terms of wages and job opportunities. While there are inevitable short-term transition costs in some sectors of the economy, the long-term benefits of free trade for all far outweigh such costs. The producers take benefit from free trade by increasing in import and export transaction among nations. Imports raise real compensation by keeping prices down, stimulating domestic competition, and increasing more jobs.)

¹⁰³ See DAVID GREENAWAY & CHRIS MILNER, TRADE AND INDUSTRIAL POLICY IN DEVELOPING COUNTRIES, 50-55(1993) (explaining that the source of enrichment is argued to be static gain from inter-industry exchange, dynamic gains from inter-industry exchange and gains from intra-industry exchange. Macroeconomic policy is directed at influencing the overall level of economic activity in the economy by focusing on the rate of growth of national income, the level of unemployment, the rate of exchange of prices and aggregate payments balance. On the contrary, microeconomic policy is primarily concerned with influencing the allocation of resources across activities-the balance between industry and agriculture. Social policy is essentially concerned with the distribution of resources between individuals and groups. In national policy, the government of developing countries identify appropriate activities to promote or encourage import or export based on legitimate interest and comparative advantages.)

¹⁰⁴ See Barton, *supra* note 11, at 473 and 487. (mentioning that in relation to free trade theory, for ‘normal’ products, each nation will be better off with free trade. The reason is that the price of goods will “equalize closest to their lowest marginal cost, minimizing consumer cost.” Although IPRs protection is essential to

Under the concept of globalization and free trade, the world is considered one market with different levels, as in society. Nation members are classified into a high (the richest with high education and technology), middle, and low (the poorest with low education and minimal technology). Generally there are two significant groups of members; developed countries such as the United States, the United Kingdom, and Japan and developing countries such as China, Thailand, and India. Free trade promotes a mutually profitable division of labor, greatly enhances the potential real national products of all nations, and makes possible higher standards of living all over the world.¹⁰⁵ When developed countries invest in developing countries, developing countries benefit from the transfer of advanced technology and knowledge. The foreign investment also decreases the amount of unemployment and increase the standard of living. On the other hand, developed countries benefit from the low cost of labor and the raw materials available in the developing countries, which in turn help reduce the cost of production and the overall product price.

Based on the fundamental trade-off among nations, free trade promotes global economic growth and also encourages the technology transfer from developed nations to developing nations. Promoting free trade by reducing tariffs and eliminating non-tariff

motivate innovation and creativity, the intellectual property rights increase the product price away from the lowest marginal cost that causes an economic misallocation. The question is "whether the intellectual property right produces a favorable trade-off between the short-term cost to consumers through higher prices and long-term benefit to consumers through increased innovation." Of course, there are different perspective between developed and developing nations in discussion of costs and benefits.) The author in this article supports price discrimination and opposes global exhaustion doctrine for intellectual property rights, and suggests that this doctrine "should be applied only to the goods that are genuinely information intensive-this can be applied in terms of the intellectual property right protected and the share of the product value that is constituted by information." *See Id.* at 495. In my opinion, parallel import may actually play a balancing role to reduce the price increases and conflicts between (1) the short-term benefit and long-term benefit, (2) perspective of developed and developing nations and (3) price discrimination and global exhaustion doctrine).

barriers decreases importation costs and supports parallel imports. The supporters of parallel importation argue that impeding the importation of gray market goods would create a non-tariff barrier that is inconsistent with the free trade principle.¹⁰⁶ Intellectual property rights protection should not itself become a barrier to legitimate trade. Proponents argue that the resulting flow of parallel imports would force market competition efficiencies envisioned by the free trade principle driving GATT and its WTO.¹⁰⁷ In other words, the effect of parallel imports would certainly match the objectives for international free trade supported by GATT.¹⁰⁸ In brief, the main rational assumption is that the policies of free movement of goods and free trade are in keeping with parallel import activities. Therefore, parallel imports should be allowed.

3.2 Opponents of Parallel Imports

The prohibition of parallel imports does not totally impede free trade. Consumers are able to buy products from authorized local distributors and the importers are also able

¹⁰⁵ See PAUL A. SAMUELSON, *ECONOMICS* 692 (9th ed. 1973).

¹⁰⁶ See Dam, *Trademarks, Price Discrimination, and the Bureau of Customs*, 7 J.L. & ECON. 45 (1964) (pointing out that hampering the importation of gray market goods would produce a barrier between two markets and allows the intellectual property owner to engage in monopolistic price discrimination.)

¹⁰⁷ Practically, intellectual property rights can be used to divide markets. The exhaustion doctrine limits the right of intellectual property owner to divide markets either domestically or internationally, depending upon whether a national exhaustion doctrine or an international exhaustion doctrine is applied.; see Barton, *supra* note 9, at 492. (mentioning that “national exhaustion attempts to give an IIP producer a larger rent, while global exhaustion doctrine attempts to facilitate trade and permit a flow of parallel imports.)

¹⁰⁸ See Document ATRIP/GVA/99/6 “Parallel Imports and International Trade” presented at the Annual Meeting of the International Association for the Advancement of Teaching and Research in Intellectual Property (ATRIP) at headquarters of WIPO in Geneva (July 7 to 9, 1999) at 8, *available at* http://www.wipo.org/sme/en/ip_busi...xport/international_exhaustion.htm. (visited Dec 6, 2001); see WILLIAMS, *supra* note 47, at 152.(explaining that the role of GATT is to facilitate trade liberalization and the expansion of trade. Liberal theorists assert that GATT provides an economic climate generally conducive to trade liberalization that in turn has contributed to the expansion and growth of the world economy. On the contrary, many economists argues that GATT was irrelevant to the reductions in trade barriers that have taken place, and that liberal theorists have exaggerated the extent of actual liberalization.)

to import those products by asking for the consent of the intellectual property owner. The restriction on the free movement of goods is out weighed by concerns over product integrity. There are many reasons to support that it is necessary for the IPRs owners to exercise their rights against parallel imports, although such prohibition might obstruct the concepts of free trade and free movement of goods. Many gray market goods are inferior or different when compared with domestic goods. The IPRs owners should be entitled to bar parallel imports because the difference in the goods destroys their reputation and adversely affects on the further sale of domestic products.¹⁰⁹

3.3 Evaluation

One scholar commenting on free trade theory indicated that the world would be better off with free trade since the price of goods will “equalize closest to their lowest marginal cost, minimizing consumer cost” and that the IPRs protection increases product price away from “the lowest marginal cost, creating an economic misallocation.” but it is essential to motivate innovation and creativity.¹¹⁰ Consequently, in my opinion, based on that rationale, if it is true that the protection of IPRs increases the price of products and creates an economic misallocation, it is not beneficial to give an overriding right to the owner of the IPRs to prohibit parallel imports. In other words, prohibiting parallel imports increase economic misallocation; thus parallel imports should be allowed, as they

¹⁰⁹ See Knoll, *supra* note 64, at 168-71.; The inferior-quality gray market goods “not only redirect the premium away from the trademark owner, but also injure the trademark owner’s goodwill, reducing the expected future stream of returns that flow from the trademark.” *Id.* at 168.

¹¹⁰ See Barton, *supra* note 11, at 487.

play an important economic role by reducing misallocation as a result of providing the IPRs protection.

In my opinion, the main purpose of encouraging the free trade and free movement of goods is to eliminate tariff and non-tariff barriers, which distort free competition in the global market. Any exercise of IPRs under the guise of protecting the integrity of domestic goods from parallel imports that is actually intended to inhibit free trade and free competition should be forbidden. However, the IPRs owners should be entitled to exercise their rights against parallel imports only if such exercise of rights complies with the intended purpose of IPRs protection because encouraging free trade without concern for the exclusive rights of the IPRs owner works to distort the purpose of IPRs protection.

On the downside, free trade does create distortion. The unqualified application of a universal free trade principle may actually detract from the global economic development that free trade is designed to promote. Although developing countries can capitalize on low labor and material costs in addition to low legal and environmental standards in order to draw investment, the developed countries derive the greater benefit. The developing nations sometimes lose their benefit in a free trade system because of low economic power and low technology capability. The developing countries have to import the new technology from developed countries at a price higher than its exports to the developed countries. Most new technology products incorporate IPRs, which mainly belong to citizens of developed countries, not developing countries. Due to an imbalance in economic power, developing countries should consolidate their negotiation power in the international free trade arena in order to gain more trade leverage in area of IPRs protection, particularly the idea of liberalizing parallel imports.

CHAPTER TWO

LEGAL ASPECTS OF INTELLECTUAL PROPERTY TO PARALLEL IMPORTS

I. INTRODUCTION

Issues concerning parallel imports always involve intellectual property rights (IPRs) protection because goods are protected under the trademark, copyright, or patent laws. The intellectual property owners have exclusive rights, particularly the right to control the circulation of intellectual property products and to take benefits from their innovation, creation, and investment. Due to the promotion on free trade and free movement of goods principles as mentioned in the previous chapter goods are readily moved from country to country and from region to region facilitating parallel import activities around the world.

Parallel imports are considered one of the most important issues because of the numerous disagreements among countries, which until now cannot be resolved at the multilateral negotiation. In terms of intellectual property issues, there is a conflict or inconsistency between developed and developing countries in relation to implementation of the principle of exhaustion of intellectual property rights to parallel imported goods. Despite developed nations such as the United States, the European Union, or Japan realize that it is necessary to eliminate or at least reduce the inconsistencies by

harmonizing the intellectual property laws under the multilateral agreements. However, there is no international legal standard in the case of exhaustion doctrine and up to now no solution to the scope and application of exhaustion doctrine has been put forward. Hence, this chapter will explain and discuss the implementation of exhaustion doctrine in both the international agreements and national laws that should be useful for determining a suitable solution in conclusion.

To analyze parallel import issues, it is very important to look at the issue at both the international and national level. Therefore, Part II will describe and expand on international treaty provisions, whilst Part III will discuss the North-South divergent perspectives, specifically on the subject of parallel imports and exhaustion doctrine. Finally, Part IV and Part V will concentrate on how developed and developing countries respectively deal with parallel imports.

II. INTERNATIONAL TREATY PROVISIONS

There are many international treaties in the area of the IPRs protection. The purposes of these multinational agreements are to strengthen the protection of the IPRs and to harmonize different intellectual property regimes throughout the world. Parallel imports are examples of the non-harmonizing subject matters as a result of an inherent tension between the free movement of goods principle and the exercise of intellectual property rights. The following section will focus on whether the issues of parallel imports, particularly in the application of the exhaustion doctrine, are solved or even

dealt with in the Paris Convention, the Berne Convention, the WTO treaties, and the TRIPs Agreement.

A. Paris Convention

The Paris Convention for the Protection of Industrial Property¹¹¹ was designed to protect industrial property, namely patents, utility models, industrial designs or models, trademarks, service marks, trade names, and indications of source.¹¹² The purpose of the Paris Convention was to eliminate discrimination at the national level by requiring the member nations to provide equal treatment to the foreign IPRs owners the same rights and protections as provided to its own citizens,¹¹³ which was known as the Principle of National Treatment. In addition, under the territorial principle and independence principle, “a patent granted in a Convention country for a given invention is independent of patents for the same invention in any other country.”¹¹⁴ However, many scholars criticized the Paris Convention and figured that there were many weaknesses in terms of national treatment principle and the enforcement of protection of IPRs.¹¹⁵ The Paris Convention provides inadequate national treatment to patent protection,¹¹⁶ and inadequate enforcement mechanisms by requiring disputes to be settled by the International Court of

¹¹¹ Paris Convention for the Protection of Industrial Property, July 14, 1976, 21 U.S.T. 1583, 828 U.N.T.S. 305 [hereinafter Paris Convention].

¹¹² Only the patent and trademark excluding copyright are mainly concentrated in the Paris Convention.

¹¹³ See Paris Convention, *supra* note 111, art.2(1).

¹¹⁴ See *Id.* art.4.

¹¹⁵ See Laurinda L. Hicks & James R. Holbein, *Convergence of National Intellectual Property Norms In International Trading Agreements*, 12 AM.U. J.INT’L L. & POL’Y 769, 779 (1997).

¹¹⁶ See Robert J. Pechman, *Seeking Multilateral Protection for Intellectual Property: The United States “TRIPS” over Special 301*, 7 MINN. J. GLOBAL TRADE 179, 181-82 (1998) (explaining that under the national treatment protection, if a country such as developing country does not provide intellectual property protection for its citizens, the foreigners should be treated the same and does not protected in such nation.)

Justice (ICJ),¹¹⁷ and does not provide specific measures for the actual enforcement of intellectual property rights.

After carefully examining the Paris Convention, there was neither the provision of the exhaustion doctrine nor the issue of parallel imports was addressed. Nevertheless, according to the principle of territoriality of patents in Article 4 bis, there is an argument based on the principle that a patent in one member nation could not be exhausted because the products incorporating such patent were marketed in another member nation. Such an argument is wrong and misinterpreted Article 4 bis both in intention and wording. Article 4 bis is inherently “concerned with the existence of a domestic patent right, while the exhaustion doctrine is concerned with acts that exhausted further economic exploitation with regard to specific goods marketed under a patent.”¹¹⁸ Therefore, one can conclude that the Paris Convention was obviously silent on the issue of parallel imports.

B. Berne Convention

The Berne Convention, signed on September 9, 1886 and implemented on December 5, 1887,¹¹⁹ is regarded as the major agreement on international copyright in which many nations participated as members of the Berne Union. It was the first multilateral copyright treaty to protect literary and artistic works embracing a wide range

¹¹⁷ See *id.* at 182.

¹¹⁸ See Christopher Heath, *Parallel Imports and International Trade*, 28 IIC 623, 628 (1997).

¹¹⁹ Berne Convention for the Protection of Literary and Artistic Works, Sept. 9, 1886, 168 Consol T.S. 185, revised Nov. 13, 1908, 1 L.N.T.S. 218, revised June 2, 1920, 123 L.N.T.S. 233, revised June 26, 1948, 331 U.N.T.S. 217, revised July 14, 1967, 828 U.N.T.S. 221 [hereinafter Berne Convention].

of works, but excluding sound recordings.¹²⁰ The Berne Convention provided for the broad exclusive rights of the copyright owner¹²¹ and further denotes the protection of moral right.¹²² The Berne Convention signatories are obliged to protect literary and artistic works over the life of the author plus a further fifty-year period.¹²³

Where both the Paris Convention and the Berne Convention provided the national treatment, only the Berne Convention added a minimum standard of protection that progressively constituted the strength and harmonization of copyright protection in the global society. Nevertheless, there are many loopholes in the Berne Convention. For example, the Berne Convention has no provision for the enforcement of copyrights and for the settlement of copyright disputes. In addition, producers of sound recordings were not protected against copyright infringement under this convention.¹²⁴

Under Article 12 of the Berne Convention, the definition of “infringing copy” only prohibited the importation of copies made illegally in the country of manufacture and extended to reproduction from countries where the work is not protected.¹²⁵ There is no obligation to prohibit parallel imports from countries where the work is protected in accordance with the Berne Convention. Moreover, although the Berne Convention

¹²⁰ Although the Berne Convention did not cover sound recordings, the WIPO Performers and Phonograms Treaty as another international treaty recognized the rights of phonogram producer in reproduction of sound recording.

¹²¹ The Berne Convention enumerate seven economic rights enjoyed by an author: right of translation, right of reproduction, right of public performance, right of communication to the public of a performance, broadcasting and related rights, right of adaptation, arrangement and other alteration and right of renewal.

¹²² See TRIPs, *supra* note 3, art.9. Article 9 incorporates the Berne Convention’s provisions as the standard of copyright protection but exceptes the protection of moral right.

¹²³ Berne Convention, *supra* note 119, art. 7(1).

¹²⁴ See Frank Romano, *Global Trademark and Copyright 1998: Protecting Intellectual Property Rights in the International Marketplace*, in INTERNATIONAL CONVENTIONS AND TREATIES, 545, 553 (1998).

¹²⁵ Berne Convention, *supra* note 119, art.16. Article 16 states:

“Infringing copies of work shall be liable to seizure by the competent authorities of any country of the Union where the work enjoys legal protection.

provides the broad exclusive rights of the copyright owner, it does not mention the right of importation. Like the Paris Convention, the Berne Convention was silent on the issues of parallel imports and did not give any mention to the exhaustion of rights principle. However, according to the principle of national treatment, the foreign copyright owner enjoys the same rights as the national copyright owner. The extent of protection shall be governed exclusively by the laws of the country where protection is claimed.¹²⁶ Therefore, the answer to those parallel imports issues including the application of exhaustion doctrine varies greatly depending on each national copyright law.

C. WIPO Treaties

The World Intellectual Property Organization (WIPO), a specialized agency of the United Nations is responsible for taking action in promoting creative intellectual activity and facilitating the transfer of technology to developing countries in order to accelerate their economic, social and cultural development.¹²⁷ Its purpose is to promote the protection of IPRs throughout the world,¹²⁸ monitor adherence to the various international conventions and treaties, and generally strengthen the international

In these countries the seizure shall also apply to reproductions coming from a country where the work is not protected, or has ceased to be protected....”

¹²⁶ See *id.* art. 5.2. Article 5.2 of the Berne Convention specifies that the enjoyment and the exercise of these rights shall not be subject to any formality; such enjoyment and such exercise shall be independent of the existence of protection in the country of origin of the work.

¹²⁷ See The World Intellectual Property Organization (WIPO), available at <http://www.wipo.int>; The WIPO is an intergovernment organization established by a Convention signed at Stockholm on July 14, 1967 and entered into force in 1970. ; see Convention Establish the World Intellectual Property Organization, July 14, 1967, 21 U.S.T. 1749, 1771, 828 U.N.T.S. 3.

¹²⁸ *Id.*

protection of IPRs.¹²⁹ Although the WIPO's treaties cover in many significant types of IPRs, the WIPO's treaties are frequently critiqued as being too ambiguous and providing inadequate IPRs protection.¹³⁰ Many developing countries do not regulated by WIPO because they are not members of the Paris Convention.¹³¹ The WIPO has a weak enforcement mechanism and a weak dispute settlement mechanism.¹³²

In relation to the exhaustion doctrine, the WIPO Treaties 1996 (The WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty) do not include a right to prevent parallel imports and leave Contracting Parties based on their interest to opt for national, regional or international exhaustion doctrines.¹³³ The WIPO Treaties fail to clarify the scope of exhaustion doctrine whether it should be national or international.

¹²⁹ The major task of WIPO is initially responsible for the administration and enforcement of the Paris Convention and the Berne Convention. Later, there are many main unions and treaties administered by WIPO besides the Paris Union, the Berne Union such as the Madrid Union, the Rome Convention, the Washington Treaty, the Madrid Protocol, and the International Union for the Protection of Plants. See Madrid Agreement Concerning the International Registration of Marks, Apr. 14, 1891, 828 U.N.T.S. 389.; Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organizations, Oct. 26, 1961, 12 U.S.T. 2377; Treaty on Intellectual Property in Respect of Integrated Circuits, 28 I.L.M. 1477 (1989); Protocol Relating to the Madrid Agreement Concerning the International Registration of Marks, adopted June 27, 1989, WIPO Pub. No. 204(E); and see International Convention for the Protection of New Varieties of Plants, Dec. 2, 1961, 815 U.N.T.S. 89

¹³⁰ See Monique L. Cordary, *GATT v. WIPO*, J. PAT. & TRADEMARK OFF. SOC'Y, 122 (1994).

¹³¹ See Faryan Andrew Afifi, Comment, *Unifying International Patent Protection: The World Intellectual Property Organization Must Coordinate Regional Patent Systems*, 15 LOY. L.A. INT'L & COMP. L.J. 453, 456 (1993).

¹³² See Pechman, *supra* note 116, at 182-3.(pointing out that in developed nations' perspective, the WIPO is unable to sanction violators and the provisions covering legal remedies are vague. The WIPO dispute settlement mechanism has been called "effectively worthless" because it relies on the voluntary cooperation of the party receiving the unfavorable ruling in enforcement.); see Romano, *supra* note 14, at 555.; and also see Evelyn Su, Comment, *The Winners and The Losers: The Agreement on Trade-Related Aspects of Intellectual Property Rights and Its Effects on Developing Countries*, 23 HOUS. J. INT'L L. 169, 184 (2000).

¹³³ See The WIPO Copyright Treaty 1996 Article 6 and the WIPO Performances and Phonograms Treaty 1996 Article 8 (performances) and 12 (phonograms). The text of the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty is available at <http://www.wipo.org> ; Both the WIPO Copyright Treaty and Performances and Phonograms Treaty allow Contracting Parties to decide upon their interest whether apply national or international exhaustion doctrine. In other words, both treaties give the freedom to Contracting Parties to decide in the issue of exhaustion doctrine. For example, Article 6 (2) of the WIPO Copyright Treaty provides " Nothing in this Treaty shall affect the freedom of Contracting Parties to determine the conditions, if any, under which the exhaustion of the right in paragraph (1) applies after the first sale or other transfer of ownership of the original or a copy of work with the authorization of

D. TRIPS AGREEMENT

As recognized by all member nations, the TRIPs Agreement is the most significant multinational agreement in the area of intellectual property.¹³⁴ Basically, the TRIPs Agreement did not essentially create a new regulation for intellectual property but rather refers to the Berne Convention for the protection of literary and artistic works, as well as the Paris Convention for the protection of industrial property.¹³⁵ However, the TRIPs Agreement provides more effective and rigorous protection of the IPRs. For example, to reduce the volume of infringement activities, the TRIPs Agreement not only adds the right of importation to be one of the exclusive rights of intellectual property owners, but also provides the enforcement measure through the dispute settlement mechanism and border measures. Under the TRIPs Agreement, if the goods are considered infringement goods, the IPRs owner can stop such importation at the border, a so-called the border measure. The TRIPs Agreement requires that WTO member countries adopt a border measure.¹³⁶ Under the border measure, the holder of IPRs who

the author.”; and also see JORG REINBOHE & SILKE VON LEWINSKI, *THE WIPO TREATIES 1996: THE WIPO COPYRIGHT TREATY AND THE WIPO PERFORMANCES AND PHONOGRAMS TREATY COMMENTARY AND LEGAL ANALYSIS* 80-87, 317-23 and 347 (2001).

¹³⁴ The TRIPs Agreement is categorized as a multilateral agreement under the WTO; therefore, any country desires to participate the WTO have to agree to abide by the TRIPs Agreement. Recently, there are many countries joined in the WTO and the TRIPs Agreement including the United States, the United Kingdom, and Japan. See World Trade Organization, *The Organization Members*, available at <http://www.wto.org/english/thewtoe/whatise/tife/org6e.htm> (visited Mar. 16, 2002).

¹³⁵ See TRIPs, *supra* note 3, art. 2 and 9; In addition, the TRIPs Agreement covers eight types of intellectual property: copyright and related rights, trademarks, geographical indicators, industrial design, patents, layout-designs of integrated circuits, trade secrets, and contractual licenses. The TRIPs Agreement outlines the minimum standards of substantive protections in each type, which the national member has to provide in their national law. See *Id.* art. 9-40.

¹³⁶ The United States also adopt the boarder measure that appear in Tariff Act of 1930 19 U.S.C. §1337(a) by filing a complaint with the International Trade Commission. To stop the importation of goods infringing copyright, the U.S. Customs has authorized under the Section 602 and 603 of the copyright law. Under Section 603(a), the Customs has power to “make regulations for the enforcement of the provisions of this title prohibiting importation.” For trademark, the Customs relies on provisions in the customs laws and the trademark law for stopping the importation of goods infringing trademark. See 15 U.S.C. §1051-1128); see

suspects that the importation of counterfeit trademark¹³⁷ or pirated copyright goods¹³⁸ make take place can submit an application with administrative or judicial authorities for suspending the release of such goods into the market by customs authorities.¹³⁹ On the other hand, the WTO member countries do not have any obligation to prohibit the importation of parallel import goods. The WTO member countries need not adopt the border measure for “goods put on the market in another country by or with the consent of the right holder”.¹⁴⁰ However, the TRIPs Agreement is not silent in the exhaustion doctrine relating to the issue of parallel imports.

In the TRIPs Agreement, the introduction of Article 6 provides that “ for the purposes of dispute settlement under this Agreement,...nothing in this Agreement shall be used to address the issue of the exhaustion of intellectual property rights.” This means that the TRIPs Agreement keeps the issue of exhaustion doctrine out of the dispute settlement mechanism. In other words, this means that whatever national, regional or international exhaustion doctrine was adopted by a member, another member cannot claim or bring the case on ground of violation of the TRIPs Agreement.¹⁴¹ Thus, member nations are free to apply their own approach in the application of exhaustion doctrine. Although the TRIPs Agreement does not specifically require members to allow or

Timothy P. Trainer, *Intellectual Property Protection Along Foreign Borders*, 21 AIPLA O.J. 313, 315-17 and 326 (1993) (mentioning that the U.S. intellectual property owners will benefit from the application of Special 301 to impose other developing nations and the use of boarder enforcement against the importation and exportation of infringing goods.); and also see TIMOTHY P. TRAINER, *BOARDER ENFORCEMENT OF INTELLECTUAL PROPERTY* (1999) (providing many interesting information not only on the customs enforcement in the areas of trademark, copyright, semiconductor chips, and patent in the United States but also on the multilateral and regional border measures.)

¹³⁷ See TRIPs, *supra* note 3, art. 51, n14(a) (providing a definition of “ counterfeit trademark goods”)

¹³⁸ See *id.*, art. 51, n14(b) (providing a definition of “pirated copyright goods”)

¹³⁹ See *id.* art. 51.

¹⁴⁰ *Id.* art. 51 n 13.

prohibit parallel imports, the legitimate intellectual property goods should be able to move freely among members in order to comply with GATT principles.¹⁴²

There is clearly no worldwide consensus about the exhaustion doctrine. The TRIPs Agreement carefully circumvents this issue by keeping the issue of exhaustion doctrine out of the dispute settlement mechanism.¹⁴³ Unfortunately, the TRIPs Agreement fails to deal with the issue of the exhaustion doctrine. Recently, the exhaustion of IPRs principle has become more uncertain and ambiguous in the international Community. This failure confronts the policy stated in the TRIPs preamble "...desiring to reduce distortions and impediments to international trade, and taking into account the need to promote effective and adequate protection of intellectual property rights." Because of different perspective among member states, the exhaustion doctrine is applied using various approaches. Lack of international harmonization in terms of the exhaustion doctrine guarantees that the free trade and free movement of goods policy will be challenged with this uncertainty. Thus the following section will discuss and concentrate on the north-south divergent perspective in the application of exhaustion doctrine.

¹⁴¹ See CARLOS M. CORREA, INTELLECTUAL PROPERTY RIGHTS, THE WTO AND DEVELOPING COUNTRIES: THE TRIPS AGREEMENT AND POLICY OPTION 83 (2000).

¹⁴² The result of prohibiting parallel imports is similar to establishing a non-tariff barrier, the typical impediment to free trade, because it creates a barrier at the border of importation. See *supra* note 6-9 for more detail and discussion.

¹⁴³ See DUNCAN MATTHEWS, GLOBALISING INTELLECTUAL PROPERTY RIGHTS: THE TRIPS AGREEMENT 48-49 (2002); and also see GERVAIS, *supra* note 44, at art.6. (providing the draft history of TRIPs Agreement); The former intellectual property agreements, such as the Paris Convention and the Berne Convention, do not touch upon this issue at all. The reason is that legislation and jurisprudence on parallel import issue is varied from country to country, with countries taking different positions on exhaustion of right in patents, copyrights and trademarks. For example, parallel imports of patented goods, including pharmaceuticals, are permitted in many developing countries. On the other hand, the U.S. has policy to prohibit parallel imports.

III. NORTH-SOUTH DIVERGENT PERSPECTIVE ON EXHAUSTION DOCTRINE

The difference of fundamental concepts between industrialized or developed countries (known as North) and developing countries (known as South) caused a dramatic conflict in respect to the IPRs protection. There are many development gaps between the North and South countries, especially in social services and physical health.¹⁴⁴ Those differences have an effect on the perceptions of developed and developing countries in many areas particularly in the field of intellectual property protection.

From the perspective of developed nations, the IPRs protection is very important for fair competition in a free trade market. The prevailing theory of the IPRs protection seems to be essentially based on the reward theory, which encourages inventors to create new work that will be beneficial to the world.¹⁴⁵ Additionally the notion of natural right has been used to convince the world Community to protect the IPRs.¹⁴⁶ The natural right theory has been asserted as the strategy of industry groups dominated by multinational corporations (MNCs) to convince their governments in developed countries to demand adequate protection of IPRs in the GATT negotiation.¹⁴⁷ The protection of IPRs plays an

¹⁴⁴ See Su, *supra* note 132, at 196, citing in THOMAS D. LAIRSON & DAVID SKIDMORE, INTERNATIONAL POLITICAL ECONOMY: THE STRUGGLE FOR POWER AND WEALTH 181 and 184 (1993).

¹⁴⁵ See WARD S. BOWMAN, JR., PATENT AND ANTITRUST LAW: A LEGAL AND ECONOMIC APPRAISAL 15-32 (1973) (explaining that under the reward theory, the state offers a time-limited monopoly right as a reward to offset and to induce inventors to invent the new invention. The reward theory has been applied as an economic theory.)

¹⁴⁶ See LAWRENCE C. BECKER, PROPERTY RIGHTS PHILOSOPHIC FOUNDATIONS 24 -56 (1977) (explaining that there are two reasons for the natural rights justifications for patents. One is the first occupancy thesis; the person who discovers or creates an invention should be entitled morally to its exclusive use. The other thesis is a labor justification for natural right. It is based on the doctrine that the person who expends labor in creating intellectual property should be morally entitled to the fruits of that labor.)

¹⁴⁷ See Paul C. B. Liu, *U.S. Industry's Influence on Intellectual Property Negotiations and Special 301 Action*, 13 UCLA PAC. BASIN L.J. 87 (1994) (describing that the multinational corporations desire the

important role in the promotion of technological progress. The long-term trend in the developed countries has headed in the direction of strengthening and upward harmonizing of the protection of IPRs.¹⁴⁸ The United States is encouraging developing countries to strengthen the protection of IPRs for their own benefits,¹⁴⁹ based on the strong conviction that a higher level of IPRs protection increases foreign direct investment.¹⁵⁰ Economists in industrialized countries recognize that there is a short-term loss of developing countries from enhancement of the protection of IPRs in the form of lost revenues from pirated goods and the reallocation of resources. The economists, however, contend that these losses will be compensated by the long-term benefits of foreign direct investment and technology transfer.¹⁵¹

On the contrary, from the viewpoint of the developing countries, the TRIPs Agreement almost closes the door for developing countries to get access to technology and consequently discourages the diffusion of new technology that developing countries

adequate protection of IPRs in developing countries, particularly in the area of patent since the infringements take place pervasively around the world especially in countries where that invention was not patented or even not patentable under the developing nation's law.)

¹⁴⁸See Carlos A. Primo Braga & Carsten Fink, *The Economic Justification for the Grant of Intellectual Property Rights: Patterns of Convergence and Conflict*, 72 CHI.-KENT L. REV. 439, 443 (1996).

¹⁴⁹See INTELLECTUAL PROPERTY RIGHTS: GLOBAL CONSENSUS, GLOBAL CONFLICT 20-21 (R.M. Gadbaw & T. Richards eds., 1988) (explaining that in the trademark area, trademark protection in developing countries will increase the local introduction of new foreign discoveries and the diffusion of information necessary to make consumer markets function efficiently by permitting consumers to make educated choices about goods of varying quality. In the copyright area, enhanced intellectual property protection stimulates local innovation and the flow of ideas from abroad.)

¹⁵⁰See Su, *supra* note 132, at 209, citing in Edwin Mansfield, Intellectual Property Protection, Direct Investment, and Technology Transfer 2 (International Finance Corporation Discussion Paper No. 27, 1995)

¹⁵¹See MacLaughlin, Richard & Kenny, *The Economic Significance of Piracy*, in INTELLECTUAL PROPERTY RIGHTS: GLOBAL CONSENSUS, GLOBAL CONFLICT 89-91 and 97-108 (R.M. Gadbaw & T. Richards eds., 1988) (pointing out that while not empirically substantiated, industrialized country economists argue that increased levels of intellectual property protection will produce a variety of short and long term benefits for developing countries. The increased levels of patent protection will: (1) encourage technology transfers and investment from the industrialized economies to the developing economies by providing an hospitable environment; (2) stimulate local innovation and technology infrastructures -by providing an environment in which local innovators are encouraged both to create and share their creation; (3) encourage domestic

need to improve economic growth.¹⁵² The protection of IPRs is considered a benefit to the industrialized nations at the expense of the developing nations.¹⁵³ The protection of IPRs does not reflect the interest of the developing countries, which perceive the protection of IPRs as a method of transferring money from the developing countries to the developed countries through the form of rent transfer.¹⁵⁴ Particularly, in a case of patent protection, although patents are commonly considered by the developing countries as the facilitation of the technology transfer, they are also simultaneously considered an impediment for the developing countries to access new technology at a low cost. Indeed, the protection and enforcement of IPRs should contribute to the promotion of technological innovation, to the transfer and dissemination of technology, to the mutual advantage of producers and users of technological knowledge and in a manner conducive to social and economic welfare, and to a balance of rights and obligations.¹⁵⁵ The TRIPs Agreement was concerned with an element of “technological protectionism” policy, which tended to strengthen an international division of labor; thereby the North countries create innovations, whilst the South countries are the market for those intellectual property products.¹⁵⁶

investment in local technology-based industries; and (4) promote exports by opening markets otherwise closed to those manufacturing without authorization.)

¹⁵² See Su, *supra* note 132, at 171.

¹⁵³ See Leaffer, *supra* note 8, at 275.; and see Carlos A. Primo Braga, *The Economics of Intellectual Property Rights and the GATT: A View from the South*, 22 VAND. J. TRANSNAT'L L. 243, 252 (1989).

¹⁵⁴ See Jean M. Dettmann, *GATT: An Opportunity for an Intellectual Property Rights Solution*, 4 TRANSNAT'L LAW. 347, 368-70(1991); Frederick M. Abbott, *The WTO TRIPs Agreement and Global Economic Development*, 72 CHI.-KENT L. REV. 382, 392 (1996); and also see Braga & Fink, *supra* note 148, at 443.

¹⁵⁵ See TRIPs, *supra* note 3, at prmb. (emphasis added).

¹⁵⁶ See CORREA, *supra* note 143, at 5.(mentioning that the aggressive policy by U.S. industries establish international rules that counter their declining competitive positions in world markets.)

Recently, there is a conflict between the developed and developing countries over the issue of parallel imports. This issue presents the inherent tension between the free movement of goods principle and the protection of the IPRs in relation to the exhaustion doctrine. It is very important to clarify on the North-South debate on the exhaustion of intellectual property rights. The exhaustion of IPRs is one of the controversial issues taking place from the interface between the protection of the IPRs and the free movement of goods and services. Relating to the application of exhaustion doctrine, there is discrepancy between the developed and developing countries in the scope of the exhaustion doctrine, which divides the world in two and constitutes a non-harmonized situation.¹⁵⁷

Most developed or industrial countries, especially the United States, adopt a national exhaustion doctrine and prohibit parallel imports. However, Member States of the European Union have adopted a regional exhaustion doctrine known as a Community-wide exhaustion.¹⁵⁸ Nevertheless the application of a Community-wide exhaustion is still based on the concept of a national exhaustion doctrine. Based on the national exhaustion doctrine, the owners of IPRs can bar parallel imports from a foreign market and guarantee their benefits or royalties from the market segmentation and price difference. The developed nations assert that applying the international exhaustion causes a serious deterrent for international companies licensing and distributing their products

¹⁵⁷ See Yusuf, *supra* note 52, at 18. (stating "The lack of a TRIPs regulation of the exhaustion of IPRs may be ascribed to the absence of consensus among the Member States as to the most appropriate manner to deal with this issue. The exhaustion of IPRs is one of the issues that have traditionally divided the developed and the developing countries. The former usually prefer and apply in their domestic legislation a territorial exhaustion of IPRs, while the latter subscribe to the more liberal international exhaustion of rights.")

¹⁵⁸ The detail and discussion on a Community-wide exhaustion will be explained later in the European Union section.

aboard.¹⁵⁹ Liberalizing parallel imports may not only reduce the profit of the owners of IPRs and the incentive to create the new work, but can also lead to an increase in the price in the low-income market, eventually harming consumers. However, some developed countries such as Japan, Australia and New Zealand, conversely apply the international exhaustion doctrine and allow parallel imports for the benefit of consumers and the support of free trade.

Developing nations, such as Thailand, Hong Kong, Brazil, India and South Africa, adopt an international exhaustion doctrine and allow parallel imports. Based on the concept that the exhaustion doctrine defines the limits of the IPRs,¹⁶⁰ developing nations recognize that liberalizing parallel imports may economically reduce or prevent the monopoly power of the owners of the IPRs in setting up the market segmentation and price discrimination on the national, regional or international scale to maximize their profits. As a result of permitting parallel imports, the consumers may benefit from low prices as well as the increased selection and availability of products in the market.¹⁶¹ In particular, consumers would be able to purchase necessities such as certain pharmaceutical products at lower prices.¹⁶²

Moreover, the international exhaustion doctrine potentially supports the TRIPS Agreement as it is more consistent with the GATT legal framework as well as with the

¹⁵⁹ See Kremen, *supra* note 6, at 163.

¹⁶⁰ See S.K. Verma, *Exhaustion of Intellectual Property Rights and Free Trade-Article 6 of the TRIPS Agreement*, 29 IIC 534, 537 (1998). [hereinafter Verma, *Exhaustion of IPRS and Free Trade*] (mentioning that the issue of exhaustion doctrine is “not a contract issue, but is a doctrine which defines the limits of the intellectual property right itself.”)

¹⁶¹ See Chapter one: The Basic Argument on Parallel Imports in Consumer Welfare.

¹⁶² See Carlos M. Correa, *Public Health and Patent Legislation in Developing Countries*, 3 TUL. J. TECH. & INTELL. PROP. 1, 38 (2001). [hereinafter Correa, *Public Health*]

liberalization of international trade.¹⁶³ In this light, the national exhaustion may be considered anti-competitive and in conflict with the GATT and TRIPs Agreement initiatives¹⁶⁴ because under this doctrine, the owners of the IPRs owner can prohibit parallel imports and divide the markets, eventually impeding the free movement of goods. Thus, allowing parallel imports of genuine goods by applying the international exhaustion doctrine shall “promote free trade, encourage competition and exert a salutary pressure for price leveling.”¹⁶⁵ Therefore, the international exhaustion of IPRs would be incorporated in a future revision of the TRIPs Agreement in order to bring it into “full conformity with the ideals of free trade underpinning the GATT.”¹⁶⁶

Many North-South conflicts of interest in the IPRs protection have been solved by providing an international legal standard in the TRIPs Agreement. However, the TRIPs Agreement does not regulate the exhaustion of IPRs and leaves it entirely to the Member States to regulate in its own style. Therefore, the following parts will describe how the developed and developing countries apply an exhaustion doctrine in the case of parallel imports under their own perspectives, which lead to a discrepancy at the global level. The inconsistent rules on parallel imports effectively impede the free movement of goods. The study of each country’s approach is absolutely useful for designing a harmonious measure for the application of exhaustion doctrine.

¹⁶³ *Id.*; and also see CORREA, *supra* note 143, at 81-88. (pointing out that the application of international exhaustion doctrine is consistent with the purposes of the TRIPs Agreement to the mutual advantage of producers and users of technological knowledge under Article 7.)

¹⁶⁴ See Hanns Ullrich, *Technology Protection According to TRIPS: Principles and Problems*, in FROM GATT TO TRIPS-THE AGREEMENT ON TRADE-RELATED ASPECTS OF INTELLECTUAL PROPERTY RIGHTS 357, 384 (Beier & Schricker eds., 1996)

¹⁶⁵ See Yusuf, *supra* note 52, at 18.

¹⁶⁶ *Id.*

IV. DEVELOPED NATIONS

As mentioned earlier in the discussion on the conflict between the developed and developing countries, this part will describe and analyze the issue of parallel imports and the application of the exhaustion doctrine from the developed nations' perspective. The United States, the European Union, and Japan were selected to represent the perspective of developed nations.

A. The United States

1. Introduction

The United States, the world's largest economy, provides a strong IPRs protection to inventors and creators. Its policy focuses on both domestic and international protection in order to influence global intellectual property safeguards. The United States has realized that the U.S. intellectual property owners lose a lot of profit from the counterfeiting and piracy in developing countries such as China, Thailand, India, and Brazil. Therefore, the expansive scope of the United States' protection of domestic and international IPRs is seen by the U.S. as necessary to address the other countries' inadequate protection of IPRs. The U.S. responded to the issue of inadequate protection of IPRs through a variety of domestic and international actions¹⁶⁷ because it believes that

¹⁶⁷Due to the United States' strong economic and political power, the U.S. can directly and indirectly force other countries, especially developing nations, to amend their intellectual property laws in the way that satisfies the United States' requirement. The U.S. government has undertaken efforts to strengthen worldwide protection of intellectual property through bilateral consultations with other countries and multilateral forum such as the General Agreement on Tariffs and Trade (GATT) and the World Trade Organization (WTO). Moreover, in response to the inadequate protection of IPRs in other countries, Congress moved to strengthen actions taken under Section 337 of the Tariff Act of 1990 -19 U.S.C. section 1337 (1988)- and created the Super Section 301 and Special 301 actions.

the lack of adequate protection of IPRs leads to trade distortions, the impairment of concessions, and the creation of non-tariff barriers.¹⁶⁸

As a world leader, many U.S. legal perspectives have been recognized as the international legal standard in many areas, particularly the intellectual property law. In the World Trade Organization (WTO) forum, the U.S. is recognized as a significant policy maker with the power to control and make policy in IPRs protection on the TRIPs Agreement through the WTO conference. Therefore, studying how the U.S. deals with parallel imports is very important because the U.S. perspective potentially influences other nations in international negotiations and may possibly become the international legal standard.

The issue of parallel imports can be analyzed and classified by relying on three types of protection of the IPRs: trademark, copyright, and patent laws. It is necessary to separate a discussion of parallel imports into three parts because the court decisions for each type of IPRs are different as they are based upon the economic and fundamental principles of each classification. Therefore, the following sections will explain and analyze the parallel import issues by separating them into three parts.

2. Parallel Imports in Trademark

Most parallel import cases in the United States involve trademark law because this law deals closely with the distribution of products, territorial restrictions on distribution channels, and consumer confusion. The United States courts did not initially

¹⁶⁸ See *U.S. Framework Proposal To GATT Concerning Intellectual Property Rights*, 4 INT'L TRADE REP. (BNA) 1371 (Nov. 4, 1987).

restrict parallel imports based on the concepts of a universality principle, two purposes of trademark protection, and the exhaustion doctrine. Later, parallel imports were treated restrictively, based on the notions of a territorial principal, and a protection of the U.S. business's benefits and local goodwill. Recently, trademark owners may use both the Trademark Act and the Tariff Act, including Customs Regulations, to bar parallel imports. In other words, the U.S. present policy allows the trademark owner to prevent the importation of parallel import goods under trademark law. The transportation of parallel import goods can be halted at the border before entering U.S. territory. The following paragraphs will illustrate the movement of court decisions from a less restrictive perspective in the past to a more restrictive perspective at present.

Before getting to the court decisions, it is important to clarify the concept of trademarks. Trademarks serve various commercial functions, such as identification for the goods or services and as identification of source and quality of the goods or services. As an incentive for trademark owners to develop new products, trademark protection preserves the trademark owner's right to obtain the economic rewards for his investments and prevents consumer confusion.¹⁶⁹ Thus, a trademark is an instrument of consumer protection against public deception about a product brand's source, quality, and goodwill.¹⁷⁰ Moreover, trademark protection has emerged to prevent unfair competition from those who use or imitate other people's trademarks that may cause consumer confusion as well as damage the reputations and economic profits of the trademark

¹⁶⁹See Brain W. Peterman, *The Gray Market Solution: An Allocation of Economic Rights*, 28 TEX. INT'L L.J. 159, 171(1993).; and also see J. THOMAS MCCARTHY, 1 TRADEMARKS AND UNFAIR COMPETITION § 2:1 (2d ed. Supp. 1989).

owners.¹⁷¹ The trademark law has a twofold purpose as in the court clarification of *Amoskeag Manufacturing Co. v. Spear*¹⁷² that trademark protects investors, promotes competition and prevents public deception; by false representation, the defendant commits “a fraud upon the public, and upon the true owner of the trade-mark.”¹⁷³

In order to take legal action in the early days, trademark protection was based on common law with the concept of passing off.¹⁷⁴ Until 1946, the Congress enacted the Trademark Act, known as the Lanham Act, to create a federal trademark system and registration of trademarks.¹⁷⁵ At present, there are two principal causes of action in trademark lawsuits: a common law in passing off and a statute law in infringement of a registered trademark. The trademark owners can sue any person who uses their trademark without consent as trademark infringement claim or passing off claim.¹⁷⁶ In relation to

¹⁷⁰ See ROTHNIE, *supra* note 24, at 10; and also see C. Fernandez-Novoa, *In Defense of the Trademark System*, 77 PAT. & TRADEMARK REV. 435, 444 -45 (1979) (explaining that goodwill is something intangible, which exists only in the mind of the purchasing public, yet has an economic value.)

¹⁷¹ See The American Law Institute, *The Restatement of The Law (Third), Unfair Competition* (Chapter 1. The Freedom to Compete); and also see Unfair Competition Act Section 1 General Principles.

¹⁷² See *Amoskeag Manufacturing Co. v. Spear*, 2 Sand. Super. 599 (N.Y. City Super. Ct. 1849).

¹⁷³ *Id.* at 607.; This notion is also affirmed by the same court in *Gillot v. Kettle*. See *Gillott v. Kettle*, 3 Duer 624 (N.Y. City Super. Ct. 1854) at 626. (The Court states: “The fraud, to the extent that it may be successful, is twofold: The public is defrauded by being induced to buy the inferior for the superior article. The plaintiff is defrauded by an unjust destruction of confidence, that his pens are put up for sale, and assorted with reference to the quality...”)

¹⁷⁴ See ROTHNIE, *supra* note 24, at 14. (explaining that passing off, as common law emerges independently of statute, protect a trader’s proprietary interest in the goodwill generated in a market by his business activities in association with name or mark.)

¹⁷⁵ See *id.* at 10-13. (explaining that in the case of registered trademarks, the trademark owners have the exclusive right to use the trademark for the purpose of indicating a connection in the course of trade with the goods or services offered.)

¹⁷⁶ Recently, the passing off action is strictly brought under Section 43 of the Lanham; thus these differences between passing off action and registered trademark action are not tremendous. See Lori H. Freedman, *Reverse Passing Off: A Great Deal Of Confusion*, Vol. 83 TMR, 305 (1993) (mentioning that the U.S. courts apply the traditional passing off analysis when considering the trademark infringement under Section 43.); Unlike the United States, in the Anglo-Commonwealth countries such as The United Kingdom, Australia, and New Zealand, their courts more focused on the issues of passing off. See *Revlon Inc. v. Cripps & Lee Ltd* [1980] FSR 85; *Champagne Heidsieck et Cie Monopole S.A. v. Scotto and Bishop* (1926) 43 RPC 101; *Colgate-Palmolive v. Markwell Finance* [1989] RPC 497; and also see Daniel Alexander, ‘*Colgate-Palmolive v. Markwell Finance-The Carving Knife Sharpened*, [1989] EIPR 456.

parallel imports, there are three relevant sections in the Lanham Act, sections 32(1), 42, and 43.¹⁷⁷

For the first U.S. parallel imports case, *Apollinaris Co. v. Scherer*, Judge Wallace's decision was based on a twofold purpose concept, an exhaustion doctrine and the principle of universality.¹⁷⁸ The plaintiff sought to block the unauthorized parallel imports, but the Court rejected to issue the preliminary injunction on ground that "the defendant is selling the genuine water...the trademark is not infringed."¹⁷⁹ Therefore, there is no harm for the public in source deception. The Court also referred to the indivisibility of world trademark based on the principle of universality.¹⁸⁰ There were many cases following the *Apollinaries* opinion that as long as the parallel import goods are genuine goods and there is no public deception, the parallel importer is not liable for trademark infringement. Further examples would be *Vistacope Co. v. United States*

¹⁷⁷ See 15 U.S.C. 1124 (1988) Lanham Act § 32, 42 and 43. Section 32(1) provides the general remedy for infringement in using trademark in commerce of any reproduction, counterfeit, copy or colorable imitation of a registered trademark, which makes consumers confuse. Section 42 states specifically for importation of products bearing marks, which copy or simulate registered trademark, enabling the registered owner of the trademark to request to Customs to seize such products at the boarder. Finally, Section 43 applies to both registered and unregistered trademarks by barring the importation of products that breach Section 43(a) providing civil liability against making false advertisements or representations, including origin, in connection with goods.

¹⁷⁸ See *Apollinaris Co. v. Scherer* 27 F. 18 (C.C.S.D.N.Y. 1886) (From the facts, the plaintiff was the exclusive distributor of bottled water in the United States and Britain under the trademark "Hunyadi Janos". Amdreas Saxlehner, the owner of this trademark, continued to market his bottled water in the continental Europe but with a notice on the label stating that this bottled water was not intended for export and that importation into the United States and Britain was prohibited. The defendant, as the third party, obtained the bottled water from dealers in Germany and sold it in the U.S. at a low price designed to compete with the plaintiff's product.); and see the British parallel import case in *Apollinairs Co. v. Snook* for comparing with the *Apollinairs* case in the United States. The British Judges mainly focus on the rights of the registered trademark and parallel importer, more than the interests of the consumer and public. See HIEBERT, *supra* note 74, at 32-34.

¹⁷⁹ *Id.* at 20.

¹⁸⁰ *Id.* at 21; see HIEBERT, *supra* note 74, at 29-32.

Phonograph Co., Russia Cement Co. v. Frauenhar, and Fred Gretsches Manufacturing Co. v. Schoening.¹⁸¹

Nevertheless, in *Bourjois v. Katzel*, the District Court did not follow the former cases instead concentrating on the investment and effort of plaintiff to create a reputation or goodwill in the domestic market. The Court stated that “it appears that plaintiff has built up, not only an extensive and important business, but also an excellent business reputation for the character of its goods.”¹⁸² Because both the proprietary goodwill (the “extensive and important business”) and the psychological goodwill (the “excellent business reputation”) belong to the U.S. company,¹⁸³ the court distinguishes this case from the previous cases. The court focused on the plaintiff’s investment and the incentive for U.S. business to invest in foreign trademarked goods. The district court also upheld that the proof of the parallel importer’s fraud and loss of the plaintiff’s sales were not prerequisites for trademark infringement and decided in favor of the plaintiff. Later the Appeal Court in *Bourjois & Co. v. Katzel*¹⁸⁴ refused the district court’s decision and determined that genuine goods cannot infringe even a registered U.S. trademark. This decision was based on former decisions in the *Apollinairis* and *Gretsches* cases that the courts focused more on the genuine status of parallel import goods and less on the domestic trademark owner’s interest. However, the Appeal Court’s decision was reversed

¹⁸¹ See *Vistacope Co. v. United States Phonograph Co.*, 83 F. 30 (C.C.D.N.J. 1897); *Russia Cement Co. v. Frauenhar*, 133 F.518 (2d Cir. 1904) (The Court stated that if the consumers receives an inferior quality of glue when obtains from defendants as parallel imports because plaintiff had chosen to reap his profit from selling the two qualities or standards of the same product under the same trademark. This case absents other evidences to show other fraud by the defendant.); and *Fred Gretsches manufacturing Co. v. Schoening*, 238 F. 780 (2d Cir. 1916). (The Court of Appeals for the Second Circuit held that section 27 was particularly limited to counterfeit goods and could not be applied to prohibit the importation of genuine goods.)

¹⁸² See *Bourjois & Co. v. Katzel*, 260 U.S. 689, 857 (1923)[hereinafter *Katzel* case]

¹⁸³ See HIEBERT, *supra* note 74, at 45.

¹⁸⁴ See *Bourjois & Co. v. Katzel*, 275 F. 539 (2nd Cir. 1921), rev’d, 260 U.S. 689 (1923).

by the U.S. Supreme Court.¹⁸⁵ The Supreme Court held that the defendant's sale of face powder in the U.S. was an infringement of the U.S. trademark owner's rights, although the defendant's goods were genuine.¹⁸⁶ The Supreme Court relied on the principle of territoriality of trademark and rejected the principle of trademark universality.¹⁸⁷

Before getting the Supreme Court's decision, Congress enacted Section 526 of the Tariff Act of 1922 to "protect the American manufacturer or producer",¹⁸⁸ to obliterate the court of Appeals' decision and to prohibit parallel imports.¹⁸⁹ In brief, after the *Katzel* case, both the Lanham and Tariff Acts generally prohibited parallel imports to protect the domestic trademark owner's right.¹⁹⁰ To implement section 526, the Customs issued regulations made under section 526 to bar parallel imports but introduced three exceptions permitting parallel imports:¹⁹¹

1. The same owner exception: Both the foreign and the U.S. trademark are owned by the same person or business entity. This exception withdrew protection if the same person, partnership, association, or corporation owned both the foreign and domestic trademark rights;

¹⁸⁵ See *Katzel* case, *supra* note 182, at 689.

¹⁸⁶ Many court decisions follow the *Katzel* decision. See *Prestonettes Inc. v. Coty*, 264 U.S. 359 (1924), and *Perry v. American Hecolite Denture Corp.*, 78 F. 2d 556 (8th Cir. 1935).

¹⁸⁷ The *Katzel* case is recognized as the case, which established the territoriality principle of American trademark law since prior to the Supreme Court decision in *Katzel*, many courts had held that there could be no likelihood of confusion in the sale of gray goods because of the university principle of trademarks.; and see SETH E. LIPNER, THE LEGAL AND ECONOMIC ASPECTS OF GRAY MARKET GOODS 18-19 (1990); and also see HIEBERT, *supra* note 74, at 129-42. (discussing on the emergence of territoriality)

¹⁸⁸ See H.R.Rep. No. 1223 at 158; Hiebert, *supra* note 74, at 116; and also see Lipner, *supra* note 187, at 19.

¹⁸⁹ 19 U.S.C. § 1337(a) and §1526 (1988) Tariff Act of 1930; There are two relevant sections on parallel imports: section 337 and 526., which are used as mechanism to bar parallel imports. Section 337 protects the U.S. industry from unfair competition in importation; section 526 states the prohibition of unauthorized importation. However, importation by persons for personal use and not for sale is allowed.)

¹⁹⁰ For example, in *Sturges v. Clark D. Pease Inc.* relying on section 526 of Tariff Act, the Court prohibited importation of car bearing the registered trademark although the car was intended only for the importer's personal use. See *Sturges v. Clark D. Pease Inc.*, 48 F. 2d 1035 (2d Cir. 1931).

¹⁹¹ 19 CFR §133.21(c) (1987).

2. The corporate affiliate or common control exception: The foreign and the domestic trademark owners are parent and subsidiary companies or are otherwise subject to common ownership or control;¹⁹²

3. The authorized use exception: The goods of foreign manufacture bear a trademark applied under authorization of the U.S. owner.

However, there is a concern that these exceptions may be too broad and derogate the enforcement of section 526.¹⁹³ This concern had been stated in the *K Mart* case, which is the most important case after the *Katzel* case. In the *K Mart* case,¹⁹⁴ the Supreme Court upheld the validity of the same owner and the common-control exception but found that the authorized use exception invalid because the Custom's authorized use exception was not a reasonable interpretation of the statutory language.¹⁹⁵

Moreover, there is an interesting court decision in relation to the affiliate or common-control exception in the *Lever* case. In *Lever Brothers Co. v. United States of America*,¹⁹⁶ there are two affiliated corporations, one operating in the United States (hereinafter referred to as Lever U.S.) and one operating in the United Kingdom (hereinafter referred to as Lever U.K.). The plaintiff was the U.S. company that made

¹⁹² In 1972, the Customs' practice and expressly denied protection when the foreign and domestic trademark or trade name owners are parent and subsidiary companies or are otherwise subject to common ownership or control. See 19 C.F.R. sec. 133.21 (c) (1972).

¹⁹³ For example, The Coalition to Preserve the Integrity of American Trademarks (COPIAT), a group of American trademark owners, concern that Section 526 has a more effect to prohibit parallel import and this exceptions derogated from Section 526. COPIAT argued that the regulation was inconsistent with the plain meaning of the words in Section 526 and sought a declaration that it was invalid. See *COPIAT v. United States*, 790 F. 2d 903 (DC Cir. 1986); and also see ROTHNIE, *supra* note 24, at 95-96.

¹⁹⁴ See *K Mart Corporation v. Cartier Inc.*, 486 U.S. 281 (1988).

¹⁹⁵ *Id.* at 293-94. (The court reasoned that Customs Service regulations in both the same person and common-control exception are permissible because they are designed to solve the ambiguous statutory language "owned by" and "merchandise of foreign manufacture." However, those phrases were not deemed ambiguous in regards to the foreign license because the goods are clearly produced by an independent foreign company.)

¹⁹⁶ *Lever Brothers Co. v. United States of America*, 877 F.2d 101 (D.C. Cir. 1989).

Shield soap and Sunlight dishwashing detergent. It had a British affiliate that made products under the same trademark. They used the same words, Shield and Sunlight, as the trademark of product that was different in material. There was a difference in both products to match different consumer tastes. Third parties imported U.K. Shield and U.K. Sunlight without authorization from Lever U.S. and Lever U.K. Therefore, Lever U.S. requested the Customs Service to stop the importation. However, under the affiliate exception, the Customs rejected Lever U.S.'s request since the trademarks were used abroad by an affiliate of Lever US. To stop the importation, Lever sought the preliminary injunction against the Customs Service's decision that relied on the affiliate exception on the ground that it violated section 42 of the Lanham Act. The district court agreed with the Custom interpretation. On the contrary, at the end the Court of Appeal disagreed and stated that under section 42, the U.S. trademark right would not be exhausted by sales of products bearing those marks that differ in terms of material to consumers from those sold in the U.S. The affiliate exception should not be used if there was a likelihood of consumer confusion as a result of different goods with identical trademark.¹⁹⁷

¹⁹⁷*Id.* at 108-09; In the case of parallel imports of second-hand goods, there is a different concept on the matter of difference between used and new goods whether it justify to allow trademark owner to bar such parallel imports of used goods. In the *Gamut Trading* case, by relying upon the difference between Gamut's Kubota-used tractor and Kubota-US's tractors, the Federal Circuit decide that Gumat's tractor were likely damage the goodwill of domestic distributor. However, the Supreme Court in the *Sanders* case decided that consumers of second-hand have lower expectations than those of new goods. So as long as it did not cause passing off, any difference or inferiority between used and new goods is immaterial. See *Gamut Trading Co. v. U.S. International Trade Commission*, 200 F. 3d 775 (Fed. Cir. 1999); *Champion Spark Plug Co. v. Sanders*, 331 U.S. 125, 129-30 (1974); and also see Sean A. Barry, Comment, *Gamut Trading Co. v. U.S. International Trade Commission: Expanding the Gamut of Trademark Protection*, 2 SAN DIEGO INT'L L.J. 209 (2001) (commenting that the Federal Circuit's decision in *Gamut Trading* case is unjustified for expanding trademark protection under the Tariff Act since the court fails to consider that Gamut's tractors were used one if the court take this fact into account, it should not be conclude that there is a material different in this case. In addition, it did not cause the consumer confusion since the customers knew that this goods in question is a second-hand one, not a new one.)

So the Customs Services' regulations can be conclusively separated into three stages by using the *Lever* case as milestone: pre-Lever case, Lever case, and post Lever case respectively. At first, in pre-Lever, the Customs relied on the affiliate exception that allowed parallel import goods if goods are made by the affiliate of the U.S. company. The U.S. trademark owner cannot bar the parallel imports although those goods differ in quality. Later on, as the result of *Lever* decision, the Customs Service interpreted the affiliate exception to distinguish between goods produced abroad that are identical and exhibit no difference from domestic goods and goods produced abroad that are physically and materially different from domestic goods. Section 42 of Lanham Act precluded Customs application of the affiliate exception with respect to the goods with physical and material difference. Finally, in post-Lever regulation, the Customs Service established the guideline for consideration of the condition to identify the physical and material difference. In the guideline, the Customs refers to the specific composition, formulation, product construction, structure, or composite product components, performance and/ or operation characteristics and other distinguishing and explicitly defined factors that cause consumer deception or confusion.¹⁹⁸

In summary, parallel imports are generally prohibited under the Lanham Act and Tariff Act. However, the U.S. trademark owner cannot prohibit parallel imports if such imported goods are manufactured by the same owner or the corporate affiliate of the U.S. trademark owner, unless there are physical and material differences between the domestic goods and the imported goods.

¹⁹⁸ See 19 CFR §133.2 (e).

3. *Parallel Imports in Copyright*

In the area of copyright law, legal scholars considered parallel imports by referring to a conflict between the copyright owners' distribution rights on the one hand and the principle of exhaustion doctrine known as the first sale doctrine, on the other. There is an inevitable connection between the exhaustion doctrine and parallel imports; whether parallel imported products can be freely imported depending upon whether the rights of the copyright owner are exhausted by the first sale of such products. This section will illustrate how the first sale doctrine was developed in the United States and how it is applied to the issue of parallel imports by using a conceptual methodology.

Some parallel import products are entirely copyrighted products such as books, music and movies. These products are clearly protected under the copyright law. Nevertheless, many products are not copyrighted subject matter per se, such as clothes and beauty products. Only some parts of the product such as the label on the packaging can be copyrighted. For example, the products in *L'anza* and *Sebastian* cases¹⁹⁹ were hair care products that were not protected under copyright subject matters, yet the packaging was protected by copyright. A trademark owner with a registered copyright in its product label can attack parallel imports as a copyright infringement. As a result of permissive trademark and tariff laws and Customs' regulations, trademark owners use the importation right under the Copyright Act in section 602(a) as an additional device to bar parallel imports when such parallel imports were permitted under trademark and tariff

¹⁹⁹ In the *Sebastian* case, the court held that the text of the labels on Sebastian's WER and Shpritz Forte products was copyrightable and determined that the copyrights were invalid. See *Sebastian Int'l, Inc. v. Consumer Contacts (PTY) Ltd.*, 664 F. Supp. 909 (D.N.J. 1987), *rev'd on other grounds*, 847 F. 2nd 1093 (3d Cir. 1988).

laws. Moreover, trademark owners prefer to bring the lawsuit under a copyright law more than a trademark law because it is difficult to prove the likelihood of confusion that would be required for trademark infringement.²⁰⁰

Basically, the copyright owner has five exclusive rights: the reproduction right, the right to prepare derivative work, the right to display, the distribution right, and the performance right.²⁰¹ Each of these rights can be subdivided, owned, and enforced separately. In relation to distribution right, section 602(a) provides the importation right to the copyright owner.²⁰² The ownership of copyright is separated from ownership of the material object in which the work is fixed. Under the first sale doctrine,²⁰³ this doctrine limits the control of the copyright owner over transfer of possession and restricts physical movement of goods into the U.S.²⁰⁴ As limitation of distribution rights, this doctrine

²⁰⁰ See Harry Rubin, *Destined To Remain Grey: The Eternal Recurrence of Parallel Imports*, 26 INT'L LAW, 597, 605 (1992); David A. Gerber, *Litigating the Copyright "Gray Market" Case*, in *Gray Markets and Parallel Importation* 269 (Practicing Law Institute Series No. 217, 1986); and Hugh C. Hansen, *Protection of Intellectual Property Rights At The Border: Continuing Battle Over "Parallel Imports"*, 536 PLT/Pat 39, 51 (1998).

²⁰¹ See 17 U.S.C. § 106.

²⁰² See 17 U.S.C. § 602(a) and § 106 (3). Section 602(a) states:

"(a) Importation into the United States, without the authority of the owner of copyright under this title, of copies or phonorecords of a work that have been acquired outside the United States is an infringement of the exclusive right to distribute copies or phonorecords under Section 106, actionable under Section 501..."

Section 106 provides:

"Subject to sections 107 through 121, the owner of copyright under this title has the exclusive rights to do and to authorize any of the following: ...

(3) to distribute copies or phonorecords of the copyrighted work to the public by the sale or other transfer of ownership, or by rental, lease, or lending;..."

²⁰³ See 17 U.S.C. § 109(a). Section 109(a) states:

"Notwithstanding the provisions of section 106(3), the owner of a particular copy or phonorecords lawfully made under this title, or any person authorized by such owner, is entitled, without authority of the copyright owner, to sell or otherwise dispose of the possession of that copy or phonorecord."

²⁰⁴ There are two policies behind the first sale doctrine. First, the common law prefers to avoid restraints on the disposal of personal property. Second, the copyright owner usually receives his rewards for use of his copyright upon the first sale and therefore has no right to demand a second payment or further control of the goods. See ROBERT A. GORMAN & JANE C. GINSBURG, COPYRIGHT: CASES AND MATERIALS 70-73, 552 (5ed. 1999); and also see DONALD S. CHISUM & MICHAEL A. JACOBS, UNDERSTANDING INTELLECTUAL PROPERTY LAW § 4E[3][c] (1992).

entitles a purchaser of a copyrighted copy to use or dispose of that copy freely without paying a royalty to the copyright owner. Thus, the purchaser obtains the distribution rights pertaining to that particular copy under the first sale doctrine.²⁰⁵

The first sale doctrine is valid only for such copies or phonorecords of a work that are legitimately produced and sold under the copyright law. If such products are unauthorized copies or distribution, the first sale doctrine does not cover it and then further distribution constitutes an infringement.²⁰⁶ The first sale doctrine is recognized to the extent that a first unconditional sale of the copyright work brings with the unconditional right to resell the work, but not to copy the work. The purpose and effect of the copyright statute is to secure to the owner thereof the exclusive right to multiply copies.²⁰⁷ In other words, the purchase bring about the right to resell the product without constituting a copyright infringement but the purchaser does not have a right to make a copy of the copyright work.²⁰⁸

In case of first sale with some conditions, in the *Straus* case, although the copyright owner provides a notice on the product about the sale price, the purchaser who obtained the products and sold them below the sale price notice does not constitute a copyright infringement. The right of the copyright owner to control these products

²⁰⁵See Neel Chatterjee, *Imperishable Intellectual Creations: The Limits of the First Sale Doctrine*, 5 FORDHAM INTELL. PROP. MEDIA & ENT. L.J. 383, 385-395(1995).

²⁰⁶See *Columbia Pictures Indus., Inc. v. Garcia*, 996 F. Supp. 770 (N.D. Ill. 1998); *Psihoyos v. Liberation Inc.*, 42 U.S.P.Q. 2d 1947(S.D.N.Y. 1997) (In this case, the plaintiff, a photographer, alleged that an Austria publisher reproduced his photograph in the pages of its magazine, copies of which were distributed in the U.S. The Austrian defendant contended that there was no violation of the U.S. Copyright Act because the reproduction had occurred in Austria. Even so, held the court, the distribution of copies of the magazine in the U.S. brought the photographer's U.S. distribution right into play.)

²⁰⁷See *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339; *Jeweler's Circular Pub. v. Keystone Pub.Co.*, 281 F.83 (C.C.A. 2d), cert. denied, 259 U.S. 581.

²⁰⁸See *Fawcett Publications, Inc. v. Elliot Publishing Co.*, 46 F. Supp. 717 (S.D.N.Y. 1942)(ruling that from the facts, the defendant has not multiplied copies but merely resold the plaintiff's under a different

exhausts after the first sale.²⁰⁹ In the case in which a copyright owner imposed a restriction clause that there cannot be any resale in the U.S. and Canada, and if the copyright owner had consented to the initial sale, the buyer who later imported this product into the U.S. did not infringe the copyright and the right of the copyright owner was exhausted after the first sale.²¹⁰ The court in the *Toys "R" US* case found that the plaintiff had consented to the sale of copies and the fact that the buyers later violated the conditions imposed on the sale did not reverse this consent. On the grounds that the copyright owner had consented to their sale, the court decided that the plaintiff's distribution rights were exhausted. The court noted that under the copyright law, conditions of the first sale do not run with the goods unlike the implied license under the patent law.²¹¹

In relation to parallel imports, U.S. copyright law provides copyright owners with some powers to control importation of copyrighted works. Copyright owners have the exclusive right to prevent the importation of goods made outside of U.S. jurisdiction into the jurisdiction under section 602(a). In practice, the Customs is authorized to prohibit

cover. The defendant's action did not infringe the plaintiff's copyright because the defendant did not copy, reprint or rearrange the plaintiff's copyrighted material nor remove the plaintiff's copyright notice.)

²⁰⁹ See *Bobbs-Merrill Co. v. Straus*, 210 US 339 (1908) affg 147 Fed. 15 (2 Cir. 1906); and also See *ROTHNIE*, *supra* note 24, at 261

²¹⁰ See *Denbicare v. Toys "R" US*, 84 F. 3d 1143 (9th Cir. 1996) (In this case, the issue is whether the foreign trade zone is in the U.S. jurisdiction and whether such previous sale is covered under the first sale doctrine. The court held that the goods were imported into the U.S. with the authorization of copyright holder and the foreign trade zone is not outside the U.S. for purpose of Section 602.)

²¹¹ *Id.* at 1150; The interested point in this case is how the court separated concept in first sale doctrine in different types of intellectual property. The products in this case are protected under copyright, trademark, and patent law. The court asserted that "the trustee's sale qualified as a first sale for copyright purpose, it is a trademark first sale as well." The plaintiff argued that doctrine from patent law to the effect that an implied license is granted to the first purchaser to use and sell the patented item applied to trademarked goods and that the injunction created an express condition, which ran with the goods as a term of implied license. The court refuse to apply the doctrine from patent rather doctrine under copyright law. *Id.* at 1151; See *Donnelly*, *supra* note 82, at 466-68.; and also see The discussion on parallel imports in patent in the next section.

the importation of illegal copies; it cannot bar parallel imports because parallel imported goods are genuine. However, the copyright owner can sue a parallel importer for copyright infringement against unauthorized importation of legitimate goods. Like patent and trademark, the importation right under copyright law must be considered in light of an exhaustion doctrine. This doctrine can be asserted as an affirmative defense by parallel importers to avoid the copyright infringement.

The argument whether the IPRs owners have the right to block parallel imports is always related to the tension between the principle of territoriality and the principle of universality upon the scope of the exhaustion doctrine. It seems that the beneficiaries of parallel imports are countries that are in the position to produce goods cheaply, such as Asian countries rather than the industrialized countries like the U.S.²¹² Sensibly, the U.S. does not adopt the international exhaustion as a legal standard but prefers to implement the national exhaustion doctrine to protect the benefits of U.S. businesses.²¹³

There is ambiguity in legislation and inconsistency in interpretation in section 109(a) the first sale exception, section 106(3) the distribution right, and section 602(a) the importation right referring to section 106(3). Even though section 109(a) covers section 602(a), it still has interpretation problem in section 109(a). It is unclear whether section 602(a) is limited by the first sale doctrine or if it is exempt from the doctrine's limitations when goods are legally first sold abroad and then imported into the U.S. According to the

²¹² Most exporting countries such as Asia nations allow parallel imports and recognize an international exhaustion doctrine. For example, Singapore and Thailand adopt and apply the doctrine of international exhaustion; see Tait R. Swanson, *Combating Gray Market Goods in A Global Market: Comparative Analysis of Intellectual Property Laws and Recommended Strategies*, 22 HOUS. J. INT'L L. 327, 359-360 (2000); and also see the European Union perspective on the exhaustion doctrine in the following section.

²¹³ See the U.S. supports a national exhaustion doctrine in the earlier discussion in Part A section III.; and Part B in section 1.2 European Union and 1.3 International Agreement.

ambiguous phrase “lawfully made under this title” in section 109(a), there are two groups of decisions depending on where the goods are made either abroad or locally.

Firstly, the first sale doctrine is applicable if such imported goods are made and sold in the United States.²¹⁴ For example, in *Columbia Broadcasting System v. Scorpio Music Distributors, Inc.*,²¹⁵ the court focused on the phrase “lawfully made under this title” to limit the scope of the first sale doctrine to goods legally produced and sold in the United States rather than imported goods. Furthermore, in the 1988 U.S. Court of Appeal decision of *Sebastian International Inc. v. Consumer Contracts(Pty) Ltd.*,²¹⁶ it was held that the first sale doctrine effectively barred a copyright holder from proceeding against a parallel importer under section 602. Section 602(a) did not assert to create an exclusive right in addition to those exclusive rights bestowed by section 106(3). Thus, it was particularly limited by the first sale doctrine under section 109(a).²¹⁷ However, the first sale doctrine can supersede the exclusive right only when those parallel imported goods are produced and sold in the U.S.

Secondly, the importation right under section 602(a) is not limited by the first sale doctrine when goods, manufactured abroad or outside the U.S., are imported without a permission. Therefore, the copyright owner can bar the parallel import and the first sale doctrine defense of importers is invalid.²¹⁸ For example, in *BMG v. Perez*,²¹⁹ the Ninth

²¹⁴ For example, *Sebastian International v. Consumer Contracts(PTY) Ltd.*, 664 F. Supp. 909 (D.N.J. 1987), vacated, 847 F.2d 1093 (3d Cir. 1988), *Neutrogena Corporation v. United States*, 7 U.S.P.Q.2d(BNA)1900 (D.S.C.1988).

²¹⁵ See *Columbia Broadcasting System v. Scorpio Music Distributors, Inc.*, 569 F. Supp. 47 (E.D.Pa. 1983)

²¹⁶ See *Sebastian International Inc. v. Consumer Contracts(Pty) Ltd.*, 664 F. Supp. 909 (D.N.J. 1987), vacated, 847 F.2d 1093 (3d Cir. 1988). [hereinafter *Sebastian Case*]

²¹⁷ *Id.* at 1099.

²¹⁸ For example, *Nintendo of American, Inc. v. Elcon Industries., Inc.*, 564 F. Supp. 937 (E.D.Mich. 1982), *Columbia Broadcasting Sys., Inc.v. Scorpio Music., Inc.*, 569 F.Supp. 47 (E.D.Pa. 1983), *BMG Music v. Perez*, 952 F.2d 318 (9th Cir.1991), cert. Denied, 112 S.Ct. 2997(1992). In *Scorpio* case, due to phrase of

Circuit Court held that the first sale doctrine was not a defense for an infringement under section 602 where the goods in question were manufactured outside of the U.S.

However, in *Quality King Distributors, Inc. v. L'anza Research International, Inc.*²²⁰ the Supreme Court stated that the first sale doctrine was applicable to imported copies.²²¹ Hence, American-based copyright owners could not sell copyrighted goods to foreign distributors and then bar the re-importation of those goods back into the United States by way of their right to limit importation.²²² The Supreme Court refused the Ninth Circuit's decision that the first sale doctrine did not prevent L'anza from enjoining importation of the copies²²³ and decided that the first sale doctrine was applicable to imported copies.²²⁴

section 109(a) "lawfully made under this title", the Court held section 602(a) was not limited by the first sale doctrine under section 109(a) since section 109(a) protected third-party purchasers of copies legally made and sold within the U.S. but not buyers of foreign-manufactured products.

²¹⁹ See *BMG v. Perez*, 952 F.2d 318 (9th Cir.1991), cert. Denied, 112 S.Ct. 2997(1992).

²²⁰ See *Quality King Distributors, Inc. v. L'anza Research International, Inc.*, 118 S. Ct. 1125 (1998).[hereinafter *Quality King Case*]

²²¹ *Id.* at 1131-33; and also see Brayan P. Stanley, Note, *Preventing The Import of Gray Market Goods in Light of Quality King Distributors Inc. v. L'anza Research International, Inc.*, 38 WASHBURN L.J. 871, 873 (1999).

²²² *Id.* at 1133-34.

²²³ See *L'anza Research International, Inc. v. Quality King Distributors, Inc.*, 98 F.3d 1109, 1116, 1117 (9th Cir. 1996). (In Appeal Court, due to unclear in copyright statue, the Court recognized that there is no express Congressional statement of intent regarding the interaction between section 602 and section 109(a). The Court concluded that the "evil" described in this testimony, "that unauthorized imports cause copyright owners to lose control over domestic distribution, thus driving prices down for goods sold through authorized channels in the United States market," supported a holding that the importation right is not limited by the first sale doctrine.); and see David A. Gerber & David Bender, *Gray Market in Copyrighted Materials*, 532 PLI/PAT 119,130 (1986).

²²⁴ The Supreme Court sought to clarify the division between the Third and the Ninth Circuits concerning the proper interplay between Sections 602, 106, 109 and 501 of the Copyright Act. In other words, the Supreme Court decision in the *Quality King* case resolve the rift between the Third Circuit and the Nine Circuit. There were a conflict between the Third Circuit's decision in *Sebastian* case and the Third Circuit decisions in the *Givenchy* and *L'anza* cases. In the *Sebastian* case, the Third Circuits ruled that once the copyright owner decided to sell his product, he had no right to control further distribution. The importation right under section 602(a) is not desperate from the distribution right under section 106 and fall within the scope of first sale doctrine under section 109. On the other hand, in the *Givenchy* and *L'anza* cases, the Nine Circuit decided that the first sale doctrine only applies to sale occurred within the US., if the goods are made and sold outside the US., the copyright owner has right to bar such importation since his right does not exhausted. In this case, the first sale doctrine under Section 109 does not supersede the importation

The Supreme Court held that the first sale doctrine precluded a copyright owner from asserting that the re-importation of its goods from overseas markets constituted a copyright infringement. The Court narrowly interpreted the statutory language of section 602(a). The Court concluded that the importation right was subject to the first sale doctrine like the distribution right because the statute stated that unauthorized importation is “an infringement of the exclusive right to distribute copies...under section 106.”²²⁵ This decision curtailed the ability of companies to use section 602(a) to prevent the unauthorized importation and resale of goods manufactured in the U.S. and legally acquired abroad. However, the decision does not prevent companies from using section 602(a) if the goods were manufactured abroad. The Court implies that distributors of copyrighted goods, which are manufactured abroad and then imported in to the U.S., may not be entitled to the first sale defense against the copyright infringement. The first sale defense to copyright infringement can only be used by the owner of the particular copy in question.²²⁶ By using a non-owner such as a bailee, licensee, or consignee to distribute goods in foreign markets, a manufacture’s action for copyright infringement will not be barred by the first sale doctrine if a non-owner attempts to divert goods back into the U.S.²²⁷

In conclusion, the first sale doctrine under section 109 is applicable to both the distribution right in section 106(3) and the importation right in section 602(a). The scope and application of the first sale doctrine depends upon where the goods were produced. If

right under Section 602. *See* Sebastian Case, *supra* note 216; *see* Parfums Givenchy, Inc. v. Drug Emporium, Inc., 38 F. 3d 477 (9th Cir. 1994); and also *see* L’anza Research International, Inc. v. Quality King Distributors, Inc., 98 F.3d 1109, 1116, 1117 (9th Cir. 1996).

²²⁵ *See* 17 U.S.C. § 602(a).

²²⁶ *See* the *Quality King* Case, *supra* note 220, at 1131.

the goods were produced and sold in the U.S. or sold abroad, the copyright owner cannot bar parallel imports of those goods. It appears that the result of the Supreme Court decision is similar to the application of an international exhaustion doctrine when the goods are produced in the U.S. and then sold to foreign buyers. On the other hand, if the parallel imported goods are produced and sold outside the U.S., the exclusive right of the U.S. copyright owner is not exhausted as it is based on the concept of national exhaustion doctrine. Thus, those goods could be prohibited for parallel imports under section 602(a).

4. Parallel Imports in Patent

By the nature of the patent law, the patent is more about territorial restriction than the copyright and trademark. The significant issue is whether the importation occurs with the patent authorization because the unauthorized importation into the United States infringes the U.S. patent. It particularly involves the contractual aspect because if the first sale of patent goods is authorized by the patent owner without contractual condition about resale and importation, the right of the patent owner is exhausted under the exhaustion doctrine.

The Patent Act, section 271, prohibits all unauthorized parallel imports and authorizes a patentee to prevent resale of a patented product after it is purchased outside the United States and imported by the third party.²²⁸ However, it is constrained by the

²²⁷ *Id.*

²²⁸ 35 U.S.C.A. § 271. Section 271 of the Patent Act provides that “ whoever without authority...offers to sell, or sells any patented invention, within the United States or imports into the United States any patented invention during the term of patent therefore, infringes the patent.” Section 271 also prohibits importation of products made by processes patented within the United States (§271(g)) and certain components for practicing a patented invention or process.(§271(c)). To comply with Article 28 of TRIPs agreement, in

exhaustion doctrine that the first lawful sale effectively exhausts the patentee's right. The Patent Act clearly grants an express right of importation to a patent owner, but does not codify the exhaustion doctrine.²²⁹ Nevertheless, this doctrine is certainly established and stated in the case law. The U.S. courts frequently apply the exhaustion doctrine to limit the ability of a patentee to prevent a resale of patented goods.²³⁰

Initially, the Supreme Court embraced the exhaustion doctrine in *Adams v. Burke*.²³¹ From the facts, the patentee assigned a patent covering an improved lid for coffins to one party for a specific territory and the remainder of the patent right to the plaintiff. The defendant, as third party, purchased patented coffins within the first assignee's territory without restriction on their use. The defendant used them in the territory granted to the plaintiff. The Supreme Court held that when a patentee or its assignee sells a patented article whose value is in its use, no restriction on such use would be implied.²³²

1994, Congress amended the Patent Act to provide an express right of importation to patentee, which became effective on January 1, 1996.

²²⁹ Unlike patent law, the copyright law clearly codifies the first sale doctrine in section 109(a) of the Copyright Act 1976. Although there is no codification of exhaustion doctrine in patent law, some scholars absolutely accepted the application of this doctrine. See William A. Birdwell, *Exhaustion of Rights and Patent Licensing Market Restrictions*, 60 J. PAT. OFF. SOC'Y 203 (1978); Walter H. Chamerlin, *Patented Articles: When Are They Emancipated From The Patent Monopoly Under Which They are Manufactured?*, 6 ILL. L. REV. 357 (1912).

²³⁰ See *Bloomer v. McQuewan*, 55 U.S. (14 How.) 539 (1852); *Chaffe v. Boston Betlting Co.*, 63 U.S. (22 How.) 217 (1859); *Adams v. Burke*, 84 U.S. (17 Wall.) 453 (1873); *Hobbie v. Jennison*, 149 U.S. 355 (1893); *Keeler v. Standard Folding Bed Co.*, 157 U.S. 659 (1895); *Straus v. Victor Talking Mach. Co.*, 243 U.S. 490 (1917); *Motion Pictures Patents Co. v. Universal Flim Mfg. Co.*, 243 U.S. 502 (1917); *United States v. General Elec. Co.*, 272 U.S. 476 (1926); *United States v. Masonite Corp.*, 316 U.S. 265 (1942); *Wilbur-Ellis Co. v. Kuther*, 377 U.S. 422 (1964); and *Aro Mfg. Co. v. Convertible Top Replacement Co.*, 377 U.S. 476 (1964).

²³¹ See *Adam v. Burke*, 84 U.S. (17 Wall.) 453 (1873); Before the *Adam* case, the U.S. court originally attempted to limit the monopoly right of patentee based on the property law, not a first sale doctrine as perceived in the *Bloomer* case. See *Bloomer v. McQuewan*, 55 U.S. (14 How.) 539, 549-50 (1852).

²³² In *Adam v. Burke*, the Court states "When the patentee, or the person having his rights, sells a machine or instrument whose sole value is in its use, he receives the consideration for its use and he parts with the right to restrict that use. The article...passes without the limit of the monopoly. That is to say, the patentee or his assignee having in the act of sale received all the royalty or consideration which he claims for the use

The *Adams* case involves distribution from one area of the United States to another, and the court asserted a nationwide exhaustion doctrine with regard to the right to use the patented goods. While the Court in *Keeler v. Standard Folding-Bed Co.*,²³³ stated that the sale of a patented article by one having authority to sell it, though within a restricted territory, gave the purchaser the right to “use and sell” such product anywhere in the U.S. In this case, an exhaustion doctrine is applied because the patentee already received the benefit for sale of a patented article²³⁴ and the Court adopted a national exhaustion doctrine.

Although the United States courts in previous cases have not characterized the exhaustion doctrine based on a contract approach analysis,²³⁵ the Court of Appeals for the Federal Circuit in *Mallenckrodt, Inc. v. Medipart, Inc.*, has held that a patentee can counteract the effect of the doctrine through express contractual provision by restricting purchasers' subsequent use or resale of the patented article.²³⁶ Unlike the U.S. approach,²³⁷ the United Kingdom and other British Commonwealth nations have based

of his invention in that particular machine or instrument, it is open to the use of the purchaser without further restriction on account of the monopoly of the patentee. ...When they are once lawfully made and sold, there is no restriction on the articles' use to be implied for the benefit of the patentee or his assignees or licensees.” *Id.* at 456-57.

²³³ See *Keeler v. Standard Folding-Bed Co.*, 157 US 659, 664 (1895)[hereinafter *Keeler* case]; and also see *Hobbie v. Jennison*, 149 U.S. 355, 361-62 (1893)(Referring to the *Adam* case, the court decided that the defendant, a licensee with exclusive right restricted to Michigan state, did not infringe for selling patented pipe in Michigan to a Connecticut company by knowing that the pipe would be used in Connecticut, where is the exclusive territory of the plaintiff.)

²³⁴ See *id.* at 670-71 (The opinion of dissenters (Fuller, Ch. J., Brown, J., and Field, J., The three dissenters considered that the first sale doctrine applied solely to patented goods that were capable of only a single use such as coffin lids and the holdings of *Adam* case and *Hobbie* case were limited to article that were exhausted or consumed in use and no longer value after a single use. However, this concept was rejected.)

²³⁵ See Margreth Barrett, *The United States' Doctrine of Exhaustion: Parallel Imports of Patented Goods*, 27 NORTH KEN L.REV. 911 (2000).

²³⁶ See *Mallenckrodt, Inc. v. Medipart, Inc.*, 976 F.2d 700 (Fed. Cir. 1992). (The Court of Appeals for the Federal Circuit refused the first sale doctrine and considered it as a separate doctrine of patent law by ruling that it is nothing more than an application of the implied license.)

²³⁷ See ROTHNIE, *supra* note 24, at 106-85 (explaining and comparing between the US. law and the UK. and Commonwealth law about parallel import on patent.)

their version of the exhaustion doctrine on a theory of implied consent on the patentee's part arising out of the act of sale.²³⁸

The earlier cases involve the exhaustion doctrine in the sale and use of patent articles from one area to another within the U.S., but the following cases involve with the sale and use of patent articles within different nation jurisdiction. It seems that the following court's decisions adopt a national exhaustion doctrine.²³⁹ In *Boesch v. Graff*,²⁴⁰ a third party manufactured lamp burners in Germany, which infringed the U.S. patent. The Court held that Boesch infringed the U.S. patent by importing the burners into the United States. When the United States patentee holds patents for the same invention in several nations unauthorized first sales under foreign patents do not exhaust the U.S. patent.²⁴¹ Thus, the Court refused to find exhaustion of patent rights because the exhaustion was limited by national boundaries. In *Dickerson v. Tinling*,²⁴² the assignee of the U.S. patent sued an infringement action against a purchaser of the patented article in Germany that imported the article into the U.S. for resale. The Court granted a preliminary injunction and held that whether the defendant bought the patented article in country outside the U.S. from the U.S. patent owner with restrictions or from a third party without restriction, the defendant infringed the U.S. patent in both cases. The Court

²³⁸ See *Zino Davidoff SA v. A&G Imports Ltd.*, [1999] 2 CMLR 1056, 30 IIC 567 (1999); see *Betts v. Willmott* [1871] L.R. 6 Chapp 239; and also see the following section in The European Union for further discussion.

²³⁹ See Barrett, *supra* note 235, at 927-28. (mentioning that there is discrepancy on the issue that whether the US adopt an international exhaustion or national exhaustion in relation to importation of patent goods which are sold abroad by the US patent owner or with this consent.)

²⁴⁰ See *Boesch v. Graff*, 133 U.S. 697 (1890).

²⁴¹ It is reasonably to conclude that the foreign sale did not exhaust the patent right in the U.S. since neither the U.S. patentee nor assignee had ever received any royalty for the use in the United States of the foreign purchased article. See *Keeler* case, *supra* note 233, at 664-65.

²⁴² See *Dickerson v. Tinling*, 84 F. 192 (CA. 8 1987).

rejected finding the patent exhaustion because there was no benefit to or no consent by the U.S. patentee in the prior sale.²⁴³

The patent owner may impose some restrictions on the contract to control the further distribution of his goods. However, the exclusive territorial arrangement or post-sale restriction might raise antitrust issues. In *Mallenckrodt, Inc. v. Medipart, Inc.*,²⁴⁴ the Federal Circuit stated “an unconditional sale of a patented device exhausts the patentee’s right to control the purchasers’ use of the device thereafter” and “express conditions are contractual in nature and are subject to antitrust, patent, contract and any other applicable law, as well as equitable considerations such as patent misuse.”²⁴⁵ It is clear that purchasers must have adequate notice of restrictions before they are bound.²⁴⁶ In this case, the Court found that the post-sale restrictions were valid by distinguishing them from other cases. Other cases involved retail price fixing of patented article or patent tying agreement that was, per se, illegal.²⁴⁷ On the other hand, the *Mallenckrodt* case involved the restriction to use a patented device for only single time that restriction on use was valid and whoever reused the device in breach of the restriction was liable for patent infringement.²⁴⁸

As mentioned above, many court decisions apply a national exhaustion doctrine. Nevertheless, there are some court decisions that seem to adopt an international

²⁴³ *Id.* at 194.

²⁴⁴ See *Mallenckrodt, Inc. v. Medipart, Inc.*, 976 F. 2d 700 (Fed. Cir. 1992). [hereinafter *Mallenckrodt* Case]

²⁴⁵ *Id.* at 708.

²⁴⁶ *Id.*; Based on the contract theory, the purchaser of goods could be bound by the restriction on the product and the patent owner has right to limit the subsequent acts of purchasers. See *Keeler v. Standard Folding-Bed Co.*, 157 U.S. 659, 666 (1895); and see *Hobbie v. Jennison*, 149 U.S. 355, 363 (1893).

²⁴⁷ See *Bauer & Cie v. O'Donnell*, 229 U.S. 1 (1913); *Straus v. Victor Talking Mach. Co.*, 243 U.S. 490 (1917); and *Boston Store of Chicago v. American Gramophone Co.*, 246 U.S. 8 (1918).

²⁴⁸ See *Mallenckrodt* Case, *supra* note 243, at 700.

exhaustion doctrine in favor of importers. In *Holiday v. Mattheson*,²⁴⁹ the Court held that once the U.S. patentee had sold a patented article in a foreign country without any restrictions on resale, the patentee could not prevent the purchaser of the patented article from using or selling that article in the United States. As a result of the failure to impose conditions on sale, the patentee had waived its right to prevent importation and sale of the goods within the United States.²⁵⁰

In addition, the court decision in *Curtiss Aeroplane & Motor Corp. v. United Aircraft Eng'g Corp.*²⁵¹ depended upon international exhaustion doctrine. The court held that if a patentee or his assignee sells a patent article, that article is free from the monopoly of any patents. If a vendor's patent monopoly consists of foreign and domestic patents, the sale frees the article from the monopoly of both foreign and domestic patents. Thus, the Defendant's parallel import act does not infringe the U.S. patent right. This case notices the intention of sale without limitation of further sale. Alternatively, if there is restriction in resale or further sale, the patent owner can prevent parallel imports.²⁵²

Nevertheless, in *Sanofi, S.A. v. Med. Tech Veterinarian Prod., Inc.*,²⁵³ the court ruled that the exhaustion doctrine applied only when the person who sells the product

²⁴⁹ See *Holiday v. Mattheson*, 24 F. 185 (C.C. S.D.N.Y. 1885).

²⁵⁰ In *Featerstone v. Ormonde Cycle*, the Court stated that although no specific restrictions attached the sale, no rights could be transferred to the purchaser, which was greater than those held by the vendor. See *Featerstone v. Ormonde Cycle*, 53 F. 110 (C.C. S.D.N.Y. 1892) (From the fact, the plaintiff is the assignee of a U.S. patent and enjoined a licensee under the corresponding British patent from selling the patented goods in the United States. The vendor was not authorized by the assignee of the U.S. patent to sell the patented goods in the U.S. However, the issue of exhaustion doctrine was not addressed since the defendant was a licensee under the corresponding British, and not a third party purchaser of the patented goods.)

²⁵¹ See *Curtiss Aeroplane & Motor Corp. v. United Aircraft Eng'g Corp.*, 266 F.71 (2d Cir. 1920) (From the facts in this case, the U.S. patentee authorized the British government to practice its patents on airplanes and motors without restriction. A Canadian company was set up to manufacture the planes during World War I, and the defendant purchased the planes after the war for sale in the United States.)

²⁵² *Id.* at 77-78.

²⁵³ See *Sanofi, S.A. v. Med. Tech Veterinarian Prod. Inc.*, 565 Supp. 931 (D.N.J. 1983). (From the facts, the French pharmaceutical Sanofi held the U.S. patent for the drug 'acerpromazine maleate' and granted

aboard has the right to sell it in the U.S.²⁵⁴ Later, in the case of *Kabushiki Kaisha Hattori Seiko v. Refac Technology Development Corp.*,²⁵⁵ the Court followed the *Sanofi* decision and affirmed that the first authorized sale outside the U.S. by a licensee that also had the right to sell in the U.S. exhausts the domestic patent rights.

In conclusion, by focusing on a territorial-based analysis, there are a significant number of cases and commentators providing that the U.S. court establishes a territorial or national exhaustion doctrine in the area of patent law.²⁵⁶ However, some cases and commentators, focusing on a contract-based analysis, perceived that the courts have established a modified international exhaustion doctrine because the patentee can use the contract restriction to avoid the exhaustion of his patent right on sales outside or inside the U.S.²⁵⁷ After analyzing those cases, it is appropriate to conclude that the U.S. mainly applied the national exhaustion doctrine in patent law, which is similar to the trademark and copyright law. However, sometimes the courts may apply the national exhaustion doctrine with the contract approach. The courts decide that if the person who sells such patent goods either in the U.S. or abroad, has the right to sell in the U.S. and if the sale

American Home Products an exclusive license to sell patented products in the United States. Sanofi sold the products in Europe, the defendant later purchased it and resold it in the United States. Sanofi and American Home, the exclusive U.S. licensee, each brought lawsuits.)

²⁵⁴ *Id.* at 939-41. (The court decided that Sanofi, having sold the product in Europe with the intent to pass with all its rights in the product, could not prohibit the imports. But the exclusive U.S. licensee's right was not exhausted by the sale and could prohibit the imports. The exhaustion doctrine applied only where the sale had occurred outside the U.S., which the vendor had the authority to make in the U.S. If the court decided that Sanofi's sale of the product exhausted the patent, it would have given rights to Sanofi than the U.S. patentee had.)

²⁵⁵ See *Kabushiki Kaisha Hattori Seiko v. Refac Technology Development Corp.*, 690 F. Supp. 1339, 9 USPQ 2d 1046 (SDNY 1988).

²⁵⁶ See John A. Tessensohn & Shusaku Yamamoto, *The BBS Supreme Court Case-A Cloth Too Short for an Obi & Too Long for a Tasuki*, 79 J. PAT. & TRADEMARK OFF. SOC. 791, 741 (1997); Ladas, *Exclusive Territorial Licenses under Parallel Patents*, 3 INTERNAT. REV. INDUS. PROP. & COPYRIGHT 335, 345-46 (1972).

²⁵⁷ See DONALD S. CHISUM, CHISUM ON PATENTS § 16.03[2][a][iv] (1998); see Donnelly, *supra* note 82, at 445; and also see Barrett, *supra* note 235, at 911.

contract does not have a restriction on resale or import, the purchaser is free to import into the U.S. and the right of U.S. patentee exhausts after the first sale.

5. Conclusion

Generally, the U.S. stands for the concept of national exhaustion doctrine and the principle of territoriality in order to protect the owners of IPRs from parallel imports. Nevertheless, there are some specific circumstances where the U.S. allows parallel imports by limiting the exclusive right of the IPRs owner. As for trademark, parallel imports are typically prohibited, except in cases where imported goods are manufactured by the same owner or corporate affiliate of the U.S. trademark owner, unless there are physical and material difference between the domestically produced goods and parallel import goods. In case of copyright, the importation right is subject to the first sale doctrine. The application of the first sale doctrine depends on where the goods are produced and first sold. If the imported goods are produced and first sold in the U.S., either for the purpose of domestic use or export to other countries, the right of the copyright owners is exhausted and they could not bar such parallel imports of those goods. However, if the goods are produced and sold outside the U.S., those goods could be prohibited for parallel imports into the U.S. because the right of the U.S. copyright owner did not exhaust. Finally, in the case of patent, the U.S. courts usually apply a national exhaustion doctrine. In some cases, however, the courts have decided that the right of the U.S. patentee may be exhausted for the overseas sale if the person who

initially sells such goods has the right to sell in the U.S. and if the sale contract does not have the restriction clause on resell and importation.

B. The European Union

1. Introduction

In recent years the European Union (EU) has generated a Community-wide exhaustion doctrine applicable to all kinds of intellectual property rights (IPRs). The Community-wide exhaustion doctrine is considered an example of regional exhaustion or intermediate exhaustion doctrine. The European Community considers that the Community-wide exhaustion doctrine would support the concept of a single market, the free movement of goods and free competition among Member States in the Community.²⁵⁸

Member States are obligated to incorporate the Community-wide exhaustion in their national laws. However, there were many interesting difficulties arising when the Member States applied the Community-wide exhaustion to parallel import cases. There are two fundamental rationales from which to discuss the difficulties. One reason is that when Member States incorporate the Community-wide exhaustion into their national law,

²⁵⁸ See GOVAERE, *supra* note 85, at 73. and also see MALCOLM A. JARVIS, THE APPLICATION OF EC LAW BY NATIONAL COURTS: THE FREE MOVEMENT OF GOODS 7 (1998) (explaining that the EC Treaty provision aims to abolish custom duties and restrictions on the free movement of goods apply “not only to goods originating in Member States, but also to good coming from non-member countries, so long as they have been duly imported into one Member State and any customs duties payable under the Common Customs Tariff have been accounted for.”); However, the Community-wide exhaustion regime remains controversial in the area of trademark. The Commission launched a study on “The economic consequences of the choice of regime of exhaustion in the area of trademarks,” which was studied by National Economic Research Associates (NERA). See The National Economic Research Associates (NERA), The Economic Consequences of the Choice of Regime of Exhaustion in the Area of Trademarks, 8 February 1999

the duty on applying this doctrine belongs to the national court. As the result of different perception in each national court, the outcome of each national court decision may be diverse and cause an unharmonious interpretation in the Community-wide exhaustion doctrine. Another reason is that before obviously establishing the Community-wide exhaustion, the international exhaustion doctrine was adopted in many Member States. The consequences of applying the international exhaustion doctrine still remain in many national courts' judiciary decisions. Although they do not straightforwardly assert the international exhaustion doctrine, the results of their decisions, which are based on other alternative reasons, are similar to the result of application of the international exhaustion.²⁵⁹

Because of divergent perspectives and different previous rules in the scope of exhaustion doctrine among the Member States, many problems took place when applying a Community-wide exhaustion. The EU experience indicates some of the shortcomings of this approach, which is based on less than international exhaustion. The EU attempt to exploit the intermediate exhaustion -not national, not international but regional- has not been a complete success. Studying the issues or shortcomings of the application of Community-wide exhaustion in the European Community is useful for finding a harmonious approach or international legal standard in the exhaustion doctrine at a global level.²⁶⁰

(London).; and also *see* more detail and discussion in Chapter Three on Current Debate in Trademark: Consumers' Movement in European Union to Liberalize Parallel Imports of Trademark Goods.

²⁵⁹ *See* Zino Davidoff SA v. A&G Imports Ltd, [1999] 2 CMLR 1056, 30 IIC 567 (1999).

²⁶⁰ After studying both the weakness or deficiency and the strong point or advantage of a Community-wide exhaustion doctrine, this thesis aims to propose the international exhaustion doctrine as the international standard. The international exhaustion doctrine should encourage free trade, the free movement of goods and the free competition in the same way a Community-wide exhaustion does in the European Community.

Therefore, in order to have a better understanding, the following parts will explain: (1) the fundamental concepts of the European Community relating to Article 28 (formerly Article 30) and Article 30 (formerly Article 36)²⁶¹ of the Treaty Establishing the European Community (EEC Treaty), and (2) the role of the European Court of Justice (ECJ). Then, the issues of application of the Community-wide exhaustion and the shortcoming of the European approach will be described and discussed.

1.1 The Principle of Free Movement of Goods and the Protection of Intellectual Property Rights in the European Union

In the European Community,²⁶² the free movement of goods principle is one of the fundamental principles, which has been codified in Article 28 (formerly Article 30).²⁶³ The underlying aim of Article 28 is to promote the free movement of goods by prohibiting all measures either a quantitative restriction or measures having equivalent effect that constitute an obstacle to free movement of goods in the Community. The

²⁶¹ As the result of Amsterdam Treaty, the Articles of the EC Treaty are renumbered. After the first of May 1999, the Amsterdam Treaty went into force and amended the EC Treaty but not in the area of IPRs.

²⁶² The European Community, presently know as "the European Union", was established in 1957 by the Treaty Establishing the European Community (EEC Treaty)-opened for signature Mar. 25, 1957, 298 U.N.T.S. 11 (1958); Consolidated Version of the Treaty Establishing the European Community, October 2, 1997, 37 I.L.M. 56 Treaty of Amsterdam Amending the Treaty on European Union, the Treaties Establishing the European Communities and Certain Related Act, October 2, 1997, [1997]O.J. C340/1. [hereinafter EEC Treaty] The purpose of EEC Treaty was to establish a common market to promote throughout the Community a harmonious development of economic activities. See art. 3 of the EEC Treaty.

²⁶³ The free movement of goods creates a better deal than simply creating a free trade area because The EC Treaty provision abolishing custom duties and restrictions on the free movement of goods. See JARVIS, *supra* note 258, at 7, citing in Article 9(2) and 10(1) EC and the ECJ's decision in Case 41/76 Doncherwolcke, [1977] 2 CMLR 535.

principle of free movement means “products can circulate internationally in the same way as domestically.”²⁶⁴

The concepts of the freedom of movement and freedom of competition between Member States are relevant to the IPRs protection. The exercise of IPRs by intellectual property owners to prevent importation may amount to “measures having the effect equivalent to quantitative restriction.”²⁶⁵ Nevertheless, the European Community also recognized the exclusive rights of intellectual property owner under Article 30 (formerly Article 36) of the EEC Treaty providing for an exception to the principle of free movement of goods for “the protection of industrial and commercial property.” The Community attempted to balance the conflict between the concepts of free movement and the protection of IPRs, especially in distribution and importation rights because the enforcement of IPRs affects the free movement of goods or free competition.²⁶⁶ Consequently, Article 28 and 30 of the EEC Treaty are the main instruments used to guarantee the freedom of movement for goods, while still preserving the IPRs. The discussion on relationship between Article 28 and 30 will be explained later on the topic of the circulation of parallel imported goods inside the European Union.

1.2 The Role of the European Court of Justice

In the process of implementing the aforementioned principles into Member States’ national laws, the European Court of Justice has been considered instrumental in

²⁶⁴ MARC STUCKI, TRADEMARK AND FREE TRADE: AN ANALYSIS IN LIGHT OF THE PRINCIPLE OF FREE MOVEMENT OF GOODS, THE EXHAUSTION DOCTRINE IN EC LAW AND OF THE WTO AGREEMENT 13 (1997).

²⁶⁵ See *EMI Records v. CBS Schallplatten GmbH*, [1976] ECR 811, 7 IIC 275 (1976).

balancing the conflict of implementing the free movement of goods principle while providing the IPRs protection. The ECJ has an important duty to enunciate and enforce the principle of supremacy of Community law over national law, which is to eliminate obstacles between Member States and reduce the inconsistency in their national laws. To ensure economic and social progress and to eliminate barriers, the European Community should be governed by its own law with effective enforcement. The rules relating to parallel imports in the European Community are derived from the interplay between national Member States' interests and supranational European Community's interests.²⁶⁷

In order to remove obstacles to the free movement of intellectual property products caused by divergent national intellectual property law,²⁶⁸ a Community-wide exhaustion doctrine was established to balance those conflicts and harmonize the exhaustion doctrine throughout Member States. The exhaustion doctrine is principally considered as "a mechanism for reconciling the concept of the single market in goods."²⁶⁹ When problems in interpretation of this doctrine occur at the national level, the EJC has a duty to answer and ensure that such interpretation is consistent with the Community law. The law of the European Community on the question of IPRs is a combination of the principle of the Treaty of Rome, some EC directives, and the interpretations of the ECJ.

²⁶⁶ See GOVAERE, *supra* note 85, at part II. (describing and discussing the application of Article 28 and 30 in the light of competition policy and free movement of goods principle in the area of IPRs)

²⁶⁷ In general, there are two interests relating to the enforcement of Community laws: the national interest of each Member State in passing its own intellectual property law and the Community's interest in making European Community laws effective. See Ysolde Gendreau, *An Intellectual Property Renaissance in European Community Law*, in INTERNATIONAL TRADE AND INTELLECTUAL PROPERTY: THE SEARCH FOR A BALANCED SYSTEM at 41-42 (George R. Stewart, Myra J. Tawfik & Maureen Irish eds., 1994); and see The EEC Treaty, *supra* note 262, at pmbl. para.3.

²⁶⁸ The example of divergent national intellectual property law is in the term of protection according to the longer term of protection given in a Member States such as Germany. See the more detail and discussion in *EMI Electrola v. Patricia* in the following section in the Parallel Imports in Copyright.

In the case of parallel imports, besides the EC directives, many rules derive from the ruling of the ECJ decisions because of the balancing role function of the ECJ. Therefore, this thesis will pay attention to the decisions of the ECJ as well. Studying and analyzing the decisions of the ECJ should be meaningful because the decrees of court decisions should be considered alongside the Community law when discussing the issues of parallel imports in the European Community.

The next sections will analyze the issues of implication and interpretation of the Community-wide exhaustion doctrine within the Community, which present the issues of application of this doctrine and the shortcoming of the European approach. The analysis will be separated into two parts based on where the parallel import goods were initially marketed: (1) circulation of parallel imported goods from outside the European Union, and (2) circulation of parallel imported goods inside the European Union. The first part will focus on the importation and subsequent distribution of legitimate goods, which are initially marketed in non-member states by the IPRs owners or with their consent, and then imported into the Community. This part will discuss whether the IPRs owner still has right to prohibit such importation under the Community-wide exhaustion doctrine. The second part will concentrate on the importation and subsequent distribution of legitimate goods from inside the Community and analyze whether the IPRs owners can assert the exclusive right to bar such parallel imports. In other words, the second part will analyze whether there are any particular circumstances in which the Community-wide exhaustion doctrine and free movement of goods principle could be overcome by the exclusive rights of the IPRs owners.

²⁶⁹See Helen Norman, *Parallel Imports from Non-EEA Member States: The Vision Remains Unclear*,

2.Circulation of Parallel Import Goods from Outside the European Union

2.1 A Community-wide Exhaustion as the Recent European Union's Position

As previously mentioned, the European Parliament proposed to limit the rule of exhaustion to a Community-wide exhaustion, and apply it only to goods put on the market within the European Community, which means the European Economic Area (EEA).²⁷⁰ The existence of a Community-wide exhaustion appears in copyright, patent and trademark with different approaches. In the case of trademark, the Community-wide exhaustion doctrine was obviously incorporated in the EU Trademark Directive, Article 7(1).²⁷¹ In the case of copyright and patent, although the Community-wide exhaustion has not been revealed in legislation, the application of the Community-wide exhaustion doctrine was recognized in the ECJ decisions.

In relation to copyright, the ECJ recognized the exhaustion doctrine in scope of Community level in *Deutsche Grammophon* case²⁷² by holding that the rights of a copyright owner were exhausted after the first sale within the EU. If the IPRs owners consent to such a sale, they cannot bar parallel imports of those goods.²⁷³ In the case of patent, the principle of the Community-wide exhaustion can be found in an ECJ decision

[2000] EIPR 159.

²⁷⁰ Under the Agreement on the European Economic Area, the term "Community" is defined as "European Economic Area (EEA)." The European Economic Area is the world's biggest free trade zone and encompasses the EC and all the EFTA countries (Austria, Finland, Iceland, Liechtenstein, Norway, and Sweden) except Switzerland. Thus, the European Economic Area consists of the fifteen nations comprising the European Union (EU) plus Norway, Iceland, and Liechtenstein. See Jeremy Brown, *Parallel Imports In the United Kingdom and The EEC*, in INTERNATIONAL INTELLECTUAL PROPERTY LAW AND POLICY 333 (Hugh C. Hansen ed., 1996).

²⁷¹ Article 7 of the First Council Directive 89/104/EEC of 21 December 1988. Article 7(1) provides that the trademark shall not entitle the proprietor to prohibit its use in relation to goods, which have been put on the market in the Community under that trademark by the proprietor or with his consent.

²⁷² See *Deutsche Grammophon v. Metro*, 1971 E.C.R. 487, 2 IIC 429 (1971).

²⁷³ See Donnelly, *supra* note 82, at 470.

in the *Sterling Drug* case.²⁷⁴ The ECJ stated that derogation from the principle of free movement of goods is not justified where the product has been put on the market legally by the patentee himself or with his consent in the Member State from which it has been imported. In other words, the patent right to bar the parallel imports was exhausted if the patentee initially put those goods into a Member State's market by himself or with his consent.

2.2 The Raised Question: Whether Member States Still Have Authority to Apply an International Exhaustion Doctrine under the Community-wide Exhaustion Policy

Inevitably, there is an interesting problem in the application of the Community-wide exhaustion in the case of goods imported from outside the European Community. The question is whether the Member State is enabled either by court decision or by legislation to recognize the application of an international exhaustion doctrine to goods that were initially sold in a non-member country. In other words, the significant question is whether the principle of a Community-wide exhaustion excludes the possible application of an international exhaustion. This problem took place when a Member State attempted to apply the exhaustion doctrine to products that were first marketed outside the Community. The ECJ's answer on this question can cause a change or modification of the Member State's national law because previously some Member States had accepted an international exhaustion doctrine.²⁷⁵

²⁷⁴ See *Centrapharm v. Sterling Drug*, 1974 E.C.R. 1147, 6 IIC 102 (1975). This rule was extended in the *Merck* case. See *Merck v. Stephar*, Case No. 187/80, 13 IIC 70 (1982); and also see more detail in both cases in Section 3.2 Parallel Import in Patent.

²⁷⁵ For example, the United Kingdom and Germany formerly applied an international exhaustion doctrine.

Prior to legislating the Trademark Directive, a number of the Member States, such as Germany and the United Kingdom, applied and adopted the international exhaustion doctrine.²⁷⁶ Historically in the drafting of the Trademark Directive, the international exhaustion principle was initially used in Article 5 of the 1979 Draft,²⁷⁷ but later obliterated because of the pressure of some industrial Member States. At present Article 7 (1) in the revised draft of December 17, 1985 contains the principle of a Community-wide exhaustion instead of the principle of an international exhaustion. In addition, before the Community itself had the Community-wide policy on the question of exhaustion, there was a decision that allowed Member States make their own choices including adoption of an international exhaustion. According to the ECJ decision in 1982,

²⁷⁶ See The Germany court decision in the *Maja* case, Supreme Court decision, 22 January 1964, 1964 GRUR Int. 202; *Cinzano v. Java*, [1974] 2 CMLR 21, 4 IIC 432 (1974); see The United Kingdom court decision in the *Revlon* case, the result of court decision was closely to the application of international exhaustion doctrine. ; see Florian Albert & Christopher Heath, *Dyed But Not Exhausted-Parallel Imports and Trademarks in Germany*, 28 IIC 24, 26 (1997).; and also see Friedrich Karl Beier, *The Doctrine of Exhaustion in EEC Trademark Law- Scope and Limits*, 19 IIC 29 (1979)[hereinafter Beier, *Doctrine of Exhaustion in EEC*]

In the *Revlon* case, the United Kingdom Court of Appeal applied the international exhaustion doctrine and refused to allow a U.S. multinational company to assert its U.K. registered trademark to prohibit parallel imports. The U.S. company wanted to bar the parallel importation of goods initially sold in the U.S. with the consent of the U.S. parent company by complaining of passing-off and breach of trade mark. The Court concluded that the plaintiffs were not entitled to complain of passing-off because no misrepresentation took place in origin, class, or quality. The plaintiff satisfies in passing-off only if the goods are inferior quality (*Spalding v. Gamage*, (1915)32 RPC 273) or show the untrue representation in goods (*Bulmer v. Bollinger*, [1978] RPC 78). See *Revlon Inc and Others v. Cripps & Lee Ltd and Others*, Court of Appeal (Civil Division) [1980] FSR 85, 22 November 1979.

In Germany, the German *Reichsgericht* held that a trademark owner was not entitled to block further distribution of trademarked goods once he had put those goods on the market. The court favored the international exhaustion doctrine and characterized the trademark right as a personal right of universal validity. The trademark right "is not a right that can be territorially limited or separated; it is not subject to territorial boundaries". The principle of territorial independence in trademark found in Article 6(3) of the Paris Convention was construed as confirming that there was no legal link between trademark rights registered in different countries, but not taken so far as to obliterate the application of international exhaustion doctrine. See Florian Albert & Christopher Health, *Dyed But Not Exhausted-Parallel Imports and Trade Marks in Germany*, 28 IIC No. 1/1997, citing in 50 RGZ 229-Kolnisch Wasser, and 51 RCZ 263-Mariani).

²⁷⁷ See Proposal for a First Council Directive to Approximate the Laws of the Member States Relating to Trade Marks, 27 Nov. 1980, Ar. 11 Doc. COM (80) 635 final, at 1, 12 IIC 381 (1981).

the ECJ held that the EC Treaty did not prohibit a member state to adopt a rule on the international exhaustion doctrine.²⁷⁸

Although the European Union has recently adopted a Community-wide exhaustion as a standard, the question remains whether the Member States can go further and adopt an international exhaustion. The most thorough discussion of this question from the ECJ is to be found in the area of trademark in the *Silhouette* case. It is significant because this is the area in which there is specific legislation on the subject. The legislation was not conclusive on the question of whether it was permissible to adopt the international exhaustion beyond the Community-wide exhaustion. The wording in the Trademark Directive does not make it clear what the position is in the light of international exhaustion doctrine because it does not clearly state to prohibit the Member State in the application of an international exhaustion doctrine. Consequently, a recent question is whether the Trademark Directive permits the Member States to allow parallel imports from outside the EEA based on an international exhaustion doctrine.²⁷⁹ This question was obviously answered by the ECJ in *Silhouette International Schmied GmbH & Co. v. Hartlauer Handelsgesellschaft* case²⁸⁰

The *Silhouette* case brought to the ECJ by the Austrian Supreme Court for a preliminary ruling under Article 177 on the interpretation of Article 7.²⁸¹ As a result of

²⁷⁸ See Case 270/80 Polydor v. Harlequin Record Shops, [1982] 1 CMLR 677, Feb. 9, 1982.

²⁷⁹ Unlike the EC Treaty establishing a customs union, the EEA Agreement creates a free trade area. The principle of free movement of goods under Article 8 EEA applies only to goods originating in the EEA.

²⁸⁰ Case C-355/96, *Silhouette Int'l Schmied v. Hartlauer Handelsgesellschaft*, [1998] 2 CMLR. 953, 29 IIC 920 (1998)[hereinafter *Silhouette Case*]

²⁸¹ *Id.* at 927. (From the facts, *Silhouette* produced high-price spectacles and *Hartlauer* was an Austrian retailer in low-price products that wanted to market the high-price *Silhouette*'s products. *Silhouette* refused to grant its permission because it believed that a low-price policy of *Hartlauer* might damage *Silhouette*'s reputation. However, *Hartlauer* obtained those outmoded spectacles from Bulgaria and later sold them in Austrian stores without *Silhouette*'s permission.)

Hartlauer's parallel imports, Silhouette commenced an action against Hartlauer. This case was dismissed by both the District Court Steyr and by the Court of Appeal Linz under the international exhaustion doctrine. Finally, Silhouette appealed to the Supreme Court. The Austrian Supreme Court decided to bring the case to the ECJ for a preliminary ruling on whether Member State's use of an international exhaustion to restrict the resale of genuine goods put on the market is contrary to Article 7(1) of the Trademark Directive.

The ECJ stated that in the terms of the Directive, Article 7(1) permits the exhaustion principle only for Community sales, not for international transactions. According to legislative history of the Directive, the international exhaustion was not intended to be adopted. Moreover, Article 7(1) derogates the exclusive right of the trademark owner under Article 5(1) and it should not be construed broadly. To harmonize the scope of exhaustion doctrine, this directive should be interpreted as excluding the international exhaustion doctrine and only adopting the Community-wide exhaustion. If the Member States were free to determine whether they permitted international exhaustion or not, the solution to parallel import issues would not be harmonized. The same gray market products might be prohibited in some Member States whilst being allowed in others.²⁸² Such a situation would cause incompatible internal regulations and raise a barrier to the free movement of goods.²⁸³ Conclusively, the Court interpreted Article 7(1) that Member States are precluded from adopting the international exhaustion.

²⁸² Under an international exhaustion doctrine, the trademark owner could not bar parallel imports from the third countries.

²⁸³ See Norman, *supra* note 269, at 163. (briefing the opinion of Advocate General Jacobs in the *Silhouette* case. In conclusion, Advocate General Jacobs advised to the Court that the Trademark Directive precluded international exhaustion doctrine based upon three supports: (1) the language and structure of the Directive, (2) Recital 3 and 9 of the Directive, the harmonization purpose of the Directive, and (3) the uniformity of national trademark law under the Community-wide exhaustion. -para. 33, 41 and 60 of the Opinion).

So the national rules providing exhaustion of trademark rights for products put on the market outside the EEA are contrary to Article 7(1).²⁸⁴

At this moment, the Member States have agreed to adopt the Community-wide exhaustion doctrine applying to all intellectual property rights.²⁸⁵ As the result of ECJ decision in *Silhouette* case, the Member State cannot apply or no longer is allowed to apply the international exhaustion doctrine to goods initially marketed outside the Community.²⁸⁶ Although the ECJ decision in *Silhouette* case seems to be based on the history and language of the Trademark Directive, the qualification on national choices with respect to exhaustion derived from the *Silhouette* case should be the qualification that applies in patent and copyright as well. Rationally, the rule on the Community-wide exhaustion should apply in the same way to trademark, copyright, and patent law in order

²⁸⁴ Nevertheless, the EFTA Court ruled in the *Mag* case ruled that EFTA Member States are free to recognize international exhaustion of rights. Recently, the Member States of EFTA are Norway, Liechtenstein and Iceland. Because of the difference in purpose and scope of the E.C. Treaty and the EEA Agreement, the decision of the ECJ and EFTA Court is different by former prohibiting international exhaustion doctrine, but latter not. See Opinion 1/91 of the Court of Justice concerning the Draft Agreement between the Community and the countries of the European Free Trade Association, relating to the creation of the European Economic Area [1991] ECR I-6079; and also see Case E-2/97 *Mag Instrument Inc. v. California Trading Company*, Norway, Advisory Opinion of December 3, 1997, [1998] 1 CMLR 331, 29 IIC 316 (1998).

²⁸⁵ The Community-wide exhaustion is apparent under the Article 7(1) of the Trademark Directive. In the case of patent and copyright, despite no specific legislation, there are the court's decisions confirming that the Community-wide exhaustion also applies to patent and copyright. See *Deutsche Grammophon v. Metro*, [1971] ECR 487, 2 IIC 429 (1971); Joined Case No. 55/80 and 57/80, *Musikvertrieb Membran & K-tle v. GEMA*, January 20, 1981, 12 IIC 526 (1981); Case No. 58/0 *Dansk Supermarket v. Imercon*, January 22, 1981, 6 IIC 831 (1981); *Centrapharm v. Sterling Drug*, [1974] ECR 1147, 6 IIC 102 (1975); *Merck v. Stephar & Exler*, [1981] ECR 2063, 13 IIC 70 (1982); see Verma, *Exhaustion of IPRs and Free Trade*, *supra* note 160, at 549 (mentioning that unlike trademark, there is no Community Directive on patents. However, the Community Patent Convention of 1975, which has not yet come into force, confirms that the Community patent is subject to the exhaustion doctrine.); and also see MELANIE FARQUHARSON & VICENT SMITH, *PARALLEL TRADE IN EUROPE* 15-16 (1998).

²⁸⁶ See *Albert & Heath*, *supra* note 276, at 25. (pointing out that in Germany, the German Federal Supreme Court in *Dyed Jeans* case eliminated the long-standing German rule of international exhaustion for trademarks based on its interpretation of Article 7 of the Trademark Directive.)

to give confidence that those laws are consistent and confined with the EU policy on harmonization.²⁸⁷

2.3 International Exhaustion Doctrine Absolutely Never Died in The European Union:

Dejă Vu of International Exhaustion Doctrine

Even though the European Court of Justice attempts either to limit the application of exhaustion doctrine in Community level or to eradicate the international exhaustion doctrine, the international exhaustion does not go away but keeps coming back in different ways. For instance, the debate on international exhaustion was reborn by the recent *Zino Davidoff* case,²⁸⁸ decided by the High Court of the United Kingdom. This case also represents one of the shortcomings of the application of Community-wide exhaustion doctrine, which realizes that the EU attempt to establish the Community-wide exhaustion doctrine (an intermediate exhaustion) has not been complete.

In the *Davidoff* case, the English High Court held that Article 7(1) does not preclude the operation of the international exhaustion doctrine when the trademark owner had given consent expressly or implicitly to a third party to market those goods within the Community. This decision effectively favors an international exhaustion not a Community-wide exhaustion because the products in question were initially marketed in Singapore, a non-member nation. Indeed, if the court had reasoned this case only under the Community-wide doctrine, the trademark owner would have the right to prohibit such parallel import because his trademark rights would not be exhausted. Some scholars

²⁸⁷ If the rule differs among copyright, patent and trademark, it may cause shortcoming, which the owners of IPRs or parallel imports wisely play with this distinction and finally cause a lot of questions to the court.

mention that the *Davidoff* case decided in favor of an international exhaustion doctrine via the back door. The English High Court neither followed nor conflicted with the ECJ decision in *Silhouette*.²⁸⁹ However, some scholars comment that the Court allowed such parallel import based on the contractual and consensual aspects of commercial transaction with respect to trademark goods but not directly based on the application of international exhaustion. Thus, it does not conflict with the *Silhouette* ECJ decision.²⁹⁰ Although the English High Court may have reliable reason under the theory of consent to support that it does not directly conflict with the ECJ decision in *Silhouette* case,²⁹¹ certainly the result of *Davidoff* case is manifestly similar to the application of an international exhaustion.

2.4 Conclusion

Member States can take neither positive legislative action via their national law nor judiciary action in their national jurisdiction to apply an international exhaustion rule for IPRs in respect of products put on the market outside the EEA. However, there is an inconsistency in the application of a Community-wide exhaustion doctrine in Member

²⁸⁸ See *Zino Davidoff SA v. A&G Imports Ltd*, [1999] 2 CMLR 1056, 30 IIC 567 (1999).

²⁸⁹ See Norman, *supra* note 269, at 159, 164 and 169.

²⁹⁰ See Irine A. Stamatoudi & Paul L.C. Torremans, *International Exhaustion in the European Union in the Light of "Zino Davidoff": Contract Versus Trade Mark Law?*, 31 IIC 123, 129-133 and 141(2000). (reasoning that the prohibition of international exhaustion imposed by the interpretation of Art. 7(1) of the Directive in *Silhouette* stands, but that leaves the rightholder free to dispose of his rights consensually and to consent to the unfettered international distribution of its goods. The *Zino Davidoff* case seems "to suggest that the *Silhouette* ruling on international exhaustion needs to be put in its proper context, rather limited because there is real life outside the *Silhouette* scenario."); and also see W.R. Cornish, *Trade Marks: Portcullis for the EEA?*, [1998] EIPR 172, 177.

²⁹¹ The discussion in the theory of consent in the *Davidoff* case will be illustrated in following section in Parallel Imports in Trademark.

States that do not directly apply an international exhaustion doctrine but the outcome of the court decision is similar to the application of international exhaustion.²⁹²

3. Circulation of Parallel Import Goods Inside The European Union

The primary issue of parallel imports within the Community is whether an IPRs owner in one Member State can prohibit parallel imports of goods that were first marketed in another Member State. In other words, it is possible that the Community-wide exhaustion does not apply and an IPRs owner in an importing Member State can assert his exclusive right to bar parallel imports from an exporting Member State.

Significantly, studying the issue of the application of Community-wide exhaustion in the European Community is useful for supporting the concept of adopting international exhaustion doctrine as the harmonious approach at a global level. The reason is that the European Community is concerned that the Community-wide exhaustion doctrine encourages the establishment of a single market, the free movement of goods and free competition in the Community, the international exhaustion doctrine should be the best instrument for supporting free trade, free movement of goods and free competition at a global level. The solution to the issue when the EU Member States apply the Community-wide exhaustion can be practically exploited by other nations in case that the similar problem occurs when applying the international exhaustion in their own jurisdiction.

²⁹² The other members cannot dispute that such national court judgment violates the Community law since it does not directly conflict with the Community law.

Up to this point, this critical commentary on EU decisions is focused exclusively on the Community-wide exhaustion. As mentioned above, some inconsistency problems result from these decisions. However, within the framework of Community-wide exhaustion the EC has developed a consistent set of rules on the limitation of exhaustion doctrine which are worth studying because this dissertation proposes that these approaches of EC might be usefully included in a more comprehensive system of international exhaustion in the EC or elsewhere. This part will not only describe the limitation of EC rulings that can teach the others about the ultimate preference of international exhaustion doctrine over national or regional exhaustion doctrine, but also discuss about some other aspects of EU law, which are more successful, particularly in the general question of exception to exhaustion whether it is international, nation or regional exhaustion.

3.1 The Complex Relationship Between Article 28 and 30 of the EEC Treaty

The application of Article 28 and 30 in connection with a Community-wide exhaustion is a subtle and important matter. The IPRs owner can assert Article 30 (formerly 36) to exclude from the application of a Community-wide exhaustion doctrine under a specific circumstance. The EJC has a duty to decide on the application of Articles 28 and 30 and has the authority to apply them when allowing or prohibiting parallel imports. However, in the case of trade with non-EU Member State, the ECJ does not have the authority to apply Articles 28 and 30.²⁹³

²⁹³ See Jessica Jones, *Does an Opportunity Still Exist for the Development of a Doctrine of International Exhaustion at a Community Level under Article 28 and 30?*, [2000] EIPR 175. (pointing out that “one of

Indeed, Article 28 (formerly Article 30) and Article 30 (formerly Article 36) of the EEC Treaty are used as driving instruments to guarantee both the principle of free movement of goods and the protection of IPRs. Article 28 recognizes the existence of intellectual property rights and Article 30 addresses the exercise of intellectual property rights. Although the national laws of Member States determine intellectual property rights, the exercise of such rights must be consistent with the rule and purpose of the EEC Treaty.²⁹⁴ The relationship between Articles 28 and 30 in the European Court of Justice's interpretation of the Treaty is called the existence/exercise dichotomy.²⁹⁵

In order to promote the free movement of goods within the Community, Article 28 prohibits all quantitative restrictions on imports and exports between Member States and all measures having an equivalent effect.²⁹⁶ However, there are some exceptions in certain circumstances under Article 30 that allow member states to overcome the free movement principle in the area of the IPRs protection.²⁹⁷ Article 30 makes an exception for restrictions justified, *inter alia*, on the grounds of the protection of industrial property.

the consequences of the application of Article 28 (formerly 30) to measures to enforce national IPRs against genuine goods from a third country might be the development of a doctrine of international exhaustion, albeit with a very limited scope.”)

²⁹⁴ The European Court of Justice frequently addressed the concept in many parallel import cases such as *Centrafarm v. Sterling Drug*, *Centrafarm v. Winthrop*, and *Merck v. Stephar*. The detail in those cases will be discussed in the following paragraph.

²⁹⁵ See GOVAERE, *supra* note 85, at 69; In the absence of adequate harmonization of intellectual property law, it is the exclusive duty of the European Court of Justice to determine the relationship between national IPRs and Community principles. The ECJ creates the existence/exercise dichotomy, which is not only applied in the context of goods but applied in the context of service as well. See Case 262/81, *Coditel v. Cine Vog Films (Coditel II)*, Judgment of October 6, 1982, [1983] 1 CMLR 49, 14 IIC 405 (1983).

²⁹⁶ See the EEC Treaty, *supra* note 262, art. 28. Article 28 of the EEC Treaty provides that “Quantitative restrictions on imports and all measures having equivalent effect shall, without prejudice to the following provision, be prohibited between Member States.”

²⁹⁷ *Id.* art. 30. Article 30 of the EEC Treaty states that “The provisions of Article 28-32 shall not preclude prohibitions or restrictions on imports, exports or goods in transit justified on grounds of public morality, public policy or public security; the protection of health and life of humans, animals or plants; the protection of national treasures possessing artistic, historic or archeological value; or *the protection of industrial and commercial property*. Such prohibitions or restrictions shall not, however, constitute a means of arbitrary discrimination or a disguised restriction on trade between Member States.” (emphasis added)

The Court stated clearly that the exception is only intended to allow the national laws to derogate the free movement of goods principle only under certain circumstances.²⁹⁸

3.2 The Limitation of Free Movement of Goods under the Specific Subject-Matter of Intellectual Property Rights in the Case of Parallel Imports

In general, when the goods are initially marketed in Member States, those goods can be freely transported from one Member State to another Member State. However, there are some exemptions that the IPRs owners still have a right to bar the parallel imports in “limited and certain circumstances,” which can be justified under the “specific subject-matter of intellectual property” in Article 30. The Court has introduced the concept of “specific subject-matter” of IPRs to determine whether the IPRs owners exercised their right properly. If the right exercised satisfies the specific subject-matter concept, it is deemed a normal use and allowed under EC law.²⁹⁹

Due to the varying perception in each type of IPRs, the Court decided the specific subject-matter of IPRs differently among trademark, patent, and copyright. Each intellectual property right has a specific function to fulfill; hence the justification of each

²⁹⁸ The ECJ stated “As an exception to one of the fundamental principles of the Common Market, Article 36 (currently Article 30) only admits derogations from the free movement of goods to the extent that such derogations are justified for the purpose of safeguarding rights that constitute the specific subject matter of this property.” *See* Case No. 192/73 *Van Zuylen Freres v. HAG AG*, July 3, 1974, 5 IIC 338, 340 (1974). In addition, the second sentence of Article 36 provides that the restrictions permitted under the first sentence shall not constitute a means of arbitrary discrimination or a disguised restriction of trade.

²⁹⁹ *See* Case 24/67, *Parke, Davis & Co v. Probell, Reese, Beintema-Interpharm and Centrafarm*, Judgment of February 29, 1968, [1968] CMLR 47. (In respect to the rule of competition, the Court ruled that the existence of the rights granted by a Member State to the patent owner is not affected by the prohibitions contained in Articles 85(1) and 86 of the Treaty. The Court introduced a triple distinction as guideline for balancing between national intellectual property rights and the Community rules on competition. Firstly, the existence of intellectual property rights is not affected by the rules on competition. Secondly, the normal exercise of those rights is not affected by the rules on competition either. Thirdly, the abusive exercise of those rights is prohibited by the rules on competition.)

intellectual property right may diverge from each other. The notion of specific subject-matter of IPRs has so far taken place primarily with respect to trademark. Similar discussion also appears in the case of patent and copyright. Consequently, the following sections will address the issue of parallel imports versus the exhaustion doctrine in the separate contexts of trademark, patent, and copyright respectively.

3.3 Parallel Imports in Trademark

3.3.1 The Relationship between Articles 28 and 30 of the EEC Treaty and Article 7 of Trademark Directive

As mentioned above, in the area of trademark, there is a specific legislation, the European Union Trademark Directive.³⁰⁰ This Directive is intended to harmonize the national law of Member States.³⁰¹ Relating to parallel imports, Article 5 codifies the rights of a trademark proprietor;³⁰² however, the rights are limited by the principle of a Community-wide exhaustion.³⁰³ The principle of Community-wide exhaustion was obviously codified in Article 7 of the Trademark Directive.

Article 7 of The Trademark Directive on the Exhaustion of the Rights Conferred by a Trade Mark states:³⁰⁴

1. The trademark shall not entitle the proprietor to prohibit its use in relation to goods, which have been put on the market in the Community under that trademark by the proprietor or with his consent.

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

³⁰⁰ Council Directive 89/104/EEC of 21 December 1988 to approximate the laws of the Member States relating to trade marks [1989] OJ L40/1. [hereinafter Trademark Directive]

³⁰¹ *Id.* (declaring in the first recital and ninth recital in the preamble of the Directive.)

³⁰² *Id.*, art. 5.

³⁰³ See the *Silhouette Case*, *supra* note 280.

³⁰⁴ See EC Trademark Directive, *supra* note 300, art. 7.

The Community policy on a Community-wide exhaustion under Article 7(1) of Trademark Directive supports the free movement of goods principle and the concept of single market under Article 28 of the EEC Treaty by reducing the obstacles to importation of goods between Member States. However, the exemption of a Community-wide exhaustion doctrine is codified in Article 7(2). The exemption is based on the concept of the legitimate reasons. Under the concept of legitimate reasons, the trademark owners still have exclusive rights to prohibit the parallel imports of goods because their right is not exhausted if there is a legitimate reason to oppose such importation. The concept of legitimate reasons is similar to the concept of specific subject-matter of IPRs under Article 30, which dilutes the free movement of goods principle under Article 28.

The interesting question raised on the relationship between Article 30 exception based on the jurisprudence of ECJ on specific subject-matter standard and Article 7(2) exception under the Trademark Directive based on the concept of legitimate reasons. The question is whether the two different articulations of standard of making exception have the same scope when mapped on one other concerning the trademark exhaustion in Community. Conceptually, the scope of Article 7(2) exception should not be bigger than that of Article 30 but rather be of the same scope. Based on the reason that Article 7(2) is just a statutory counterpart of the specific subject-matter of Article 30; thus, it should get the same result one way or another.³⁰⁵ Rationally, if at least Article 7(2) permits

³⁰⁵ The positive affirmation to support this conception may be seen in the opinion of Advocate General Stix-Hackl in the ECJ's *Davidoff* case. "In accordance with the relationship outlined between the free movement of goods and the exercise of the rights deriving from the trade mark, the exercise of these latter rights under Article 7(2) in the context of trade within the Community is understood as an exception to the free movement of goods which is permissible only so long as it is justified for the safeguarding of rights constitution the specific subject-matter of the right conferred by the trade mark." See The Opinion of Advocate General Stix-Hackl, in Joined Cases C-414/99, C-415/99 and C-416/99 *Zino Davidoff SA v. A&G Imports Ltd, Levi Strauss & Co and Levi Strauss (UK) Ltd v. Tesco Stores, Tesco plc and Costco*

exception that should not be permitted under Article 30 specific subject-matter standard, it should conflict with the fundamental principle of free movement of goods under Article 28 of the Treaty of Rome. Based on the concept of supremacy, the application of the EC directive should not conflict with the Treaty of Rome. In other words, it may be considered that the exception based on Article 7(2) legitimate reason should not be more permissive than the exception based on Article 30 specific subject-matter.

In conclusion, the structure of the relationship between Article 7(1) and (2) of Trademark Directive typically imitates the structure of the relationship between Article 28 and 30 but only the former specifically applies to trademark and the latter generally applies to all kinds of IPRs. The scope of exemption based on legitimate reason standard under Article 7(2) should not be more permissive than that of exemption based on specific subject-matter standard under Article 30. Hence, at this stage, the following sections will discuss the specific subject-matter of trademark under Article 30 and then analyze the application and relationship between Articles 7(1) and 7(2).

3.3.2 *The Specific Subject-Matter of Trademark*

In relation to parallel imports, it is important to focus on the ECJ's interpretation of "specific subject-matter" in trademark protection under Article 30. The Court's decisions seem to indicate two main functions of trademarks: guaranteed use of the trademark and a guarantee of the product quality for the perspective consumers. The

Wholesale UK Ltd., delivered on 5 April 2001, at para.116, available at <http://www.curia.eu.int> (visited Feb. 27, 2002). [hereinafter Opinion of Advocate General Stix-Hackl in ECJ's Davidoff Case]

courts analyzed these two purposes in the light of concerns about the free movement of goods and the exclusive rights of the trademark owner.

With respect to the first function of trademark, the “specific subject-matter” of the trademark was characterized as a guarantee of exclusive use of the trademark owner to put trademark products into circulation. As revealed in *Centrafarm v. Winthrop* case, the Court used the words “the specific subject-matter of the trademark” to refer to the function of a trademark as the guarantee of a trademark owner’s exclusive right to use and prohibit others from using the trademark without permission.³⁰⁶ The trademark was therefore intended to protect the owner against competitors, who took advantage of the status and reputation of trademark by illegally selling products bearing that trademark.

In the second function of trademark, trademark serves as the guarantee of the product quality and the source of origin. In *Terrapin v. Terranova*, the Court addressed the function of trademark as a quality indicator by stating, “the basic function of the trademark is to guarantee to consumers that the product has the same origin.”³⁰⁷ As a result of consumer confusion, the trademark owner can assert his exclusive right to prohibit the importation of goods lawfully made in another Member State without violating the principle of free movement of goods.³⁰⁸ In addition, if the trademark owner in the exporting country and in the imported country is either the same person or if they

³⁰⁶ See Case 16/74, *Centrafarm BV and Adriaan De Peijper v. Winthrop BV*, Judgment of October 31, [1974] 2 ECR 1183, 6 IIC 110 (1975).

³⁰⁷ Case 119/75 *Terrapin v. Terranova*, Judgment of June 22, 1976, [1976] ECR 1183, 7 IIC 520, 542 (1976).

³⁰⁸ Whether the consumer confuses original products with imported products is a matter for national trademark law to determine because of absence of unity among Member States in this issue. The right of the trademark owner to bar importation is subject to the prohibition of arbitrary discrimination or disguised restrictions on intra-Community trade under the second sentence of Article 30. See Case C-317/91 *Deutsche Renault AG v. Audi AG*, Judgment of November 30, 1993, [1993] ECR I-6227, at para. 29-39.

are several persons who are *economically linked* to one another,³⁰⁹ it seems that the functions of trademark as a source indication and a quality indicator are not impaired as revealed in the *Ideal Standard* case.³¹⁰ In other words, the *Ideal Standard* case ruled that the functions of a trademark to indicate the origin of goods and to guarantee the consistency of quality³¹¹ were not impaired by allowing parallel imports with the same trademark as the domestically sold goods.³¹² In brief, due to the court's decisions, the specific subject-matter of trademark is mainly to guarantee the exclusive rights, the quality of product, and the function of trademark as a source indicator.³¹³

3.3.3 Article 7(1) of Trademark Directive A Community-wide Exhaustion: The Consent as the Important Requirement for Exhaustion Doctrine

3.3.3. 1 *Introduction on Theory of Consent*

One basis on which exception to Community-wide exhaustion may be justified if the IPRs owner in such case gives consent to the circulation of goods. Of course, the

³⁰⁹ There are many patterns of economical link such as the parent / subsidiary company, wholly own subsidiary, licensor/ license, or exclusive distributor.; See Fernando Coastillo De La Torre, *Trade Marks and Free Movement of Pharmaceuticals in the European Community: To Partition or Not to Partition the Market*, [1997] EIPR, 304, 311. (mentioning that if the those products have been produced under the control of the same undertaking, the products are "original.")

³¹⁰ Case c-9/93, IHT International Heiztechnik v. Ideal-Standard, [1994] 3 CMLR 857, at para. 34. [hereinafter *Ideal-Standard* case]

³¹¹ See *Albert & Health*, *supra* note 276, at 29. (pointing out that if only based upon the doctrine of the "common origin of goods," the international exhaustion might be applicable, but the additional functions of trademark as guarantee of quality make worldwide exhaustion doctrine inapplicable.)

³¹² See *Ideal-Standard* case, *supra* note 310, at para.2-12 (From the facts, the American Standard group owned the "Ideal Standard" trademark in both France and in Germany. There were two different subsidiaries that owned the trademark: the French "Ideal-Standard AS" and the German "Ideal-Standard GmbH." The Ideal Standard in Germany objected to imports of the same trademark and obtained a ruling in the German court of first instance upholding its right to block the importation. The Oberlandesgericht (Higher Regional Court) inquired into the interpretation of Articles 30 and 36 EEC.)

³¹³ However, there is another role of trademark, which is to guarantee the reputation or goodwill of trademark owner that the court also considers whether such parallel import impairs the trademark owner's

concept of consent is complicated. There are different types of consent: explicit or express consent, implied consent, and constructive consent. The consent of the IPRs owner may be expressed explicitly in the contract. However, the consent may be implied by considering all circumstances. Under this concept, at least the IPRs owners must know that once they sell their goods, those goods may be resold and still agree to sell those goods to the buyer. Thus merely silence may not be considered as implied consent to resale or import those goods to other jurisdictions.³¹⁴ In addition, there is another type of consent, a fictional consent (so-called constructive consent), which is the consent that the law impose on the party who neither expressed nor implied and maybe never even though but the law assumes that such person gave his consent.³¹⁵ Nevertheless, in the issue of consent, it depends on the court interpretation whether such consent is sufficient to trigger the exhaustion doctrine or to consider as having the IPRs owner's consent to importation into the Community.

reputation because if it impairs, such parallel import should not be allowed. It should be considered as a part of the specific subject-matter.

³¹⁴ See JOHN D. CALAMARI & JOSEPH M. PERILLO, *CONTRACTS* 83 (1987) (explaining that in contract law, merely silence does not constitute an acceptance of an offer, unless the relationship of the parties and the circumstances may reasonably conclude that silence is acceptance, which is so-called acceptance by silence or implied in fact contracts.)

³¹⁵ *Id.* at 89, citing in *Miller v. Stevens*, 224 Mich. 626, 195 N.W. 481 (1923) (Under the contract law, it is possible that acceptance arise by affirmative conduct, "a contract implied in fact arises under circumstances which, according to the ordinary course of dealing and common understanding of men, show a mutual intention to contract... A contract is implied in fact where the intention is not manifested by direct or explicit word between parties, but is to be gathered by implication or proper deduction from the conduct of the parties, language used or things done by them, or other pertinent circumstances attending the transaction."); and also see Richard A. Epstein, *Article, Consent, Not Power, as the Basis of Jurisdiction*, U. CHI. LEGAL F1 (2001). (pointing out the issue of consent, particularly in the implied consent, involve with the jurisdiction matter.)

3.3.3.2 Consent as the Important Requirement for Community-wide Exhaustion Doctrine under Article 7(1) and Unharmonious Answer in Question of Consent Whether It Should be Only Express Consent or Include Implied Consent.

Under the exhaustion doctrine, the right of the trademark owner is exhausted after the first sale of the goods bearing such trademark either by himself or by his consent. The consent of the trademark owner is considered as one important requirement for triggering the exhaustion doctrine. The concept of consent has been scrutinized and developed by the European Court of Justice in many cases. By referring to the consent theory, the ECJ was faced with the question of what constituted the placing of the goods on the market in the Community with the trademark owner's consent. The parallel importers always argued either that the trademark right is exhausted after the trademark owner consents to initially market his products or that the products were imported with the consent of the trademark owner either through express or implied consent.

The Court ruled in the *Hag II* case that when the product was placed in the market by the trademark owner or by "economically linked" person with his consent, the trademark right was exhausted by such consent.³¹⁶ The Court relied on the doctrine of consent set out in *Hag II*³¹⁷ and also infused the concept of control into consent

³¹⁶ See Case C-10/89, SA CNL-Sucal NV v. Hag GF AG, [1990] 3 CMLR 571. at para. 34. [hereinafter *HAG II* case]; and also see *Ideal-Standard* case, *supra* note 310, at para. 40. (The Oberlandesgericht's question is whether the same principles apply where there is no economic link with the assignor. In other words, the ECJ considered whether an assignment of trademark rights exhausted the trademark rights.)

³¹⁷ In respect of consent doctrine, the Court in the *Hag II* case adopted the doctrine of consent and stated that the exhaustion of IPRs takes place only with the owner's consent to put its product into circulation. The Court focused on the difference between licenses and assignment in ownership and possibility of control the quality of products. The licensee can control the quality of the licensee's products by means of inserting the contract clause in quality control. In case of a contract of assignment, due to absence of any economic link, the assignor does not have right to control the quality of products. Thus, "the consent implicit in any

analysis.³¹⁸ In the case of assignment, different quality goods could be manufactured under the same trademark and cause consumer confusion.³¹⁹ Consequently, the Court in *Ideal-Standard* case reasoned that, due to a lack of control, consent to an assignment is not the consent required for exhaustion.³²⁰

Additionally, there are two interesting cases worth discussing in the issue of consent: the *Sebago* case,³²¹ and the *Davidoff* case.³²² The former case was decided by the European Court of Justice; the latter was decided by the English High Court. Although the facts and arguments in both case are similar, the outcome of the court' decisions is not consistent. The former prohibits such parallel imports and the latter allows it. Thus, as the result of this inconsistency, it is important to explain and analyze the facts and arguments in both cases

In the *Sebago* case, the facts are that GB-Unic had advertised for sale some 2,561 pairs of Dockside Sebago shoes for sale in its Belgian hypermarkets. The shoes were genuine goods, manufactured in El Salvador and acquired by an intermediary specializing in parallel imports. Sebago, a U.S. company, and its exclusive distributor sued for

assignment is not the consent required for the application of the doctrine of exhaustion of rights." See *HAG II* case, *supra* note 316, at para. 43 and 37-41.

³¹⁸ In relation to concept of control, the determinant element is not the actual exercise of control but rather be the possibility of control over those goods. See Case C-267/95 and C-268/95 *Beecham Group v. Europharm of Worthing Ltd. and Merck & Co. Inc. v. Primecrown Ltd.*, [1996] ECR I-6285, 29 IIC 184 (1998).

³¹⁹ Although the court decision focuses on protecting consumers in their expectation of quality, it also benefits proprietors of trademarks by allowing them restrain parallel imports.

³²⁰ See *Ideal-Standard* case, *supra* note 310, at para. 43.

The Court clarified:

"The consent implicit in any assignment is not the consent required for the application of the doctrine of exhaustion of rights. For that, the owner of the right in the importing State must, directly or indirectly, be able to determine the products to which the trade mark may be affixed in the exporting State and control their quality. That power is lost if, by assignment, control over the trade mark is surrendered to a third party having no economic link with the assignor."

³²¹ Case C-173/98-*Sebago Inc. and Ancienne Maison Dubois et Fils SA v. GB-Unic SA*, [1999] 2 CMLR 1317, 31 IIC 587 (2000).[hereinafter *Sebago* case]

trademark infringement under the provisions of Article 13A (8) of the Uniform Benelux Law on Trade Marks, as amended. In the ECJ decision, the Advocate General noted that paragraph 8 of the judgment in *Centrafarm v. Winthrop* used the phrase “put into circulation” to describe the event which gives rise to intra-Community exhaustion. The phrase could only refer to a particular batch of goods, and so a trademark owner would retain all rights in relation to any batches still remaining in the warehouse. The exhaustion did not concern other sales of the same type of goods, but rather the subsequent dealings of individual products following the first sale.³²³ The Community law principle of the exhaustion of trademark rights relates to individual goods or batches of goods, not whole product lines.³²⁴

By relying on the concept of implied license, GB-Unic argued that by not imposing an export ban on its licensee in El Salvador, Sebago had given its consent to sale within the Community. In response to that argument, the ECJ stated that Article 7(1) of the Trademark Directive did not give a direct answer to the question of whether consent must be express or implied. Inevitably, implied consent quite simply meant introducing international exhaustion through the “back door”³²⁵ that conflicts with the purpose of Article 7(1). The Directive expressly limits the application of exhaustion doctrine only to goods put on the market in the Community not to goods put on outside

³²² See *Zino Davidoff SA v. A&G Imports Ltd.*, [1999] 2 CMLR 1056, 30 IIC 567 (1999).

³²³ This ruling was re-affirmed by the English High Court. In the *Davidoff* case, the English High Court also ruled that the principle of exhaustion concerned only specific individual goods not the product lines or types of products.

³²⁴ See *Sebago* case, *supra* not 321, at para. 24. (referring to the phrase “further commercialization” in Article 7(2) and to the previously cited paragraphs in the *Christian Dior* and *Deenik* cases showed that the principle of exhaustion concerned only specific goods.)

³²⁵ See more discussions and details in the *Davidoff* case in the following paragraph.

the Community.³²⁶ Finally, the Court rejected GB-Unic's argument based on implied consent. The Court decided that the right of trademark owner was not exhausted because putting those goods outside the Community did not exhaust the proprietor's right to oppose the importation of those goods without his consent.

In the *Davidoff* case, the defendant's principal argument was based on the consent theory, similar to the *Sebago* case. The important question was whether the plaintiff had actually consented to an onward sale of those products. There was no importation restriction clause in the contract. It is not clear whether the trademark owner's consent while marketing his products in Singapore also implicitly extended to the free circulation and sale of those products throughout the world. The defendant argued that the resale of the parallel goods still left the distributor to sell in the contract territory either without restricting the purchasers' freedom to supply whomever they want or by notifying the purchasers of the legally binding obligations on them.³²⁷ The Court agreed with the defendant's argument. This was consistent with the decision in *Roussell Uclaf v. Hockly*

³²⁶In addition, there is an interesting question of who bears the burden of proving consent for the sale of trademarked goods inside. Until now, the European Court of Justice and the EEA did not clearly answer this question. In the *Silhouette* case and the *Sebago* case, the court was silent on the issue of which party bears the burden of proof. Since neither the Trademark Directive nor the European Court of Justice could specify who the burden of proof, the burden of proof is considered as a matter of national law. See Thomas Hays, *The Burden of Proof in Parallel-Importation Cases*, [2000] EIPR 353-58. (discussing on the issue of the burden of proof in parallel import cases in the EU.)

³²⁷ See Sramatoudi & Torremans, *supra* note 290, at 130. (pointing out that according to no restriction clause in the sale contract, it means that the silence in the sale contract implicitly consent the buyer or distributor to further distribute those goods in other states. Indeed, the IPRs owner free to dispose of his rights and consent to the free international distribution of its goods or free to impose the restriction in circulation of goods. Moreover, the IPRs owner can also consent to re-importation into the Community of the trademarked products and waive its non-exhausted rights under the Community-wide exhaustion doctrine. The confirmation of this concept can be found in the Advocate General's conclusion in *Silhouette* case, stating "if *Silhouette* had consented to marketing in the EEA the answer to the first question would clearly be that *Silhouette* could not oppose the imports of its products into Austria."-para. 27)

International Ltd.,³²⁸ in which the court ruled that everyone further down the chain of distribution had to know of restriction clauses that limited where the goods could be sold. However in the *Davidoff* case, there was no notice of a distribution restriction on the product. The plaintiff argued that only explicit consent was effective to trigger exhaustion. The Court rejected this argument and relied on the rule in the *Betts* case,³²⁹ which stated that consent could be either implied or express.

In addition, in the *Davidoff* case the plaintiff's products were considered high-cost luxury products. The trademark owner's exclusive licensee manufactured the products in France and the products were distributed and marketed throughout the world under the trademark Davidoff. The defendant obtained the products and removed the batch code. The question was whether the removal of the batch codes by the defendant amounted to "mental impairment" of the trademark envisaged by the Court's ruling in the *Christian*

³²⁸ See *Roussel Uclaf v. Hockley International Ltd.*, [1996] 14 R.P.C. 441, 443-44. (The English court decision by Judge Jacob ruled that the notice of the limitation must be "brought home first to the person originally supplied and, second, to subsequent dealers in the product." From the facts, Roussel sued Hockley for patent infringement because the defendant imported the patent products into the United Kingdom, which was prohibited under the restriction notice. The notice in this case was on the label stated that "FOR USE IN PRC ONLY. RE-IMPORT FORBIDDEN." The Court also noticeably stated "limited licenses require that notice be brought to the attention of every person down the chain of supply."); The notice of restriction must be brought home to the defendant *before he acquired the products*. See *Hazeltine Corporation v. Lissen Ltd* (1939) 56 R.P.C. 62. Moreover, in *Betts v. Willmott*, the court also stated "when a man has purchased an article he expects to have control of it, and there must be some clear and explicit agreement to the contrary to justify the vendor in saying that he has not given the purchaser his license to sell the article, or to use it wherever he pleases as against himself." See *Betts v. Willmott*, [1871] L.R. 6 Chapp 239 at 245; and also see David Wilkinson, *Breaking the Chain: Parallel Imports and the Missing Link*, [1997] EIPR 319, 320. (mentioning the Jacob J's judgment was contrary to earlier English and Commonwealth authorities on parallel imports and if *Roussel v. Hockley* now represents the law, worldwide exhaustion of patent rights has effectively been introduced through the back door by the imposition of evidential requirements which may, be virtually impossible to satisfy. In order to succeed in an infringement action on breach of limited license, the chain of notice has to be unbroken. This requirement made a successful lawsuit difficult for the plaintiff to achieve because the chain of notice was hard to prove.)

³²⁹ See *Betts v. Willmott* [1871] L.R. 6 Chapp 239.

Dior case.³³⁰ In the plaintiff's argument, the plaintiff asserted that the effect of the batch removal on the original product caused the "mental impairment" of the trademark.³³¹ Even though there had been damage to the physical or mental condition of the goods, Article 7(2) of the Directive would not be triggered unless such damage was substantial. In this case, the removal or obliteration of bar codes, which the plaintiff claimed hindered recall and damaged the appearance of the goods, was determined to have caused little harm.³³² Therefore, the plaintiff could not oppose such parallel importation.

On the subject of consent, the *Davidoff* decision was incompatible with the ruling of the Court in the *Sebago* case. In the *Sebago* case, the Court rejected the importer's argument that failure to impose an export ban created implied consent to import into the Community. On the other hand, the Court in the *Davidoff* case ruled in opposite way and its effect was similar to the application of international exhaustion 'by the back door',³³³ that allowed the parallel imports of goods initially marketed in non-member states.

In conclusion, the consent within the meaning of Article 7(1) must relate to each individual item of the product that has been initially put in the market by the consent's trademark owner, not relate to the type of goods. By referring to the "further

³³⁰ Case C-337/95 *Parfums Christian Dior SA and Parfums Christian Dior BA v. Evora B*, [1998] 1 CMLR 737.

³³¹ The batch codes were required under the Community's Cosmetics Directive. See Directive 76/768 [1976] O.J. L262/169.

³³² See *Zino Davidoff SA v. A&G Imports Ltd.*, [1999] 2 CMLR 1056, 30 IIC 567 (1999); and also see Norman, *supra* note 269, at 169.

³³³ The English High Court held that Article 7(1) does not preclude the operation of the international exhaustion doctrine when the trademark owner had given consent expressly or implicitly to a third party to market those goods within EEA. Some scholars commended that the Court decide in favor of international exhaustion doctrine which some scholars comment that the *Davidoff* case did not followed the *Silhouette* and conflict with the ECJ decision in *Silhouette*. See *id.* at 164 and 169. In contrast, some scholars comment that the Court allowed such parallel importation based on the contractual and consensual aspects of commercial transaction with respect to trademark goods but not directly based on the application of international exhaustion; consequently, it does not conflict with the *Silhouette* case. See Stamatoudi &

commercialization of goods” in Article 7(2), it shows that the principle of exhaustion concerns only specific goods but not the type of goods.³³⁴ However, it is not clear whether the consent should be only express consent or include implied consent because Article 7(1) does not mention this point. In the *Sebago* case, the ECJ court decided that the parallel importer could not assert that the trademark owner allowed him to import those goods inside the EU under the implied consent. In contrast, the English High Court ruled that in case of no obvious importation restrictions, the distributor or parallel importer was free to supply whomsoever or import into wherever. It seemed that the trademark owner gave the implied consent to sell or import those goods and the right of the trademark owner had been already exhausted after the first sale. The trademark owner can no longer prohibit the parallel import of those goods. The main reason why the ECJ decision and the English High Court decision are inconsistent in this issue is because of having different legal conceptions. Most common-law countries particularly the United Kingdom accept the implied license theory considered as the optional exhaustion,³³⁵ but many countries in continental Europe accept the principle of exhaustion (so-called automatic exhaustion).³³⁶

Torremans, *supra* note 290, at 129-33; and also see more detail in this discussion in the former part: Section 2 Circulation of Parallel Imported Goods from Outside the European Union.

³³⁴ See *Sebago* case, *supra* note 321, at para. 20.

³³⁵ Under the implied license theory, the sale of goods by an intellectual property proprietor contains an implied license that the purchaser may freely to use the goods for reasonable purpose. However, the proprietor can preserve his right by imposing the restriction in the sale contract, which make his exclusive right not exhaust. On the other hand, in the absent of any restriction, the right of intellectual property proprietor exhaust and purchaser will freely dispose of the goods. The exhaustion of the exclusive rights is based on “the discretion of title-holder.” See Yusuf & Hase, *supra* note 27, at 117-118.

³³⁶ Under the exhaustion doctrine as applied in Europe especially Germany, the exclusive distribution rights of intellectual property proprietor automatically exhaust after the first distribution by himself or by his

3.3.3.3 *The Decision of The European Court of Justice to Harmonize in the Interpretation of Consent under Article 7(1) of the Trademark Directive*

The scope of the Community-wide exhaustion is unavoidably related to the concept of consent. However, each Member State has its own perception on the concept of consent that may lead to an unharmonious situation and the application of international exhaustion doctrine. For example, the results of three judgments of the High Court of Justice of England and Wales, Chancery Division (patent court) [Zino Davidoff SA v. A&G Imports, Levi Strauss v. Tesco Stores, and Levi Strauss v. Costco] are in favor of the parallel importers by ruling that the consent of the trademark owner can be either express or implied. The High Court also ruled that merely no clear restriction on distribution was considered as implied consent to import into the Community.³³⁷ Due to rising unharmonious perspectives in the concept of consent among the Member States, it should be an honor duty of the European Court of Justice to interpret and clarify in the concept of consent under Article 7(1). Consequently, the ECJ attempted to solve this issue and ruled the standard of consent under Article 7(1) in the joined cases Zino Davidoff SA v. A&G Imports, Levi Strauss v. Tesco Stores, and Levi Strauss v. Costco.³³⁸ The questions were referred by the High Court of Justice to the European

consent. See Stern, *supra* note 29, at 122-24. (analyzing and comparing between the doctrine of implied License and the exhaustion Doctrine.)

³³⁷ According to the defendants in all three cases arguing that there were no effective contractual restrictions in the distribution chain of brand owners, the High Court decided that in the case of absence of clear restriction on importation, the purchasers or parallel importers are free to import such goods which purchased from outside the Community into the Community and the trademark owner cannot assert his right to bar such importation since his right exhausted after the first sale. It seems that the parallel importers have right to import those goods inside the Community under the implied license of trademark proprietors.

³³⁸ See Joined Cases C-414/99, C-415/99 and C-416/99, Zino Davidoff SA v. A&G Imports, Levi Strauss & Co Ltd, Levi Strauss (UK) Ltd v. Tesco Stores, Tesco plc and Costco Wholesale UK Ltd., Judgment on 20 November 2001, available at <http://curia.eu.int> (visited Mar. 26, 2002). [hereinafter The ECJ Judgment in

Court of Justice to interpret and clarify the concept of consent, to determine the circumstances in which exhaustion takes place, and to interpret legitimate reasons under Article 7 of the Trademark Directive.

The ECJ considers that is necessary for providing a uniform interpretation of the concept of consent to the marketing of goods within the Community in order to avoid inconsistency. Due to the national legal system of Member States, the difference in the concept of consent might conflict with the harmonization purpose of the Trademark Directive.³³⁹ The diversity of interpretation on the concept of consent might lead to the application of international exhaustion doctrine.³⁴⁰ Thus the meaning of consent for the purposes of Article 7(1) should be interpreted at the Community level.³⁴¹

To make clear the concept of consent, the ECJ court ruled that the consent of a trademark owner to marketing within the EEA of goods placed on the market outside the EEA must be expressed positively.³⁴² In addition, the factors taken into consideration in finding implied consent must *unequivocally* demonstrate that the trademark proprietor has renounced any intention to enforce his exclusive rights. The Court stated that it is not

the Davidoff Case] The summary of this judgment is provided in Press Release No 58/01 of Press and Information Division, which is available on <http://europa.eu.int/cj/en/cp/cp01/aff/cp0158en.htm>. (visited Mar. 26, 2002).

³³⁹ In question of whether consent under Article 7(1) of the Trademark Directive is to be treat as a concept of nation or of Community law, Advocate General Stix-Hackl reasoned that if the consent to placing the goods on the market within the EEA can be determined under national law, it should certainly cause the unharmonious interpretation on the concept of consent as a result of diversity of national legal system. See The Opinion of Advocate General Stix-Hackl in ECJ's Davidoff Case, *supra* note 305, at para. 55 and 56.

³⁴⁰ *Id.* at para. 59 and 60.

³⁴¹ *Id.* at para. 64 and 65.

³⁴² See The ECJ Judgment in the Davidoff Case, *supra* note 338, para. 45 and 46. "In view of its serious effect in extinguishing the exclusive rights of the proprietor of the trade mark, consent must be expressed in such a way that an intention to renounce those rights is *unequivocally* demonstrated. This intention will normally be gathered from an express statement of consent. Nevertheless, it may in some cases be inferred from facts and circumstances prior to, simultaneous with or subsequent to the placing of the goods on the market outside the EEA which unequivocally demonstrate that the proprietor has renounced his rights."

for the trademark proprietor to demonstrate absence of consent, but rather for the trader alleging consent to prove it. Thus, the burden of proof is on the parallel importer.³⁴³

The Court stated that implied consent to the marketing within the EEA of goods put on the market outside that area could not be inferred from the mere silence of the trademark owner.³⁴⁴ Based on the reason that “implied consent cannot be inferred from the fact that contractual reservations were not imposed at the time of the transfer of ownership of the goods bearing the mark, or from the fact that the trademark owner has not communicated his opposition to marketing within the EEA or from the fact that the goods carry no warning of a prohibition on their being placed on the market within the EEA.”³⁴⁵ The Court decided in favor of the trademark owner by limiting the circumstances, which can be deemed as implied consent. However, it still has room for the notion of implied consent if in that circumstance, the parallel importer has enough evidence to prove the implied consent of the trademark owner to market those goods inside the Community.

3.3.4 The Legitimate Reasons under Article 7(2) of Trademark Directive to Exempt from the Application of Community-wide Exhaustion Doctrine

There are some exemptions of Community-wide exhaustion doctrine under the concept of legitimate reasons in Article 7(2). If the trademark owner has the legitimate reasons to oppose the parallel import of those goods, his exclusive right does not exhaust

³⁴³ *Id.* at para. 53-54.

³⁴⁴ *Id.* at para. 55

³⁴⁵ *Id.* at para. 56.

under the Community-wide exhaustion.³⁴⁶ Article 7(2) gives some important examples of legitimate reasons that is “where *the condition of the goods* is changed or impaired after they have been put on the market.” It means there are other reasons or situations that the trademark owner can assert his legitimate reason to bar parallel imports such as the mental condition of goods (the substantial damage of trademark’s reputation). The following will focus on the discussion in legitimate reason under Article 7(2).

In practice, the trademark owner will attempt any measures to assert his right to bar parallel imports. There is one case that focused on the trademark right in advertising and expanded the exhaustion doctrine to advertisement rights. In the *Parfums Christian Dior* case,³⁴⁷ the court stated that the exhaustion doctrine under Article 7 extends to the advertising of trademark goods because the right to prevent others from “using the sign on business papers and in advertising” was provided for in Article 5(3)(d) and falls within the exhaustion doctrine under Article 7.³⁴⁸ The plaintiff brought an action to prevent the defendant from making any publication or reproduction of Dior’s trademarks in unauthorized catalogues, brochures, advertisement, or otherwise. The ECJ held that unauthorized advertising of parallel products might only be opposed when the result of such advertising significantly damaged the trademark owner’s reputation.³⁴⁹ In other words, the trademark owner could bar parallel imports if there was ‘significant damage’

³⁴⁶ The placing of goods in the market in the meaning of Article 7(1) does not relate to sale to the end user but connect to “the transfer of the immediate power to dispose of the products concerned.” In contrast, to determine whether the trademark owner has right to oppose further commercialization of the products within the EEA on the ground of Article 7(2) concern “the sale to the end users.” See Opinion of Advocate General Stix-Hackl in *Davidoff Case*, *supra* note 305, at para. 104.

³⁴⁷ Case C-337/95 *Parfums Christian Dior SA and Parfums Christian Dior BA v. Evora BV*, [1998] 1 CMLR 737.

³⁴⁸ *Id.* 30-33.; also See Douglas R. Hegg, *Parfums Christian Dior SA & Anor v. Evora BV*, 27 DENN. J. INT’L L. & POL’Y. 669 (1999).

³⁴⁹ *Id.* at para. 43 and 61.

created by the parallel import's advertising.³⁵⁰ The Court distinguished the 'condition of the goods' under Article 7(2) from the 'mental condition of goods.' The former merely refers to the condition of goods inside the packaging, but the later refers to the damage to reputation, which is another example of a 'legitimate reason' within Article 7(2).³⁵¹ In other words, the court identified two categories of legitimate reason: (1) adverse alteration to the original physical condition of products and (2) adverse alteration to the mental condition of products. Either adverse on physical condition or adverse on mental condition can be considered as legitimate reason only if such damage is substantial but whether there is a risk of significant damage is a question of fact for the national court.³⁵²

In the *Davidoff* case, which has been discussed earlier, the English High Court stated that the batch number removal from the original product might cause the 'mental impairment' of the trademark. However, Article 7(2) of the Directive would not be triggered unless such damage was substantial. In this case, the plaintiff could not oppose such parallel importation because the removal or obliteration of bar codes, which the plaintiff claimed hindered recall and damaged the appearance of the goods, was determined to have caused little harm.³⁵³

There is another interesting decision in the *Microsoft* case,³⁵⁴ which was decided by the English High Court in the issue of removal of packaging. The issue was whether

³⁵⁰ *Id.* at para. 46 and 47.

³⁵¹ *Id.* para. 38 and 58; and also see Article 7 (2) provides an exemption of exhaustion doctrine by stating "Paragraph 1 shall not apply where there exist *legitimate reasons* for the proprietor to oppose further commercialization of the goods, especially where the condition of the goods is changed or impaired after they have been put on the market." (emphasis added)

³⁵² *Id.* para 50.

³⁵³ See *Zino Davidoff SA v. A&G Imports Ltd.*, [1999] 2 CMLR 1056, 30 IIC 567 (1999); and also see Norman, *supra* note 269, at 169.

³⁵⁴ See Ng-Loy Wee Loon, *Exhaustion of rights in Trade Mark Law: The English and Singapore Models Compared*, [2000] EIPR 320, citing in *Microsoft Corporation v. Computer Future Distribution Ltd.*,

removal of packaging constituted a legitimate reason for the trademark owner to oppose the importation. Unlike the *Davidoff* case, the court in the *Microsoft* case held that the plaintiff was able to prohibit the defendant's importation. In the *Microsoft* case, the defendant imported the plaintiff's A.E. version software produced for the U.S./Canada from the United States and sold them in the United Kingdom through removal of the outer packaging and elimination of the limited distribution A.E. sticker. From the facts, Microsoft made a distribution policy for sales of its software in the U.S., which prohibited distributors and software dealers from distributing its products outside the U.S. or Canada.³⁵⁵ Microsoft brought a lawsuit against the defendant on the basis of trademark infringement and passing off.³⁵⁶

The court had to decide whether the plaintiff had a legitimate reason to oppose the defendant's reselling of its product. From the facts, the defendant marketed the product in plain brown boxes was not per se an action likely to cause adverse effects on the condition of the software itself. But there were other circumstances permitting the plaintiff to oppose the importation. The defendant's intentional destruction of the outer packaging concealed from U.K. purchasers that the products were designed and intended solely either for the North American market or for North American academic users. The

Judgment of the English High Court dated February 25, 1998 ETMR. (analyzing the *Microsoft* case of the U.K. and compared with the Singapore trademark law in favor of international exhaustion doctrine.)

³⁵⁵ *Id.* at 321 (explaining the facts of the *Microsoft* case. In the outer packaging of the U.S./Canada products, it had a sticker stating "Made in U.S.A. For Distribution in U.S.A./Canada only." Occasionally, the U.S./Canada products also bore the "Academic Edition (A.E.)" mark which meant that those products were intended only for certain qualifying end users such as students, educational institutions, hospitals, and non-profit organizations since the plaintiff sold those products at a discounted price.)

³⁵⁶ *Id.* (explaining that for the passing off claim, the Court held that even though the defendant was dealing with genuine Microsoft products, there would nevertheless be passing off when "the dealing with the products has been such as to give rise to a misrepresentation about the goods such as to cause damages or to be likely to do so." In this case, the misrepresentation made by the defendant was that the software sold was licensed for use in the U.K.)

software support for the U.S./ Canada products was provided by means of North American telephone numbers and such support was not available to purchasers in the U.K. In this case, the defendant's removal of packaging of the U.S/ Canada goods constituted a legitimate reason for plaintiff to oppose such parallel imports. Legitimate reasons for barring removal packaging and parallel import included: (1) its relation to the product's originally intended function, (2) the specific-matter of the trademark, and (3) its guarantee of quality, and (4) to provide software support for the products.³⁵⁷

3.3.5 Repackaging and re-affixing of Trademark in Pharmaceutical Products

In general, the repackaging does not bar the application of exhaustion doctrine and the right of trademark still exhausts. However, if the trademark owner can justify exception on the specific subject-matter under Article 30 or on the legitimate reason under Article 7(2) to prohibit such repackaging, the right of the trademark owner does not exhaust. The issues of repackaging and re-affixing of trademark are heavily discussed in the pharmaceutical business. In the case of pharmaceutical products, there are controversial issues involving parallel imports: (1) whether the parallel importers can repackage and subsequently re-affix a trademark without the trademark owner's consent, and (2) whether the parallel importers can affix a different trademark, which is known in the importing country, to products that the trademark owner registered under a different trademark in a different country. These issues involve the application of Article 7(2) of

³⁵⁷ *Id.* at 325. (comparing between the *Davidoff* case and the *Microsoft* case. Unlike the *Microsoft* case, in the *Davidoff* case, the defendant's removal or partial obliteration of the bar codes from the packaging of the goods because such removal or obliteration prevented the recall of the goods if they proved to be faulty, it was held that this complaint had "little to do with enforcing trade mark rights.")

Trademark Directive and Article 30 of the EEC Treaty. Whether the repackaging or re-affixing a trademark constituted a "legitimate reason" for the trademark proprietor to oppose such parallel importation under Article 7(2) of Trademark Directive or whether the trademark owner still has the right to bar such importation based on "specific subject-matter of trademark under Article 30 of the EEC Treaty.

Before 1988, the court applied the concept of the specific subject-matter under Article 30 to consider whether the repackaging should be allowed or not because at that time the Trademark Directive had not been enacted. However, after codifying the Trademark Directive in 1988, the court alternatively applied the concept of legitimate reason, which will be described in the following sections.

In relation to repackaging in the EU, repackaging by a parallel importer is generally permitted, if repackaging has met the necessary conditions set by the ECJ in the *Hoffmann*, *Pfizer* and *Panorava* cases. The ECJ has defined narrow and limited circumstances where trademark rights could be used to prevent parallel imports. In 1978 and 1982, respectively, the Court decided in the *Hoffmann-La Roche*³⁵⁸ and *Pfizer*³⁵⁹ cases that unauthorized repackaging or reaffixing of a trademark does not automatically give the trademark owner the right to restrain parallel imports. The trademark owner is

³⁵⁸ Case 102/77 Hoffman La-Roche v. Centrafarm, [1978] ECR 1139, 9 IIC 580 (1978). [hereinafter *Hoffman La-Roche Case*] There are four necessary requirements for allowing repackaging: (1) the parallel importer notifies the trademark owner of his intended sale, and provides a sample of the repacked good; (2) the repackaging does not directly or indirectly effect the condition of the product; (3) the new packaging clearly states the identity of the repackager and the original manufacturer; and (4) the repackaging is not liable to damage the reputation of the trademark owner.; see Stephen Whybrow & Peter Jennings, *Parallel Imports and the Exhaustion of Trade Mark Rights: Judgments by the European Court of Justice in Three Recent Related Cases*, "The McKenna Law Letter, Autumn 1996, available at <http://www.mckenna.co.uk/news/1lau96/index2.html> (visited Mar. 26, 2002); and also see Sarah Faircliffe, *Repackaging of Parallel Imported Pharmaceuticals in the EU -- the ECJ Gives a Long-Awaied Ruling*, Update: The journal of the European Pharam Law Centre, *Issue 54*, September 1996, available at <http://twobirds.com/library/pharma/repackage.htm>. (visited Mar. 26, 2002).

entitled to prevent repackaging only it was justified under the first and second sentence of Article 36 (now, after amendment Article 30).³⁶⁰ The prevention of marketing repackaged products constituted a disguised restriction on Member States' trade.³⁶¹

After balancing between the freedom of trade and the trademark owner's interest, the Court stated the circumstances in which the owner cannot assert repackaging to counter such parallel imports of repackaged goods:³⁶² (1) identical products put on the market in several Member States in various forms of packaging, which has the effect of artificially partitioning of the markets between Member States;³⁶³ (2) the repackaging cannot adversely affect the original condition of the product either directly or

³⁵⁹ See *Pfizer v. Euri-Pharm*, [1982] 1 CMLR 406.[hereinafter *Pfizer* case]

³⁶⁰ See The EEC Treaty, *supra* note 262 art. 30. Article 30 of the EEC Treaty states that "the provisions of Article 30-34 shall not preclude prohibitions or restriction on imports...justified on ground of...the industrial and commercial property. Such prohibitions or restrictions shall not, however, constitute a means of arbitrary discrimination or a disguised restriction on trade between Member States."

³⁶¹ See *De La Torre*, *supra* note 309, at 309. (pointing out that both *Hoffmann-La Roche* and *AHP* were based on the concept of disguised restriction of trade (Art. 36, second sentence). The method used in the *Hoffmann-La Roche* and *AHP* could suggest that the specific subject-matter is covered by the first sentence, but the second sentence can be used to prevent the abused of this right even within this subject-matter.); see G. Marengo & K. Banks, *Intellectual Property and the Community Rules on Free Movement: Discrimination Unearthed*, E.L. Rev., 224 (1990).

³⁶² Condition 1 to 5 and 7 were constituted by the *Hoffman-La Roche* case and condition 6 and 8 were added by the *Bristol-Myers Squibb* case to strictly confirm that the repackaging does not affect in the original condition of product and damage the trademark owner's reputation by giving trademark owner the right to check product before put its on sale.; See David Perkins, Marleen van Kerckhove & David Rosenberg, *Exhaustion of Intellectual Property Rights*, 574 PLI/Pat 41, 69-70; and also see Nicholas Shea, *Parallel Importers' Use of Trade Marks: The European Court of Justice Confers Rights but also Imposes Responsibilities*, [1997] EIPR 106-7.

³⁶³ To rely on the second sentence of Article 30, there are two standards of test to find "artificial partitioning of the market": subjective test and objective test. The former concerns whether the manufacturer or trademark owner must intend to partition the Community market, which considered as a necessary condition. The later is whether it is adequate to present that in fact the exercise of his trademark right does partition the Community market or the other word, the objective fact of partition of the markets is sufficient. In *Centrafarm v. American Home Products* case, the Court confirmed that the subjective test was a sufficient condition when different are used for the same product in different Member States. On the other hand, in the *Pfizer* case, the Court applied the objective test and stated that the importer does not need to present that the trademark owner deliberately sought to partition the market. Partitioning is artificial if the trademark owner's reliance on his right cannot be justified by the need to safeguard the essential function of the trademark or act within the specific subject-matter of trademark. See Shea, *supra* note 362, at 105-6. ; and also see *De La Torre*, *supra* note 309, at 306-8.

indirectly;³⁶⁴ (3) the repackaging is necessary in order to allow the product to be imported and marketed in the Member State of importation;³⁶⁵ (4) the packaging is not defective, low quality, untidy or dirty in order to damage the reputation of the trademark owner; (5) the name of the person who repackaged the product is clearly indicated on the external packing; (6) the name of the manufacturer who manufactured the product is clearly stated on the new packaging; (7) the importer must give a notice to the trademark owner before the repackaged product is put on sale; and (8) the importer has to send an example of the repackaged product to the trademark owner before it is available on sale in the market.

Consequently, repackaging following the aforementioned requirements is allowed in the EU and the trademark owner cannot bar the importation of repackaged parallel import goods. Moreover, repackaging does not cause consumer confusion. The consumer will know that these goods are parallel import goods and the reputation of trademark owner is not destroyed by such imports. The consumer can take advantage of the lower price of pharmaceuticals offered by parallel imports.

In 1996 after the Trademark Directive was already codified, the ECJ further clarified its doctrine on repackaging based on the concept of legitimate reason under Article 7(2) of the Trademark Directive in the *Paranova* case.³⁶⁶ The plaintiff was

³⁶⁴ For example, it did not impair the original condition if importers mere removed of blister packs and placed in new box that contained a window which customers can see an original label shown the trademark. (see *Pfizer v. Euri-Pharm*, [1982] 1 CMLR 406.) The original condition of product did not impair if just proving the addition of new user instructions or the insertion of an extra article or repackaging operations, which are authorized and supervised by a public remains intact or for operations consisting in the fixing of self-stick labels to flasks, phials, ampoules or inhalers. (see *Hoffman La-Roche Case*, *supra* note 358, at para.60-61, and 64.)

³⁶⁵ For example, affixing to the external packaging a new label in the language of the Member State of importation.

³⁶⁶ See *Bristol-Myers Squibb v. Parnova*, [1996] ECR I-3457, 28 IIC 715 (1997); and also see GRAEME B. DINWOODIE, WILLIAM O. HENNESSEY, & SHIRA PERLMUTTER, *INTERNATIONAL INTELLECTUAL PROPERTY LAW AND POLICY*, Ch. VII, 253 and 355-367(2001).

Bristol-Myers Squibb, which marketed pharmaceutical products manufactured by itself or an associated company in various Member States. The defendant was Paranova, a pharmaceutical distributor of gray market products. For the purposes of sale in Denmark, Paranova had repackaged all the medicines in new external packaging with a uniform appearance, but using the same colors as used in the manufacturer's original packaging. The new label bore the trademark of Bristol-Myers Squibb together with the indications "manufactured by Bristol-Myers Squibb" and "imported and repackaged by Paranova."

The court decided that Bristol-Myers Squibb could not bar the parallel imports of Paranova because its right did exhaust under Article 7(1) and there was no legitimate reason for the trademark owner to oppose such importation under Article 7(2). Article 7(1) precludes the trademark owner from relying on his exclusive rights in order to prevent an importer from marketing a product put on the market in another Member State by the owner or with his consent. Article 7(2) provides an exception of Article 7(1). An exception is made when there are "legitimate reasons" for the proprietor to oppose further commercialization. For instance, where the condition of the goods is changed or impaired after they have been put on the market.

On the subject of re-affixed different trademark, the issue is whether the trademark owner can stop the importation of goods in which the importer removed the original trademark and re-affixed a different trademark to them. Such re-affixed trademarks, belong to the same trademark owner, but are used and recognized by the consumers in the country of importation. In *Centrafarm v. American Home Products*

Corporation,³⁶⁷ which was decided by the EJC in 1978, the Court made it clear that the registration of two different marks for the same product in two Member States is not in itself prohibited. The trademark owner is able to register two different trademarks in two different countries and use such different trademark for the same product. The Court held that remarking was not permitted and infringed on the trademark owner's right, unless the trademark owner exercised his right in a way to disguise the restriction on trade. Consequently, the Court reiterated its definition of the "specific subject-matter" of trademark and considered whether the exercise of the trademark right could be a disguised restriction on trade prohibited under Article 30.

In addition, the Court's rule in repackaging of pharmaceutical products could be applied to repackaging of other types of products such as liquor, perfume or luxury products. For instance, in the *Frits Loendersloot* case,³⁶⁸ the Court reiterated its position taken relative to pharmaceutical products in its consideration of the re-labeling for bottled whisky. There was no trademark infringement if there was (1) no effect on original condition of product, (2) adequate presentation and (3) notification on the label of the repackaging.³⁶⁹

As mentioned above, the trademark owner is generally not allowed to prevent the importer from repackaging or re-affixing the trademark to the repackaging of product. Of

³⁶⁷ See Case 3/78 Centrafarm v. American Home Products, [1978] ECR 1823.

³⁶⁸ Case C-349/95, *Frits Loendersloot v. George Ballantine & Sons Ltd.* [1997] ECR I-6227.

³⁶⁹ *Id.* From the facts, the parallel importer had removed identification numbers from bottles of Scotch whisky and re-affixed other labels in order to add information or remove words on the label as required by local laws. The Court ruled that if the producer applied identification numbers for specific purposes other than to detect parallel imports, such as to enable the recall of faulty products, the numbers could not be removed. In other words, if the identification number were applied to products for detecting parallel imports, the removal of them by parallel importers would not be prohibited. However, the parallel imports should not remove labels if the application of sticker with the additional information would be sufficient to fulfill the national conditions required by law. See FARQUHARSON & SMITH, *supra* note 285, at 17.

course, regardless of the classification of goods in question, there are the limitations of permission. Only in some circumstances may trademark rights be used to restrain parallel imports under Article 30 or under Article 7(2) when the trademark owner can prove his justification to prevent parallel imports. For example, because of different style and quality in product, the repackaging or re-affixing of a trademark may destroy the trademark's reputation and cause consumer confusion. In this circumstance, the trademark owner has the right to bar such repackaging. In case of re-affixed different trademarks, it is possible that the same product with different trademarks in different countries may be distinct in style and quality. The trademark owner can prevent a parallel import if the difference in style and quality could destroy the trademark owner's reputation and cause consumer confusion.

3.3.6 Conclusion

The Community-wide exhaustion was codified in the Trademark Directive that member states had to adopt into their national laws. Under Community-wide exhaustion, the trademark owner in an importing Member State can only assert his exclusive right to prevent the parallel import of goods from outside the Community. On the other hand, if the trademark goods were imported from another Member State, the trademark owner in the country of importation could not prohibit such parallel imports because his right was exhausted.

However, within limited and certain circumstances, the trademark owner still had the right to prevent the parallel importation from other Member States under Article 30 of

the EEC Treaty and Article 7(2) of Trademark Directive. The specific subject-matter of trademark under Article 30 is consistent with the limitation of a Community-wide exhaustion, codified in Article 7(2). Under Article 30, if the result of such importation opposed the specific subject-matter of trademark, the trademark owner can bar such importation. Under the Article 7(2), if the trademark owner has a legitimate reason to oppose further commercialization of the parallel import goods (for example the condition of the goods is changed or impaired after they have been put on the market), the Community-exhaustion is not applicable and the right of trademark owner is not exhausted. Thus, such importation of goods should be prohibited even though such goods were imported from a Member State. Yet, the exercise of trademark rights to prohibit parallel importation should constitute neither arbitrary discrimination nor a disguised restriction on trade between Member States and it should be consistent with the rule of competition.³⁷⁰

3.4 Parallel Imports in Patent

From the 1960s to 1970s, most cases of the European Court dealt with trademark. However, during the 1980s the Court dealt with the other intellectual property rights such

³⁷⁰ See FARQUHARSON & SMITH, PARALLEL, *supra* note 285, at 20-31. (explaining in competition rule that the E.U. competition rules particularly have a dual purpose: to achieve undistorted competition and to achieve market integration within Europe. There are two main provisions: the control of agreements that distort competition (Article 85 of E.C. Treaty) and the control of market power or abuse of dominance (Article 86 of E.C. Treaty); and also see Ulrich Loewenheim *Intellectual Property Before the European Court of Justice*, 6 IIC 829, 844-47(1998). (explaining in the Article 85 and 86 of the EC Treaty.); and also see *Sirena v. Novimpex*, February 18, 1971, Case No. 40/70, 10 CMLR 260 (1971); *Deutsche Grammophon v. Metro*, 4 IIC 429, 433 (1971); *EMI Records v. CBS*, 7 IIC 275, 285 (1976).

as patent and copyright more frequently.³⁷¹ Although the notion of specific subject-matter of intellectual property have so far taken place primarily with respect to trademark, a similar discussion should be applied for patent as well. The specific subject-matter of the patent was explained and discussed by the European Court of Justice in many cases.

The specific subject-matter of patent was recognized by the ECJ in *Centrapharm v. Sterling Drug*.³⁷² The Court clearly stated that the specific subject-matter of the industrial property in the case of patent was to guarantee a reward for the creative efforts of the inventor. The patentee was to have the exclusive right to use his patented invention to manufacture industrial products and circulate them in the market by himself or by granting the license to third parties. The patentee also had a right to oppose patent infringements.

From the facts, Centrapharm obtained low priced pharmaceuticals from Britain and sold them in the Netherlands at a higher price. Sterling Drug Inc. owned the patent for the products in both countries and brought an action in the Dutch court to prevent the parallel importation by Centrapharm. The Dutch court asked the ECJ to rule whether exercising the patent right to prevent parallel imports was compatible with Articles 30 and 36 (now, after Amendment Articles 28 and 30). Regarding the specific subject-matter of patent, the ECJ decided that the free movement of goods principle in Article 30 would be violated if the patent owner was permitted to prevent parallel imports. The Court reasoned that Centrapharm initially put its products into the market and received

³⁷¹ See Loewenheim, *supra* note 370, at 836. There are also cases dealing with other intellectual property right for designs in the *Keurkoop* case or protecting plant varieties in the *Nungesser* case. See Case No. 144/81 *Keurkoop v. Nancy Kean Gifts*, September 14, 1982, 14 IIC 515 (1983) and see Case No. 528/78 *Nungesser v. EC Commission*, June 8, 1982, 14 IIC 256 (1983).

³⁷² See Case 15/74 *Centrapharm v. Sterling Drug*, [1974] E.C.R. 1147, 6 IIC 102, 106 (1975)

benefits of such sales. The patentee already received reward for his creativity. Therefore, prohibiting parallel import goods was not justified under Article 36 “where the product has been put on the market in a legal manner, by the patentee himself or with his consent in the Member State from which it has been imported.”³⁷³ The patentee should not have right to prevent parallel import of such goods and receive double benefit.

However, there is a problem for the first sale in a country that does not provide patent protection. The question arose whether the patent right to control further sales of the patented good was exhausted by the first sale because the patent does not receive a royalty from the first sale. In *Merck v. Stephar & Exler*,³⁷⁴ certain drugs patented in the Netherlands were being sold in Italy, where at that time, patent protection was not available. Merck decided to sell its drugs in Italy. Later, Stephar imported the drugs from Italy into the Netherlands. In an action brought by Merck to stop such parallel imports, Merck argued that the function of rewarding an inventor’s creative effort would not be fulfilled in case of sale in country that patent was not available. The Court applied the Community-wide exhaustion doctrine regardless of the lack of patent protection in the country where the drugs had been first sold.³⁷⁵

³⁷³ *Id.* at para. 11.

³⁷⁴ See Case No. 187/80 *Merck v. Stephar & Exler*, [1981] ECR 2063, 13 IIC 70 (1982).

³⁷⁵ *Id.* at para. 11. The Court stated “That *right of first placing a product on the market* enables the inventor, by allowing him a monopoly in exploiting his product, to obtain the reward for his creative effort *without, however, guaranteeing that he will obtain such a reward in all circumstances*. It is for the proprietor of the patent to decide, in the light of all the circumstances, under what conditions he will market his product, including the possibility of marketing it in a Member State where the law does not provide patent protection for the product in question. *If he decides to do so he must then accept the consequences of his choice as regards the free movement of the product within the Common Market*, which is a fundamental principle forming part of the legal and economic circumstances which must be taken into account by the proprietor of the patent in determining the manner in which his exclusive right will be exercised.” (emphasis added)

Therefore, if products are marketed with the patent owner's consent, they may circulate freely in the Common Market regardless of whether or not the marketing has taken place in a country without patent protection.³⁷⁶ Such sales are sufficient to trigger the exhaustion doctrine. Allowing the patent owner to prohibit parallel imports can create one of two problems: it can become an obstacle to the free movement of goods or it can create the ability to partition off a national market even though the products had been marketed with the patent owner's consent.³⁷⁷ It seems that the Court deliberated on the free movement of goods and the consent of patent owner more than the reward function of patent. Even though the patentee did not receive his royalty from the first sale because there was no patent protection in the country of first sale, his patent right still exhausted because he intentionally decided or consented to market those products in such country.

Relying on the concept of consent, in case of compulsory licensing, the patent proprietor did not willfully consent; thus there was the problem of whether the marketing of patented products under a compulsory license triggered the exhaustion doctrine. In the *Pharmon* case,³⁷⁸ the Court answered the question of specific subject-matter for patent used with compulsory licenses. The marketing of patented products on the basis of a compulsory license issued in one Member State does not necessarily mean that the

³⁷⁶ The ECJ confirmed its decision in *Merck v. Stephar* in recent cases such as joined Case C-267/95 and C-268/95, *Beecham Group v. Europharm of Worthing Ltd. and Merck & Co. Inc. v. Primecrown Ltd.*, judgment of December 5, 1996, [1996] ECR I-6285, 29 IIC 184 (1998).

³⁷⁷ See Case 15/74 *Centrapharm v. Sterling Drug*, [1974] ECR 1147, 6 IIC 102, 106 (1975) at para. 11-12. The Court stated "if a patentee could prevent the import of protected products marketed by him or with his consent in another Member State, he would be able to partition off national markets and thereby restrict trade between Member, in a situation where no such restriction was necessary to guarantee the essence of the exclusive rights flowing from the parallel patents."

³⁷⁸ See Case 19/84 *Pharmon v. Hoechst AG*, July 9, 1985, 17 IIC 357 (1986).

patent owner consented to the marketing; therefore the importation of such products into other Member States can be prohibited.³⁷⁹

The Court was concerned on the essential function of the patent (to reward the patentee's creative effort) and whether the exercise of the patent right to prevent parallel importation was justified under Article 30. The court decision that allowed the patentee to oppose the parallel importation complied with both a reward theory and a consent theory. Based on the reason that the royalty under a compulsory license was lower and the patent proprietor was considered to have involuntarily consented to market its patent products. Nevertheless, in case of price-control by government, the prohibition of sales at higher prices by the national authorities of the exporting State has the foreseeable consequence of substantial exports taking place. The patent owner cannot prohibit parallel imports of those products. Although this creates a distortion of competition, it does not justify derogation from the principle of free movement.³⁸⁰

In conclusion, unlike trademark, there is no Community Directive on patents.³⁸¹ Although there is no provision on a Community-wide exhaustion of rights, the European Court of Justice constantly applies a Community-wide exhaustion and the concept of specific subject-matter under Article 30 of EEC Treaty in patent cases. For the specific

³⁷⁹*Id.* at para. 25 and 26. The Court reasoned "the competent authorities of a Member State granted a third party a compulsory license... the patentee cannot be deemed to have consented to the operation of that third party. Such a measure *deprives the patent proprietor of his right to determine freely the conditions under which he markets his products*... The substance of a patent right lies essentially in according the inventor an exclusive right for first placing the product on the market so as to allow him *to obtain the reward for his creative effort*. It is therefore necessary to allow the patent proprietor to prevent the importation and marketing of products manufactured under a compulsory license *in order to protect the substance of his exclusive rights under his patent*." (emphasis added)

³⁸⁰See Verma, *Exhaustion of IPRs and Free Trade*, *supra* note 160, at 549.

³⁸¹*Id.* (mentioning that the Community Patent Convention of 1975 Article 76, which has not yet come into force, confirms that the Community patent is subject to the exhaustion doctrine. There should be a specific

subject-matter of patent, the court concern on the consent of patentee in first sale and the free movement of goods more than the reward function of patent. In addition, the discussion on the specific subject-matter of trademark, and the consent theory should be applied to the patent as well. The best course of action would be for the Court's decisions to rely on the same application of the exhaustion doctrine in both trademark and patent cases. Differences in application will bring the troublesome issue of interpretation of exhaustion doctrine and will cause inconsistent results for parallel import case. In the end, the purpose of the European Community, to encourage the free movement of goods within the Community, would be distorted by unclear and unharmonized regulations regarding exhaustion doctrine.

3.5 Parallel Imports in Copyright

3.5.1 Whether “the Industrial and Commercial Property” in Article 30 Includes Copyright

Article 30 only mentions industrial and commercial property and does not specifically refer to copyright. This could cause an initial misunderstanding that the copyright protection did not directly impede or affect the function of internal market and free movement of goods concept. Indeed, the copyright law grants exclusive rights to the copyright owner in order to prohibit other persons from making a profit without paying

convention that clearly addresses the exhaustion doctrine as applied to patents, such as is found in the Trademark Directive.); and also see FARQUHARSON & SMITH, *supra* note 285, at 15-16.

the royalty. The copyright affects economic rights and creates the same effect to the internal market as patents and trademarks.³⁸²

The issue was whether Article 30 could be applied to copyrights and neighboring rights because Article 30 refers to only “industrial and commercial property” and does not mention either copyrights or neighboring rights. In 1971, the Court had only expressed the assumption that neighboring rights may fall under Article 30.³⁸³ The Court clarified that copyright and akin rights come under the scope of the EEC Treaty in so far as economic rights are concerned. As recognized in the *Deutsche Grammophon* case, which was discussed earlier, the reward and incentive functions of copyrights could in themselves duly safeguard the Member State of parallel exportation, so that no further restrictions on the free movement of goods would be necessary in the Member State of importation to protect intellectual property rights. Recently, it is clearly expressed in *Musikvertrieb Membran & K-tel v. GEMA*³⁸⁴ that Article 30 could be applied to copyright as well.

³⁸² See Loewenheim, *supra* note 370, at 841. (pointing out that unlike other IPRs protection, the rights of copyright owners cover both economic and moral rights. Thus when determining a specific subject matter, the protection of the moral right should also be taken into account. The reason why the Court overvalues the economic aspects of a copyright, and subsequently neglects the moral aspects, is because the perspective of common law countries differs from that of civil law countries. Common law countries view a copyright as a property right and thus focus on the interest of publishers and producers, where as civil law countries aim focus on protection of the person/author. As result, the different views on moral right might present an obstacle in trade between Member States if the copyright owner tries to prevent the importation of goods by asserting a claim based on his moral rights.)

³⁸³ See *Deutsche Grammophon v. Metro*, 1971 ECR 487, 2 IIC 429, 432 (1971)

³⁸⁴ See *Joined Case 55/80 and 57/80 Musikvertrieb Membran & K-tel v. GEMA*, January 20, 1981, 12 IIC 526, 528 (1981). The Court reasoned “if is true that copyright comprises moral rights of the kind indicated by the French Government. However, it also comprises other rights, notably the right to exploit commercially the marketing of the protected work, particularly in the form of licenses granted in return for payment of royalties. It is this economic aspect of copyright which is the subject of the question submitted by the national court and, in this regard, in the application of Article 36 of the Treaty there is no reason to make a distinction between copyright and other industrial and commercial rights.” *Id.* at para.12.

3.5.2 Specific Subject-Matter of Copyright

In nature of copyright, there are many types of copyright works and different appearances of commercial exploitation of copyrighted works. It is hard to find a general definition of the specific subject-matter of copyright as did in prior trademark cases or patent cases. Generally, a “specific subject-matter” of a copyright can be found by focusing on its general purpose to protect the author and his interests in his work. Due to many forms of exploitation of copyrighted works, such as reproduction right, distribution right, rental right, and performance right, the following parts will be explained and discussed by focusing on the type of copyright.

3.5.2.1 *Distribution Right*

Generally, the copyright owner has an exclusive right to distribute copies of his work and has the right to oppose other forms of distribution of his copyright works without his permission. The European Court of Justice considers the distribution right of the copyright owner in the *Musikvertrieb Membran & K-tle* case.³⁸⁵ This case involves the protection of sound recording. The sound recordings in this case were first put on the British market and subsequently imported into Germany, which provided different royalty rates. The Court held that it is impossible to bar parallel imports for the purpose of equality in the royalties because the sound recordings were produced and marketed in those countries with the copyright owner’s consent.³⁸⁶ Based upon a consent theory, the

³⁸⁵ *Id.*

³⁸⁶ The Court ruled that the exploitation of a copyright in a given market was a matter for the free choice of the owner and after making his choice, he must take any consequences of his decision. The Court stated

difference in the rates of remuneration within different Member States could not justify reliance on the particular IPRs of one member when the copyright owner had already consented to distribution in other Member States. The Court held that the fact that the lower royalties in the Member State of exportation were due to restrictions imposed by national law was irrelevant. Thus, the exhaustion of rights prevented the German collecting society from recovering the difference in royalties.

In relation to parallel imports of second-rate goods, in *Dansk Supermarked v. Imerco*,³⁸⁷ the Court had to decide whether national provisions concerning both copyright and trademark could be invoked to prohibit the parallel importation of second-rate goods that had been marketed with consent in another Member State.³⁸⁸ The Court ruled that imports of substandard pieces into Denmark could not be prevented even if they were of an inferior quality. The Court stated that “the exclusive right guaranteed by the legislation on industrial and commercial property is exhausted when a product has been lawfully distributed on the market of another Member State by the actual proprietor of the right or with his consent.”³⁸⁹

Due to the disparity of copyright protection among Member States, the problem arose of whether a copyright owner in a country of importation, where the term of copyright was still enforceable, could prevent importation from a country of exportation,

“make that choice according to his best interest, which involve not only the level of remuneration provided in the Member State in question but other factors such as, for example, the opportunities for distributing his work and the marketing facilities which are further enhanced by virtue of the free movement of goods within the Community.” *Id.*; and also see FARQUHARSON & SMITH, *supra* note 285, at 19. (explaining that the principle of exhaustion of rights prevented GEMA (the German collecting society) from recovering the difference between the British and Germany royalty rates.)

³⁸⁷ See Case 58/0 *Dansk Supermarked v. Imerco*, January 22, 1981, 6 IIC 831 (1981).

³⁸⁸ The right to put the product on the market for the first time is concerned as distribution right in copyright perspective.

³⁸⁹ *Id.* at para. 11.

where the term of copyright had already expired. In *EMI Electrola v. Patricia*,³⁹⁰ the sound recordings had been lawfully marketed in Denmark where the term of copyright protection had already expired. The recordings were imported to Germany where the copyright protection was still in force as a result of a longer term of protection. The Court held that such import could be prevented on the basis of the German copyright. It reasoned that the problem arose not from the consent given by the copyright owner, but from the differences in the respective national legislation. The disparity between national laws may give rise to restrictions on intra-Community trade in sound recording and such restrictions are justified under Article 30 of the Treaty if they are the result of a difference between the rules governing the period of protection.³⁹¹

3.5.2.2 Rental Right

The copyright owner also has an exclusive right to rent his works to the public. The rental right can be considered separately from other types of exclusive right. In *Warner Brothers v. Christiansen*, the subject matter in dispute was the rental right in videocassettes. The ECJ held that Articles 28 and 30 were applicable and intra-Community trade could be indirectly impaired by exercise of the rental right and the rental had to be acknowledged as a separate market, of which the copyright owner should not be deprived.³⁹² Similar reasoning can be found in *Cinetheque et al. v. Federation Nationale des Cinemas Francais*, in which French legislation prohibited films shown in movie theaters from being sold on videocassettes before a certain period of time had

³⁹⁰ See Case 341/87 *EMI Electrola v. Patricia*, January 24, 1989, 21 IIC 689 (1990).

³⁹¹ *Id.* at 691

expired. The Court ruled that although such legislation could produce restrictions of intra-Community trade, it was justified because of its effect of promoting the production of films.³⁹³

In addition, the Court also recognized the distinction between distribution right and the rental in sound recordings in the *Metronome Musik* case.³⁹⁴ The Court stated that although the distribution right under Article 9 of Council Directive 92/100/EEC³⁹⁵ was exhausted when a product had been lawfully distributed on the market in another Member State by the proprietor of a copyright, the rental right was not exhausted. The sale or release into circulation of a sound recording “cannot therefore, by definition, render lawful other forms of exploitation of the protected work, such as rental, which are of a different nature from sale or any other lawful form of distribution.”³⁹⁶

3.5.2.3 Performance Right

With respect to the performance right, in *Basset v. SACEM*³⁹⁷ and *Ministere Public v. Tournier*,³⁹⁸ the Court held that an additional royalty raised by collecting societies for the public performance of imported sound recordings did not violate Articles 28 and 30. This case concentrated on the public performance of music work and not on

³⁹² See Case 158/86 Warner Brother and Metronome Video v. Christiansen, 19 IIC 666 (1988).

³⁹³ See Loewenheim, *supra* note 370, at 839-40, citing in Case 60/84 and 61/84 Cinetheque et al. v. Federation Nationale des Cinemas Francais and Chateau v. Federation Nationale des Cinemas Francais, July 11, 1985, 1986 GRUR Int. 114.

³⁹⁴ See Case 200/96 Metronome Musik GmbH v. Music Point Hokamp GmbH, 29 IIC 793 (1998). [hereinafter *Metronome Musik* Case]

³⁹⁵ The Council Directive 92/100/EEC of 19 November 1992 on Rental Right and Lending Right on Certain Rights Related to Copyright (OJ 1992 L 346, p.61), 25 IIC 553 (1994). This Directive complies with the TRIPs standard. Article 11 and 14 of TRIPs provides an exclusive right to authorize or prohibit the commercial rental of the phonograms.

³⁹⁶ See *Metronome Musik* Case, *supra* note 394, at 793.

the sound recording itself. Thus, the result of the court judgment was distinguishable from the decision in the *Musikvertrieb* case.³⁹⁹ It seems that the specific subject-matter of performance rights differ from that of distribution rights. In regard to the prior case in the *MusikVertrieb* case, the copyright owner could not obtain the difference in royalties for a sound recording, but could obtain royalties in performance rights because it was considered necessary to maintain the essential function of the copyright.

In the case of broadcasting and cable transmission of motion pictures, the transmissions are considered a service and not goods.⁴⁰⁰ The rights, which involve the performance rights in films, are treated under Article 59 on the freedom to provide service. In the *Coditel I*⁴⁰¹ and *Coditel II* cases,⁴⁰² the exclusive right to perform the movie "Le Boucher" in movie theaters, and by television broadcast, was granted to Cine Vog for Belgium;⁴⁰³ while the right to broadcast the film in Germany was conferred to a German television company. The Belgian cable television company, Coditel, picked up the film broadcast in Germany by means of its antenna in Belgium and transmitted it by cable to its customers in Belgium. The issue was whether an assignee of performance rights in a film could prohibit the exhibition of that film via cable transmission when it was broadcast in another Member State with the consent of the original owner of the right. The Court held that the problems arising in connection with the broadcasting of films are different from those arising in connection with the marketing of copyrighted

³⁹⁷ See Case 402/85 Basset v. SACEM, April 9, 1987, 19 IIC 368 (1988).

³⁹⁸ See Case 395/87 Ministère Public v. Tournier, July 13, 1989, 22 IIC 65 (1991)

³⁹⁹ See Loewenheim, *supra* note 370, at 840.

⁴⁰⁰ *Id.*

⁴⁰¹ See Joined Case 62/79, Codite v. Cine Vog Films (Coditel I), [1981] 2 CMLR 362, 12 IIC 207 (1981).

⁴⁰² See Case 262/81, Coditel v. Cine Vog Films (Coditel II), [1983] 1 CMLR 49, 14 IIC 405 (1983).

works in material like books or sound recordings. Films are marketed by frequently repeated performance; therefore the right to require fees for each public performance of the film is part of the essential function of copyright. The Court decided that Cine Vog was able, on the basis of copyright, to prevent Coditel from transmitting the film in Belgium. By analogy, the existence/exercise dichotomy under Article 30 is applied where the rights are exercised in the context of the movement of services.⁴⁰⁴

3.5.3 Conclusion

The European Court of Justice did not give a general definition of the specific subject-matter of copyright as it did in the case of trademark and patent because of “the different appearances of commercial exploitation of copyrighted works in material and works in immaterial form-differences.”⁴⁰⁵ Generally, a “specific subject-matter” of a copyright can be found by focusing on its general purpose to protect the author and his interests in his work. However, there are many forms of exploitation of copyright works, such as reproduction right, distribution right, rental right, and performance right. The nature of each right should be considered to determine whether the proprietor received protection of the essential purpose and function of the copyright.⁴⁰⁶ In other words, the

⁴⁰³ Cine Vog obtained an exclusive license to exhibit “Le Boucher” in Belgium for a period of seven years with one condition that the film should not be broadcast on Belgian television until 40 months after its first cinema showing. *Id.*

⁴⁰⁴ *Id.* at 408; see Lowwenheim, *supra* note 370, at 840.

⁴⁰⁵ See Loewenheim, *supra* note 370, at 841; and also see D.WYATT & A. DASHWOOD, THE EUROPEAN COMMUNITY LAW 586 (1993) (pointing out that copyright emerges in a complex form of property, reflecting the diversity of the works with which it incorporate.)

⁴⁰⁶ In other words, the application of exhaustion doctrine should be differently treated depending upon the type of rights. For example, although a distribution right in a sound recording is exhausted when a product has been lawfully circulated in the market, it does not mean that a rental right in such sound recording is also exhausted. The copyright proprietor still has right to control the rentals of his sound recording.

specific subject-matter of copyright was difficult to define because of the many types of copyright subject (such as literary, sound recording, or audiovisual work) and the many forms of exclusive rights. Consequently, the ECJ must define copyright specific subject-matter based on a case-by-case analysis and decide whether parallel importation should be prohibited or allowed under Article 30. The determinations must encourage the free movement of goods inside the common market and balance the conflict between protecting individual IPRs and fostering competition, as well as promoting the harmonization of domestic laws of member states in areas of intellectual property.

4. Conclusion

In order to create a single market and increase the free movement of goods and free competition among Member States, the European Community introduced the concept of a Community-wide exhaustion. Currently in the European Community, the Community-wide exhaustion, considered as an example of the regional exhaustion doctrine approach, applies strictly to trademark, patent and copyright. Thus, the parallel imports of goods first marketed in Community are free to move from one Member to other Member unless they fail in some specific exceptions such as difference in material or other legitimate reasons. In contrast, the Community market is closed to parallel imports of goods from outside the Community. The owner of the IPRs can assert his right to bar such parallel imports because the right of the owner of IPRs does not exhaust under the concept of Community-wide exhaustion.⁴⁰⁷

⁴⁰⁷The concept of Community-wide exhaustion may be considered as the protectionist approach and not be entirely consistent with the WTO trend on global trade and free movement of goods.

C. Japan

1. Introduction

Generally, the phenomenon of parallel imports occurs when there is a price difference among nations for the same product. In Japan, parallel imports have become notorious business because the average market price of products is typically higher than those in other developed and developing countries.⁴⁰⁸ Parallel imports seem to be permitted under the Japanese law because domestic consumers have few product alternatives and the available products are high priced.⁴⁰⁹ A survey by the Japanese Fair Trade Commission showed that based on the strong Yen, parallel imports brought benefits to Japanese consumers.⁴¹⁰ Japanese consumers particularly favor parallel imports because they can purchase parallel imported products more cheaply.

On the other hand, the owners of the IPRs and the sole exclusive distributors in Japan attempt to bar parallel imports based on the intellectual property law because the parallel import goods implicate the intellectual property protections of trademark, patent

⁴⁰⁸For example, the average prices for goods in Japan are thirty seven percent higher than in the U.S. See Charlene Barshefsky, *The Future of U.S.-Japan Trade Relations*, 25 L.&POL'Y INT'L BUS. 1287, 1292(1994).; see Industrial Policy Bureau, Price Policy Division, METI, Survey on Foreign and Domestic Price Differentials for Industrial Intermediate Input, June 6, 1999, available at <http://www.meti.go.jp/english/report/data/gIP9907e.html>. (visited Feb. 28, 2002); and also see International Comparison of Price Indexes, as of 2000, available at <http://jin.jcic.or.jp/stat/stats/05ECN33.html>. (visited Mar. 6, 2002).

⁴⁰⁹ See Barshefsky, *supra* note 408, at 1293. (pointing out that there are few foreign companies to do production and distribution business in Japan since the Japanese producers, suppliers, and distributors impede market access for foreign competitors. Therefore, the Japanese domestic market is more limited and difficult to access by foreign competition than other countries' markets. Because of Japan's closed market and subsequent inflated price for goods, the burden plunges heavily on Japanese consumers.)

⁴¹⁰ See Roderick Seeman, Parallel Imports: Fair Trade Commissions: Antimonopoly Law, THE JAPAN LAWLETTER, January 1987, available at <http://www.japanlaw.com/lawletter/jan87/fau.htm>. (visited Dec. 13, 2001) (mentioning that the consumers prefer to buy brand name goods at lower prices. For instance, in the case of scotch whiskey, the authorized import agents sell at 8000 yen per bottle while parallel importers sell at lower price approximately 4000 yen per bottle. There are other products that are imported by parallel importers such as teabags, chocolates, and handbags.)

and copyright. Due to conflict of interest between consumer and IPRs owners including exclusive distributors, it is very important to study how Japan deals with this conflict. Generally characterizing the Japanese approach, the national law approach is more favorable to consumer and less favorable to business or IPRs owners than the approach of other countries. Moreover, the Japanese approach might exert an influence on other Asian countries since Japan is the only nation in Asia regarded a developed country. Consequently, in order to understand the Japanese approach adopted in dealing with parallel imports, the following parts will discuss the issues implicated by parallel imports relative to trademark, patent and copyright, respectively.

2.Parallel Imports in Trademark

No Japanese laws, including Trademark Law and Custom Duties Act prohibit the parallel imports of genuine goods. There is a prohibition against the counterfeit goods, which obviously does not apply to the genuine goods.⁴¹¹ Under the Japanese trademark law, the importation of counterfeit goods of a registered trademark constitutes infringement upon the trademark right or the exclusive use right of trademark owner.⁴¹² The Customs Duties Act of Japan prohibits the importation of goods that would infringe a domestic patent, utility model, industrial design, trademark, or copyright.⁴¹³

⁴¹¹See Kaoru Takamatsu, *Parallel Importation of Trademarked Goods: A Comparative Analysis*, 57 WASH. L. REV. 433, 439(1982);

⁴¹²See The Trademark Law (Shohyo Ho, Law No 127 of April 13, 1959 as amended by Law No. 220 of December 22, 1999), Article 37 (v), available at <http://www.jpo.go.jp/shoukaie/shohyo.htm> (visited Mar. 26, 2002).[hereinafter Japanese Trademark Law]

⁴¹³See Tariff Measures Law (Kanzel Teiritsu Ho) article 21, available at <http://www.jpo.go.jp> (visited Mar. 26, 2002)

Although no specific law or regulation prohibits parallel imports, in the past, the Tokyo District court has held in the *Nestle* case that importation by a parallel importer without consent infringed on the trademark right of the Japanese subsidiary.⁴¹⁴ Based on the principle of territoriality of trademark,⁴¹⁵ the Court stated that importation of parallel goods constituted infringement of the exclusive use right possessed by Petitioner under the Trademark Act.⁴¹⁶ However, in recent times, an opposite determination was made by the Osaka District Court in the *Parker* case,⁴¹⁷ which held that parallel imports were not to be prohibited. As the result of the court decision in *Parker* case, the trademark owner can no longer bar parallel imports of goods with his trademark. The court judgment in the *Parker* case has become a precedent that other subsequent cases have followed. At this stage, it would be useful to analyze the court decision in the *Parker* case. The following paragraphs will discuss the court's rational and judgment in the *Parker* case and their consequences.

From the facts in the *Parker* Case, the plaintiff was the exclusive distributor of Parker Pens in Japan. The plaintiff sought injunctive relief to stop the third party for importing genuine Parker Pens into Japan from Hong Kong. Later, the parallel importer also brought suit because the Japanese Customs had refused entry of the pens on ground that such importation was without the trademark owner's consent. Contrary to the Tokyo

⁴¹⁴ See TERUO DOI, DIGEST OF JAPANESE COURT DECISIONS IN TRADEMARKS AND UNFAIR COMPETITION CASES 66 (1971), citing in *Nestle Nihon K.K. v. Sankai Shoten* (unreported case, Tokyo Dist. Ct., May 29, 1965); and also see Takamatsu, *supra* note 410, at 440.

⁴¹⁵ Based on the principle of territoriality of trademark, Petitioner, as a Japanese subsidiary company and the owner of the exclusive use right of such trademark in Japan, can prohibit the parallel imports by Respondent since Petitioner has the exclusive right to use Parker trademark in Japan.

⁴¹⁶ See Japanese Trademark Law, *supra* note 412, art. 30 and 37(v) and (vii).

⁴¹⁷ See *N.M.C. Co. v. Schulyro Trading Co.*, 234 Hanrei Taimuzu 57 (Osaka Dist. Ct. 1970), reprinted in English in 16 JAIL 113 (1972). [hereinafter *Parker* case]

Court in *Nestle* case,⁴¹⁸ the Osaka District Court held that parallel imports are not prohibited because such goods do not affect the function of trademark, which is to guarantee the origin and quality of the goods. The court mentioned that the trademark serves as an indication of source and a guarantee of quality in products. Thus, parallel imports are acceptable under the Japanese law when the Japanese trademark owner and the person who sold the trademark products to the parallel importer are the same or can be considered to be the same and the quality of parallel import goods is not different from that of the domestic products.⁴¹⁹ In other words, parallel import is not prohibited under Trademark Act and Custom Duties Act because it does not affect the function of a trademark. In contrast, if the quality of parallel import goods is different, the trademark owner can assert his right to bar such importation.⁴²⁰

The Osaka District court held that the parallel importation did not constitute an infringement because there was no effect on the function of trademark. The Defendant's action could not be considered to be illegal in substance under Article 37(5) of the Trademark Law.⁴²¹ The Court decided that Schulyro could not prohibit the importation

⁴¹⁸ Unlike the *Nestle* case, which prohibited parallel imports based on the principle of territoriality, the Court in the *Parker* case stated that the application of the principle of territoriality should be decided by focusing on the function of trademark. *Id.*

⁴¹⁹ This concept is similar to the common control exception and affiliate exception under the U.S. approach as recognized in the *Lever* case. The Japanese approach is similar to the U.S. approach by concerning on the physical and material difference between the imported products and the domestic products.

⁴²⁰ There are some possible examples of situation, which this exception allows the restriction on parallel imports if there is difference between imported goods and domestic goods. For example, in case of automobile industry, the Japanese brand-name car such as Honda and Toyota may be produced worldwide with the different standard. In the Asia zone, the quality of the material and interior decoration of the car, which was build for sale in Asia, may be lower than that of the car, which was build for sale in Europe, the United States and Japan. The Japanese patentee can bar such unauthorized parallel imports of the low quality car from abroad into Japan because there is difference in quality.

⁴²¹ Although this case was decided under Trademark Act, the Court applied the criminal theory of "illegal in substance" to the parallel import case. This theory was applied to decide whether an alleged infringement of trademark violated the purpose of trademark law since if it violated in substance, it would be considered as the trademark infringement. In other words, if such alleged infringement did not or slightly affect on the

and sale of Parker pens by parallel importer. The Court also refused to allow the Customs Service to block the parallel import goods imported by a third party.⁴²² Due to the District Court's decision in favor of the parallel importer, Schulyro appealed to the Japanese High Court. The High Court confirmed the District Court's decision that parallel imports did not infringe on the trademark right and could not be blocked by the Customs Service or barred by the trademark owner.⁴²³

In order to confirm the rule in the *Parker* case and eliminate further conflict between trademark owner and parallel importer, in 1972, the Customs Division of the Ministry of Finance promulgated regulations for parallel importation of trademark goods under the Customs Duties Act. The regulation stated that the parallel imports of genuine goods are not considered as infringement of intellectual property and that the Customs Office has no authority to stop the importation of those goods. The regulation also provided that parallel importation by the third parties can not be barred at the Customs Office "where the domestic trademark owner also holds the foreign trademark and is supplying the goods to the parallel importer, or where the domestic and foreign trademark

function of trademark, it should not infringe the trademark right. In order to decide whether parallel import should be prohibited, the court applied the criminal theory of illegal in substance and refused to apply the exhaustion doctrine. The court focused on the following factors: (i) the internationally well-known as the origin of the goods; (ii) the other imported Parker Pens were equal in quality to those sold by Schulyro; (iii) Schulyro's goodwill as the exclusive distributor was based on the reputation of Parker goods in the world market; (iv) the parallel importer did not take advantage of Schulyro's advertisements of Parker goods; and (v) parallel importation may promote fair and free competition in price and servicing of the products. See Takamatsu, *supra* note 411, at 442 and also see Harold C. Wegner, Patent Parallel Imports in Japan Consumer Promise or Patent Peril: The Aluminum Wheels Parallel Imports Case, at 7, available at http://www.foleylardner.com/PG/IP_BIOT/pate25_alum.html (visited Nov. 11, 2001).

⁴²² See Wegner, *supra* note 421, at 7. (explaining that the court refused to consider the principle of territoriality of trademark rights as an irrelevant issue in the parallel import case and focused on the purpose of trademark as indicators of source and guarantee of quality.)

⁴²³ See Takamatsu, *supra* note 411, at 442, citing in N. MC. Co. v. Schulyro Trading Co., Osaka High Ct., Aug. 6, 1971, 267 Hanrei Taimuzu (Law Times Reports) 243.

owners should be considered the same entity by virtue of their special relationship.⁴²⁴ In other words, parallel imports are permitted when there is an element of common control such as when the domestic and foreign trademark owners are the same entity.⁴²⁵ In addition, under the new regulation, the parallel importation of genuine goods for personal use was not considered an infringement of trademark rights. However, if the parallel imported products substantially differed in quality from those products sold or distributed by the authorized distributors, then parallel imports would be prohibited.⁴²⁶ If the differences between domestic products or parallel imported products were not substantial, parallel imports would be legal and allowed under the Japanese Trademark Law.⁴²⁷ In

⁴²⁴ See Takamatsu, *supra* note 411, at 443, citing in The Procedures for Application of Import Prohibitions of Goods Infringing Intellectual Property Rights, Finance Ref. No. 1443 of 1972.

⁴²⁵ See Sally Yu Shih, Parallel Importation of Trademark Goods in the United States, Japan and China: A Comparative Analysis 19-20 (1997) (unpublished Thesis, the George Washington University Law School) (on file with the George Washington University Law School Library) (comparing between the U.S. approach and Japanese approach in the issue of common control. Under the U.S. trademark, the common control is greater in degree because the U.S. uses the word "must" while Japan uses the word "should" before the phrase "be the same person." The U.S. considers the common control as the effective control but Japan requires only an element of common control.)

⁴²⁶ See Takamatsu, *supra* note 411, at 443.

⁴²⁷ See Yoriko Noma, Parallel Importation: A Comparative Study of the U.S. and Japanese Trademark Laws 45 (1992) (unpublished LLM Independent Research, University of Washington, School of Law) (on file with University of Washington, School of Law Library), citing in *La Chemise Lacoste SA v. Shinshin Boeki Co.*, 1141 Hanrei jiho 143 (Tokyo Dist. Ct. 1984); In my view, there is an interesting concern on the conjunction between the concept of common control and the different quality whether such parallel imports should be prohibited or not if the imported goods are produced in different quality but in the same brand name and same manufacturer as the intention of the brand owner. For example, The U.S. manufacturer of cooking pan produces a cooking pan with the cheap material since according to the U.S. consumers' preference in the low price rather than the high quality, which differs from the Japanese consumers who care more about the product quality than the product price. So the cooking pans are made under the same brand but with the different material (the cheap material for U.S. consumers and the high-quality material for Japanese consumers). In this case, the products in question have the same brand name and are made with the same manufacturer but they are different in the quality. Whether it is considered as a case of common control under the 1972 regulation. As a result of lawful parallel imports in the *Parker* case, the regulation introduces the concept of common control. So if the imported goods are different in quality but produced in the same manufacturer (the same control), is there the exception of exception even though it has the different quality but there is a common control? From this example, the Japan subsidiary of U.S. company attempts to stop those goods as a result of unlawful parallel imports. The importer may argue that it is not unlawful under the concept of the common control. In relation to the theory of illegal in substance, whether the core function of trademark law has been infringed. The answer is 'No' since the brand owner decided to produce the products in different quality. The question is whether the exception of exception swallows up the exception since it is possible that the concept of common control provides the exception to

the same year (1972), the Fair Trade Commission of Japan as a government agent also published guidelines for the sole import distributorship agreement. In order to promote antitrust and free competition laws, this guideline makes it illegal to prevent overseas suppliers from supplying products to a parallel importer.⁴²⁸ It stated that unjustifiably hindering parallel imports of goods covered by a distributorship agreement was to be considered an unfair business practice under the Japanese Antimonopoly Act.⁴²⁹

The court rule in the *Parker* case has been adopted and further expanded by the following cases. In the *Mercury* case, the Tokyo District Court followed the *Parker* case but in this case there was no evidence identifying any special relationship to present the element of control. Thus, the court decided that the parallel import in this case was illegal.⁴³⁰ Furthermore, in the *Lacoste* Case,⁴³¹ the court held that a trademark registrant could not prevent the unauthorized sale of genuine goods made in the U.S. by the exclusive licensee of the registrant's subsidiary.⁴³² Although the court followed the

exception in the case that the products are made in the same manufacturer with the difference in quality, and parallel imports may be permitted under the concept of common control.

⁴²⁸ Under the U.S. law, the trademark owner is able to create an exception in distribution clause by establishing a territorial restriction term in the licensing agreement and preventing parallel imports. By comparing with the U.S., it seems that Japan is more welcome the parallel import on trademark goods than the U.S.

⁴²⁹ See Takamatsu, *supra* note 411, at 443, citing in Antimonopoly Act Guidelines for Sole Import Distributorship Agreements, Fair Trade Commission of Japan (Nov. 21, 1972)

⁴³⁰ See Noma, *supra* note 427, at 42-43, citing in K.K. Asahi v. Ashhi Tsusho K.K., Judgment of August 31, 1973, Tokyo Chiho Sabansho (Tokyo District Court), Japan, 301 Hanrei Taimuzu.

⁴³¹ See *id.* at 45, citing in La Chemise Lacoste SA v. Shinshin Boeki Co., 1141 Hanrei jiho 143 (Tokyo Dist. Ct. 1984).

⁴³² The Tokyo District Court has rejected a lawsuit by Lacoste Company of France and its Japanese license to prohibit parallel imports of Lacoste goods produced by Lacoste's U.S. license, which were imported by two Japanese parallel importers. Referring to two primary functions of trademark (the source identification and the guarantee of quality), the Court decided that the goods in this case were genuine goods since Plaintiff had retained control of trademarks and quality of Lacoste products. Although there were slight difference between imported goods and domestic goods in quality, the Court consider that such differences did not harm the Plaintiff's business reputation or consumer and conclude that Defendant's parallel imports were not illegal in substance. See *id.* at 46-48.; see Roderick Seeman, Parallel Imports: Trademark Rights, THE JAPAN LAWLETTER, Feb. 1985, available at <http://www.japanlaw.com/lawletter/feb85/doh.htm>. (visited Dec. 13, 2001).; and also see Shih, *supra* note 425, at 15.

Parker case, it seems that the result of this case is broader than the *Parker* court ruling. The *Parker* case only allows the parallel imports if there is an element of control between the foreign trademark holder and the domestic trademark holder such as parent and subsidiary company or some other corporate body. On the other hand, the *Lacoste* case broadens the *Parker* case rule by considering the exclusive license as a part of the element of control. Compared to the U.S., the Japanese courts regarded the authorized use as part of special relationship to allow parallel imports, which contrasted to the U.S. court judgment in the *K Mart* case, which decided that parallel imports could not be allowed under the authorized use exception.⁴³³

Although the Japanese policy has emphasized the protection of IPRs for the manufacturer as “a key to the introduction of new products,”⁴³⁴ conversely in the case of trademark rights relative to parallel imports, Japan has focused more on the benefits to consumers as recognized in the *Parker* case.⁴³⁵ So it is appropriate to conclude that parallel imports do not infringe the exclusive right of trademark owner. The trademark owner cannot prohibit parallel imports unless the quality of imported goods differs from that of the local or domestic goods that may cause consumer confusion and damage the trademark owner’s reputation. Like the U.S. and ECJ courts, the Japanese courts significantly focus on the functions of trademark as source of origin and guarantee of

⁴³³ See the details of the *K Mart* case in the earlier section in the context of parallel imports in the U.S.

⁴³⁴ See Wegner, *supra* note 421, at 7.

⁴³⁵ See Christopher Heath, *From “Parker” to “BBS”-The Treatment of Parallel Imports in Japan*, 24 IIC, 179, 184 (1993) [hereinafter Heath, *From Parker to BBS*], cited in “Heikoyunyu mitomeru”, Nihon Keizai Shinbun of August 7, 1991. (mentioning that in order to reduce import barriers, the MITI set up a study group in September 1991 to draft parallel import guideline that was expected to prohibit parallel imports of machinery, electronics and other patent products and to permit parallel imports of clothing and other brand-name products embodied trademark, as well as to permit parallel imports of both copyright product (such as CDs and books) and semiconductors and computers covered by the Semiconductor and Integrated Circuits Law.)

quality to decide whether such parallel imports should be allowed or prohibited. Although the courts do not directly rely on exhaustion doctrine,⁴³⁶ the results of the court decisions are similar to the application of international exhaustion doctrine with a specific exception.

Most developed nations, particularly the U.S. prohibit parallel imports and adopt a national exhaustion doctrine. But Japan, one of the more wealthy developed nations, reaches an opposite conclusion by permitting parallel imports and recognizing an international exhaustion doctrine. With regard to the U.S approach, the U.S. courts focus substantially on the exclusive right of the trademark owner and the likelihood of consumer confusion. In contrast, the Japanese courts seem to place the low-price advantage of parallel imports above the exclusive rights of the trademark owner⁴³⁷ by focusing less on consumer protection. Parallel imports are primarily allowed under Japanese trademark law unless there is quality difference between imported products and domestic product. Thus, the Japanese approach is more permissive in parallel imports than the U.S. approach.

In the area of trademark, Japan takes a different approach from other developed countries because of high product price in Japan, strong consumer groups, and the support of government. By learning from trademark, the Japanese patent law has led a similar path of trademark law beginning with relative hostility to parallel imports and proceeding to more relaxed-permissive legal regime. In other words, the shift of judicial

⁴³⁶ Unlike trademark, in case of patent, the Japanese legal system has taken affirmative steps to protect parallel importers by applying the exhaustion doctrine as recognized in *BBS Kraftfahrzeugtechnik AG v. Racimex Japan KK*; *Jap Auto Products KK.*, which will be discussed in the following section.

⁴³⁷ See Shih, *supra* note 425, at 23.

and legislative pattern approach to trademark parallel imports in Japan has helped to stimulate a similar shift in the law of patent.

3.Parallel Imports in Patent

In the past, parallel imports were basically prohibited under Japanese patent law. However, recently the perception of parallel imports has changed under the application of an international exhaustion doctrine. Parallel imports do not constitute patent infringement because the exclusive right of the patentee exhausts under the exhaustion doctrine. This concept is definitely recognized by the Japanese Supreme Court. The landmark decision of the Supreme Court in *BBS Kraftfahrzeugtechnik v. Jap Auto Products*,⁴³⁸ held that a Japanese patent was not infringed upon parallel imports of goods produced under a foreign patent.⁴³⁹ The Court stated that parallel imports did not constitute patent infringement and it was in the best interests of Japanese consumers to allow parallel goods to be imported. Before discussing the detail of the *BBS* case, the following paragraph will elucidate the previous Japanese perception on parallel imports to better understand the development of Japanese court decision in this issue.

⁴³⁸ See Case No. H7-(wo) 1988, July 1, 1997, *BBS Kraftfahrzeugtechnik AG v. Racimex Japan KK.; Jap Auto Products KK.*, translated in 29 IIC 331(1998)[hereinafter called *BBS v. Jap Auto*, Supreme Court Decision]; and also translated in Jinzo Fujino, *Parallel Imports on Patented Goods: The Supreme Court Talks About Its Legality*, available at <http://www.okuyama.com/c3v01ok.htm> (visited Nov. 10, 2001).

⁴³⁹ Whether it is critical that the goods produced under foreign patent is distinct from the lawfully produced goods in Japan. For example, there is a difference between domestic-produced goods and foreign-produced goods. Although there is different between legally produced in foreign, it may be considered as the legitimate produced goods under the license or the same entity ruling that is really cover and cannot be exclude from Japan. Or in another example, in country A has patent, but no patent whether no patent protection or it expired in country B. Produce goods in country B where is no patent. Those goods make by the same entity. The question is whether the court decree in *BBS* case applies to those goods or not.

3.1 The Preceding Japanese Position on Parallel Imports

Prior to the *BBS* case, there was a court decision prohibiting parallel imports. The Osaka District Court held that parallel imports infringed on patent right, in *Brunswick Corporation v. Orion Kogyo K.K.*⁴⁴⁰ This case dealt with the importation of a second-hand machine from Australia via Hong Kong and the plaintiff was an American company that owned a patent for the machine in both Japan and Australia.⁴⁴¹ Brunswick sued Orion for patent infringement based on Orion's importation and resale of bowling pin devices in Japan.⁴⁴² The Osaka District Court granted the plaintiff an injunction prohibiting the importation of the patented product first marketed abroad by the Plaintiff's licensee and subsequently imported into Japan by the Defendant. The Court considered parallel imports as an infringement of the patent right under section 101⁴⁴³ and 2(3) of Japanese Patent Act.⁴⁴⁴

Based on the exhaustion doctrine, Orion argued that the Brunswick's sublicense in Australia had exhausted Brunswick's patent right upon the sale of those products. Hence, Brunswick could not have right to sue for patent infringement against the purchasers of its product. However, the Court rejected this argument by depending on a strict territoriality principle of patent protection and decided in favor of Brunswick.⁴⁴⁵

⁴⁴⁰ See Matthew R. Hicks, note and comment, *Japanese-Auto Products v. BBS: A Threat to Exacerbate U.S. - Japanese Trade Relations?*, 19 LOY.L.A. INT'L & COMP. L. REV. 479, 491-94 (1997), citing in *Brunswick Corp. v. Orion Kogyo Kabushiki Kaisha*, 1 Mutai Saishu 160 (Osaka District Ct., June 9, 1969).

⁴⁴¹ See *Health, From Parker to BBS*, *supra* note 435, at 181.

⁴⁴² See *Kremen*, *supra* note 6, at 165.

⁴⁴³ See The Patent Law No.121 of April 13, 1959 as amended by Law No. 220 of December 22, 1999, Section 101, available at <http://www.jpo.go.jp/shoukaie/patent.htm> (visited Mar. 26, 2002).

⁴⁴⁴ *Id.* section 83 and 2(3) describe the exclusive right, which covers importing the product produced by a patented process or the importation of a patented product.; and also see Tessensohn, & Yamamoto, *supra* note 256, at 730.

⁴⁴⁵ See Hicks, *supra* note 440, at 491-92.

Unquestionably, the court seems to place the protection of patent right and the benefit of patent owner over the benefit of consumer by allowing the patent owner to bar the parallel imports of patent goods although those products were marketed with the patentee's consent. By focusing on the strict territoriality principle of patent protection the court mentioned the exhaustion doctrine and decided that the scope of this doctrine only applied on the initial sale of patented products in Japan (so-called national exhaustion).

3.2 The Current Japanese Position on Parallel Imports

As mentioned before, recently Japanese's position has been changed in favor of parallel importers and consumers. In the *BBS* case, the Japanese Supreme Court held that a Japanese patent could not bar parallel imports of goods produced under a foreign patent. The Court stated that parallel imports did not constitute patent infringement and it was in the best interests of Japanese consumers to allow parallel goods to be imported.

From the facts in the *BBS* case, BBS was the holder of the Japanese patent rights to an invention entitled "A Wheel of an Automobile." BBS sold and licensed the aluminum wheels made under the patent in both Japan and Germany, but the price in Germany was cheaper than that in Japan. Jap-Auto bought the patented aluminum wheels made by the Germany licensee and imported them into Japan in order to profit from the price difference. Due to the fact that BBS lost profits from Jap-Auto's importation, BBS filed a patent infringement lawsuit at the Tokyo District Court. By referring to the national exhaustion doctrine, the Tokyo District Court held that the parallel imports

infringed BBS's Japanese patent rights by following the approach of the *Brunswick* case.⁴⁴⁶

Jap-Auto appealed the district court's decision and argued that the distribution in Germany exhausted BBS's patent right in Japan based on the international exhaustion doctrine rather than the domestic or national exhaustion doctrine.⁴⁴⁷ The Tokyo High Court reversed the Tokyo District Court's decision by applying the international exhaustion doctrine.⁴⁴⁸ After considering whether the plaintiff had already received the benefit of its patent, the Court pointed out that in this case the benefit of the patent was already paid to the patentee when the purchase was made across the border. Consequently, the patentee should have no right to control the further sale of the patented products.⁴⁴⁹ The Tokyo High Court reasoned that if the patent right had not been exhausted after the first authorized sale and the right to control a subsequent resale of patented products is restored, allowing patent owner to thwart the subsequent distribution of products would certainly harm the improvement of industry and the business security on prospects of commerce.⁴⁵⁰

As a result of the Tokyo High Court's decision, BBS appealed the case to the Supreme Court to decide whether the Tokyo High Court's decision that this parallel

⁴⁴⁶ See Case No Hei 4 (wa) 16565, *BBS Kraftfahrzeugtechnik AG v. Racimex Japan KK.; Jap Auto Products KK.* (Tokyo District Court, 22 July 1994), *translated in* 27 IIC 546 (1996). [hereinafter *BBS v. Jap Auto*, Tokyo District Court Decision] ;In accordance with exhaustion doctrine, the court confirmed that Japanese patent law does include a first sale or exhaustion doctrine although there is no such express provision in the patent law. Based upon national exhaustion doctrine, the district court explains that the doctrine only applied to first sales in Japan, not overseas. *Id.* at 547-48.

⁴⁴⁷ See *BBS v. JAP Auto*, Supreme Court Decision, *supra* note 438; and also see *Hicks*, *supra* note 440, at 481-82.

⁴⁴⁸ See Case No Hei 6 (ne) 3272, *Racimex Japan KK; Jap Auto Products KK v. BBS Kraftfahrzeugtechnik AG.* (Tokyo High Court, 23 March 1995), *translated in* 27 IIC 550 (1996). [hereinafter *Jap Auto v. BBS*, Tokyo High Court Decision]

⁴⁴⁹ *Id.* at 554.

import did not infringe on BBS's patent right was incorrect. The Supreme Court confirmed the Tokyo High Court's decision that unauthorized parallel importation of patented goods did not infringe on a domestic patent right.⁴⁵¹ The Supreme Court had reached the same conclusion by applying the international exhaustion doctrine. However, the Supreme Court not only explained the rational of decision more fluently and clearly than the Tokyo High but also substantially introduced the new concept on the exception of international exhaustion.⁴⁵² This exception to permitting parallel imports is based on the theory of implied license and provides an exception from the international exhaustion doctrine.⁴⁵³

The Supreme Court applied the international exhaustion doctrine in its decision and reasoned that the patentee should not have the right to receive the double benefit from his patent right. The Court mentioned, "it would not seem necessary to give the patentee or the license rights beyond the first act of marketing, as the patentee would then obtain an unnecessary double reward in the course of further distribution."⁴⁵⁴ Therefore, there is no need to permit the patentee to acquire double benefits in the distribution

⁴⁵⁰ *Id.* at 552-53; and also see Tessensohn, & Yamamoto, *supra* note 256, at 724.

⁴⁵¹ The Court stated that under section 68 of the Patent Act 1957 the patentee has the exclusive right to work or license a patent and 'work' means manufacture, use, assign, lease, import, or offer for assignment or lease of the product. However, his patent right exhausted after the first sale of those products. see BBS v. Jap Auto, Supreme Court Decision, *supra* note 438, at 333.

⁴⁵² Furthermore, the Supreme Court also examined Article 4 bis of the Paris Convention for the Protection of Industrial Property. The Court held that Article 4 bis (1) and (2) deny the interdependence of patent rights and assert the independence of patent rights in various countries. Furthermore, the court interpreted the Paris Convention with regards to the principle of territoriality. It means that the effect of a patent right is only valid within the boundaries of that country. Thus, whether the patentee can exercise his patent rights in Japan arguably should be purely a matter of interpretation of the Japanese patent law. However, the Court found that the Paris Convention and the principle of territoriality were irrelevant to the complications of the parallel import case. Under the principle of territoriality, it means that patent in each country are subject to domestic legal provisions and the patent rights only have effect within the geographical limits of such country. *Id.* at 333.

⁴⁵³ See Ako Shimada William, *International Exhaustion of Patent Rights Doctrine: Is Japan's Move a Step Forward or Back From The Current Harmonization Effort?*, 7 J. INT'L L. & PRAC. 327, 348 (1998).

process of a patented product that has been assigned from the patentee or licensee. Moreover, the Japanese Supreme Court also addressed the application of the exhaustion doctrine and concurred with the Tokyo High Court that if the initial sale of patented products abroad was either subject to a fixed price under a compulsory license or limited by a national price control the right of the patentee should not be exhausted and the exhaustion doctrine should not be applied to the situation.⁴⁵⁵

In addition, once an assignee has acquired the right to commercial use of a patented product, the assignee may freely distribute, import or sell such patented products without the patentee's consent. Prohibiting parallel imports was considered an impediment to smooth market distribution and non-consistent with the aim of patent law.⁴⁵⁶ The Court decision, which allows parallel imports, could enhance the policy of free movement, distribution, and importation of goods and promote consumer interests in encouraging competitive pricing. So the patentee is only guaranteed protection of a limited scope in order to harmonize patent right protections with the public interest.

Nevertheless, the court introduced a notable limitation on parallel imports. A patentee can agree with an assignee at the time of assignment to exclude Japan from the authorized region of the sale or use of the patented product. Such restriction should clearly appear on the patented product and a subsequent purchaser should be able to recognize the restriction.⁴⁵⁷ In the *BBS* case, there was no notice on the products

⁴⁵⁴ See *BBS v. Jap Auto*, Supreme Court Decision, *supra* note 438, at 334.

⁴⁵⁵ See *Jap Auto v. BBS*, Tokyo High Court Decision, *supra* note 448, at 554.

⁴⁵⁶ *Id.* at 333.

⁴⁵⁷ *Id.* at 335. The Supreme Court stated "If the patentee reserve his rights at the date of transfer with respect to the use in Japan when selling the patented products abroad, at the time of transfer the patentee has agreed with the transferee that sale or use of the product should not be allowed in Japan. If *clearly indicated on the product, such restriction is also valid against subsequent purchasers* of the patented product *along the distribution chain* even with the number of intermediaries." (emphasis added); see

indicating a territorial restriction that prohibited the sale of the patented products in Japan. Thus, the defendant could not be bound with any restriction on resale or import.

3.3 The Effects of the Supreme Court Decision in the BBS Case

Some scholars have commented that the Supreme Court's decision in favor of parallel imports was flawed by ignoring "the practical reality of conducting transnational commercial transaction in the business world and industry"⁴⁵⁸ and by creating novel questions pertaining to the new theory of exemptions of international exhaustion doctrine.⁴⁵⁹ Although the new exemption was created by the Supreme Court, it may be difficult to employ. In practice, there may be a time lag for patentees to insert these type of clauses into their future contracts.⁴⁶⁰ It is difficult to notify everyone in the chain or those likely to be involved in dealing with the products with a no-export or no-resale restriction in Japan either by labeling, by letter and including advertisement.⁴⁶¹ Allowing parallel imports possibly causes adverse effects either to foreign and Japanese patentee or

Thomas Hays, *BBS Kraftfahrzeugtechnik AG v. Racimex Japan KK; Jap Auto Products KK: Japan Opens the Door to Parallel Imports of Patent goods*, 2 MELB. J. INT'L L. 191, 197-98 (2001). [hereinafter Hays, *BBS Case Japan Open Door to Parallel Import*] (mentioning that to avoid the issue of privity of contract, the court ruled that such restriction should be clearly indicated on the product that subsequent purchasers through the chain could acknowledge such restriction, which can help the patentee to eliminate the issue of privity of contract.); and also see Tessensohn, & Yamamoto, *supra* note 256, at 744. (pointing out that it seems that the Japanese Supreme Court attempted to find the middle solution between prohibiting parallel imports and allowing parallel imports. But this approach constituted many practical problems. There are many patent product sold without restriction clause for no exportation into Japan since during the time of making contract, the patentee expected that the Japanese patent law prevent parallel imports of patent products.)

⁴⁵⁸ See Tessensohn & Yamamoto, *supra* note 256, at 731.

⁴⁵⁹ See Fujino, *supra* note 438, at 8.

⁴⁶⁰ See Tessensohn & Yamamoto, *supra* note 256, at 733.

⁴⁶¹ *Id.* at 735 and 739. (mentioning that an agreement prohibiting exporting or reselling may breach antitrust or competition laws of the country of sale or violate a licensing agreement. The licensing agreement always falls within the scope of antitrust law since the intellectual property owner may attempt to maintain his power and exercise his exclusive rights in abuse manner through the licensing agreement.)

to Japanese consumers.⁴⁶² In addition, the outcome of the *BBS* case could impact on U.S. companies and threaten U.S.-Japanese trade relations.⁴⁶³ Japanese trade barriers have been relaxed and make it possible for U.S. businesses to sell parallel import products in Japan.⁴⁶⁴ The court's decision in the *BBS* case may harm Japanese businesses because many goods produced in Japan and then imported into the U.S. could legally be re-imported into Japan by parallel importers. Such a sequence of trade would enable U.S. businesses to make a profit on parallel imports resold in Japan.⁴⁶⁵

Indeed, on the bright side, the Supreme Court decision, by allowing parallel imports, primarily benefits consumers and encourages free trade.⁴⁶⁶ The consumer should have various choices of products available on the domestic market and with lower prices. It is well known that the average products' price in Japan is higher than other countries,

⁴⁶²These scholars also argue that parallel imported goods will increasingly flow into Japan as long as products in overseas markets are priced cheaper than in the Japanese market. As such, both the foreign and Japanese patentees will suffer from the effects of parallel imports and eventually parallel imports will cause an adverse effect on Japanese consumers, particularly in the area of pharmaceutical industry. The innovation of new drugs requires pharmaceutical companies to spend tremendous amounts of money for research, development, and testing. Allowing parallel imports would make it difficult for pharmaceutical companies to recoup their investment and could diminish the incentive for the pharmaceutical companies to create the new drugs. *Id.*; and also see Kremen, *supra* note 6, at 168-73. (pointing out the overall effects of the *BBS* case on the world's top companies such as General Electric, Royal Dutch Shell, or Coca-Cola Company.)

⁴⁶³ See Hicks, *supra* note 440, at 498-503; see Teresa Riordan, Tokyo Court Ruling Could Set Off New Trade Rift with the United States over Protection of Patents, N.Y. TIMES, Apr. 17, 1995, at D2.(explaining that the strength of Yen and the high desirability of U.S. goods provide an incentive for importers to circumvent Japanese patents held by U.S. companies and to import low-priced goods into Japan.); However, there are many patented products which are imported from Japan to the U.S. and cause a problem to local authorized dealers such as Kubota tractors. see Department of Labor and Industries, Hazard Control & Alerts, Gray Market Kubota Tractors, March, 1997, available at <http://www.lni.wa.gov/wisha/hazalerts/haz971.htm> (visited Dec. 13, 2001)

⁴⁶⁴ *Id.* at 505; and also see Elliott J. Hahn, *Patents: Recent Japanese Ruling on "First-Sale" Doctrine May Exacerbate U.S.-Japan Trade Relations*, CEB CAL. BUS. L. REP., July 1995, at 25.

⁴⁶⁵ See Hicks, *supra* note 440, at 502-3.

⁴⁶⁶ The Japanese Supreme Court concerned the conflict between the flow of products in international trade and the patentee's right. The Court states that "in light of the fact that international trade is being conducted on a tremendously broad and sophisticated basis, it is necessary that freedom of trade including freedom to import should be paid utmost respect when a dealer in Japan imports a patented product marketed in a foreign country to put it in a distribution channel in Japan." See *Jap Auto v. BBS*, Tokyo High Court Decision, *supra* note 448; and also see Fujino, *supra* note 438, at 4.

the parallel imports would encourage the free competition in the Japanese market, which finally may lead to a reduction in the price of domestic products.⁴⁶⁷ In reality, the IPRs owners basically set up the product price differential among various markets. It should be sufficient to facilitate the IPRs owners to take advantage of the higher price and receive any profits from sales in every market. Thus, the IPRs owners should not have the right to get a double benefit by having a right to bar parallel imports since they already receive this benefit from the first sale.

Allowing parallel imports would promote the free movement of goods and free trade in both domestic and global level and simultaneously reduce both the monopoly power of patentee and the very restricted control of distribution system in Japanese market. With regard to limited access to the Japanese market, the distribution system is quite limited not only for foreign distributors to access but also their foreign products to be marketed and distributed in the Japanese market. The trading and distribution system in Japan is based on the concept of protectionism⁴⁶⁸ that could be considered as a restriction to free trade, which might conflict with the purpose of GATT. Consequently, the result of the *BBS* case might loosen the solid distribution system in Japan and create

⁴⁶⁷ In theory, the price of product should be determined by the demand and supply. However, in practice there are other factors determining the product price such as the business strategy of intellectual property owners and the variable cost of manufacturing and distributing the intellectual property products.

⁴⁶⁸ Some scholars comment that Japan is considered as neo-mercantilism, believing that countries should run surpluses with its trading partners. They mention that allowing parallel imports generally can not make effects on Japanese industry since the structure of Japanese industry in general or distribution channels (such as keiretsu distribution system which facilitates manufacturers' effort to control product, accessories and service, and price, as goods flow from factories to consumers) will thwart parallel imports and Japanese strategies involve either reducing a cost of production or eliminating price differential in areas that would face with parallel import competition. Moreover, the lenient regulation of monopolies, anti-competitive agreements, and cartels encumber all imports including parallel imports. See Paul Lansing & Joseph Gabriella, *Clarifying Gray Market Gray Areas*, 31 AM. BUS. L. J., 313, 329-38 (1993); see Robert E. Weigand, *The Gray Market Comes to Japan*, 24 COLUMN. J. WORLD BUS. 18 (1989); and also see Robert L. Cutts, *Capitalism in Japan: Cartels and Keiretsu*, 70 HARV. BUS. REV. 48-49 (1992).

additional opportunity for the foreign distributors and foreign products to access the Japanese market.

Nevertheless, the Court also realized the benefit to the patentee for controlling the commercial circulation of patent products. To balance the protection of patent with public interest, the court creates the no-resale or no-export in Japan restriction exception to escape from the application of an exhaustion doctrine, which is considered as the middle way approach. Under this exception, the patentee cannot bar parallel imports unless patentee or assignee at the time of assignment obviously impose the restriction clause to exclude Japan from the authorized region of the sale or use of the patented product, so long as the restriction clearly appears on the patented product and a subsequent purchaser is able to recognize the restriction. According to this exception, the patentee still has the right to control the movement of patented product by using the contractual approach to exclude Japan's market from the commercial distribution of goods outside Japan.

There are two interesting cases that the court follows after the *BBS* case and further clarifies the exhaustion doctrine under the *BBS* Supreme Court decision. First, in *The Welcome Foundation Ltd. v. Sawai Seiyaku K.K.I.*,⁴⁶⁹ the Tokyo High Court ruled that the exhaustion doctrine does not apply to act of changing the legally purchased patented article. The exhaustion doctrine applies only to use and assignment but does not apply to manufacturing. In this case, the court concluded that the accused infringement act, which is the act of isolating an active ingredient gives rise to manufacturing, considered as a use

⁴⁶⁹ See Toshiko Takenaka, Isolating Ingredients from Legally Purchased Pharmaceutical Compound is Within Authority of Owner: *The Welcome Foundation Ltd. v. Sawai Seiyaku K.K.I.*, CASRIP Newsletter, Winter 2002, available at <http://www.law.washington.edu/casrip/newsletter/newsvqi1jp1.pdf> (visited Sep. 04, 2002), citing in *The Welcome Foundation Ltd. v. Sawai Seiyaku K.K.I.*, Judgment of Tokyo High Court, November 29, 2001.

not as a manufacturing. Thus, the defendant's act did not constitute an infringement because such act fell within the scope of exhaustion doctrine.⁴⁷⁰ Second, in the disposable camera case,⁴⁷¹ the Tokyo District Court decided that the act of defendant constituted a patent infringement because the exhaustion doctrine did not apply in this case as it considered as replacing a main element of the essential structure, film, in the patented disposable camera.⁴⁷²

From those two cases, one can conclude that the Court emphasized the substantial identity between the product that was purchased and the product that was repaired or modified.⁴⁷³ If such changes, repairs, or modifications do not constitute a substantial difference in product identity, the exhaustion doctrine still applies to those acts. On the other hand, if those acts constitute a substantial difference in product identity, it does not fall within the scope of the exhaustion doctrine and those acts infringe the patent right. Such rational is more in line with the U.S. court decision in broadly interpreting the permissible scope of repair of patent articles.

3.4 Conclusion

To summarize, in recent times Japanese patent law has firmly favored parallel imports. The Supreme Court's current decisions to allow parallel imports reversed the previous decisions that prohibited parallel imports. The Supreme Court is the highest

⁴⁷⁰ *Id.* (The court decision is based on the reason that if an act is considered a manufacturing and this act violates a patent if a patented product has been substantially changed to the extent that the resulted product is no longer regarded as the same product that was purchased. In this case, the exhaustion doctrine does not apply.)

⁴⁷¹ See Toshiko Takenaka, Reconditioning a Disposable Camera is Infringement, CASRIP Newsletter Autumn 2000 at 9, citing in Disposable Camera case, Judgment of Tokyo District Court, August 31, 2000.

⁴⁷² *Id.*

court in Japan and its decision sets the standards for the interpretation and application of Japanese laws by the lower courts. Japanese consumers are expected to positively benefit from the Supreme Court's ruling to allow parallel imports, as it should increase the variety of lower priced goods available to consumers.⁴⁷⁴

In comparison to the U.S. court decisions on parallel imports of patent goods, the Japanese approach differs from the U.S. approach. The difference between the decisions of the U.S. and Japanese courts is attributable to the cultural differences between the two countries. The U.S. patent law focuses on protecting the individual patent holder's rights to enable them to reap the rewards of their work. However, Japanese patent law focuses on the dissemination of technology as a means to benefit society as a whole and seeks to protect the greater society over granting exclusive rights to inventors.⁴⁷⁵

4. Parallel Imports in Copyright

In relation to copyright, the parallel imports seem to be permissible with fewer disputes than in area of trademark and patent. Under Japanese copyright law, the copyright owner basically has the exclusive rights to reproduce his work,⁴⁷⁶ to perform

⁴⁷³ See Takenaka, *supra* note 469.

⁴⁷⁴ See Kremen, *supra* note 6, at 167-68.

⁴⁷⁵ See Tessensohn & Yamamoto, *supra* note 256, at. 742-45. (pointing out that the prohibitive approach in the *Curtiss* case is a better and more practicable approach than the permissive and lenient tack taken by the Japanese Supreme court and suggesting that the Japanese Supreme Court should use the same approach as the U.S. court do by fundamentally prohibiting parallel imports with specific exemptions such as the U.S. court stated in the *Curtiss* case. From the *Curtiss* case, if the importer of patent products had the clear an unambiguous mandate from the patentee to sell such products in anyway including in the United States which is provided by the express contractual terms between the patentee and the initial purchaser, such importation was not infringed the U.S patent right and the right of patentee was exhausted upon such first sale.); and also see the more detail of the *Curtiss* case in the pervious section in the context of the United States on parallel imports in patent.

⁴⁷⁶ See The Copyright Act 1899, art. 1 and 21, translated in Yukifusa Oyama, Copyright Research and Information Center (CRIC) October, 2001, available at http://www.cric.or.jp/cric_e/clj/index.html (visited

his work publicly,⁴⁷⁷ to present his work in public,⁴⁷⁸ to make the public transmission of his work,⁴⁷⁹ and to distribute copies of his work.⁴⁸⁰ Thus, the importation of copyrighted goods does not normally constitute copyright infringement. However, certain acts of importing copyrighted goods constitute infringement under Article 113(1).⁴⁸¹ Such copyright infringement is classified as secondary or indirect infringement.⁴⁸² Only importation of infringed goods constitutes a secondary infringement. If the imported products are genuine goods, not infringed goods, then the importation does not infringe on the right of copyright owner. The parallel import goods were made with the copyright owner's authorization and considered as genuine goods. Therefore, the parallel imports of the genuine goods do not constitute a secondary infringement and the copyright owners do not have a right to bar such importation.

Regarding an exhaustion doctrine, the exhaustion doctrine clearly appears in the Japanese copyright law. The exhaustion doctrine was positively applied in the parallel import case by the Japanese court, which decided in favor of parallel importers. Under

on Nov. 20, 2001) [hereinafter The Copyright Law of Japan]; and also see Teruo Doi, Japan, § 1[2] JAP-6 in INTERNATIONAL COPYRIGHT LAW AND PRACTICE (Melville B. Nimmer & Paul Edward Geller ed., 1988).

⁴⁷⁷ See The Copyright Law of Japan, *supra* note 476, art. 22.

⁴⁷⁸ *Id.* at art. 22 bis.

⁴⁷⁹ *Id.* at art. 23.

⁴⁸⁰ *Id.* at art. 26.

⁴⁸¹ See Doi, *supra* note 476, at § 8[1][a][ii] JAP-49.; see The Copyright Law of Japan, *supra* note 476, art. 113. Article 113 provides:

“The following acts shall be considered to constitute infringements on moral right, copyright, right of publication or neighboring rights:

- (i) the importation into this country, for distribution, of objects made by an act which would constitute an infringement on moral rights, copyright, right of publication or neighboring rights if they were made in this country at the time of such importation;
- (ii) the distribution or the possession for distribution of objects made by an act infringing moral rights, copyright, right of publication or neighboring rights (including those imported as mentioned in the preceding item) by a person who is aware of such infringement.”

⁴⁸² See Katsunari Goto, “Indirect Infringement” of Copyrights in a Multimedia, *available at* http://www.cric.or.jp/cric_e/cuj/cuj98/cuj98_4.html (visited Nov. 22, 2001)

the application of an exhaustion doctrine, the copyright owner cannot assert his exclusive right to bar parallel imports because his right is already exhausted after the first sale of his copyright products. The court applies the exhaustion doctrine in copyright case in the same way as does in trademark and patent case. There are some court decisions, which support that the courts take a similar position on the unauthorized sale of gray market goods under copyright law as has been taken with trademark and patent law in parallel import cases.

For instance, the Supreme Court⁴⁸³ confirmed the Osaka High Court decision based on the exhaustion doctrine in the *Akuto* case.⁴⁸⁴ This case dealt with distribution right⁴⁸⁵ and involved the sale of used or second hand TV game software, which the Court considered as a cinematographic work. The Court also found that TV game software is recognized as a distribution right under Article 26 of Japanese Copyright Act.⁴⁸⁶

⁴⁸³ See Tsunashige Shirotori, Japan's Supreme Court Decision on the Sales of Used TV Game Software, CASRIP Newsletter (Autumn 2002), available at <http://www.law.washington.edu/casrip/newsletter/newshome.html> (visited Feb. 8, 2003), citing in the Judgment of Supreme Court of Japan, April 25, 2002, 1785 Hanrei Jiho 3.

⁴⁸⁴ See Toshiko Takenaka, Sale of Used TV Game Software is Legal: K.K. Enikkuru v. K.K. Josho, *Akuto* etc v. K.K. Sega, CASRIP Newsletter, Winter 2001, available at <http://www.law.washington.edu/casrip/newletter/newsv811jp1.pdf> (visited Dec. 6, 2001), citing in *Akuto* etc. v. K.K. Sega, Judgement of Osaka High Court, March 29, 2001.

⁴⁸⁵ See Doi, *supra* note 476, at JAP-52. (explaining that in relation to the distribution right, the distribution right is defined in Article 2(1)(xix) as including both the assignment of tangible-property rights in embodiments and the rental or lending of same to the public, with or without consideration. In the case of a cinematographic work or a work reproduced in a cinematographic work, distribution refers to such acts "or the purpose of making the work available to the public. Only in cinematographic works, as well as works reproduced in cinematographic works, in Article 26, recognized a right of distribution. Thus Article 2 allows the owner of copyright in cinematographic works to control both selling and renting or lending copies, such as the unauthorized rental and lending of videotapes whether these tapes are made illegally or legally.)

⁴⁸⁶ In contrast, in K.K. Enikkusu v. K.K. Josho, Judgement of Tokyo High Court, March 27, 2001, the Tokyo High Court did not agree with the Osaka High court and stated that the TV game software was a cinematographic work but denied a distribution right. Therefore, it did not infringe the right of copyright owner. See Takenaka, *supra* note 484. (pointing out that there is a conflict between the Tokyo High Court and the Osaka High Court. In the beginning, the Tokyo District Court decided that TV game software was held to not a cinematographic work and thus it did not have a distribution right under Article 26. There is no copyright infringement-Judgment of Tokyo District Court, May 27, 1999, Hanrei Jiho No. 1679, 3,

Nevertheless, based on the exhaustion doctrine, the Supreme Court held that the sale of used cinematographic works without the purpose of making available to the public did not infringe copyright because the exclusive right of copyright owner was exhausted after the first sale.⁴⁸⁷ By alluding to the *BBS* Supreme Court decision, the court concluded that the same policy reasons for applying the exhaustion doctrine in patent case are applicable to copyright case as well.⁴⁸⁸ The Court also distinguished between the rental right and the distribution right of software copies. Although the copyright law does not prevent the implication of the exhaustion doctrine to the distribution right uniquely associated with cinematographic works, the court accepted that the exhaustion doctrine does not apply to the rental right related to cinematographic works.⁴⁸⁹

In conclusion, the Japanese copyright law does not grant the importation right to the copyright owner. The importation of genuine goods does not primarily constitute a

Hanrei Taimuzu No. 1004, 98. On the contrary, the Osaka District Court reached an opposite conclusion finding TV game software to be a cinematographic work that has a distribution right.-Judgment of Osaka District Court, Oct. 7, 1999. As the result of such inconsistency, the Tokyo and Osaka High Courts attempted to resolve a conflict between two lower district courts by concluding that TV game software was a cinematographic work but had a different view in the distribution right. The Tokyo High Court ruled that there was no distribution right but the Osaka High Court held that it had a distribution right. By comparing between those two high court decisions, the Tokyo High Court's limitation is broader than the Osaka High court's limitation because no distribution is available. The Osaka High Court's exhaustion theory applies only when the copyright enforcement interferes with the free flow goods in the market. However, at the end, both high court decisions had the same outcome by deciding that there was no copyright infringement but based on different rationale.); As the result of these aforementioned conflicts, the Supreme Court clarified in this issue and made its decision in line with the Osaka High Court decision. See Shirotori, *supra* note 483, at 2.

⁴⁸⁷ See Shirotori, *supra* note 483, at 3.; and also see *Keep K.K. v. K.K. Pony Canyon*, Hanrei Jiho (No. 1501) 78 (Tokyo Dist. Ct., July 1, 1994), *translated in* 27 IIC 570 (1996). (The Tokyo District Court decided in favor of the domestic authorized distribution by dismissing the lawsuit. For the facts, the plaintiff, a parallel importer of the US film ("101 Dalmatians" by Walt Disney) sue the defendant, who was granted the sole right of distribution in Japan, by claiming that the defendant's action (circulating a warning letter to inform public) in alerting potential purchaser to the unlawfulness of parallel imports is an unjustified interference with this business activities and claim for damages since the plaintiff was unable to sell the parallel import products.)

⁴⁸⁸ See Shirotori, *supra* note 483, at 3. (pointing out that the Supreme Court attempted to secure the free and smooth flow of commodities at markets and so on. The Court confirmed that the reasons under the BBs

copyright infringement. However, the importation of copyright infringed goods constitutes a secondary infringement because the parallel imports are associated with the genuine goods, the parallel imports do not infringe copyright. In addition, the Japanese court also recognized the application of the exhaustion doctrine. Although most cases are involved with distribution right, those court decisions confirmed that the first sale or exhaustion doctrine is definitely present in Japanese copyright law and was applied by the Japanese courts. It can be concluded that the exhaustion doctrine also applies in the copyright case the same as in the patent and trademark case and the parallel imports are not prohibited under the copyright law. The result of parallel import case in copyright law should be consistent with that in patent and trademark cases by allowing parallel imports and limiting the exclusive right of intellectual property owners to bar parallel imports.

5. Conclusion

Unlike the United States, Japan reaches an opposite conclusion by permitting parallel imports and recognizing an international exhaustion doctrine in area of trademark, patent and copyright law. In the area of trademark, the Japanese court and agencies seem to place the economic advantages of parallel importation above the exclusive rights of trademark owner protection.⁴⁹⁰ Parallel imports are primarily allowed under the Japanese trademark law unless there is quality difference between imported products and domestic product. In the case of patent, Japanese patent law has firmly

case dealing with the transfer of ownership of patent product should be applied in the field of copyright with respect to the right of the transfer of ownership as well.)

⁴⁸⁹ *Id.* at 3.

⁴⁹⁰ See Shih, *supra* note 425, at 23.

favorable parallel imports. The Supreme Court's decisions in the *BBS* case to allow parallel imports reversed the previous decisions that prohibited parallel imports. Japanese consumers are expected to positively benefit from the Supreme Court's ruling to allow parallel imports, as it should increase the range of lower priced goods available to consumers.⁴⁹¹ The Japanese patent law focuses on the dissemination of technology as a means to benefit society as a whole and seeks to protect the greater society over granting exclusive rights to inventors.⁴⁹²

V. DEVELOPING NATIONS

As mentioned earlier, there is a conflict between developed and developing countries on the issue of parallel imports and application of exhaustion doctrine. The previous section discusses the perspectives of developed countries. Thus, this part will describe and analyze the issue of parallel imports and the application of exhaustion doctrine from the developing countries' perspective to portray the probable scheme that might be presented and supported by developing countries as an international legal standard. Thailand, as my home country and Hong Kong are selected to represent the perspective of developing nations on parallel imports and to present how an exhaustion doctrine was applied.⁴⁹³

⁴⁹¹ See Kremen, *supra* note 6, at 167-68.

⁴⁹² There are some scholars suggest that the Japanese Supreme Court should use the same approach as the U.S. court approach by fundamentally prohibiting parallel imports with specific exemptions. See Tessensohn & Yamamoto, *supra* note 256, at. 742-45. (pointing out that the "prohibitive approach of the *Curtiss* case is a better and more practicable approach than the permissive and lenient tack taken by the Japanese Supreme court.")

⁴⁹³ On the issue of parallel imports, there are more perspective of developing countries, such as South Africa, India and Brazil, which will be discussed in Chapter Three in the context of Current Debate on Patent.

A. Thailand

1. Introduction

Currently, Thailand has integrated the exhaustion doctrine in both patent and trademark law but with different approaches. Patent legislation makes the idea of exhaustion doctrine more obvious in content of patent law. In case of trademark, although the exhaustion doctrine has not been codified in Thai trademark law, there is a special court recognizing exhaustion doctrine by a fairly straightforward interpretation of trademark law by the Intellectual Property and International Trade Court (hereinafter IP & IT Court).⁴⁹⁴ In case of copyright, the question of exhaustion doctrine is not clearly answered because this doctrine has been revealed neither in legislation nor in judicial decision. However, predictably the judicial decision in a copyright case should follow the trademark decision, which was decided by the IP & IT Court and so the result should be along the same track.

To deal with parallel imports issues, a discussion of the exhaustion doctrine and how the exhaustion has developed under Thai intellectual property laws is unavoidable. Hence, the following sections will explain and discuss the issues of parallel imports by

⁴⁹⁴ The Thai government voluntarily set up the Intellectual Property and International Trade Court, the only specialized court in Thailand, which has exclusive jurisdiction over both criminal and civil cases throughout the country. The establishment of the IP & IT Court is an answer to the strong enforcement of intellectual property rights under TRIPs although Article 41(5) of TRIPs does not require the signatory nation to establish a special judicial system for intellectual property. *see* Arkarawit Sumawong, *The Role of the Central Intellectual Property and International Trade Court in Thailand*, at 1 (a paper presented at the International Symposium on Intellectual Property and International Trade in the New Millennium, on Nov. 29-30, 1999, Bangkok, Thailand); and also *see* Ulrich Schatz, *Emerging Standards in Intellectual Property Rights Protection*, The Region Symposium on Intellectual Property, Economy and Social Justice, at Bangkok, Thailand, on Nov. 30, 1998, at 1-2.; By establishing this special court, the judges were insightful and improved the field of intellectual property laws both in theory and in practice. The judges should effectively create better interpretation of intellectual property laws and move Thai intellectual property laws in such a direction as to meet international standards.

separating them into three parts based on types of intellectual property laws: patent, trademark, and copyright.

2. Parallel Imports in Patent

Prior to 1999, the concept of exhaustion doctrine had never been codified or mentioned in the Thai Patent Act. Under the TRIPs Agreement, the issue on the scope of exhaustion doctrine has not been settled and leaves the decision upon each individual member country.⁴⁹⁵ Thailand as signatory of the TRIPs Agreement chose to adopt and codified an international exhaustion doctrine in the Thai patent law. This principle is quite new and this is a challenge to both judges and lawyers to interpret and implement in the context of parallel imports. The Thai Patent Act has been developed under international pressure from the U.S. and the TRIPs commitment. Thus, the first part will provide an introduction to the Thai Patent law whilst the second part will address the issue of parallel imports and the detail of the exhaustion doctrine. Finally, the last part will focus on the emergence and application of the exhaustion doctrine.

2.1 Introduction on Thai Patent Law

The first draft of Thai patent law named “Law on Patent”, written in English language, was established on July 7, 1913 and later revoked as being an obstacle to industrial development in 1965. The new Patent Act 1979 came into force on September 12, 1979 and is in effect to this day. The Patent Act 1979 was amended by the Patent Act

⁴⁹⁵ See TRIPs, *supra* note 3, art.6.

(No.2) 1992 and later by the Patent Act (No.3) 1999.⁴⁹⁶ In relation to the exclusive right, the patent owner grants the right to prevent third parties from making, using, offering for sale, selling, or importing the product without the consent of patentee.⁴⁹⁷ The patent owner has the exclusive right to mark, use, sell, offer for sale, or import the patented product. For commercial benefit, the patentee may authorize use by other persons by granting a license and receive royalties.

2.2 Emergence of Exhaustion Doctrine in Patent Law

Under the Thai Patent Act 1979 before being amended in 1992 and 1999, the patentee has the rights to produce, or sell his or her product under the Thai Patent. There were three exceptions where patent infringement was permissible: use for education, good faith use before the publication of the application, or selling or possessing for sale patented products acquired in good faith.⁴⁹⁸ As codified, the exclusive patent rights were

⁴⁹⁶ Thailand Patent Act B.E. 2522 (1979) [hereinafter Patent Act 1979] as amended by Thailand Patent Act (no.2) B.E. 2535 (1992) [hereinafter Patent Act as amended in 1992], and by Thailand Patent Act (no.3) B.E. 2542 (1999) [hereinafter Patent Act as amended in 1999]; According to in adequate intellectual property rights protection, particularly patent and copyright, in 1986 the United States requested Thai Government to amend and improve the protection of intellectual property rights. On February 27, 1992, Thailand's National Legislative Assembly approved extensive revisions of the laws governing the acquisition and enforcement of patent rights in Thailand, and amended the Patent Act (so-called the Patent Act 1992). In 1999, the reasons for amendment the Thai patent law were enumerated as (1) to provide adequate patent protection, (2) to reward innovators, (3) to offer an incentive to Thai innovators to create the new inventions, and (4) to encourage the transfer of technology. As a member of the World Trade Organization (WTO), Thailand is required to implement the TRIPs agreement. This is the main reason why Thailand amended the Thai patent law, even though some amendments are a disadvantage to Thailand. The Patent Act 1999 is complied with the TRIPs requirement.

⁴⁹⁷ Article 36 of the Patent Act 1999 provides: "the patentee shall have the exclusive rights:

- (1) in the case of product patents, the right to produce, use, sell, possess for sale, offer for sale or import into the Kingdom the patented products;
- (2) in the case of process products, the right to use the process stated in the patent, produce, use, sell, possess for sale, offer for sale or import into the Kingdom products made by the application of the patented process."

⁴⁹⁸ Article 36 of the Patent Act 1979 provides:

limited and did not satisfy international standard. The Patent Act 1979 did not address whether a patentee had the right to import the patented products. Moreover, the exceptions were quite unclear in terms of “in good faith” and differed depending upon the court interpretation. Professor Chaiyos Hemarajata commented that the term “in good faith” in Article 36 (3) has quite a broad meaning. However, he stated that in the case of parallel imports, the purchase or receipt of parallel goods by an importer without knowledge of exclusive distribution of the prohibition on importation would constitute a “good faith” exception.⁴⁹⁹ Therefore, such parallel imports do not constitute a patent infringement and the patent owner could not bar such imports.

After the amendment of Thai Patent Act 1979 in 1992, the patent act remains ambiguous on the issue of parallel imports. The Patent Act as amended in 1992 stated that the patentee has the exclusive right to produce, use, sell, possess for sale, offer for sale or import the patented product.⁵⁰⁰ But this patent act still provides that any act connected with products acquired in good faith is exempt from an assertion of infringement by the patent holder.⁵⁰¹

“Subject to Section 77, no other person except the patentee shall have the right to produce the produce the product or apply the patented process, sell or have in the possession for sale the patented product or the product produced by the application of the patented process.

The Provisions of the first paragraph shall not apply to:

1. the use of the patented product or application of the patented process for purposes of study, research, experimentation or analysis.
2. the manufacture of the patented product or application of the patented process, provided that the manufacturer or the user, in good faith, has manufactured or made serious preparations with a view to such manufacture before the publication of the application.
3. the sale or possessing for sale of the product which the seller or possessor has acquired *in good faith*.” (emphasis added by the author)

⁴⁹⁹ See CHAIYOS HEMARAJATA, CHARACTERISTIC OF INTELLECTUAL PROPERTY LAW 175-176 (B.E. 2539).

⁵⁰⁰ Article 36(1) of the Patent Act 1992.

⁵⁰¹ Article 36(3) of the Patent Act 1992.

Nevertheless, the Patent Act as amended in 1999 grants importation rights to the patent owner under Article 36 and manifestly permits parallel imports if such imported goods are made or sold with the patentee's permission under Article 36 (7).⁵⁰² It is clear that the patentee cannot bar the importation of products made or sold with the patentee's consent. In the case of drugs, the Patent Act as amended in 1999 prohibits the importation of generic copies of patented drugs made without the patentee's consent.⁵⁰³ It clearly prohibits the importation of generic copies of patented drugs made without authorization, but the importation of patented drugs made with authorization is legal under Article 36(7). Thus, parallel imports are permitted under Thai patent law.

However, it is unclear whether such consent of the patentee should be given only to goods produced or sold in Thailand or extended to other countries. The answer to this question will significantly determine whether Thai patent law adopts a national/ territorial exhaustion doctrine or an international/universal exhaustion doctrine. Most legal scholars mention that the applicable scope of the exhaustion doctrine should be the international exhaustion doctrine as interpreting the text of Article 36(7).⁵⁰⁴ The consumer will receive

⁵⁰² Article 36 of the Patent Act 1999 provides:

“ The patentee shall have the following exclusive rights:

- (1) In case of product patent, the rights to produce, use, sale, possession for sale, offer for sale or import of patented products
- (2) In case of process patent, the rights to use such process patent, sale, possession for sale, offer for sale, or import of products produced by the application of the patented process

The provisions of the first paragraph shall not apply to:

....(7) the use, sale, possession for sale, offer for sale or import of patented products if the patentee *permits or gives consent to the manufacture or sale of the aforesaid products.*”
(emphasis added)

⁵⁰³ Article 36(7) of the Patent Act 1999

⁵⁰⁴ See YANYONK PAUNRATH, PATENT LAW, 91 (BE 2543); WAT THINGSAMIT, PATENT: PROVISION WITH COMMENT AND SUPREME COURT'S DECISION, 37-38 (BE 2542); Jagkrit Kuanpot, Comment on The Supreme Court decision No. 2817/ 2543, Document on Seminar: Parallel imports: Exhaustion of Rights (Faculty of Law, Thammasat University, 5 February, 2542); and also see Kitisak Prokati, Concept in the exhaustion of intellectual property right principle: Lesson from Germany and Europe Union, The

a greater benefit from liberal trade and competition in the free market under the international exhaustion doctrine. Thai consumers could purchase gray market goods at lower prices, and exclusive distributors could not derive large revenues from their monopoly power in the Thai market. Most developing countries apply the international exhaustion doctrine to promote their own interests and benefit their local consumers by allowing parallel imports.

3.Parallel Imports in Trademark

The first part will provide the background of Thai trademark law in order to have better understanding of trademark protection in Thailand. Following on from that the issues of parallel imports and the application of exhaustion doctrine as it relates to trademark will be discussed.

3.1 Introduction on Thai Trademark Law

The main legislation to protect trademark is the Trademark Act B.E. 2534 (A.D. 1991),⁵⁰⁵ amended by the Trademark Act (No. 2) B.E. 2543 (A.D. 2000).⁵⁰⁶ The main purpose of a trademark is to function as identification of goods and service, which enables the public or consumers to distinguish goods under the trademark from other

Intellectual Property and International Trade Law Form: Third Anniversary, Special Issue 2000 2543 at 113-4 and 129.; and Interviewed Judge Vichai Ariyanuntaka and Judge Jagkrit Jenjesada on August 14, 2001.

⁵⁰⁵ The Thai Trademark Act B.E. 2534 (A.D.1991)[hereinafter the Thai Trademark Act 1991] repealed the Trademark Act B.E. 1474 (A.D.1981) and the Trademark Act No.3 B.E.2504 (A.D.1961)

⁵⁰⁶ The Thai Trademark Act (No. 2) B.E. 2543 (A.D.2000) [hereinafter the Trademark Act (No. 2) 2000] was published in the Royal Thai Government Gazette on April 1, 2000 and effected on June 30, 2000.

goods.⁵⁰⁷ Under the principle of territory, a trademark has to be registered in Thailand before being protected under Thai trademark law.⁵⁰⁸ The registration of a mark is valid for a ten-year period from the date of filing the application and can be renewed thereafter. Under the Trademark Act 1991, after registration, the trademark owner has the exclusive right to 'use' his trademark for his products and trade, while also having the right to take action against an infringer and receive effective remedies.⁵⁰⁹

To answer the question what the exclusive right to 'use' means or what the scope of this use right consists of is a significant task for judges. The court has to interpret the law and consider whether such actions infringe the trademark right or not. After examining and summarizing the trademark law, criminal law and court interpretations, it finally concludes that whoever deceptively uses, forges, or imitates registered trademark or imports goods bearing forged or imitated trademarks, is considered an infringer.⁵¹⁰ However, in the case of parallel imports whether the parallel imports as importation of genuine goods infringe the exclusive right of trademark owner will be carefully analyzed in the next section.

⁵⁰⁷ Article 7 of the Thai Trademark Act 1991 provides that trademarks which are distinctive features are trademarks which have feature cause the public or persons using the goods to know and to understand that the goods using the trademark are different from other goods.

⁵⁰⁸ See Article 28 of Thai Trademark Act 1991.

⁵⁰⁹ Although Thai trademark law provides adequate trademark protection, counterfeit goods are still widespread. This situation has attracted serious notice from the international business community. Counterfeit goods are exported out of Thailand daily and imported into Europe, Africa, and the Middle East. In those countries, importers sell the fakes as genuine items. This misrepresentation of the origin of goods destroys the manufacturer's and trademark owner's reputation because most counterfeits are usually of inferior quality. See *IP Violation Battle Still Far From Won*, The Sunday Nation Newspaper, July 23, 2000, at B7.

⁵¹⁰ Article 44 of Thai Trademark Act 1991 provides: "Under section 27 and section 28, after trademark was registered. The person who owned such registered trademark has the exclusive right to use such trademark for listed products."; and also see Article 272, 273, 274 and 275 of The Thai Criminal Code (amended 1979).

3.2 Emergence of Exhaustion Doctrine in Trademark Law

The principle of the exhaustion of IPRs has never been codified in the Thai Trademark Act. In the initial decisions, the Supreme Court always made a decision based upon the exclusive right of the trademark owner to prohibit parallel imports. Later, the Supreme Court in *WAHL* case did not follow previous Supreme Court decisions and instead applied the exhaustion doctrine to allow parallel imports

Section 44 of the Trademark Act 1991 provides that the trademark owner who has registered his trademark in Thailand has the exclusive right to ‘use’ such trademark for the products that it has been registered. However, there is no clear definition of the word ‘use’ in the Trademark Act. Consequently, judges have a major duty to interpret whether a defendant’s actions are considered a use of the plaintiff’s trademark that constitutes a trademark infringement.

In 1965, the Supreme Court released a significant decision interpreting the scope of exclusive rights of a trademark owner.⁵¹¹ The Supreme Court decided that a trademark owner, who had registered his trademark in Thailand, had the right to import goods embodying the trademark into Thailand. Therefore, the importation of genuine goods into Thailand without authorization of the trademark owner violated the trademark owner’s right. Only the trademark owner or the proprietor of the register trademark is able to sue for trademark infringement. Thus, the assignee of the trademark who exclusively distributes trademarked products in Thailand has the exclusive right to use such a trademark on the registered products and file a lawsuit to bar parallel imports. But

a contracting distributor or exclusive distributor has no rights to sue for trademark infringement unless he possesses a letter of power from the trademark owner permitting a lawsuit to be filed.⁵¹²

Unexpectedly in 1999 (B.E. 2542), the Intellectual Property and International Trade Court,⁵¹³ a new special court, changed track and did not follow previous Supreme Court decisions on parallel import cases.⁵¹⁴ Recognized as a landmark case, the Intellectual Property and International Trade Court Case No. IP 16/2542 ruled on a case involving parallel imports of trademarked goods and overruled the previous Supreme Court decisions. There were two plaintiffs in this case. The first plaintiff was Wahl Clipper Corporation Co. Ltd., an Illinois registered company that owned the trademark of “WAHL.” The trademark was duly registered in the United States and other countries including Thailand. The second plaintiff was Sakunthai Co. Ltd., as the agent of Wahl Clipper Corporation Co. Ltd., and the exclusive distributor of the WAHL hair clipper in Thailand. The defendant was P.C. L. Co., Ltd., a registered company in Thailand.

From the facts, the defendant imported hair clippers bearing the “WAHL” trademark from Singapore into Thailand. The plaintiffs, as the owner of the registered WAHL trademark in Thailand, claimed that the defendant had infringed their trademark rights by importing hair clippers under the WAHL trademark into Thailand for sale without the plaintiff’s consent. In addition, the defendant packaged WAHL hair clippers

⁵¹¹ The Supreme Court Decision No. 1271-1273/ 2508

⁵¹² The Supreme Court Decision No. 1271-1273/2508, No. 2031-2032/2516 and No. 1669/2523

⁵¹³ The IP & IT Court just was established on December 1, 1997 (B.E. 2540) and had a jurisdiction over the cases involving intellectual property law and international trade. The IP & IT court decision can be appealed directly to the Supreme Court. The judges in the IP & IT Court are more expertise in intellectual property than those in the regular Civil or Criminal Courts.

in packaging bearing the plaintiff's trademark and provided a guarantee with the defendant's address for service as well. The defendant argued that it did not know that such a trademark was registered in Thailand and belonged to Wahl Clipper Corporation Co. Ltd., and Sakunthai Co. Ltd. was the agent and exclusive distributor of the WAHL hair clipper in Thailand. Conclusively, the Court determined this case and separated into two issues: (1) whether the defendant's importation infringed the plaintiff's exclusive rights, and (2) whether the creation by the defendant of additional packaging and a guarantee bearing the plaintiff's trademark, was an intentional act of infringement.⁵¹⁵

In relation to the first issue, the IP & IT Court had to decide whether both plaintiffs had a right to take legal action in this case. The Court decided that both plaintiffs had such right under the trademark law as the trademark owner and as the authorized agent, respectively. Based on the facts, the imported hair clippers in question were the genuine product sold by Wahl Clipper Corporation to its customer in Singapore. Although this parallel import was against the two plaintiffs, the Court decided that such importation of a genuine product did not infringe the plaintiffs' trademark rights. Since there was no law providing that parallel imports constitute a trademark infringement, the defendant was neither prohibited from importing such goods, nor required to obtain consent or authorization from the trademark owner. In addition, the Court reasoned that the exclusive right is exhausted when the original trademark owner sells the product. After legally selling a product, the trademark owner shall not be entitled to enforce his

⁵¹⁴ As known the Thailand's legal system is a civil law, thus the lower courts or subsequent courts are not bound to follow previous Supreme Court decisions. It is legally that the Supreme Court and the Intellectual Property and International Trade Court could subsequently overrule the previous Supreme Court decisions.

⁵¹⁵ The Intellectual Property and International Trade Court Case No. IP 16/2542, delivered on May 13, 2542, at para. 7. [hereinafter The IP & IT Case No. 16/2542]

exclusive right against the purchaser of the product. The product is free from any rights of monopoly under the exhaustion doctrine. The purchaser, therefore, has the right to do anything with the product, including the right to sell or import the product to compete with the product of the trademark owner. The Court stated that parallel import is fair because the trademark owner has already benefited from the sale of the registered product. Consequently, based upon the exhaustion doctrine, the defendant as a parallel importer was not liable to both plaintiffs.⁵¹⁶

In the second issue, the plaintiffs claimed that the defendant had created additional packaging and a guarantee bearing the plaintiff's WAHL trademark but using the defendant's address. As result of defendant's action, the public or consumers could believe that the defendant had rights to the trademark and was therefore an intentional act of infringement. The IP & IT Court held that from the facts and evidence presented, the plaintiff could not show that the defendant made such materials. Indeed, the packaging obtained by the plaintiff was obtained from another distributor and there was insufficient evidence to show that the defendant joined with a distributor in production of said materials. Based upon those facts, the defendant did not need to accept any responsibility to the plaintiff on this issue and was hence not an intentional act of infringement.⁵¹⁷

⁵¹⁶ See *id.*, at para. 6 and 7; and also see Weerawit Weeraworawit, Parallel Import in Perspective of Copyright, Trademark, and Patent, Document on Seminar on Parallel Imports and Issues of the Intellectual Property Infringement, The Intellectual Property and International Trade Court, March 2-3, 1998. (agreeing that when the trademark law does not clearly provide that the importation of legitimate trademark goods is the exclusive right of trademark owner and prohibits other from importation, the trademark owner cannot bar the parallel imports.)

⁵¹⁷ See The IP & IT Case No. 16/2542, *supra* note 516, at para.4, 5 and 7.

As the result of the IP & IT Court decision in favor of the defendant, the plaintiff appealed the case directly to the Supreme Court.⁵¹⁸ In the Supreme Court Decision No. 2817/2543, the Supreme Court affirmed the IP& IT Court decision by allowing parallel imports of WAHL hair clipper. The Supreme Court decided that the trademark owner has exclusive right to use their trademark, but once the trademark owner has sold the goods embodying such a trademark, those exclusive rights are exhausted by such a sale. The legitimate purchasers of such goods have the further right to sell or import the goods and the trademark owner has no further right to prevent or control the importation of those products. As the imported goods in the WAHL case were clearly genuine, the purchaser or the importer was not deemed to have used a counterfeit trademark. Thus, the defendant's action did not constitute a trademark infringement. In addition, the Supreme Court held that the packaging and guarantee was merely the defendant providing maintenance services that the plaintiff did not provide. Consequently, the guarantee on the packaging did not use the trademark in manner to cause public confusion over whether the defendant was the licensed user of such WAHL trademark.⁵¹⁹

The decision of the Supreme Court affirming the IP & IT Court's decision in the WAHL case is significant for all trademark owners, parallel importers, intellectual property lawyers, and legal scholars because this is the first time that the Supreme Court decided on a trademark case by applying an exhaustion doctrine. The Supreme Court decision obviously applied an international exhaustion doctrine because the WAHL hair clippers, as parallel import goods, were first sold in Singapore and later imported into

⁵¹⁸ As the IP & IT Court has special procedures, the plaintiff or defendant can appeal the decision of the IP & IT Court directly to the Supreme Court bypassing the Court of Appeal.

⁵¹⁹ The Supreme Court Decision No. 2817/2543.

Thailand. As is known Thailand is a civil law country but the exhaustion doctrine has never been codified in the Thai trademark law. Therefore, an important question is how the Supreme Court and the IP & IT Court can apply the exhaustion doctrine in the WAHL case and what law or regulation allows or authorizes the court to use such a doctrine. Although the IP & IT Court did not clarify an exhaustion doctrine or what the status of the exhaustion doctrine is, it is possible that the Court applied the exhaustion doctrine as the general principle of law under Article 4.⁵²⁰ Some lawyers commented that the exhaustion doctrine is neither the local custom nor the general principle of law and that the duty of the court is to find the law, not create the law. However, some judges suggested that the Supreme Court used the exhaustion doctrine to decide this case because it is the best means of striking a balance between the interests of the trademark owner and the interests of the public in parallel import cases. Under such a way of thinking, the court can freely assert any proper reasons to support its decision, including an exhaustion doctrine.⁵²¹

Later, the IP & IT Court decided to not issue an interim or preventive injunction in case NO. Kor Kor 2/ 2542 by following the Supreme Court's decision based upon the principle of exhaustion of rights. The defendant imported and distributed the De Dong A

⁵²⁰ See Suthiphon Thaveechaiyakarn, Remarks on the Intellectual Property and International Trade Court's Decision Case. No. IP 16/2542. *The Intellectual Property and International Trade Law Form: Second Anniversary, Special Issue 1999*, at. 426.

Article 4 of the Civil and Commercial Code states:

"The law must be applied in all cases which come within the letter or the spirit of any of its provisions.

Where no provision is applicable, the case shall be decided in accordance with the local custom. If there is no such custom, the case shall be decided by analogy to the provision most nearly applicable, and in default of such provision, by the general principle of law."

⁵²¹ Interviewed judges in the Intellectual Property and International Trade Court: Judge Vichai Ariyanuntaka and Judge Jagkrit Jenjesada on August 14, 2001.

Libo Korean newspapers in Thailand without either of the plaintiffs' consent. Consequently, the plaintiffs claimed that the defendant was liable for trademark infringement by importing and distributing newspapers in Thailand without consent and by knowingly selling the papers in competition with the plaintiffs without proper authorization. The plaintiffs claimed damages from the defendant's action and requested the IP & IT Court to issue an injunction to stop the unauthorized importation and distribution. By following the Supreme Court decision, the Court refused the plaintiff's request for an injunction because the imported goods were not counterfeit products. The Court decided that the defendant was not guilty of imitating the plaintiff's trademark under section 110(1) and 108. Trademark Act 2534 does not prohibit parallel imports and no provision bars importation of genuine goods without the trademark owner's authorization. Due to the lack of a clear provision barring parallel imports, the Court reasoned that allowing parallel imports based on the exhaustion doctrine benefits consumers by encouraging competition within the market and reducing the monopoly power of the trademark owner.⁵²² Thus, it is clear that parallel imports are not prohibited under the Thai trademark law.

To summarize, before 1999, the Supreme Court decided that the importation right belonged to the trademark owner and prohibited parallel imports. Importing goods into

⁵²² See The Intellectual Property and International Trade Court Case No. Kor Kor 2/ 2542, delivered on July 22, 2542. This case was a parallel import case involving the importation into Thailand of genuine goods produced by the trademark owner. From the facts, the complainants/plaintiffs were De Dong A Libo Co.Ltd. (Chinese language) as the first plaintiff and H Huan Trading Co. Ltd., as the second plaintiff and the defendant was Zojin Co. Ltd. The first plaintiff was the owner and producer of a daily newspaper under a registered trademark De Dong A Libo sold and distributed newspaper in Korea and other foreign countries including Thailand. For the right to distribution in Thailand, the first plaintiff has licensed the second plaintiff the exclusive rights to distribute and use the "De Dong A Libo" trademark for newspaper products. The second plaintiff legally registered the Chinese language trademark for newspaper products in Thailand.

Thailand without authorization from the trademark owner was an infringement of the trademark owner's exclusive rights. However, in 1999, the IP & IT Court did not follow the previous Supreme Court decisions and ruled that parallel imports were not prohibited under Thai trademark law by applying the exhaustion doctrine. The IP & IT Court and the Supreme Court consequently overruled the previous Supreme Court decisions that prohibited parallel imports.

In my view, the IP & IT Court's decision is suitable and reasonable by ruling that parallel imports do not infringe the right of the trademark owner. The trademark law has not clearly addressed whether the parallel imports infringe trademark rights. If this conduct is not obviously prohibited, it should be allowed for the following reasons. Firstly, in the absence of an obviously prohibited parallel import provision in trademark law, the parallel import conduct should be permitted because if the Thai trademark law intentionally prohibits parallel imports, it should be clearly stated in the law. Secondly, recognized as the rule of law in interpretation, the interpretation of law involving criminal penalty has to be strictly interpreted if the law does not clearly prohibit such action. The court cannot interpret and decide the case in a way that constitutes adverse effects to the defendant. Thai trademark law provides both civil remedies and criminal penalties for punishing infringers;⁵²³ thus, the court has to strictly construe the law in the case of parallel imports. Indeed, the Court was able to decide this case only by asserting the content of trademark law and the court's interpretation without being concerned with how the Court applied the exhaustion doctrine in this case either under Article 4 of the Civil and Commercial Code or as a reason that the exhaustion doctrine is appropriate dogma

for applying in parallel import cases. The Court rationally asserted that the international exhaustion doctrine was another reason to support the Court's decision to limit the exclusive right of the trademark owner and to permit parallel imports. Under the international exhaustion doctrine, the right of the trademark owner to control trademarked products was exhausted after the initial sale and receiving their benefit from the first sale of such products without regarding to whether the first sale took place in domestic or international territory. After the first sale, the trademark owners can no longer bar the parallel importation of those products.

Moreover, the result of IP& IT Court's decision is consistent with the free trade and free movement of goods principle. Recognized as one significant reason behind the Court's decision aside from the consumer's benefit consideration, the philosophical ideas of free trade and free movement of goods have become more influenced by the court's decision. These notions caused the court to consider in the economic aspect of trademark in international trade. Furthermore, the judges in IP&IT Court as a special court have more expertise and experience in intellectual property laws than judges in regular court and certainly the IP&IT Court had good reason in support of its decision by not following the previous Supreme Court's decisions.

Although the exhaustion doctrine is not codified in the Thai Trademark Act, the judges applied the exhaustion doctrine to allow parallel imports and to limit the exclusive right of the trademark owner. It is logical to apply the exhaustion doctrine in trademark cases because there is an example of exhaustion doctrine that was codified in patent law to support the IP&IT Court's decision by asserting exhaustion doctrine and allowing

⁵²³ Article 108, 109 and 110 of Thai Trademark Act.

parallel imports of trademark goods. Without question, the courts applied the international exhaustion doctrine to encourage the free trade and free movement of goods, which is consistent with WTO's purpose and promotes competition in the domestic market by allowing parallel imports. In addition, Thai consumers would benefit from lower prices and greater availability of products.

4.Parallel Imports in Copyright

To better understand the copyright system in Thailand, the first section will describe the background to Thai copyright law. The second section will focus on whether parallel imports are allowed or prohibited under Thai copyright law and whether the court applies the exhaustion doctrine when dealing with copyrights.

4.1 Introduction on Thai Copyright Law

Thailand is a member of the Berlin Act of the Berne Convention held in July 1931. Thailand had the first copyright law that was consistent with international standards, namely the Act for the Protection of Literary and Artistic Works B.E. 2474. However, this act was amended by the revision of the Copyright Act of 1978 and later was replaced by the Copyright Act B.E. 2537 (1994). Thus, the current copyright law is the Copyright Act B.E. 2537 (1994).⁵²⁴ Thailand as a signatory to the Berne

⁵²⁴ The Copyright Act B.E. 2537(A.D.1994) was approved by the parliament on December 9, 1994 and effected from March 21, 1995. [hereinafter the Copyright Act 1994] Thai government has enacted the Copyright Act B.E. 2537 (1994) by substituting the Copyright Act B.E. 2521 (1978); and also *see* Weerawit Weeraworawit, Copyright in Thailand, the First Anniversary: The Intellectual Property and International Trade Law Forum: Special Issue 1998, at.47.

Convention⁵²⁵ is obligated to provide copyright protection to works of other contracting states of the Berne Convention. The Copyright Act 1994 provides a list of works to be protected as copyright works (literary, dramatic, artistic, musical, audiovisual, cinematographic, sound recording, sound and video broadcasting work or any other work in the literary, scientific or artistic domain)⁵²⁶ and computer programs or software are clearly protected under copyright as literary works.⁵²⁷ The period of copyright protection is for the life of the author plus an additional fifty years. Like the copyright law of other nations, the Thai copyright law has been codified to create a fair balance between the original creators and the entrepreneurs whose contribution is necessary for the widespread dissemination and distribution of the copyright works.⁵²⁸

Copyright piracy has become a serious issue not only for foreign companies but also for the Thai Government, which has attempted to stamp out piracy.⁵²⁹ The piracy of compact discs (CDs) in Thailand has become a serious issue because many compact disc factories have been forced out of China and Malaysia and have relocated to Thailand, where they produce compact discs for local distribution and exportation.⁵³⁰ Because Thailand is located in the center of South East Asia and has a good transportation system, pirated goods not only circulate within the country, but are illegally exported due to high

⁵²⁵ The Berlin Act of 1908, Berne Additional Protocol 1914 and the Administration Provisions of the Paris Act 1971.

⁵²⁶ See The Copyright Act 1994, *supra* note 524, art. 6.

⁵²⁷ *Id.* at art.4.

⁵²⁸ See Weeraworawit, *supra* note 524, at 51.

⁵²⁹ See Steven J. Metalitz, IPRs Enforcement and Penal Policy, The Regional Symposium on Intellectual Property, Economy and Social Justice, on December 1, 1998, Bangkok, Thailand. at.3. (mentioning that copyright piracy is a highly profitable business since the cost of pirate goods are nothing since the raw materials are cheap and no royalty cost. They are no risk on unsuccessful music, films, or computers since they steal only the 'hits'. Pirates pay no taxes, observe no censorship laws, do not need to advertise and do not care about proper labeling or maintaining ongoing customer relations.)

⁵³⁰ See IP Violation Battle Still Far From Won, The Sunday Nation Newspaper, July 23, 2000, p.B7.

price differentials with those countries.⁵³¹ Music piracy causes not only foreign entertainment companies to lose profits, but also injures Thai entertainment companies such as Grammy Co. and RS Promotions Co. as well.⁵³² To better combat CDs piracy, the Thai government issued the Control of the Manufacturing of CD Bill (hereinafter the CD Bill) as a new control mechanism.

Besides copyright piracy, the issue of parallel imports or gray market goods is also important. Many gray market goods are produced in Thailand and then exported to other countries, or produced outside Thailand and imported into Thailand. Although there has been no court decision in the area of copyright law regarding parallel imports, it is still important to study and discuss the trend of the court's decision. It is possible that one day an intellectual property owner may file a lawsuit based upon copyright law to bar parallel imports after recognizing that patent and trademark law offers no restriction on parallel imports.

4.2 Emerging of Exhaustion Doctrine in Copyright Law

Under the Thai Copyright Act of 1994, the copyright owner has both economic and moral rights. The copyright owner has five exclusive economic rights: (1) the right of reproduction and adaptation, (2) the right of communication to the public, (3) the right of rental of a computer program's audiovisual work, cinematographic work, and sound recording, (4) the right to give benefits accruing from the copyright to other persons, and

⁵³¹ *Id.* (quoting the statement of Mr. Weerawit Weeraworawit, the Assistant Director General of the Department of Intellectual Property and Associate Judge of the Central Intellectual Property and International Trade Court.)

⁵³² *Id.*

(5) the right to license.⁵³³ The copyright law does not mention the right to import. Thus, it is important to identify whether the right of communication to the public includes the importation right.

The “communication to public” means making the work available to public by means of performing, lecturing, playing music, causing the perception by sound or image, construction, distributing or by any other means.⁵³⁴ The copyright owner has the exclusive right to distribute the products embodied his copyright. From the report of the Committee on Drafting the Copyright Act, the Committee was concerned with whether distribution only means the right to distribute the first time. In the end, the Committee did not come to a final answer on this issue.⁵³⁵ However, the meaning of distribution clearly does not include importation because if the copyright law intends to grant the importation right to the copyright owner, it should be expressed in the Copyright Act 1994. Moreover, there has been no international standard on importation in regard to copyright protection. The TRIPs Agreement only grants importation rights to patent holders, subject to the exhaustion doctrine,⁵³⁶ but does not stipulate importation rights for copyright and trademark owners.

In addition, under the Thai copyright law, importation is only classified as a secondary infringement. In the Thai Copyright Act 1994, there are two categories of copyright infringement: the direct and secondary infringements. The direct infringement is the exercise of rights exclusively reserved for the copyright owners without their

⁵³³ See The Copyright Act 1994, *supra* note 524, art. 15.

⁵³⁴ *Id.* art. 4.

⁵³⁵ See The Council of State of Thailand, Conference Report of Thai Law No.3/36 dated July 15, 2536.

⁵³⁶ See TRIPs, *supra* note 3, art. 28 and the footnote to Article 28(1)(a) (stipulating that the exclusive right is subject to Article 6: exhaustion)

authorization.⁵³⁷ Secondary infringement is to import or sell the infringing copies with knowledge or a reasonable basis to know about the infringement.⁵³⁸ Thus, only importation of infringing copies causes infringement. Conversely, the importation of genuine goods does not infringe on the exclusive rights of the copyright owner.

To balance the interests of society against those of the copyright owner, exceptions for copyright infringement are permitted in certain circumstances. Those circumstances are based on the concept of fair use for educational, personal, or public interest purposes.⁵³⁹ All exceptions are subject to two broad principles, which are that there is explicitly no conflict with a normal exploitation of the work and no unreasonable prejudice to the legitimate interests of the copyright owner.⁵⁴⁰ Even if the copyright owner is granted an importation right, parallel imports shall fall within the scope of the exception for copyright infringement. Parallel imports do not conflict with a normal exploitation of the work and do not unreasonably prejudice the legitimate interests of the copyright owners because the copyright owners have already received their benefit from the first sale of the copyright goods. The importation of genuine goods does not cause any damage to the protected rights of copyright owner. In addition, parallel imports encourage free trade and free movement of goods, free competition, and benefits consumers. Furthermore, in the *De Dong A Libo Newspaper* case, as previously mentioned, although the case focused on trademark law, the newspaper was also protected under copyright law as a literary work. Consequently, if the trademark owner had brought this issue as a copyright infringement case, the outcome of the court decision

⁵³⁷ See The Copyright Act 1994, *supra* note 534, art.27-30.

⁵³⁸ *Id.* art. 31.

⁵³⁹ *Id.* art 32-42.

should be similar to the trademark case by allowing parallel imports under the international exhaustion doctrine.

In summary, the Thai Copyright Act 1994 does not grant the copyright owner the right of importation and there is no provision for the exhaustion doctrine under Thai copyright law. Until now, there has been no court decision on the issue of parallel imports and exhaustion doctrine under copyright law. However, it is possible that the court could apply the international exhaustion doctrine in the same way that was applied to trademark and patented products. The court's decisions in patent, trademark, and copyright cases should be harmonious by applying the international exhaustion doctrine in all three contexts. If the court decided a parallel import case under copyright law differently from under other intellectual property cases, intellectual property owners might avoid filing a lawsuit under patent or trademark law but choose to take an action under copyright law instead. These inconsistent decisions would cause adverse effects not only on parallel importers but also on consumers.

5. Conclusion

In Thailand, the Patent Act 1999 grants importation rights to the patent owner under Article 36 but manifestly permits parallel importation if such imported goods are made or sold with the patentee's permission under Article 36 (7). Article 36(7) clearly codifies the concept of international exhaustion doctrine into the copyright law. It is clear that the patentee cannot bar the importation of products made or sold with the patentee's consent. In the case of trademark, although the exhaustion doctrine is not

⁵⁴⁰ *Id.* art. 32. The text of Article 32 imitates the wording of Article 13 of TRIPs Agreement.

codified in the Thai Trademark Act, the court applied the international exhaustion doctrine to allow parallel imports and to limit the exclusive right of the trademark owner. It is logical to apply the exhaustion doctrine in trademark cases in the same way as patent law does. In the case of copyright, the Copyright Act neither grants importation right to copyright owner nor codifies the exhaustion doctrine. However, potentially the Thai court may apply the international exhaustion doctrine in the same way that it does in trademark and patent cases. The court's decisions in patent, trademark, and copyright cases should be harmonious by applying the international exhaustion doctrine in all three contexts. Allowing parallel imports should finally provide benefit to Thai consumers and encourage free trade and the free movement of goods, which is consistent with the purpose of WTO.

B. Hong Kong

1. Introduction

There are four main reasons that make Hong Kong interesting on the topic of parallel imports and there are worth discussing in this thesis. First, Hong Kong is a relatively small place but plays a significant role in the global arena. Hong Kong plays a significant role in international trade being the world's busiest container port and may be influential on other countries, which means the approach to parallel imports taking place in Hong Kong may influence the approach of China itself and indeed other countries.⁵⁴¹

⁵⁴¹ There are many secondary documents supporting the idea that Hong Kong has many significant influences on China, particularly in terms of economic, political and education. See Lau Nai Neung, Hong Kong's Role within China, HKDF Newsletter Issue 19 January 2002, available at http://www.hkdf.org/newsletters/0201/0201_3.htm (visited Aug. 1, 2003) (explaining that Hong Kong had

As a result of being a colony of the United Kingdom for over 150 years, the legal system and intellectual property laws are well established in Hong Kong. Although there were some changes to the legal system as a result of the handover to China in 1997,⁵⁴² Hong Kong still has a sophisticated well-developed intellectual property law. In order to maintain the reputation of having a strong IPRs protection system, Hong Kong has not only enacted many intellectual property laws but also adjusted the structure of administrative bodies for better enforcement. Thus it is possible that Hong Kong law may have an influence on other countries, which may choose to follow Hong Kong's approach.

a special role in shaping China in areas of social and legal culture and education. Many officials came from the Mainland to Hong Kong to study and many businessmen were invited to participate in a major project.); see The University of Hong Kong, Study Guide on Hong Kong Government and Politics, Part 1.3 Hong Kong's Influence on China, available at http://www.hku.hk/hkcsp/ccex/text/studyguide/hkpolitics/1_3.html (visited Aug. 1, 2003) (mentioning to Andrew Scobell's article, which points out that Hong Kong has significant influences on China.); Adrian Lai, One Country, Two Systems: A Brief Comparison of the Economic Systems of Hong Kong and China, Apr. 2002, available at http://econc10.bu.edu/economic_systems/Country_comparisons/Hong_Kong_China.htm (visited Aug. 1, 2003); and also see David L. Grossman, Scenarios for Hong Kong's Future, available at <http://www.askasia.org/frclasrm/lessplan/1000078.htm> (visited Aug. 1, 2003); Hong Kong developed as a center of labor-intensive manufacturing and became the world's largest producer. see Liu Pak Wai, Chapter 4 The Asian Financial Crisis and the Hong Kong Economy, in HONG KONG IN CHINA: THE CHALLENGES OF TRANSITION, at 99 (Wang Gungwu & John Wong ed. 1999); and also see Yun-wing Sung, The Hong Kong Economy-To the 1997 Barrier and Beyond, in THE CHINESE AND THEIR FUTURE: BEIJING, TAIPEI, AND HONG KONG 331-33 (Zhiling Lin & Thomas W. Robinson eds. 1994) (explaining that since Hong Kong's market is open, free and flexible, Hong Kong has played the role of middleman both in commodity trade and in services trade, particularly financial services. Hong Kong is an extremely open economy and a major international financial center. Because of the launch of the open-door policy, China has established numerous direct links with the rest of the world. The middleman role of Hong Kong is becoming more outstanding, and a rising share of China's commodity trade.)

⁵⁴² On July 1, 1997, the great historical event of the transfer of Hong Kong's sovereign from Britain to the People's Republic of China ("P.R.C.") occurred and started the actual action under the "one country, two systems" policy. See J.F. Mathew, Essay, *The Legal System of the Hong Kong: Special Administrative Region*, 18 U. PA. J. INT'L ECO. L. 3 (1997); see Kuan Hsin-chi, Chapter 2 Is the "One Country, Two Systems" Formula Working? in HONG KONG IN CHINA: THE CHALLENGES OF TRANSITION 24 (Wang Gungwu & John Wong ed. 1999); and also see ENBAO WANG, HONG KONG, 1997: THE POLITICS OF TRANSITION 42 (1995). (explaining on the original of the concept of One Country, Two Systems and mentioning that Deng Xiaoping and his followers gradually developed the concept of one country, two systems for the reunification of Taiwan, Hong Kong, and Macao with the Chinese mainland.)

Second, Hong Kong is a jurisdiction where the parallel import issues are quite political and controversial. Its decision to impose a strict prohibition on parallel imports in copyright law has turned out to be visibly unpopular decision. Outsiders may not noticeably perceive the last issue about parallel imports in Hong Kong. Parallel imports intensively take place in Hong Kong and the issue of parallel import and statute on parallel imports are influx and controversial. Third, Hong Kong is a place that has a famous tradition of commitment to free trade and the free market by having few regulations governing economic activity. Certainly, Hong Kong is a shining example of free trade which other countries would like to follow. Therefore, the restriction of parallel imports by imposing both civil and criminal penalties is not inline with Hong Kong's free trade policy and damages its reputation for free trade.

Finally, Hong Kong's approach is interesting because how Hong Kong handles parallel imports might be what China will do in the future. China may in some way follow Hong Kong's example. The restriction on parallel imports approach by Hong Kong could have an effect in China.⁵⁴³ With the highest population in the world, China

⁵⁴³ There is a mutual link between Hong Kong and China as a result of handover. The future economic fortunes of Hong Kong will be increasingly dictated by the China's factors. Most of western developing countries are more interested in the future and role of China in the global free trade and perceive that Hong Kong might be used as the appropriate link and good mechanism for China to step forward to be the significant leader of all Asian developing nations in term of global trade. The integration between Hong Kong and China considerably benefits to both regimes in production and trade since China can be the center of production and simultaneously Hong Kong can be the hub of trade and transportation. In other words, Hong Kong's continued usefulness to China as valuable service center (similar to New York City served as financial center of the U.S.) meaning that the Hong Kong economy should continue to cater to China's needs and exploit China's potential. For instance, according to the low labor and land costs in South China, Hong Kong manufacturers took such advantage by shifting their 'labor-intensive low value-added production operations' to China. Products made in China are generally re-exported through Hong Kong that makes the Hong Kong's export trade growth rapidly and Hong Kong also providing the well services such as transportation, storage, insurance, and trade finance to support those activities. *see* Wai, *supra* note 538, at 76-77; and also *see* Analysis of Hong Kong's Retained Imports, 1989-1994, Hong Kong Monthly Digest of Statistics, February 1996.

has vast consumer market.⁵⁴⁴ If China adopts the same approach as Hong Kong by restricting parallel imports, consumers in China could possibly be faced with the issue of high prices and less availability of products. If this were occur it would unavoidably reduce the international trade volumes and diverge from the concept of free trade.

The next section will clarify the background of IPRs protection in Hong Kong both prior to the handover, during handover and after. Then the following section will begin the specific discussion concerning parallel imports in Hong Kong. The discussions on parallel imports are separated into three topics depending upon the types of IPRs protection: copyright, trademark, and patent. Finally, the last section will summarize the overall discussion and clarify Hong Kong's position and perspective on parallel imports.

2. Intellectual Property Protection in Hong Kong

2.1 Pre-Handover 1997

Prior to the transfer of Hong Kong's sovereignty to China in 1997, Hong Kong had the reputation of having a strong intellectual property law, which was the result of being a British colony. The intellectual property laws of Hong Kong relied on the U.K. law. Although having a strong protection of IPRs system, Hong Kong was placed on the Watch List of the United State Trade Representative in 1996 because of the increasing

⁵⁴⁴See Countries with The Largest Population, available at <http://geography.about.com/library/weekly/aa051198.htm>. (visited Dec. 12, 2002) (reporting that China has the highest rate of population and follows by India and the United States.); see Science Council of British Columbia, Chinese Market, available at http://www.scbc.org/Init_Info/inin_inbude_chst_ma.html. (visited Dec. 12, 2002); and also see Edward Leman, The Biggest Market in Asia, The Asian Wall Street Journal, Monday July 3, 1995, available at http://www.Chreod.com/publications/2002011_18275419950703.pdf. (visited Dec. 12, 2002).

volume of IPRs infringements, particularly piracy, in the region.⁵⁴⁵ However, the Hong Kong Government attempted to solve those infringement problems by strengthening both the laws and enforcement of the law. So the handover of sovereignty in 1997 provided Hong Kong with a valuable opportunity to modernize, localize and strengthen its intellectual property legislation. During the handover process, many legislations and regulations were enacted and amended including those in the area of parallel imports.

2.2 Handover 1997

On July 1, 1997, Hong Kong's sovereignty was transferred from Britain back to the People's Republic of China. Under the "one country, two systems" policy,⁵⁴⁶ Hong Kong has become the Hong Kong Special Administrative Region ("S.A.R.") of China.⁵⁴⁷ Hong Kong continued governed by the previous Hong Kong laws and the legislature of the Hong Kong Special Administrative Region. This notion has been repeatedly declared in the Basic Law.⁵⁴⁸ Hong Kong also needed to have new laws and the urgency of this need was not only just formal compliance with the Basic Law but also as matter of

⁵⁴⁵ See Hong Kong Protests United States' Section 301 Decision, 10 NO. 6 J. Proprietary Rts. 21 (1998).

⁵⁴⁶ See Mathew, *supra* note 539, at 3; see Hsin-chi, *supra* note 539, at 24; and also see WANG, *supra* note 539, at 42.

⁵⁴⁷ The transfer of sovereignty, the future administration of Hong Kong, and the conservation of Hong Kong's economic, political, and legal system, are governed by the Sino-British Joint Declaration signed in December 1984. see Sino-British Joint Declaration on the Question of Hong Kong, 19 December 1984, U.K.T.S. 1984 No. 26, 23 I.L.M. 1366, reprinted in YASH GHAI, HONG KONG'S NEW CONSTITUTIONAL ORDER: THE RESUMPTION OF CHINESE SOVEREIGNTY AND THE BASIC LAW Appendix Four 510 (2nd 1999).

⁵⁴⁸ The Basic Law was enacted by the National People's Congress of the People Republic's China as the constitutional framework for Hong Kong as from July 1, 1997. See Basic Law of the Hong Kong Special Administrative Region of the People's Republic of China, 3d Sess., 7th National People's Congress (N.P.C.), 4 April 1990, 29 I.L.M. 1519, available at <http://www.info.gov.hk/bas-law/fulltext/index.htm> (visited on 04/03/02) [hereinafter Basic Law]; see P. Wesley-Smith, The Legal System and Constitutional Issues, in THE BASIC LAW AND HONG KONG'S FUTURE, at 172 (P. Wesley-Smith & A.H.Y. Chan eds., 1988) (explaining and analyzing the basic law); and also see GHAI, *supra* note 544, at 139.

economic necessity or economic importance, which Hong Kong needed to maintain the legal ability to attract investment.

As the result of the Basic Law and the 'one country, two systems' policy, it is stated that Hong Kong common law and legal precedent prior to the handover shall be maintained, but not including the laws specifically derived from other U.K. laws and bilateral agreements.⁵⁴⁹ Because of the discontinuation of these law applicable to the UK., Hong Kong had to enact many laws to incorporate those legal principles into Hong Kong law.⁵⁵⁰ Specifically in the area of intellectual property, in order to sustain the strong system of IPRs protection, the Basic Law provides and ensures the future perception of Hong Kong on the IPRs protection.⁵⁵¹ It provides a good opportunity for Hong Kong to create a strong set of intellectual property laws and to adjust the structure of administrative bodies for better enforcement. However, the new Hong Kong legislation clearly follows the laws of U.K. in many aspects. For instance, regarding parallel imports, before 1997 Hong Kong had applied the doctrine of secondary infringement based on "hypothetical manufacture," which derives from U.K. law. This concept still remains in Hong Kong law after the handover 1997. In short, the source of law is different but the substance seems to be the same.

⁵⁴⁹ See *id.* art. 8. Article 8 of the Basic Law provides "The laws previously in force in Hong Kong, that is, the common law, rules of equity, ordinances, subordinate legislation and customary law shall be maintained, except for any that contravene this law, and subject to any amendment by the legislature of the Hong Kong Special Administrative Region."; see Paul Tackberry, Article, *Intellectual Property Laws in the Hong Kong S.A.R.: Localization and Internationalization*, 42 MCGILL L.J., 579, 583-84 (1997).; and also see Mathews, *supra* note 539, at 9-10.

⁵⁵⁰ For example, as the result of handover Hong Kong enacted many intellectual property laws such as the Copyright Ordinance (Cap 528), the Patent Ordinance (Cap 514), and the Trademark Ordinance (Cap 559).

⁵⁵¹ The Basic Law provides the basic principle and purpose of intellectual property rights protection in Hong Kong in Article 118, 139 and 140. see Basic Law, *supra* note, art.118, 139 and 140.

2.3 Post-Handover 1997

After the handover in 1997, some indications suggest that the IPRs enforcement in Hong Kong has improved since 1997. The Hong Kong S.A.R. was removed from the Special 301 Watch List as stated in an announcement of the United States Trade Representative made on February 20, 1999.⁵⁵² Thus Hong Kong will not be subject to trade sanctions and will no longer be monitored by the Trade Representative. Nowadays, the international appraisal of Hong Kong as a favorable place to invest relates to the strong IPRs protection and to its affluence and level of economic activity.⁵⁵³

Nevertheless, these laws sometimes disregard the terms of enforcement and it remains true that after 1997 Hong Kong might have new legislations but they are not fully enforced. So Hong Kong is still faced with the issue of IPRs protection. As is well known, there are plentiful IPRs infringement activities taking place in China that are clearly sufficient to get attention from many developed nations but mainly the U.S.⁵⁵⁴ Hong Kong is used as a transportation hub not only for counterfeit products but also for genuine goods. The genuine goods are legally produced either in China or in Hong Kong

⁵⁵² See Matthew K. Miller, *Legal Update: Hong Kong Removed from U.S. Trade Representative's Special 301 Watch List*, 5 B.U. J. SCI. & TECH. L. 12 (1999).

⁵⁵³ See Anna M. Han, article, *Hong Kong's Economy Under Chinese Rule: Prosperity and Stability?*, 22 S. Ill. U. L. J. 325, 326(1998).

⁵⁵⁴ China is one of the developing countries in which provide the low standard of IPRs protection and have a lot of IPRs infringement. The United States include the China in the Special 301 Priority Watch List since many U.S. businesses particularly pharmaceutical and software products lost a lot of benefits from those infringements in China. For example, the Motion Picture Industry of America (MPA), the Recording Industry of America (RIA), Business Software Alliance (BSA), and Pharmaceutical Research and Manufactures of America (PhRMA). In addition, PhRMA requested that China be included in the 2001 "Special 301" Priority Watch List. See Pharmaceutical Research and Manufactures of America (PhRMA), PhRMA "Special 301" Submission 2001, available at <http://www.phrma.org/intnatl/all.phtml?prefix=reg> (visited Dec. 2, 2001)

and then imported into other countries without authorization.⁵⁵⁵ Hong Kong thus may be recognized as the source of piracy and parallel import goods.

In relation to parallel imports, parallel imports have become a significant and controversial issue in Hong Kong both during drafting of the new set of intellectual property laws and after the date that the new laws were enforced. There is disagreement between consumer groups and IPRs owners. The consumer groups want the laws to allow parallel imports but simultaneously the IPRs owners want laws that strictly prohibit parallel imports with high civil and criminal penalties. The next section will focus on the issue of parallel imports whether under the current intellectual property laws prohibiting or allowing parallel imports under Hong Kong law. A discussion on the future trend of Hong Kong to parallel import issue will also be included.

⁵⁵⁵ In addition, it is possible that the goods licensing for sale in China find their way through Hong Kong into various other markets that make the law of parallel imports in Hong Kong becoming a special interesting topic. However, Hong Kong prohibits parallel import from other countries into Hong Kong but not prohibit the exportation of parallel import goods into other countries. If the IPRs owner attempts to stop the shipment of those goods in Hong Kong, the question is what legal basic that the owner use to bring a claim on such action in Hong Kong since the wrongful importation into Hong Kong may be brought the case in Hong Kong but not included the wrongful exportation from Hong Kong to other countries. The legal claim on parallel imports depends on the law of imported country but not the law of exported country and the case can be brought to the court in imported country (the destination country for such importation).; see LOVELL WHITE DURRANT, *IP PROTECTION IN CHINA AND HONG KONG* 33-34 (1998) (suggesting that "as it may not be possible to stop the actual production of infringing goods without taking action in China, the goal of taking action in Hong Kong must be to make it economically unviable to use Hong Kong as a transit point for fake products." In order to fight with counterfeit goods, taking the legal action in Hong Kong might be the best solution to fight with infringement activities since Hong Kong provides not only the good set of intellectual property laws but also the sufficient enforcement mechanism.); In my view according to English endorsing as one of official language in Hong Kong that make it easy for English-speaking countries to bring the infringement cases to Hong Kong's court more than China's court that can avoid the communication problem in Chinese language.)

3. *Parallel Imports in Hong Kong*

3.1. Under Copyright Ordinance

3.1.1 Background

Before 1997, Hong Kong did not have its own copyright law, but was governed by the United Kingdom Copyright Act 1956 (as amended) under the Hong Kong Copyright Ordinance (Cap. 39) Laws.⁵⁵⁶ The right of the copyright owner to control importations reveals part of a secondary infringement under the U.K. law,⁵⁵⁷ which differ from the U.S. law that clearly provides the importation right to the copyright owner.⁵⁵⁸ Under the U.K. copyright law, parallel imports are prohibited because the parallel

⁵⁵⁶However, later The Copyright Ordinance (Cap 39) was replaced by The Copyright Ordinance (Cap 528) as the result of the handover in 1997.; The amendment of the Copyright Act 1956 was extended to Hong Kong by the Copyright (Hong Kong) Orders of 1972 and 1979. *see* Donna Nicholls, Robin Bridge & John Liu, Hong Kong in INTERNATIONAL INTELLECTUAL PROPERTY LAW: GLOBAL JURISDICTIONS 65 (Dennis Campbell & Susan Cotter eds. 1996); and also *see* The Copyright, Designs and Patents Act 1988, available at http://www.hmso.gov.uk/acts/acts1988/Ukpga_19880048_en_1.htm (visited Mar. 26, 2002). [hereinafter The CDPA 1988]

⁵⁵⁷*See* ROTHNIE, *supra* note 24, at 194. (explaining that under the secondary infringement, the plaintiff has to prove that the defendant (1) has imported into the domestic jurisdiction; (2) without the license of the copyright owner in the domestic jurisdiction; (3) an article the making of which (a) infringed copyright, or (b) would have infringed copyright if it had been made in the domestic jurisdiction; (4) with knowledge that the article so infringed, or would have infringed, the copyright subsisting in the domestic jurisdiction.)

Although the parallel imports are considered as infringement action and copyright owner has right to bar such importation either in the U.K. approach or the U.S. approach, it is based on different concept or framework. Under the U.K. approach, the right to control importation is in a part of secondary infringement, which is different from a primary infringement since under secondary infringement (similar to the concept of contributory infringement in U.S. copyright law), the copyright owner has to prove the knowledge of infringer that the imported article is unlawfully produced or known as infringing. If the copyright owner cannot prove on this element, the importer will not be subject to a secondary infringement. Thus unlike the U.K. approach, the U.S. copyright law directly grants an importation right to copyright owner. So the person who imports copyright goods into the US without authorization constitutes the direct or primary copyright infringement and the copyright owner does not have to prove in such knowledge of importer in order to take legal action. Nevertheless, actually the British approach under the concept of a secondary infringement in effect functionally work out the same thing as the U.S. approach under a straightforward importation right does.

Currently, in Hong Kong parallel imports are prohibited under the Copyright Ordinance (Cap. 528) of Hong Kong and subject to a secondary infringement section 30. However, under the concept of secondary infringement, if the defendant can prove that he did not have reason to believe that the copy was an infringing copy, he can defense himself for this ground under section 36 of Copyright Ordinance (Defense for the purpose of section 30 and 31). *See* section 30, *infra* note 495.

⁵⁵⁸*See* 17 U.S.C. § 602 (a).

imports goods are considered as an “infringing copy” within the definition of “infringing copy” in section 27.⁵⁵⁹

Referring to parallel imports, the prohibition on importing and selling “hypothetically infringing copies” is the most important consideration.⁵⁶⁰ Parallel import articles definitely are genuine goods not infringing goods. Therefore, parallel imports are concerned as a secondary infringement only if they fall within the meaning of “hypothetically infringing copies” by referring to the words in section 27 (3) “its making in the United Kingdom would have constituted an infringement of the copyright” (so-called the hypothetical manufacturing requirement).⁵⁶¹ If the imported goods are considered as the infringing copy of the work, the right of the copyright owner is infringed by importing those goods into the jurisdiction unless the copyright owner in such jurisdiction consents to such importation.⁵⁶² However, even though the goods fail under hypothetical manufacture, there is still a defense for the parallel importer, which is the consent to import. In order to bar the parallel imports, the copyright owner must

⁵⁵⁹ See The CDPA 1988, *supra* note 556, section 27. Section 27 defines the term “infringing copy”:

“(2) An article is an infringing copy if its making constituted an infringement of the copyright in the work in question.

(3) An article is also an infringing copy if-

(a) it has been or is proposed to be imported into the United Kingdom, and
(b) its making in the United Kingdom would have constituted an infringement of the copyright in the work in question, or a breach of an exclusive licence agreement relating to that work.

...

(5) Nothing in subsection (3) shall be construed as applying to an article which may lawfully be imported into the United Kingdom by virtue of any enforceable Community right within the meaning of section 2(1) of the European Communities Act 1972.”

⁵⁶⁰ See ROTHNIE, *supra* note 24, at 189 and 194-246. (explaining and discussing on hypothetically infringing copies.)

⁵⁶¹ *Id.* at 199. (pointing out that under the hypothetical manufacturing requirement, the court concerns whether the actual maker has authority or a legal right to make the article in the place of importation. If the actual maker does not have such authority, the import goods shall be considered as an infringing copy and subject to a secondary infringement.); and also see *Pitt Pitts v. Geroge & Co.* [1896] 2 Ch. 866 (CA).

⁵⁶² See The CDPA 1988, *supra* note 556, section 22 and 23.

demonstrate that the importation occurred without its license or consent and the consent may be expressed or implied.⁵⁶³ A sale abroad of copyright goods may imply a license to import those goods into the domestic jurisdiction.⁵⁶⁴ Hence, if the parallel importers can prove that the goods are imported in to the United Kingdom with the copyright owner's consent either expressed or implied, the copyright owner cannot bar such importation.⁵⁶⁵ The copyright law imposed both civil and criminal sanctions for parallel importation and only the copyright owner has the right to sue parallel importer.⁵⁶⁶

However, as the result of the transfer of sovereignty of Hong Kong in 1997, U.K. laws are no longer applicable to Hong Kong. But undeniably the legal principles of the U.K. copyright law still remain and appear both in the new copyright ordinance and in the case laws of Hong Kong. In particular, the new Copyright Ordinance adopts the U.K. approach by considering the parallel import goods as an "infringing copy" by definition and pursuing to the concept of a secondary infringement.

3.1.2 The Current Perception of Hong Kong in Parallel Imports

The disagreement on the issue of parallel imports reflected the wide difference in opinion that existed in Hong Kong at the time of enactment of the law on this issue and continued to exist. During the drafting of the Copyright Ordinance, the proponents argued

⁵⁶³ See *Interstate Parcel Express Co. Pty Ltd. v. Time-Life International (Nederlands) B.V.* (1977) 138 CLR 534, at 542-45. (reasoning that the High Court of Australia ruled that the copyright statute did not require an express license; therefore a license may be implied in some circumstances.)

⁵⁶⁴ See ROTHNIE *supra* note 24, at 230.

⁵⁶⁵ See *Revlon Inc. v. Cripps & Lee Ltd* [1980] FSR 85; and also see David Kitchin, *The Revlon Case: Trade Marks and Parallel Imports (UK)*, [1980] EIPR 86.

⁵⁶⁶ See The Copyright Act of 1956 (UK) Section 110(1); and also see Kristi Heim, *Distributors, Retailers Battle Over Ban On Parallel Imports*, ASIAN WALL ST. J., June 16, 1997 (H.K. Week), at 1.

for the best interest of copyright owners and exclusive licensees, primarily foreigners (external force). They asserted that parallel importers deceive consumers by distributing low quality products and take advantage of the copyright owner's or exclusive licensee's marketing and advertising campaigns.⁵⁶⁷ On the other hand, the opponents, mainly Hong Kong consumers and retailers (internal force) argued for the best interest of consumers.⁵⁶⁸ The Hong Kong Consumer Council argues "parallel imports lower prices, increase variety and ensure that all kinds of goods are available locally without delays."⁵⁶⁹ At the end, the proponents successfully lobbied the government to prohibit parallel imports which resulted in the enactment of the Copyright Ordinance. Under the new Copyright Ordinance, parallel imports are considered as a secondary infringement⁵⁷⁰ and subject to both criminal and civil penalties.⁵⁷¹

⁵⁶⁷ See Alison L. Morr, *Hong Kong's Copyright Ordinance: How the Ban on Parallel Imports Affects the U.S. Entertainment Industry and Hong Kong's Free Market*, 21 HASTINGS COMM & ENT. L.J. 393, 404 (1999).

⁵⁶⁸ See Intellectual Property Department of Hong Kong S.A.R., Status of New Legislation: Copyright Bill. (lasted modified Nov. 4, 1997). The opponents, mainly consumer groups and retailers contested the prohibition on parallel imports. See Richard Covington, Megastores Rock 'n' Roll Into Asian Markets Changing Musical Tastes Spark Rapid Growth, INT'L HERALD TRIB. June 1, 1996, available in 1996 WL 4091148.

⁵⁶⁹ See Heim, *supra* note 566, at 1.

⁵⁷⁰ See The Copyright Ordinance Cap. 528 (1997) Section 30, available at <http://www.justic.gov.hk> (visited Apr. 3, 2002) and available in LexisNexis database (528 LOHK). [hereinafter The Copyright Ordinance Cap.528] Section 30 provides "The copying in a work is infringed by a person who, without the licence of the copyright owner, imports into Hong Kong or export from Hong Kong, otherwise that for his private and domestic use, a copy of the work which is, and which he knows or has reason to believe to be, an infringing copy of the work."; see THE INTELLECTUAL PROPERTY DEPARTMENT OF HONG KONG S.A.R., INTELLECTUAL PROPERTY PROTECTION IN THE HONG KONG SPECIAL ADMINISTRATIVE REGION 25 (1998) [hereinafter INTELLECTUAL PROPERTY PROTECTION IN HONG KONG] (explaining that it is a defense for the accused to prove that he did not know and had no reason to believe that the copy in question was an infringing copy of the copyright work. (Section 118(3)) As to what constitutes "reason to believe," statutory pointers have been laid down in some detail. (Section 35 (6) and (7)) The legislature's objective was to strike a balance among the interests of the copyright owner, exclusive licensee and the importer and the consumer.)

⁵⁷¹ See *id.* section 118; see Emma Stopford, Parallel Importation, at 1, available at <http://www.hk-lawyer.com/1999-2/Feb99-54.htm> (visited Apr. 3, 2002) (explaining that the proponents successfully lobbied for amendments to the original draft to secure criminal penalties for parallel importation, additionally the proposed civil sanctions since in the original draft, the government has at first proposed to

Therefore on June 27, 1997, Hong Kong's Legislative Counsel (LegCo) enacted the Copyright Ordinance (Cap 528).⁵⁷² Under this Copyright Ordinance, parallel imports are currently prohibited and considered as a secondary infringement, which follows the U.K. approach. Due to restriction on parallel imports, the Copyright Ordinance was subject to many controversial concerns. In regard to an open society policy, the Copyright Ordinance, which hampers free trade by banning parallel imports, may substantially change this framework and adversely affect Hong Kong retailers and consumers.⁵⁷³ It seems that the new Copyright Ordinance imposes more restrictive rules on parallel imports than the previous one.⁵⁷⁴

decriminalize parallel imports by encouraging copyright owner and exclusive licensee to protect their copyright through civil action.)

⁵⁷² See H.K. Ord. No. 92 (1997). The Copyright Ordinance is the first change in Hong Kong's copyright law after long time following the Copyright Act (UK) 1956 and the Copyright, Designs, and Patent Act (UK) 1988. So the current copyright law of Hong Kong is The Copyright Ordinance (Cap. 528); Later in 2000, there was amendment of copyright law, The Intellectual Property (Miscellaneous Amendments) Ordinance 2000, passed on July 6, 2000 and come into force on April 1, 2001. The purpose of this amendment was to clarify the meaning of the expression "for the purpose of trade or business" as used in the Copyright ordinance, particularly in area of criminal offences. However, as the result of this amendment, which extended the scope of criminal liability, the Administration decided to suspend this amendment through The Copyright (Suspension of Amendments) Ordinance 2001 Cap. 568 on June 22, 2001, which effected until at least July 31, 2002. See the Intellectual Property (Miscellaneous Amendment) Ordinance 2000 and The Copyright (Suspension of Amendments) Ordinance 2001, *available at* <http://www.justic.gov.hk>. (visited Apr. 3, 2002)

⁵⁷³ See Morr, *supra* note 564, at 399.

⁵⁷⁴ For example, prior to enacting the new Copyright Ordinance, Hong Kong copyright law, which is consisted of the Copyright Act (UK) 1956 and the CDPA 1988, imposed both civil and criminal sanctions for parallel imports, only copyright owner excluding licensee can take a legal action against copyright infringement. Responding to this concern, the Copyright Ordinance strengthen Hong Kong's rules of importation by prohibiting parallel imports and allowing exclusive copyright licensees in Hong Kong to take civil action against parallel imports as long as the copyright owner is joined as plaintiff. Allowing licensee to prosecute in parallel import case may make the enforcement of Copyright Ordinance more effective and possibly reduce the parallel import activities in Hong Kong. See Morr, *supra* note 546, at 400-01; see Heim, *supra* note 566, at 1; and also see The Copyright Ordinance Cap.528, *supra* note 570, section 113(1)(2).; At this point, the opponents of banning parallel import also assert that due to allowing exclusive licensees to take a legal action, the exclusive licensees is able to control distribution and market would be dominated and consumers depend on the exclusive license for selection and pricing. See Morr, *supra* note 546, at 405; and also see Jonathan Hill, Copyright Warning on CD Prices, S. CHINA MORNING POST. Dec. 12, 1995, available in 1995 WL 13317805.

The meaning of “infringing copy” in the Copyright Ordinance remains identical to the definition provided in the U.K. Copyright Law by including the parallel import goods into the definition of “infringing copy.”⁵⁷⁵ Thus, if the copyright owner licensed a foreign licensee to produce the copyright work only in a foreign territory and implicitly or explicitly denied the foreign licensee to manufacture in Hong Kong, the parallel imports of those goods infringed the copyright even though those imported goods are lawfully produced in a foreign country.⁵⁷⁶ Those imported goods are considered as an “infringing copy” under section 35(3). On the other hand, if a foreign licensee can show that the scope of copyright license includes Hong Kong territory either expressly or by implication, those parallel import goods are not considered as an “infringing copy” and the copyright owner cannot bar such importation.

In addition, an “infringing copy” is also defined for the purposes of the criminal provisions of the Copyright Ordinance.⁵⁷⁷ It is considered as an infringing copy if a copy would be an infringement of the copyright of the work or a breach of an exclusive license agreement and it has been or is proposed to be imported into Hong Kong within 18 months at the first day of publication of the work in Hong Kong or elsewhere. In other words, the Copyright Ordinance allows for both civil and criminal remedies within the

⁵⁷⁵ See The Copyright Ordinance Cap.528, *supra* note 570, section 35(3).

Section 35(3) states:

“(3) A copy of work other than a copy of an accessory work is also an infringing copy if-
 (a) it has been or is proposed to be imported into Hong Kong; and
 (b) its making in Hong Kong would have constituted an infringement of the copyright in the work in question, or a breach of an exclusive license agreement relating to that work.

⁵⁷⁶ See MICHAEL D PENDLETON, LAW OF INTELLECTUAL AND INDUSTRIAL PROPERTY IN HONG KONG: A GUIDE TO TRADE MARKS, COPYRIGHT, PATENTS, REGISTERED DESIGNS AND OTHER PROTECTED COMMERCIAL INFORMATION, 218-9 (1989), citing in *Polydor & Ors v. Hong Kong Records*, HCA No. 2601 of 1976.

⁵⁷⁷ A person who commits the offence is liable to a maximum fine of HK \$ 50,000 per infringing copy and up to four years imprisonment. See The Copyright Ordinance Cap.528, *supra* note 570, section 119(1).

first 18 months of the first publication of the copyright work. And after 18 months only civil remedies are available to copyright owner and exclusive licensee under section 35(4).⁵⁷⁸ It should be noted that Hong Kong's border control measure does not apply to parallel imports and only applies to pirated goods.⁵⁷⁹ In addition, the Copyright Ordinance allows parallel imports after 18 months of the copyright work's first publication or release worldwide when the product is unreasonably withheld or supplied on unreasonable terms.⁵⁸⁰

However, the importation of goods for the purpose of private and domestic use does not constitute a secondary infringement of copyright.⁵⁸¹ Moreover, this prohibition against parallel imports applies only where the substance of the parallel imported goods itself infringes copyright, but it does not apply to accessory works such as labels, packages, and instructions.⁵⁸² That is different from the United State's perception because the U.S. Supreme Court ruled in the *Quality King* case that the IPRs owner could use the copyright in label on the hair care products to stop the parallel imports.⁵⁸³

The Hong Kong copyright law after 1997 contains a contradiction between the implementation of international exhaustion doctrine and the restriction on parallel

⁵⁷⁸ See Morr, *supra* note 546, at 408.; and also see The Copyright Ordinance Cap.528, *supra* note 570, section 35(4).

⁵⁷⁹ *Id.* section 35(5).

⁵⁸⁰ *Id.* section 36(3); and also see Copyright Bill: Speech by STI Resumption of Second Reading Debate for LegCo sitting on 24 June 1997, available at http://www.houston.com.hk.80/hkgipd/sti_spch.html.; and also see Morr, *supra* note 546, at 408. (mentioning that LegCo fail to define the word 'unreasonable')

⁵⁸¹ See *id.* section 30 and 118(1)(b).

⁵⁸² *Id.* section 35(8) and 35(9); Under Section 35(9), a parallel imported copy includes a copy of a work made in a country, territory or area where there is no law protecting copyright in the work or where the copyright in the work has expired.

⁵⁸³ See *Quality King Distributors, Inc. v. L'Anza Research International, Inc.*, 523 U.S. 135 (1998). (The Supreme Court decided that the copyright owner could not bar the parallel imports because the right of copyright owner was exhausted under the first sale doctrine and the victory belonged to parallel importers.)

imports.⁵⁸⁴ The result is in preference to the prohibition of parallel imports rather than the exhaustion doctrine. In other words, the copyright law seems to primarily allow parallel imports under the concept of international exhaustion but in effect prohibit parallel imports under the concept of secondary infringement (infringing copy). In relation to the exhaustion doctrine, the copyright owner has the exclusive right to initially issue copies of a work to the public,⁵⁸⁵ but the right of initial release into circulation of copies of work is limited by the first sale doctrine under section 24 (3)(a) and (b).⁵⁸⁶ Section 24(3)(a) and (b) adopted an international exhaustion doctrine, consistent with the concept of free circulation of goods by providing that once particular copies of a work have been issued to the public in *Hong Kong or elsewhere* by or with the consent of the copyright owner, the subsequent sale, distribution, or importation into Hong Kong does not constitute copyright infringement. Nevertheless, parallel imports are still prohibited under the Copyright Ordinance because the parallel import goods are defined as an “infringing copy.” The parallel imports cannot argue that the right of the copyright owner is exhausted as the result of the exhaustion doctrine. Thus, parallel imports infringe the right of the copyright owner and are prohibited under the Copyright Ordinance.

In conclusion, parallel imports are not allowed under the new copyright ordinance, which is similar to the U.K. law by defining “infringing copy” including parallel import goods. However, unlike the U.K., Hong Kong inserts “the 18 month rule” to determine whether the parallel import should be allowed or not. Actually, parallel

⁵⁸⁴ In other words, it seems like the law of Hong Kong after 1997 internally contradictory; on the one hand the law engages international exhaustion and on the other hand the law prohibits parallel imports.

⁵⁸⁵ See The Copyright Ordinance Cap. 528, *supra* note 570, section 24.

⁵⁸⁶ *Id.* section 24(2) and (3).

import goods are genuine but by definition it is considered as an “infringing copy” under the hypothetically infringing copies. The parallel imports infringe the copyright regarded as a secondary infringement. However, parallel importers can defend themselves by asserting that such importation is consented by the copyright owner either expressly or by implication. If the importers can prove that the copyright owner consent to such importation, such parallel importations do not constitute the copyright infringement. To put it another way, if the parallel importer can demonstrate that those parallel import goods do not fall within the meaning of “infringing copy” under the hypothetically infringing copies, such imports are not considered as a secondary infringement.

3.1.3 Critiques in Consequences of Copyright Ordinance and Future Amendment

Consumer groups are concerned that Hong Kong’s parallel import restriction creates monopolies detrimental to consumers. The Copyright Ordinance should be amended to lift the ban or impose less restrictive measures by some compromise between the protection of the copyright owners’ right and the benefits to the Hong Kong public for accessing parallel import goods.⁵⁸⁷ As a result of banning parallel imports, the government not only damages consumer choice and available selection, but also leads to increase in product prices.⁵⁸⁸ The Hong Kong government acted in favor of

⁵⁸⁷ See Morr, *supra* note 546, at 417; and also see Legislative Council Panel on Trade and Industry Parallel Importation of Copyright Articles, September 1998, available at <http://www.lego.gov.hk/yr98-99/english/panels/ti/paper/ti10106e.htm>. (visited Apr. 1, 2002) (stating that the purpose of Copyright Ordinance in the parallel import is “to strike a balance of interests among copyright owners, exclusive licensees, distributors, and consumers.”)

⁵⁸⁸ *Id.* at 421. Parallel imports gainfully help the copyright owner to provide a broader dissemination of copyright work. Banning parallel import might hurt copyright owners by limiting their distributing channel to meet consumers’ demand. See Heim, *supra* note 566, at 1.

protectionism and betrayed its tradition of free trade.⁵⁸⁹ Indeed, Hong Kong has been recognized as one country that the fundamental government policy always encourages the free market and international competition.⁵⁹⁰ Restriction on parallel imports is contrary to those notions. Therefore, the Hong Kong SAR should not prohibit parallel imports and continually walk in the same path under the government policy supporting free market and international competition to sustain its economic achievement in the global market.

In addition, it should not be considered as an appropriate approach to group parallel imports and pirated goods together by attaching parallel import goods to the definition of infringing goods to strengthen the copyright protection. Based on the reason that the parallel imports goods are not counterfeit goods per se but genuine, lawfully produced goods.⁵⁹¹ The parallel import goods should not be treated in the same way as pirated goods. Hence, the Hong Kong SAR should amend the Copyright Ordinance to provide a separate treatment between parallel imports goods and pirated goods.⁵⁹²

At present, consumer groups are being successful in the area of computer software.⁵⁹³ LegCo, a legislative body of Hong Kong, has decided that the parallel import

⁵⁸⁹ *Id.* at 418.

⁵⁹⁰ See Consumer Council, Consumer Council Submission to the Bills Committee on the Trade Marks Bill, 28 December 1999.

“Hong Kong has always been proud of its acclaimed international competitiveness, and its tradition as a free market. Indeed, it can be assumed that Hong Kong’s economic success has been largely built on its reputation as a free port and by a commitment by Government not to intervene and put restrictive barriers in the way of access to Hong Kong markets. Imports have become an important source of products for both Hong Kong consumers and business. Where competition has been allowed to develop, in that there has not been private sector market distortion through restrictive practices, consumers and business have benefited from this open environment.” *Id.*, at 1

⁵⁹¹ See Morr, *supra* note 546, at 429

⁵⁹² *Id.*

⁵⁹³ See Consumer Council, Consumer Council Submission in Response to Consultation Paper Proposal to Liberalize Parallel Importation of Computer Software under the Copyright Ordinance, available at <http://www.consumer.org.hk> (visited Apr. 1, 2002)

of computer programs will be allowed.⁵⁹⁴ In the Copyright (Amendment) Bill 2001, the amendment has removed the civil and criminal liabilities related to parallel importation of and subsequent dealing in computer software under the Copyright Ordinance.⁵⁹⁵ Recently, the parallel imports of computer software do not infringe the right of the copyright owner and that genuine computer software is not considered as an “infringe copy.” As the result of strong support from consumer groups and widespread purchase on copyright works over the Internet, there is a potential trend that Hong Kong will possibly liberalize the parallel imports of movies and musical works⁵⁹⁶ that will benefit consumers by giving more choice and more access to those copyright works with reasonable time and price. Liberalizing parallel imports will create a better competition within the DVD sale and rental markets which finally should benefit consumers.⁵⁹⁷ Moreover, the future legalization of parallel imports in relation to copyright works (such as computer software, movies and musical works) in Hong Kong is more in line with the current approach of

⁵⁹⁴ See Legislative Council Brief: Copyright Ordinance(Chapter 528) Copyright (Amendment) Bill 2001, available at http://www.info.gov.hk/cib/ehhtml/pdf/page_16/brief_e_2001_12_05.PDF. (visited Apr. 3, 2002)[hereinafter Council Brief on Copyright (amendment) Bill 2001]

“ The Legislative Council and users of computer software have expressed the strong view that the current restrictions on parallel importation of computer software should be removed. They believe that allowing parallel importation of computer software would increase competition and availability of products in the market, resulting in more choices and lower prices for consumers. This would help to ease the financial burden especially of small and medium enterprises in replacing their pirated computer software with legitimate products to comply with the new end-user criminal provisions in the Ordinance that came into effect on 1 April 2001.” *Id.* at 2.

⁵⁹⁵ The Copyright (Amendment) Bill 2001 was finally gazetted on 27 April 2001. see Newsletter of Legislative Council, 18 May 2001, available at http://www.margaretng.com/mng_lego/003n_letters. (visited on 04/03/02); and also see Commerce and Industry Bureau, Legislative Council Brief: Copyright Ordinance(Chapter 528) Copyright (Amendment) Bill 2001, December 5 2001, available at http://www.info.gov.hk/cib/ehhtml/pdf/page_16/brief_e_2001_12_05.PDF. (visited Apr. 3, 2002).

⁵⁹⁶ See Council Brief on Copyright (amendment) Bill 2001, *supra* note 591, at para. 7 and 8.

⁵⁹⁷ See Jenny Cheung, Submission of Blockbuster Hong Kong Ltd.: Regarding the Consultation Document on Review of Certain Provisions of Copyright Ordinance, December 20, 2001, available at <http://www.legco.gov.hk>. (visited Apr. 3, 2002); and also see Alex Kaung, Review of Parallel Import Law Welcome, The Letter to The Editor, South China Morning Post (sep. 21, 1998), p.20.

New Zealand and Australia, implementing an international exhaustion doctrine, which will be explained later in Chapter Three.

3.2. Under Trademark Ordinance

3.2.1 Introduction

The current Trade Mark Ordinance (Chapter 559), gazetted on June 16, 2000 and brought into force in 2002, liberalizes parallel importations. The New Ordinance follows the Trade Mark Act of U.K. in many respects. It may be expected that case laws from the U.K. and other common law countries would be continually applied in Hong Kong including those in relation to parallel import cases. The New Ordinance deliberately legalizes parallel imports and allows the importation of parallel import goods.

Previously before 2002, the Trade Mark Ordinance (Cap 43),⁵⁹⁸ adopted the Trade Mark Act 1938 of U.K.,⁵⁹⁹ which provides the framework for the Hong Kong SAR's system of registration of trademark and trademark protection.⁶⁰⁰ Trademark infringement is a criminal offence under the Trade Descriptions Ordinance, which gives the Customs

⁵⁹⁸ The Trade Mark Ordinance Cap 43 L H K 1964, available at <http://www.justice.gov.hk> (visited Apr. 3, 2002). [hereinafter The Trademark Ordinance Cap.43]

⁵⁹⁹ The Trade Marks Ordinance is significantly different from the governing British statute, the Trade Marks Act, 1938. See PENDLETON, *supra* note 576, at 331. (explaining and comparing between the Trade Mark Ordinance and British law).

⁶⁰⁰ The Hong Kong SAR's trademark registration system is separate from the China's system. Therefore, trademark must be registered in the Hong Kong SAR for getting trademark protection under the Trade Mark Ordinance. Registered trademark is protected under the Trademark Ordinance and unregistered trademark may be protected by the common law action of passing off. See Intellectual Property in Hong Kong, at 6, available at http://www.info.gov.hk/ipd/eng/information/publication/ip/iphk_c.htm. (visited Apr. 9, 2002).

and Excise Department of the Hong Kong Government extensive powers of enforcement.⁶⁰¹

In the case of parallel imports, Hong Kong adopted the U.K. approach. Under the U.K. law, the trademark owner cannot bar importation of trademark goods, which are made by the trademark owner, or the subsidiary company as decided in the *Revlon* case and the *Champagne Heidsieck* case.⁶⁰² However, there is an exception in the case that the imported goods are actually different in quality. In that circumstance, the court decided in the *Colgate* case that the trademark owner could bar such importation.⁶⁰³ So under the Trade Mark Ordinance in Hong Kong, parallel importation of trademark goods could be considered as the infringement act. However, there is a defense that parallel importers can use to and this defense can be established when the following conditions are satisfied: (1) the trademark was used in relation to goods connected in the course of trade with the proprietor; and (2) the proprietor (a) has applied the trademark to the goods and had not subsequently removed or obliterated it; or (b) the proprietor has at any time given express or implied consent to the use of the Hong Kong trademark.⁶⁰⁴ This basically indicates that if genuine products have been manufactured abroad with the

⁶⁰¹For border measures, the trademark owner may apply to the Court for a detention order where he has reasonable ground for suspecting that the importation of goods constituting infringement may take place under the Trade Description Section 30A-30K. See INTELLECTUAL PROPERTY IN HONG KONG *supra* note 570, at 59.

⁶⁰²In both cases, trademark infringement was denied because the trademark as the badge of origin conveyed the same message wherever it was used. See *Revlon Inc. v. Cripps & Lee Ltd.*, [1980] FSR 85; *Champagne Heidsieck et Cie Monopole S.A. v. Scotto and Bishop*, [1926] 43 RPC 101; and also see ROTHNIE, *supra* note 24, at 18.

⁶⁰³In the *Colgate* case, the court distinguished this case from *Revlon* case because of the quality differences. If the parallel imports goods are not different in quality to the domestic goods, the status of registered trademark could apply equally. *Id.* at 39.

⁶⁰⁴See The Trademark Ordinance Cap. 43, *supra* note 599, art. 27, 27A, 28 and 28A; and also see Wong Wing Sing, Legal Issues Relating to Parallel Importation, at 3, available at http://www.webcast.tdctrade.com/webcast_c/2002/0304_2/Chi/Eng%20Ref%20%20latest.rtf (visited Apr. 16, 2002)

consent of the trademark proprietor, then they can be imported into Hong Kong if the trademark proprietor has implicitly consented to the use of the Hong Kong trademark.⁶⁰⁵ However, if the foreign subsidiary was only a licensee but not the agent of the trademark proprietor, it does not fall within the scope of this defense because the condition in (2)(a) is not satisfied and such parallel imports infringe the trademark right.⁶⁰⁶ Although the trademark ordinance provides some defense for parallel importers, it is considered as very limited exemptions for parallel importers. For example, a defense relying on the ground of express or implied consent is not easy to prove and inconsistent since consent is a matter of facts and depends on the circumstances in each case.

As a result of the prohibition of parallel imports, consumer groups and importation businesses attempted to put pressure to the government to remove such restrictions.⁶⁰⁷ From the consumers' perception, prohibition of parallel imports would "distort the market by restricting the choices of consumers whilst keeping prices artificially high."⁶⁰⁸ Such efforts have succeeded and a proposal to allow parallel imports into Hong Kong was a part of the draft trademark legislation published in April 1998 by the SAR's intellectual property department. Finally, a new Trade Marks Ordinance was passed and the parallel imports are now legitimate under the new trademark law.

⁶⁰⁵ See Emma Stopford, Parallel Importation, at 3, available at <http://www.hk-lawyer.com/1999-2/Feb99-54.htm>. (visited Mar. 3, 2002), citing in *Wellcome Foundation Ltd v. AG* [1992] 1 HKC 171. (The court held that if an overseas licensee had legitimately applied the trade marks to goods in the country of manufacture, it could not be said that the licensee had applied a Hong Kong trade mark law. Whether or not the trademark proprietor had impliedly consented to the overseas licensee using the Hong Kong trademark would depend on the facts which are evidenced by the distribution policy of the proprietor and the international nature of the trademark concerned.)

⁶⁰⁶ See Wing Sing, *supra* note 604, at 4. (commending that it is quite difficult to meet with the requirement in part of (2) (a).)

⁶⁰⁷ See Consumer Council, Consumer Council Submission to the Bills Committee on the Trade Marks Bill, available at <http://www.consumer.org.hk>. (visited Apr. 1, 2002); and also see *Authorities Unveil New Trade Mark Measures*, *Managing Intellectual Property*, June 1999 Issue 90, p8.

3.2.2 *The Liberalization of Parallel Imports by Adopting an International Exhaustion Doctrine into A New Trade Mark Ordinance*

The current Trade Mark Ordinance (Chapter 559) deliberately legalizes parallel imports and obviously allows the importation of parallel imports goods into Hong Kong. Under Section 20 of the new Ordinance,⁶⁰⁹ a registered trademark is not infringed by the use of the trademark in relation to goods which have been put on the market anywhere in the world under that trademark by the owner or with his consent. The importations of genuine goods do not infringe the trademark right if such goods have been released into the domestic or overseas market by the trademark owner or with his consent. However, there is an exemption to protect both the reputation of the trademark owners and consumers. The new rule does not apply where the condition of the goods has been changed or impaired after they have been put on the market, and the use of the registered trademark in relation to those goods is detrimental to the distinctive character or repute of the trademark.⁶¹⁰ This exception is in line with the purpose of trademark protection and consistent with other countries' approach such as Japan, Thailand, the United States, the United Kingdom, and the European Union.⁶¹¹

⁶⁰⁸ See Trade and Industry Bureau, Bill Committee on Trade Marks Bill: Parallel Importation of Trade Mark Articles, November 1999, at 2, available at <http://www.legoco.gov.hk> (visited Apr. 4, 2002).

⁶⁰⁹ Section 20 provides

“(1) Notwithstanding section 17 (infringement of registered trade mark) a registered trade mark is not infringed by the use of the trade mark in relation to goods, which have been put on the market anywhere in the world under that trademark by the owner or with his consent (whether express or implied unconditional).

(2) Subsection (1) does not apply where the condition of the goods had been changed or impaired after they have been put on the market, and the use of registered trade mark in relation to those goods is detrimental to the distinctive character or repute of the trade mark.”

⁶¹⁰ See Baker & McKenzie Intellectual Property Group, New Trade Marks Ordinance in Hong Kong, April 2001, at 6.; and also see Wing Sing, *supra* note 604, at 4.

⁶¹¹ See Article 7(2) of the Trademark Directive of EC (The exemptions of Community-wide exhaustion doctrine; and also see Colgate Case (The United Kingdom);, Parker Pen case (Japan): N.MC. Co. v.

The new Ordinance adopts the principle of international exhaustion for allowing parallel imports. Hong Kong supports free trade by attempting to open all markets for economic growth and believes in the free operation of market forces. Hence, the application of international exhaustion doctrine is in line with the free trade policy, the most important foundation of Hong Kong's economic success. Moreover, allowing parallel imports encourages competition and ensures the availability of goods in Hong Kong's market at best prices for consumers.⁶¹² It is also consistent with the concept of trademark protection because the trademark law should not be used as a method of distribution control that might abuse the concept of trademark.

3.3 Under Patent Ordinance

3.3.1 Introduction

The Patent Ordinance (Cap 514), as a current Hong Kong patent law, came into effect on 27 June 1997, providing the Hong Kong SAR with its own independent patent law and replacing the previous Registration of Patent Ordinance.⁶¹³ The current law grants the importation right to the patentee and prohibiting parallel imports. The law provides that parallel imports constitute patent infringement unless importers can prove having the patentee's consent to import, which follows the U.K. law. Previously

Schulyro Trading Co., 234 Hanrei Taimuzu 57 (Osaka Dist. Ct. 1970), the WAHL case (Thailand): The intellectual Property and International Court Case No. IP 16/2542, and Lever case (The United State): Lever Brothers Co. v. United States of America, 877 F.2d 101 (D.C. Cir. 1989).

⁶¹² See Trade and Industry Bureau, Bill Committee on Trade Marks Bill: Parallel Importation of Trade Mark Articles, November 1999, at 2.

⁶¹³ The Patent Ordinance (Cap 514), come into effect on June 27, 1997, available at <http://www.justice.gov.hk>; Like trademark, Hong Kong SAR patent law is territorial and the Hong Kong patent system separate from China. See Intellectual Property in Hong Kong, at 8, available at http://www.info.gov.hk/ipd/eng/information/publication/ip/iphk_c.htm. (visited Apr. 9, 2002).

before 1997, patent protection in Hong Kong depended on the United Kingdom patent law applied through local legislation.⁶¹⁴ The patent proprietor has an exclusive right to import the patent article into the jurisdiction. Under section 60(1) of the U.K. Patent Act, importation into the U.K. without the patentee's consent constitutes a patent infringement. Therefore, when considering parallel imports, the crucial question becomes how far the patentee's consent to importation can be inferred from some association between the domestic patentee and the marketing overseas of a product made according to the patent.

3.3.2 *The Current Perception of Hong Kong in Parallel Imports under the Patent Ordinance*

Under the new Patents Ordinance, the patent proprietor has exclusive rights to prevent other from importing, using or putting the patented articles in Hong Kong without his consent. It may constitute a patent infringement if those acts are done without the consent from the patent owner. Regarding the delicate link between consent and parallel imports, the outcome is different between the patent articles produced overseas by the patent proprietor and by the licensee, which adopts the law of United Kingdom as mentioned in earlier sections. If the patent proprietor grants a license to others to manufacture products overseas under that license, it does not imply consent to sell or import such patent articles produced overseas in Hong Kong. The parallel imports of those goods constitute a patent infringement. On the other hand, if the patented goods are

⁶¹⁴*Id.* at 8. (The Patents Ordinance (Cap 42) provided for the registration in Hong Kong of United Kingdom patents and of European Patents designating the United Kingdom.)

manufactured by the patent proprietor himself or his agent overseas, the parallel imports of those goods in Hong Kong will not infringe the patent right. However, if there is a restriction on sale in Hong Kong of those parallel imports goods and such restriction is brought to the notice of the parallel importers when they acquired those goods, the importations of those goods infringe the right of the patent owner.⁶¹⁵ Hong Kong's notion of restriction on sale and import is similar to the Japanese Supreme Court decision in the *BBS* case and the case laws of the United Kingdom.

4. Conclusion

The best theoretical framework for looking at the whole issue of parallel imports is that of free trade. The restrictive rule on parallel imports in Hong Kong seems to be apart from its dominant free market ideology. Hong Kong is the shining beacon of free trade that others might follow. The philosophy of free trade and international exhaustion let the market take care itself and when businesses make their choice, they have to live with the result. However, in case of parallel imports, the Hong Kong Government already picks the winner and does not let the market select the winner by itself. Under the free trade framework, the Government should not interfere in this issue.

In order to answer the question whether the parallel imports in Hong Kong are legitimate or not, the answer depends on the types of IPRs. Under the copyright ordinance, although the copyright ordinance provides the international exhaustion doctrine in Section 24, that parallel imports are prohibited and subject to a secondary infringement under Section 30. The parallel imports goods are treated as an "infringing

⁶¹⁵ See Wing Sing, *supra* note 604, at 5.

copy” under Section 35 and the law imposes both civil and criminal penalties. Because of pressure from consumer groups, the Copyright Ordinance 2001 removed the parallel imports restriction for computer software and it is possible that in the future there might be further liberalization regarding movies and musical industries. In the case of trademark, parallel imports are basically legitimate and only infringe trademarks under very limited circumstances. To support the free trade policy, Hong Kong obviously incorporated the international exhaustion doctrine into the Trademark Ordinance. In relation to patent, the parallel imports of patent articles constitute a patent infringement unless having the consent (either express or implied) of the patent proprietor to import into Hong Kong. Because Hong Kong believes in free trade and a global market and that consumer groups in Hong Kong are very strong, it is feasible that the Government may loosen restrictions on parallel imports in the future.

The intellectual property laws of Hong Kong follow the laws of the U.K. in many respects. However, Hong Kong interestingly introduces its own perceptions into the new set of laws including noticeably adopting the implementation of international exhaustion doctrine. By relying on the free trade policy, Hong Kong attempts to keep its position by ensuring the concept of free flow of goods by its own laws, which may not be perceived in the U.K. laws. It is not impossible that Hong Kong may adopt the international exhaustion doctrine into other laws for the sake of free trade and consumers’ benefit.⁶¹⁶

⁶¹⁶For example, section 6(1) of the Layout-design (Topography) of Integrated Circuits Ordinance Cap. 445, which came into force on March 31, 1994, states that the right of owner is exhausted after the import, sale or distribution for commercial purposes of a layout-design of an integrated circuit, which has been put onto the market anywhere in the world by, or with the consent of the right holder. See INTELLECTUAL PROPERTY PROTECTION IN HONG KONG, *supra* note 570, at 72.

CHAPTER THREE

CURRENT DEBATES ON PARALLEL IMPORTS

I. INTRODUCTION

Parallel imports implicate a complicated issues and an uneasy balance between the IPRs protection and the liberalization of trade (as mentioned in Chapter One and Two). Parallel imports occur in a different mode depending on changes of relevant factors such as changes in technology, economic, political, consumer or social health needs and the health care policy in each nation. Nowadays, there are many subject matters involving parallel imports, which are currently being debated at both national and international levels. Those problems are not yet resolved at the international level because each nation has a different policy and attempts to protect its own interest rather than finding the harmonized solution in those issues. The purpose of this chapter is to enlighten and analyze some important current controversial issues in parallel imports that should benefit to every nation seeking a reasonable realistic harmonized approach. Chapter four will then address the application of the international exhaustion doctrine by concluding and proposing a harmonious solution in the issues of parallel imports.

The consumers' pressure to liberalize parallel imports is a major motivation for the future trend of removing restrictions on parallel imports. Regarding the liberalization of parallel imports, Australia and New Zealand are considered the best examples in the area of copyright. Consumers in Australia and New Zealand are concerned about the price of copyright goods, whilst increasingly consumers in the European Union have concerns about the unnecessarily high-price of trademark goods; and consumers in the developing and least-developed countries have concerns regarding the high price of pharmaceuticals that affect their life and death. Such consumers' pressures and arguments expressly point to the future movement in favor of consumers in terms of low prices and more availability by adopting an international exhaustion doctrine. Consequently, this chapter will select merely remarkable parallel imports issues by dividing the current debate into the issues of copyright, trademark and patent, respectively.

II. CURRENT DEBATE IN COPYRIGHT

Consumers' pressure is a major factor motivating the future tendency to liberalize parallel imports in the area of copyright by adopting the international exhaustion doctrine. For example, because of the high prices and low availability of copyright works in domestic markets, particularly in Australia and New Zealand, consumer groups have put a great deal of pressure on their governments to allow parallel imports of copyright goods. The high prices and low availability could limit the consumers' consumption in those copyright works and conclusively diminish the dissemination of copyright work. Restrictions on parallel imports in copyright works oppose not only the purpose of

copyright but also the current movement of consumers. Thus, the following part will explain and discuss the triumphant consumers' movement in Australia and New Zealand.

A. The Consumers' Movement to Liberalize Parallel Imports in Copyright Law:

The Recent Parallel Imports Situation in Australia and New Zealand

Both Australia and New Zealand have had a long-standing prohibition on parallel imports under the copyright laws. However, the current movements of both the consumer and political groups have been a driving force supporting copyright reform by eliminating the parallel import restriction and adopting the international exhaustion doctrine.⁶¹⁷ Subsequently, in July 1998, the Australian Federal Government amended the copyright law to allow the parallel imports of books in specific circumstances and generally permit the parallel imports of musical compact disk, and later in June 2000, the Government amended the Copyright Act of 1968 to allow the parallel imports of software into Australia. To permit more parallel imports of a larger variety of copyright works, the Copyright Amendment (Parallel Importation) Bill 2002 of Australia currently clarifies that parallel imports of both print and electronic books, recorded music, computer software and computer games do not constitute a copyright infringement under the copyright law.⁶¹⁸ In New Zealand, the Government also amended the Copyright Act of 1994 to allow parallel imports in general in 1998. The main reason for removing the

⁶¹⁷ There are many groups that support the removal on parallel import restrictions under copyright law. For example, The Australian Competition and Consumer Commission (ACCC), The Price Surveillance Authority (PSA), The Australian Consumer Association, and The New Zealand Institute of Economic Research (NZIER).

⁶¹⁸ See The Copyright Amendment (Parallel Importation) Bill 2002, *available at* <http://www.apc.gov.au> (visited Sep. 23, 2002)

prohibition on parallel imports was to decrease the price of goods because parallel import restrictions raise the price of goods on the domestic market.⁶¹⁹ New Zealand appears to be liberalizing parallel imports in copyright law more than Australia and is more progressive than Australian, being one step closer to the concept of free trade and the application of international exhaustion doctrine.

Therefore, the following part will focus on the current movement of both Australia and New Zealand in a way that will benefit domestic consumers and encourage the global free movement of goods by opening the domestic market to parallel imports in copyright goods. Although such an amendment is currently applicable only to copyright law, it is possible in the future that trademark law and patent law may follow the change in copyright law by permitting parallel imports. Indeed, the result of removal of the parallel import restriction in copyright law is closely related to the application of the international exhaustion doctrine. This event can obviously support the assumption that the international exhaustion should be the best choice for international legal standard in the scope of the exhaustion doctrine.

1. The Reasons to Remove Parallel Import Restrictions: Consumer Pressure

Restrictions on parallel imports are anti-competitive and unfavorable for businesses and consumers because these restrictions confine competition in both

⁶¹⁹ The Copyright (Removal of Prohibition on Parallel Importing) Amendment Act 1998; The New Zealand Institute of Economic Research (NZIER) researched in the parallel import and concluded that substantial welfare gains would be made from the removal of the parallel import restriction. See The New Zealand Institute of Economic Research, Parallel Importing: A Theoretical and Empirical Investigation, Report to Ministry of Commerce on February 1998. [hereinafter NZIER Report]

wholesale markets and distribution areas that provide copyright owners and licensees with the opportunity to set prices above the prices that could be achieved in a fully competitive market.⁶²⁰ The removal of restrictions not only provides consumers with greater product choice and potentially lower prices, but it also enables e-commerce to become more competitive internationally.⁶²¹

In fact, the price of copyright works in Australia and New Zealand is quite higher than other developed nations such as the U.S. and U.K., and some works are not available in the market in terms of delayed release and range of product.⁶²² The domestic market of Australian and New Zealand is manifestly oligopolistic;⁶²³ thus restrictions on parallel imports provide a good opportunity for copyright owners to segregate the market and create the artificial barriers that prevent individuals from importing and selling products from low-priced markets into high-priced markets.⁶²⁴ Parallel imports prevent copyright owners from charging “what the market would bear”⁶²⁵ because the importation right

⁶²⁰ See Copyright Reform: Parallel Importation of Software Products, available at <http://www.ag.gov.au/publications/factsheets/softwarefactsheet.htm>. (visited May 1, 2002).

⁶²¹ *Id.* (reasoning that retailers will be free to source their inventory from the most advantageous source according to customer needs, price and service.)

⁶²² See The Series Reports of Prices Surveillance Authority (PSA): PSA (1989), Book Prices, Reports No. 24 and 25; PSA (1990), The Prices of Sound Recordings, Report No. 35; PSA (1992), Prices of Computer Software, Report No. 44 and 46.

⁶²³ For example, there are only six major music companies dominating the Australian recording market: Sony Music, Polygram, Warner Music, EMI, BMG, and Universal. The recording companies have monopoly control over the reproduction and distribution of the sound recordings. See Theo Papadopoulos, *Copyright, Parallel Imports and National Welfare: The Australian Market for Sound Recording*, 33 AUSTL. ECO. REV., 337 (2000), available at EBSCOhost p.3.

⁶²⁴ See *Id.* at 3-4 (mentioning that the copyright is divisible, a license may be limited to a specific act, a specific territory, or a specific period of time. A conflicting consequence of exclusivity is a restriction in the dissemination of the intellectual property that reduces consumption levels.); and also see Jill Walker, *Parallel Imports: A View from Australia*, 9 CONSUMER POLICY REVIEW: LONDON, 130 (1999).

⁶²⁵ See Van Melle, *supra* note 29, at 72.

facilitates the IPRs owners to “partition the global market into national segments” and charge monopoly prices and extract monopoly profits.⁶²⁶

Advocates of parallel import restrictions state that such restrictions are expected to bolster the protection of copyright and impede the importation of pirated and counterfeit goods. Opening markets for parallel imports might increase the piracy.⁶²⁷ However, there is no substantial evidence suggesting that an increase in piracy is a consequence of the removal of parallel import restrictions.⁶²⁸ Indeed, parallel imports do not cause an increase on piracy; rather, they eliminate the price difference among markets and simultaneously reduce the motivation of piracy.⁶²⁹ As the result of parallel imports, the differential between the domestic price and the marginal cost of production decreases. Lowering the domestic price would lower the volume of smuggling.⁶³⁰ In other words, parallel imports reduce the price of domestic products, simultaneously reduce the incentive to smuggle, and finally reduce the amount of piracy. Thus, the removal of parallel import restrictions should decrease the rate of piracy rather than increasing it.

⁶²⁶ See *Id.* at 65 (pointing out that the restriction on parallel imports would basically protect local publishing industries, rather than protect the copyright itself and its incentives to create.); and also see Papadopoulos, *supra* note 623, at 2, citing in The Prices Surveillance Authority 1990, Inquiry into the Prices of Sound Recordings, Report no.35, PSA, Melbourne.

⁶²⁷ See Papadopoulos, *supra* note 624, at 9. (explaining that The ARIA stated that pirated sales of sound recordings in Australia represent about 5 per cent of the market and estimated that parallel imports will increase piracy levels up to 30 per cent.)

⁶²⁸ In the report commissioned by the IPCRC, the Australian Institute of Criminology (AIC) found no substantial evidence of an increase in CDs piracy as a consequence of the removal of parallel import restrictions on sound recordings in July 1998. Both the Australian Competition and Consumer Commission (ACCC) and AIC report concluded that piracy was independently upon parallel imports.

⁶²⁹ See Papadopoulos, *supra* note 624, at 9. (pointing out that restriction on parallel imports provides the economic incentive for smuggling and compensates the risk taker for the cost of smuggling and the risk of detection (and subsequent penalties). The larger the price differential, the greater the return to smuggling. The slope of the smuggling supply curve is determined by: (i) the returns of smuggling (the price-cost differential); (ii) the probability of detection; and (iii) the size and nature of the penalties.)

⁶³⁰ *Id.* at 10.

The removal of parallel import restrictions by a small net-importer of intellectual property such as Australia and New Zealand may be welfare-enhancing for the nation largely at the expense of foreign copyright owners.⁶³¹ As it represents a small amount of world music sales, Australia is “a price taker” for international repertoire.⁶³² Consequently, parallel imports would reduce the domestic price, increase the volume of trade and move the market closer to the best outcome for society.⁶³³

2. Australian Approach to Remove Parallel Import Restrictions in Copyright Law

In general, the copyright owners or exclusive licensees have the right to prevent the importation of copyright works into Australia even though those products have been legitimately acquired overseas under section 37 and 102 of the Copyright Act 1968. The copyright is infringed when a person imports into Australia an article for the ‘purpose of trade’ without authorization from the copyright owner and when such a person (importer) knows that the making of the article would have constituted an infringement, if it had been made by the importer in Australia.⁶³⁴ This act functions to allow an oversea

⁶³¹ *Id.*

⁶³² *Id.* at 6 (explaining that Australia is a price-taker for international repertoire since Australia represents about 2 per cent of world music sales, a small country model. Changes in domestic quantity traded are so small as not to impact on prices in other international territories. Moreover, reciprocal importation rights enable MNE record companies to segment international territories and thereby maintain territorial price differentials.)

⁶³³ *Id.* at 8.

⁶³⁴ See Section 37 and 102 of The Copyright Act 1968. The text of The Copyright Act 1968 is available at <http://www.apf.gov.au>. (visited Sep. 25, 2002) [hereinafter The Copyright Act 1968]; see *Computermate Products (Australia) Pty Ltd v. Ozi-Soft Pty Ltd* (1988) 20 FCR 46; Moreover, in the case of no restriction terms on subsequent sale or distribution, the parallel importer cannot assert that the copyright owner has an implied license for importing into Australia. Although the parallel importer acquired those products from overseas and there is no express restriction on subsequent sale, the copyright owner in Australia still has right to bar such parallel imports. Merely not taking any actions to stop infringement does not mean the copyright owner has authorized an infringement and mere silence will not suffice to constitute an authorization. See *Interstate Parcel Express Co Pty Ltd v. Time Life International (Nederlands) BV* (1977) 138 CLR 534.; *Nationwide News Pty Ltd v. Copyright Agency Ltd* (1996) 34 IPR 53 and *Powerflex*

copyright owner to appoint exclusive licensee in Australia with the sole right to import copies of works into Australia and thereby establish exclusive distribution network.⁶³⁵

Under the Australian copyright law, restrictions on parallel imports are very rigid and constitute the monopoly right of copyright owner in terms of product distribution. In response to those concerns, there are movements by consumer groups and political groups suggesting that the Government remove such parallel import restrictions in copyright law. The Copyright Law Review Committee⁶³⁶ released a report in 1988 by concluding that the parallel import restriction should continue to be applicable, but the scope should be restricted in certain specified ways and certain sorts of goods. At present, Australia removed the parallel import restrictions on books, sound recordings, software and packing and labeling of physical items. Those types of copyright works have been removed from parallel import restrictions within these three amendments made under the consumer pressure: (1) the Amendment in 1991, (2) the Amendment in 1998; (3) the Amendment in 2002.

2.1 The Copyright Amendment in 1991

As a result of the higher price of books in Australia as compared to other countries, The Price Surveillance suggested that the Australian Government should

Service Pty v. Data Access Corp (1997) AIPC 91-325.; and also see PATRICIA LOUGHLAN, INTELLECTUAL PROPERTY: CREATIVE AND MARKETING RIGHTS 56 and 60 (1998).

⁶³⁵ See LOUGHLAN, *supra* note 634, at 59.

⁶³⁶ The Copyright Law Review Committee is a committee of judges and professor and other knowledgeable persons established in 1983 to advise the Attorney-General on reform of copyright laws in specific areas referred to it.

remove restrictions on parallel imports.⁶³⁷ Finally, some minor amendments to the Copyright Act to lessen the problems of restricted availability of foreign books.⁶³⁸ In response to intensely high prices and the unavailability of books in Australia, the Australian Parliament amended the Copyright Act in 1991 to loosen up the restrictions on parallel imports of foreign books legally produced in foreign countries (the country of origin).⁶³⁹ Thus, overseas books, which referred to books that are first published outside Australia and are not published in Australia within 30 days of first publication elsewhere, are classed as “non-infringing books” and can be imported without the license of the copyright owner.⁶⁴⁰ Moreover, parallel imports of books ‘first published in Australia’ is allowed: (1) to provide a single copy for a customer; (2) to provide one or more copies for a non-profit library, and (3) to satisfy local orders that have been unfilled for more than 90 days, known as “the 30/90 day rule.”⁶⁴¹

⁶³⁷ The Price Surveillance Authority released its 1989 *Inquiry Into Book Prices* and advocated an abolition of parallel import provisions with respect to books on the basis that the Australian public was paying considerably higher prices than it otherwise would and should.

⁶³⁸ See LOUGHLAN, *supra* note 634, at 60. (explaining that the substance of the amendments is that importing non-pirated copies of books for commercial trade is allowed where the book has not in fact been made available in reasonable quantities within a reasonable time by the copyright owner or the copyright owner’s exclusive license.)

⁶³⁹ The “30 day rule” was introduced by providing that if the Australian rights holder fails to publish the book in Australia within 30 days of it being published in another country, then parallel importation of legitimate copies are permitted. The Copyright Act allows for the parallel importation of non-infringing books. A non infringing books is a book made otherwise than under a compulsory license, without infringing the copyright subsisting in any “work” or “published edition” in a country specified in the Copyright Regulations section 10(1).

⁶⁴⁰ On the contrary, for the books first published inside Australia (including those published in that country if within 30 days of first publication elsewhere), the copyright owner retains full rights to control parallel imports for commercial purposes with two narrow exceptions in response to consumer demand under section 44A and 112A of the Copyright Act 1968. See Louise Londgin, *Parallel Importing Post TRIPS: Convergence and Divergence in Australia and New Zealand*, 20 INT’L & COMP. L.Q., 54, 59 (2001).

⁶⁴¹ See Mary Anne Nelisen & Law and Bills Digest Group, Copyright Amendment (Parallel Importation) Bill 2002, Bill Digest No.133 2001-02, 15 May 2002, at 3, available at <http://www.aph.gov.au>. [hereinafter The Bill Digest]

2.2 The Copyright Amendment in 1998

The Australian Consumers Association has become a strong advocate of copyright reform to obtain lower prices and greater availability of products.⁶⁴² The Prices Surveillance Authority has recommended that the importation provisions of the Copyright Act should be removed in respect to sound recordings and computer software on the grounds of being a disadvantage to the Australian consumers.⁶⁴³ However, in the end, the Copyright Amendment Act (No.2) 1998 only sound recording was allowed for parallel imports, but did not include software.⁶⁴⁴

The Copyright Act 1968 was amended in July 1998 to allow the parallel importation of sound recordings. Unlike the amendment in 1991, partially permitting the parallel imports of books, the Copyright Amendment Act (No.2) 1998 adopted the principle of international exhaustion⁶⁴⁵ and fully opened the market for sound recordings by permitting parallel imports from all countries with effective copyright protection.⁶⁴⁶ The result is that sound recordings legitimately produced abroad can now be imported into Australia without authorization by the copyright owner.

⁶⁴² See Walker, *supra* note 624, at 5.

⁶⁴³ The most controversial of the Australian reforms was the decision to allow the parallel importation of sound recording subject only to certain minimal limitations. The finding of the Price Surveillance Authority showed that Australian sound recording prices were higher than in other countries including the United Kingdom, the United States, Canada and New Zealand.

⁶⁴⁴ In the case of computer software, the parallel imports of software are later allowed under The Copyright Amendment (Parallel Importation) Bill 2002.

⁶⁴⁵ See Papadopoulos, *supra* note 624, at 11.

⁶⁴⁶ See The Copyright Act 1968, *supra* note 634, section 10AA. Under section 10AA of the Copyright Act 1968, a sound recording will be considered as a non-infringing copy if: (1) the copy is made by, or with the consent of the owner of the copyright in the 'copy country'; (2) the making of a copy does not infringe copyright in the copy country, and (3) the 'copy country' is either a party to the Berne Convention, or a member of the World Trade Organization and complies with TRIPS.

With respect to packaging and labeling, the Copyright Amendment Act 1998 has prevented copyright owners from prohibiting the importation of goods into the country by asserting copyright in the packaging or labeling of imported goods.⁶⁴⁷ The Copyright Law Review Committee (CLRC) recommends removing restrictions on parallel imports when the copyright exists only in a label or package⁶⁴⁸ because in the past the IPRs owners artfully used copyright in a label or package as literary and artistic work to bar parallel imports.⁶⁴⁹ In other words, such misuse of copyright was removed by inserting into the copyright statute the concept of a “non infringing accessory,”⁶⁵⁰ which can be extended to: labels affixed to, displayed on or incorporated in imported articles; packaging or containers enclosing such articles; written instructions, warranties and manuals; and instructional sound recordings or films reasonably related to the performance or use of imported articles. This concept provided that the copyright owner

⁶⁴⁷ The packaging and labeling amendments came into effect in January 2000. The Copyright Amendment Act (No.2) enforced on 30 July 1998, Schedule 2 of the Act will reform the copyright law relating to the importation of packaging and labeling, with effect from the end of January 2000.

⁶⁴⁸ See Copyright Law Review Committee (1998), *The Importation Provisions of the Copyright Act 1968*, September AGPS, Canberra.

⁶⁴⁹ The business with exclusive distribution rights for various non-copyright imported goods would be able to use the copyright in the packaging and labeling of those goods to prevent parallel imports. The Copyright Law Review Committee reasoned that it is not the purpose of copyright to allow the owner of the goods to exclude other from marketing similar goods by using the copyright in a label or a package. See Copyright Law Review Committee (1998), *The Importation Provisions of the Copyright Act 1968*, September AGPS, Canberra, at 224-225.; see Copyright Reform: Changes to Copyright Rights in Packaging and Labeling under Schedule 2 of the Copyright Amendment Act (No.2) 1998, available at <http://www.ag.gov.au/publications/copyrightfactsheetv2.htm>. (visited May 1, 2002); see LOUGHLAN, *supra* note 634, at 61.(pointing out that effectively, the new statute shall reverse the court rule in the *Bailey* case, which allowed using copyright in a label to prohibit parallel imports.); see *R A & A Bailey & Co Ltd. v. Boccaccio Pty Ltd.*, (1986) 6 IPR 279; The IPRs owner may prefer to bar parallel import through copyright law more than trademark law because the Trademark Act provides limited and uncertain rights against parallel imports. See *Montana Tyres Rims and Tubes Pty Ltd v. Transport Tyre Sales Pty Ltd* (1998) 411 PR 301.

⁶⁵⁰ This approach is similar to the Hong Kong law, which stipulates that the copyright owner cannot use the copyright law in labeling and packaging to prohibit parallel imports. See *Parallel Import in Hong Kong* in the pervious chapter: Chapter Two.

in the country of manufacture approves the use of copyright material in or on the accessory, its importation into Australia will no longer infringe.⁶⁵¹

2.3 The Copyright Amendment in 2002

On 27 June 2000, the Australian Government announced its intention to amend the Copyright Act to allow the parallel imports of legitimate software (including computer-based games), books, printed music, and periodical publications. In response to the Intellectual Property and Competition Review Committee's recommendations, the Government introduced the Copyright Amendment (Parallel Importation) Bill 2001 to the Parliament on 28 February 2001. Finally, this bill was passed on 13 March 2002 and is known as The Copyright Amendment (Parallel Importation) Bill 2002.

The Copyright Amendment (Parallel Importation) Bill 2002 allows free competition from parallel imports in a wide variety of products.⁶⁵² This Bill draws a distinction between electronic and printed books, periodicals and music into two separate Schedules. Schedule 1 amended the Copyright Act 1968 to allow the parallel imports of computer programs, electronic literary and music items.⁶⁵³ Schedule 2 amended the Copyright Act 1968 to allow the parallel imports of printed books, music and periodicals.⁶⁵⁴ The purpose of this Bill is to allow the parallel imports of electronic and

⁶⁵¹ See Londgin, *supra* note 640, at 60.

⁶⁵² See Allan Fels, Meeting on Competition, Trade & Development: Intellectual Property, Competition & Trade Policy Implications of Parallel Import Restrictions, May 23 2001, available at http://accc.gov.au/speeches/2001/Fels_Rome_June_22_2001.htm. (visited Nov. 10, 2001)

⁶⁵³ Electronic literary or music items are books, periodicals or sheet music in electronic form, regardless of whether there is a printed form. (item3)

⁶⁵⁴ The commencement of Schedule 2 is delayed for one year. The Government has decided to postpone the implementation of the amendment to assist the publishing and printing industries and authors to make the necessary adjustment in both their business practices and legal preparations. See The Parliament of The Commonwealth of Australia, House of Representatives, Explanatory Memorandum: Copyright Amendment

printed books, periodicals, music and software products, including computer games, video arcade games and business software, from “qualifying countries.”⁶⁵⁵

In the area of books, the new section 44A not only revoked the 30/90 day rule under the old section 44A but also replaced it by providing that copyright in a work that has been published in Australia or a qualifying country is not infringed by a person who imports into Australia a ‘non-infringing’ printed book, periodical or piece of music even though such items are imported for commercial purpose.⁶⁵⁶

At present, the parallel imports of sound recording, computer programs, electronic or printed literary and music are no longer considered copyright infringement.⁶⁵⁷

However, this does not include ‘cinematographic films,’ such as in the form of DVDs.⁶⁵⁸

Thus, the parallel imports of cinematographic films still constitute a copyright infringement.⁶⁵⁹ In addition, since copyright products such as computer software, sound

(Parallel Importation) Bill 2002, available at <http://www.aph.gov.au>. (visited Sep. 25, 2002) [hereinafter The Explanatory Memorandum].

⁶⁵⁵ A ‘qualifying country’ is a country that is either party to the Berne Convention or a member of the World Trade Organization with a copyright law consistent with the TRIPS Agreement.; Under the new amendment, the new definition of a non-infringing copy of sound recording, of computer program, of electronic literary or music item, and of printed literary or music item will be defined in section 10AA, section 10AB, section 10AC, and section 10ACA, respectively. In relation to the burden of proof, the copyright owner has to prove that a copy of copyright work has been imported and offered for sale or trade in Australia and then the burden falls on the defendant or importer to prove that the imported item is a ‘non-infringing copy.’ See The Copyright Act 1968, *supra* note 634, section 130B and 130D.

⁶⁵⁶ The new amendments will only apply to printed books, periodicals or sheet music imported into Australia after the commencement of the Schedule.

⁶⁵⁷ See The Copyright Act 1968, *supra* note 634, section 44E (computer program), 44F (electronic books, periodicals and sheet music) and 44A (printed books, periodical or piece of music).

⁶⁵⁸ See The Bill Digest, *supra* note 641, at 15; see J. Revesz, Trade-Related Aspects of Intellectual Property Rights, Staff Research Paper, Productivity Commission, May 1999, at 51 (stating that “the piecemeal approach adopted in the past to reform parallel importing item-by-item (books, sound-recordings and packages) cannot be justified on economic grounds. It might be preferable to reform in one step the entire copyright law.”)

⁶⁵⁹ According to technological convergence, one product may contain both software and other copyright material, such as cinematograph films and the division between these categories is gradually more difficult to make. The copyright may use the film element in such product to stop the parallel imports. To avoid this problem, the new amendment defines the definition of ‘feature film’ that means a cinematograph film that (a) is produced wholly or principally for exhibition to the public in cinemas or by way of television

recordings and books are embodied and protected under the trademark at the same time, the trademark owner may assert his trademark right to bar the parallel imports of those copyright goods.⁶⁶⁰ To prevent such maltreatments, the new amendment inserted a provision to ensure that trademark assignments cannot be used to overcome parallel imports that are permitted in relation to computer software, sound recordings and books.⁶⁶¹

3. New Zealand Approach to Remove Parallel Import Restrictions in Copyright Law

In the past, to deter the diffusion of international piracy into New Zealand, copyright law initially prohibited the unauthorized import of legitimately copyright goods. Although the exhaustion doctrine is well-established regarding the domestic sale,⁶⁶² the scope of this doctrine is always an issue when dealing with importation, whether it should have a territorial or universal approach.⁶⁶³ Prior to the amendment, the Copyright Act prohibited the importation of “infringing copies” and provided a broad meaning of “infringing copies,” including parallel imported goods. The importation into New Zealand other than for private and domestic use constituted the copyright

broadcasting; and (b) is more than 20 minutes in duration. *See* The Explanatory Memorandum, *supra* note 682, at 6.; and also *see* The Copyright Act 1968, *supra* note 634, section 10AD

⁶⁶⁰ *See* The Explanatory Memorandum, *supra* note 654, at 2.

⁶⁶¹ *See* The Copyright Act 1968, *supra* note 634, section 198A

⁶⁶² *See* Section 9(1) of The Copyright Act 1994. The Copyright Act 1994 for the Government Print web site, available at <http://www.gplegislation.co.nz/welcome.html>. (visited May 1, 2002). [hereinafter The Copyright Act 1994]

⁶⁶³ *See* Van Melle, *supra* note 625, at 64; and also *see* Ministry of Economic Development, New Zealand, A Discussion Paper: Parallel Importing and The Creative Industries, Dec. 2000, at 13-14, available at http://www.med.govt.nz/buslt/int_prop/creatdisc/creatdisc.pdf. (visited Oct. 18, 2002) [hereinafter A Discuss Paper]

infringement,⁶⁶⁴ if the importer knew or had reason to believe was an infringing copy.

“Infringing copy” was defined in a two-limb definition.

Section 12(3) of the Copyright Act provided:

“An object that a person imports, or proposes to import, into New Zealand is an infringing copy if-

- (a) If, had that person made the object in New Zealand, that person would have infringed copyright in the work in question; or
- (b) If the making of the object, by whomever it was made and where it was made, constituted an infringement of the copyright in the work in question.”

The first limb of this definition deals with parallel import goods and the second limb deals with pirated goods. In the first limb, it is the “notional maker” test: if the importer had made the goods in New Zealand without permission, copyright would have been infringed.⁶⁶⁵ Obviously, the New Zealand copyright law gave a copyright holder the unconditional exclusive right to import genuine goods and to prohibit parallel imports. The copyright holder has complete control over the specification of goods to consumers because in the law does not require that the copyright holders actually have to import or manufacture the goods themselves if other persons were prohibited from importations.⁶⁶⁶

The NZIER 1998 report on the investigation of three markets (computer software, spare part for cars, and books) stated that the prices for copyright goods in New Zealand are significantly higher than price in other countries. Allowing parallel imports could increase competition, not currently available because of current parallel import

⁶⁶⁴ See A Discussion Paper, *supra* note 690, at 14. (mentioning that the goods were imported for a person’s private and domestic use including goods purchased by international mail order or during overseas travel.); *Id.* at 47 (“Parallel-importing bans can only effectively restrict the importation of goods for retail sale. They cannot restrict private and domestic use such as mail order or personal imports by overseas travelers. Parallel-importing bans cannot effectively restrict the importation of copyright goods via telecommunications systems-for example, digital distribution over the Internet.)

⁶⁶⁵ See Van Melle, *supra* note 29, at 65. (explaining that the notional maker tests)

⁶⁶⁶ *Id.* at 71.

restrictions, and finally reduce the price of goods in domestic market.⁶⁶⁷ The report concluded that in all three markets substantial net welfare gains would be made by allowing parallel imports.⁶⁶⁸

As the result of such monopoly power and the higher price of copyright products in New Zealand, the Government intended to remove parallel import restrictions. Unlike Australian approach, the New Zealand government preferred to remove all existing parallel import restrictions in one single legislative act that benefited all consumers.⁶⁶⁹ The definition of infringing copy with respect to importation in section 12(3) was amended to permit parallel imports by the inclusion of the exceptions in subsection (5A).⁶⁷⁰ So the importation of goods into New Zealand does not constitute a copyright infringement if such goods are made by or with the consent of the copyright owner in the

⁶⁶⁷ See The NZIER Report, *supra* note 619, at iii.

⁶⁶⁸ See *id.* at iii and 61. (The NZIER investigated three distinct markets: computer software, spare part for cars and books.)

⁶⁶⁹ The rationale for legalizing parallel imports was to “allow the New Zealand consumer to benefit from lower prices for goods as a result of competition.” See Lynne Eagle, Lawrence Rose & Brendan Moyle, *Shades of Gray: The Impact of Gray Market/ Parallel Importing on Brand Equity and Values*, Working Paper Series No. 00.02, Department of Commerce, Massey University, Auckland, at 2. [hereinafter *The Working Paper of Massey University*], citing in D. Ewart, *Parallel Importing- Threat or Opportunity?*, Presenting to Employers and Manufacturers’ Association Seminar on Parallel Importing, Auckland, 20 November 1998.

⁶⁷⁰ See The Copyright Act 1994, *supra* note 662, section 12(3).

Section 12 (3) An object that a person imports, or proposes to import, into New Zealand is an infringing copy if-

- (a) The making of the object constituted an infringement of the copyright in the work in question in the country in which the object was made; or
- (b) The importer would have infringed the copyright in the work in question in New Zealand had the importer made the object in New Zealand, *unless the object is one to which subsection (5A) or subsection (6) applies.* ...

(5A) An object that a person imports or proposes to import into New Zealand is *not an infringing copy* under subsection (3) (b) if-

- (a) It was *made by or with the consent* of the owner of the copyright or other equivalent intellectual property right, in the work in question in the country in which the object was made; or
- (b) Where no person owned the copyright, or other equivalent intellectual property right, in the work in question in the country in which the object was made, any of the following applies:
 - (i) The copyright protection (or other equivalent intellectual property right protection) formerly afforded to the work in question in that country has expired;” (emphasis added)

countries that the goods are made.⁶⁷¹ However, if there is no copyright protection in the country of origin of parallel import goods, such parallel imports are not permitted under section 12(5A), which is similar to the Australia's concept of a 'qualifying country.'⁶⁷² Under section 12(5A)(b)(i) of the New Zealand Copyright Act, if the copyright has already expired in the country of origin, the goods made in such a country can be lawfully imported into New Zealand even though the period of copyright protection in New Zealand has not expired. The copyright holder cannot bar such parallel imports.

4. Conclusion

Although there are many controversial arguments and pressures from outside and inside the Australia and New Zealand movements to lift the parallel import restrictions in copyright law,⁶⁷³ Australia and New Zealand have still decided to legalize the parallel imports in area of copyright products to benefit all customers in terms of more choices

⁶⁷¹ In other words, this means counterfeit and quasi-counterfeit goods are still prohibited from import into New Zealand market but genuine parallel imported goods are permitted. Quasi-counterfeit goods refer to the goods that legally made in countries where the copyright work was not protected or had ceased to be protected. See Berne Convention, *supra* note 119, art. 16.

⁶⁷² The Australia approach might be more effective since a 'qualifying country' is a member of Berne or a TRIPS signatory, which its laws fulfill with these agreement. The New Zealand approach only mentions to the country that provides the copyright protection, but does not consider whether its copyright law and enforcement mechanism meet with the TRIPS standard or not. See Longdin, *supra* note 640, at 74.

⁶⁷³ For example, The British High Commissioner, Sir Roger Carrick, warned that any moves by Australia to relax its import rules on CDs and other goods could lead to erosion of copyright standards and would make the Australian market less attractive to importers. See Nina Field, *UK Joins Chorus of Concern Over Relaxing Import Rules*, AUSTRALIAN FINANCIAL REVIEW 3 (Feb. 20, 1997); Australian Internet Industry Association (AIIA) has attacked the Government for lifting software import restrictions ahead of the final report on the issue. There was no concrete evidence for the Government's assertion that parallel imports of software have any impact on software prices. Business Software Association of Australia asserts that lifting restrictions would encourage piracy. See Dominique Jackson, *Import Changes Favour Pirates: AIIA*, THE AUSTRALIAN, July 4, 2000 at 36; As the result of lifting parallel import restriction, the United States issued a section 301 notice under the U.S. trade law and reviewed on New Zealand's actions. The U.S. concerned that removing the parallel import restriction is an invitation to piracy. See Jane Dunbar, *Kiwis Ruffle US Feathers with Bold Law on Parallel Imports*, THE AUSTRALIAN, Finance Section, May 26, 1998, at 32.

and lower prices. Both governments are committed to the concept of global free trade and have determined that the intellectual property protection should not be limited by means of national boundaries, allowing intellectual property owners to segment markets.

One of the most persuasive arguments in favor of parallel imports aside from the wider consumer choice and lower domestic prices is the rapidly changing world of technology. Most copyright works can be sold and delivered on the Internet directly to customers bypassing retailers. So the prohibition on parallel imports can no longer exist in the Cyberspace.⁶⁷⁴ Although the U.S. issued a section 301 notice under the U.S. trade law and reviewed New Zealand's actions on removing parallel import restrictions, the removal on parallel import restrictions on copyright work is actually consistent with the U.S. Supreme Court decision in the *Quality King* case: as a result of the first sale doctrine, the copyright owner cannot use copyright to prevent competition from re-importing products. It seems that the U.S. exclusive branch significantly places a foreign policy to other countries than the U.S. court does.

B. International Exhaustion Doctrine as a Proper International Legal Standard

As a result of digital technology moving forward faster than intellectual property law, one can expect that a new legal issue dealing with the new technology can emerge

⁶⁷⁴The New Zealand Commerce Minister John Luxton stated that "many copyright works such as CDs, books, and computer software can be sold on the Internet and the Internet has already by-passed existing law; consequently, parallel import bans quite frankly are not going to work in Cyber world." See Pamatutau Richard, *Copyright Act in Line for Change Parallel Importing May Be Legalized*, THE DOMINION (WELLINGTON) April 6, 1998, Monday, at 1; and also see A Discussion Paper, *supra* note 663, at 47-50.

any day.⁶⁷⁵ The government has a duty to solve this issue by considering each group's interest and public's interest and balancing them. According to the borderless characteristic of Internet, the issue of parallel imports in the digital world should be solved at international level either via an international or a multinational agreement. If each nation provides a different regulation on parallel imports in digital works, it will result in many inconsistencies and lead to unharmonious situation that might defeat the contemporary concept of free trade and free movement of goods.

Consequently, there should be a harmonization rule on the parallel imports in the digital environment,⁶⁷⁶ and it is the proper time for harmonization of this rule. Since digital technology creates a single global territory, it is inappropriate to apply different rules in different countries regarding the copyright protection issue in the digital world.⁶⁷⁷ An incoherent rule may impede the free flow of goods among nations, which will inevitably obstruct either the current movement on promoting the free trade or obstruct the harmonization of the intellectual property laws throughout the world. Such movements in Australia and New Zealand in the area of copyright law have contended

⁶⁷⁵ This situation has challenged businesses, legal scholars, and governments to find the proper way for implementing the existing laws to the new issues that may go beyond the intention of such legislation when was enacted.

⁶⁷⁶ The approaches taken in each member nation such as Australia and New Zealand that apply the international exhaustion doctrine are useful in finding the harmonizing answer. The best way to generate a harmonizing multinational agreement is (1) Firstly, to conduct a research on nations that have faced or are currently faced with this issue and find out how they solve it; (2) Secondly, to select good parts of each nation's regulation; and (3) Finally, to analyze and organize each proper regulation into one agreement that member nations can accept. The harmonizing solution to this issue will be stated in Chapter Four.

⁶⁷⁷ The Green Book of the European Commission on Copyright from 1995 stated "whereas, in classical copyright it has been possible to live with different rules in different countries which were tied together through the international conventions, this is not viable in the digital environment, where we have only one 'country', the internet. There are no frontiers, customs, or controls. Different concepts in different territories, different rules for identical ways of exploitation are not only meaningless: a lack of worldwide coherent solution would end in discrimination against all regions, which have a high standard of protection of intellectual creations and cause encouragement for countries or regions with a low level of protection. The inevitable result of course would be the expropriation of rightholders-be it authors, industries, publishers."

that parallel imports in copyright goods should be free and without restriction. It is possible that in the future, the TRIPs conference members might bring the issue of parallel imports in copyright goods to the panel and propose that the application of international exhaustion is consistent with the digital technology and with the current trends to allow parallel imports in the area of copyright law. Thus, with the worldwide pervasion and borderless characteristic of Internet, the dissemination purpose of copyright law and the strong pressure of consumers, the harmonious approach should be allowed on parallel imports of copyright works in both physical and digital forms under the application of international exhaustion doctrine. Moreover, if there is a strong movement of consumer groups in order to legalize parallel imports in other areas such as trademark and patent, it would be possible that, as with copyright, the parallel imports of trademark and patent goods should be allowed, which will be discussed in the following sections.

III. CURRENT DEBATE IN TRADEMARK: CONSUMERS' MOVEMENT IN EUROPEAN UNION TO LIBERALIZE PARALLEL IMPORTS OF TRADEMARK GOODS

As the result of the application of a Community-wide exhaustion, consumers have suffered adverse effects of high prices and low availability of goods. Consumer groups are attempting to pressure the European Union to change the rule to allow parallel imports from outside the Community. This movement is in favor of parallel imports and supports the concept of the international exhaustion doctrine. This issue of exhaustion of

trademark right has been discussed at some length, and it may be possible to change from the Community-wide exhaustion to the international exhaustion. Hence, the following section will explain the effects of the application of the Community-wide exhaustion on consumers and then consumers' encouragement of the application of the international exhaustion doctrine in the area of trademark to allow parallel imports from outside the Community.

A. The Effects of a Community-wide Exhaustion on Consumers

As the result of the *Silhouette* decision, the ECJ decision that holding Member States could not apply the international exhaustion doctrine, the EU market was shut from outside parallel imports under the strong implementation of the Community-wide exhaustion.⁶⁷⁸ This circumstance causes many effects on consumers in terms of product price and availability in their domestic market. Although the European Community has relied on a concept of single market, the big price disparities remain, as compared between one Member State and the other Member States or between Member States and non-community countries. For example, the price of Levis jean in the European Union is higher than the price in the United States.⁶⁷⁹ The high margin of price disparities appeals to the parallel importer's attention to arbitrage in price difference.

⁶⁷⁸ However, in the *Silhouette* case by failing to address the circumstances in which consent can be implied, the ECJ has left it open for member states to determine this issue based on their own national laws, which will lead to disparity as later recognized in the *Davidoff* and *Levi* cases.

⁶⁷⁹ See Parallel Imports: Hardly the Full Monti, *The Economist* February 28-March 5, 1999, available at <http://www.wright.edu/~tdung/parallel-imports.htm> (visited Nov. 16, 2002) "French 501s cost more than twice as much as American ones. ... Legalising parallel imports would benefit European consumers." ; The retail price of Levis's 501 jeans in a British department store is around £45 (\$70) but the price in Tesco's supermarkets is £30 (\$48). The source of these parallel import goods is from Eastern Europe, Asia, and the

Although the European Community established the Community-wide exhaustion as the community legal standard in a Council Directive 89/104/EEC, there are some national court decisions in favor of parallel import under the concept of implied consent. The outcome of those decisions is similar to the application of international exhaustion. In the United Kingdom, wholesalers and retailers, as parallel importers, actively imported low price products from outside the Community for the consumers' benefits, but the brand owners brought the lawsuit to the court in order to stop the parallel imports on the grounds of trademark infringement. In the *Davidoff* and *Levi* cases,⁶⁸⁰ the U.K. court decided in favor of parallel importers by ruling that in case of an absence of restriction clauses on importation, it seems that importer as a buyer had obtained an implied consent from the trademark owner to import into the United Kingdom. However, those cases were brought to the European Court of Justice to clarify the concept of consent. The ECJ ruled in favor of trademark owners, holding that the consent may be either implied or express, but mere silence cannot be deemed as consent, and consent should be 'unequivocal.'⁶⁸¹ As a result of the ECJ decisions, the U.K. High Court finally decided in favor of the trademark owners. In other words, it seems that via broad interpretation in the concept of consent, the U.K. attempts to open the market to parallel imports from outside the Community for consumers' benefit in terms of lower prices and more availability. But the ECJ still strictly restrains those movements by the limitation on the

United States. See William Shade of Gray: American Brand Names in the British Gray Market, available at <http://www.geocities.com/williambdnewton/graymarket.htm> (visited Nov. 16, 2002)

⁶⁸⁰ See *Zino Davidoff SA v. A&G Imports Ltd.*, [1999] 3 All ER 711 (Ch.D.), *Levi Strauss (UK) Ltd. v. Tesco Store*; and *Levi Strauss & Co and Levi Strauss (UK) Ltd. v. Costco Wholesale UK Ltd.*

⁶⁸¹ See *Joined Cases C-414/99, C-415/99 and C-416/99, Zino Davidoff SA v. A&G Imports, Levi Strauss & Co Ltd, Levi Strauss (UK) Ltd v. Tesco Stores, Tesco plc and Costco Wholesale UK Ltd.*, Judgment on 20 November 2001. The summary of this judgment is provided in Press Release No 58/01 of Press and Information Division, available at <http://europa.eu.int/cj/en/cp/cp01/aff/cp0158en.htm>. (visited Feb. 27, 2002).

interpretation of implied consent that may be used as the back door to the international exhaustion doctrine.

B. The Consumer and Political Movements for Proposing the Application of International Exhaustion Doctrine in the Area of Trademark

According to the strong commitment of the ECJ in the Community-wide exhaustion as mentioned earlier, it appears that the way to change from Community to international regime of exhaustion doctrine cannot succeed in the judiciary section. The most effective way would be a political scheme, with the support of the consumers' movement and their governments, in order to change the current Community regime as mentioned in the following discussion.⁶⁸²

In the European Community, the issue of trademark exhaustion has been discussed in the Internal Market Council because the consumer groups have complained that EU trademark owners use the Community-wide exhaustion to bar parallel imports from outside the Community in order to maintain higher prices on the EU market.⁶⁸³ In

⁶⁸² See Sabago Puts Pressures Back on Politicians, *MANAGING INTELLECTUAL PROPERTY*, Issue 8 May 1999 (London) at 5. (mentioning that "amidst growing pressure for change, the Advocate General gave a clear indication that the Court's hands are tied when it comes to interpreting the Trade Mark Directive, and any change to the law must come from Europe's politicians.")

⁶⁸³ See Europa, Communique from Commissioner Bolkestein on the Issue of Exhaustion of Trade Mark Rights, available at http://europa.eu.int/comm/internal_market/en/indprop/tm/comexhaust.htm (visited Nov. 16, 2002). [hereinafter Europa, Commissioner Bolkestein] (stating "At the Internal Market Council on May 25, 2000, the Ministers had an exchange of views on the basis of the outcome of recent discussions at expert level. At this meeting Commissioner Bolkestein informed the Member States' Ministers that the Commission has, at this stage, decided not to propose a change to the current Community-wide exhaustion regime. For Member States strongly supported the Commission approach, while eight Member States regretted the Commission's position and emphasized the need for a change. The remaining Member States did not express a position on this issue."); and also see Europa, Exhaustion of trademark Rights: Commission Organises Meetings with Member States and Interested Parties, available at http://europa.eu.int/comm/internal_market/en/indprop/tm/185.htm (visited Dec. 11, 2002). [hereinafter Europa, Exhaustion of Trademark]

1999, the European Commission arranged a meeting with Member States and interested parties on the issue of trademark exhaustion doctrine and the possible consequences of changing from Community-wide to international exhaustion. The Commission appointed the National Economic Research Associates (NERA) in London to study “the economic consequences of the choice of regime of exhaustion in the area of trademarks.” The NERA Report revealed that by considering the complex issue, a change from Community to international exhaustion would affect not only the prices but also other aspects, such as the product availability, distribution agreement, and market segmentation.⁶⁸⁴ The Report concluded that changing to the international exhaustion doctrine might slightly reduce the product price and would not outweigh the adverse consequences, such as an impact on product quality or after-sales service and employment in Europe.⁶⁸⁵

Consequently, after considering the argument of both proponents and opponents of change,⁶⁸⁶ on May 25, 2000 at the Internal Market Council, Commissioner Bolkestein notified the Member States’ Minister that, at this stage, the Commission had decided not

⁶⁸⁴ See The National Economic Research Associates (NERA), *The Economic Consequences of The Choice of Regime of Exhaustion in the Area of Trademarks*, 8 February 1999 (London). [hereinafter *The NERA Report*]

⁶⁸⁵ *Id.* at 5-7 and 10.

⁶⁸⁶ The United Kingdom, Sweden, Belgium, Finland, Ireland, Denmark, and the Netherlands supported a change from current Community-wide to international exhaustion doctrine. In contrast, France, Germany and Italy opposed to the relaxation of the current regime. The opponents of change suggest that an international exhaustion would reduce the economic value of trademark rights, damage innovation, decrease investment and increase in the rate of piracy as the result of a strong link between parallel trade and counterfeiting. The proponents of change argument concentrate mainly on consumer benefits in terms of low prices and wider product availability. See Europa, *Exhaustion of Trademark*, *supra* note 683; and also see Steve Seidenberg, *Levi’s Blues: Brand Owners Beware: A Recent Ruling May Wash the European Import Market Gray*, IP Worldwide, July 25, 2001, available at <http://lists.essential.org/pipermail/pharm-policy/2001-July/001327.html> (visited Nov. 16, 2002); The NERA Report, *supra* note 684; and also see Stephenson Harwood, *Parallel Imports and the Exhaustion of Rights: The World Focus*, available at <http://www.shlegal.com/docs/parallelimports.pdf> (visited Mar. 6, 2002) (critiquing the NERA report that “The report is explicitly not intended to provide definitive interpretations of the relevant legislation or comment on particular legal issue; nor is it intended to develop economic arguments for or against particular points of view on the subject of international exhaustion, or to adjudicate on the case for or against the extension of an EEA exhaustion regime.”)

to propose a change from the current Community-wide to the international exhaustion doctrine. Doing so would not lead to a significant reduction of prices but rather would damage trademark owners, reduce investments and jobs in the EU, and decrease a competitive advantage of EU to non-member countries.⁶⁸⁷

Nevertheless, the issue of Community-wide exhaustion regime still remains controversial in the European Union because the consumer groups, wholesale and retailer groups and some Member States, particularly the United Kingdom and Sweden, continually attempt to pressure the European Union to change the exhaustion doctrine from the Community-wide to international regime. For example, in the Eight Report of U.K.,⁶⁸⁸ the U.K. government challenged the Community-wide exhaustion resulting from the *Silhouette* decision and lobbied the Commission to revise the Trademark Directive. The Eight Report pointed out that consumers would benefit from repealing the prohibition on parallel imports of goods initially marketed outside the EEA and introducing the concept of the international exhaustion doctrine.⁶⁸⁹ The U.K. government, with the support of the Swedish government, strongly recommended that the EU change

⁶⁸⁷ See Europa, Commissioner Bolkestein, *supra* note 683.

⁶⁸⁸ See The Eight Report from the Trade and Industry Committee (Session 1998-99) on Trade Marks, Fakes and Consumers (HC 380) published on 8 July 1999, available at <http://www.parliament.the-stationery-office.co.uk> (visited Dec. 16, 2002) [hereinafter The Eight Report]

⁶⁸⁹ *Id.* at para. 90. "In our opinion, in the area of clothing and shoes, perfumes and toiletries, and motor vehicles, the potential consumer benefit of international exhaustion of trade mark rights outweigh the dis-benefits. In some sectors the consumer benefits may, however, be outweighed by the problems that international exhaustion would bring with it; particularly in the pharmaceutical and music industries. Whilst a seamless approach to international exhaustion would be preferable, we do not see the justification for retaining EEA-wide exhaustion for trade mark rights for all sectors in order to protect one or two sector. We recommend that the Government and the European Commission work towards adopting of a broad principle of international exhaustion of trade mark rights, allowing grey imports of goods but affording exceptional protection to those sectors where such a principle could be shown to have severe detrimental effects. Such a flexible approach would not only lead to cheaper goods for consumers, but would address the different needs of different sectors." (emphasis added)

from the Community-wide to the international exhaustion for the sake of the EU consumers.⁶⁹⁰

The Consumers in Europe Group (CEG) pointed out that benefits to consumers will diminish if the legal protection of the IPRs extends too far and restricts competition. The restriction on parallel imports from outside the Community causes adverse effects on consumers in terms of high price and less product choice. The international exhaustion regime should introduce greater competition and consumer choice and a lower product price.⁶⁹¹ On behalf of wholesale and retailer, the European Parallel Importers Coalition (EPIC) stands for a change from the Community-wide to the international exhaustion regime relating to trademark law because the current EU position is contrary to consumer interests, international law, and allows abuse of trademark law.⁶⁹² Moreover, the Foreign Trade Association (FTA) believes that the restriction of parallel imports of trademarked goods is a non-tariff barrier to trade that distorts the internal market. The international exhaustion is a major important issue for the future development of a global market

⁶⁹⁰ In April 1999, the governments of Sweden and the United Kingdom releases a five-country survey, which showed that the prices for many consumer items are significantly lower in the United States than in many EU countries. In May at a European conference of consumer ministers, representatives from the UK and Sweden pointed to the report as evidence that EU law should be changed in order to allow more parallel imports by recognizing international exhaustion instead of Community-wide exhaustion in area of trademark. See Steve Seidenberg, *Levi's Blues: Brand Owners Beware: A Recent Ruling May Wash the European Import Market* Gray, IP Worldwide, July 25, 2001, available at <http://lists.essential.org/pipermail/pharm-policy/2001-July/001327.html>. (visited Nov. 16, 2002); The Swedish Government, in support of international exhaustion, pointed out that by focusing on the function of trademark, if the function is to indicate origin, it is not part of that function to enable the owner to divide up the world market and exploit price differentials. So an international exhaustion can promote price competition and benefit to consumers by promoting price competition. See Norman, *supra* note 269, at 163.

⁶⁹¹ See The Eight Report, *supra* note 688, at Appendix 3: Memorandum Submitted by Consumers in Europe Group.

⁶⁹² See The European Parallel Importers Coalition (EPIC), *The Case for Re-introducing Global Trademark Exhaustion in EU Legislation*, Jan. 2001, available at http://www.europarl.eu.int/hearings/20010410/juri/5_frenkel.pdf (visited Nov. 16, 2002)

without protectionist barriers. Thus, the FTA favors the application of international exhaustion doctrine and advises the EU to adopt it.⁶⁹³

The draft Report of MEP Hans Peter Mayer, the European Parliament's rapporteur for trademark law, issued on February 15, 2001, advocated a properly thought out transition from the Community-wide exhaustion to the international exhaustion and called on the Commission to submit legislative proposals to this effect.⁶⁹⁴ In the interview, Hans Peter Mayer (EEP-ED, Germany) pointed out his concerns on "the question of exhaustion and the abuse of trademark law for market segmentation" and suggested "price differences, to the disadvantage of EU consumers, must be eliminated."⁶⁹⁵ He mentioned "how increased consumer trading on the Internet has led many people to question the legitimacy of current EU trademark laws,"⁶⁹⁶ and finally he said on the interview that "we need to promote international exhaustion for branded goods and eliminate the Commission's proposal to maintain the existing EU-wide exhaustion."⁶⁹⁷

⁶⁹³ See Foreign Trade Association (FTA), Exhaustion of Trademark Rights, Press Release Brussels, March 2001, available at http://www.fta-eu.org/en/new/press/004_ftapress_en.pdf (visited Nov. 16, 2002).

⁶⁹⁴ See Draft Report on The Problem of the Exhaustion of Trademark Rights (SEC (1999) 2033-C5-0354/2000- 2187/2000(COS)) Committee on Legal Affairs and the Internet Market, Rapporteur: Hans-Peter Mayer, Feb. 15, 2001, European Parliament., available at <http://www.europarl.eu.int/meetdocs/committees/juri/20010227/431875en.doc> (Visited Dec. 18, 2002) [hereinafter Draft Report]

⁶⁹⁵ *Id.* at 9 on Explanatory Statement. ("Internet trading is a significant new factor. Consumers can search the Internet to find the best deals throughout the world and prices will fall. The present exhaustion arrangements could hamper this development."); and also see Shane Cogan, Trademark Law Goes Public: Interview with Hans Peter Mayer MEP (EPP-ED, Germany), Parliament Rapporteur, Vol. 1 Issue 6, 9-13 April 2001 at 1, available at <http://www.psoe-pe.org/doc/articulos/7/Rapporteur.pdf> (visited Dec. 15, 2002)

⁶⁹⁶ See Cogan, *supra* note 695, at 1.

⁶⁹⁷ *Id.* at 12.; There is an interesting criticism in the Commission Paper stating that "The Commission Paper has not sufficiently considered recent developments in international trade and telecommunications; the impact of illegal parallel imports on consumers' behavior has also been underestimated since parallel imports would attract more affordable imports of products in the EU market, thereby attracting consumers that would not normally be able to afford these goods." See Business Alert-EU, Issue 5, Mar. 3, 2000, available at <http://www.tdctrade.com/alert/eu0005a.htm> (visited Apr. 1, 2002).

C. Conclusion

With the strong movements of advocates of parallel imports, it is possible in the future that the EU position may change from the current the Community-wide exhaustion regime to the international exhaustion regime. Refusing the international exhaustion causes the portioning of the international market and price discrimination strategies all the way down to retail trade.⁶⁹⁸ It is not consistent with the Community's declared aim of free competition and free trade. So a rethinking of the EU position on international exhaustion is needed.⁶⁹⁹ In other words, a change to the international exhaustion regime would lower prices and increase product availability and consumption in the Community. The objection to the international exhaustion seems to conflict with current global market, free competition and EU consumer's interest.

IV. CURRENT DEBATE IN PATENT: PARALLEL IMPORTS IN PHARMACEUTICAL PRODUCTS

A. Introduction

The current TRIPs treatment on parallel imports is a good sign for developing countries. Countries are allowed to choose the exhaustion doctrine rule that will apply to parallel imports. This is beneficial to developing countries, as the TRIPs Agreement does not require developing countries to apply a restrictive rule on parallel imports. However, it would be more beneficial to developing countries if the TRIPs Agreement specifically

⁶⁹⁸ See Ullrich, *TRIPs: Adequate Protection, Inadequate Trade. Adequate Competition Policy*, 4 PAC. RIM L. & POL'Y J. 192 (1995), citing in Soltysinski, International Exhaustion of Intellectual Property Rights under the TRIPs, the EC and the Europe Agreements, 1996 GRUR Int. 316, 321.

⁶⁹⁹ See Stamatoudi & Torremans, *supra* note 290, at 141.

designated that the international exhaustion as the applicable international legal standard, which allows parallel imports and supports the free trade.⁷⁰⁰ The current TRIPs Agreement incorporates strong patent protections and the rigorous restriction on compulsory licensing for pharmaceutical products. In relation to drug patents, liberalization on the parallel imports of pharmaceutical products enables developing countries to obtain medical drugs that are otherwise priced higher than poor patients can afford.⁷⁰¹ In other words, allowing parallel imports in pharmaceutical products lessen the effect of strong patent protections and the rigorous restriction on compulsory licensing because the strong patent protection with limited utilization of compulsory licensing causes an adverse effect on developing countries in terms of high prices and low availability of essential drugs.

Under the TRIPs Agreement, there are two possible solutions for increasing access to essential drugs: compulsory licensing and parallel imports. However, under the current provision on compulsory licensing, developing countries cannot continually rely on compulsory licensing to solve the problems of low availability and high prices of essential drugs. A compulsory licensing solution is complicated and difficult for

⁷⁰⁰ Parallel imports should be allowed for developing countries since parallel import drugs are lawful and not dangerous like counterfeit drugs. Restriction on parallel imports is unfair to consumers, especially in poor countries. Pharmaceutical industries already receive a benefit from the first sale of the product. To allow drug companies to stop parallel imports permits the companies to capture a double benefit at the expense of poor people. Allowing parallel imports not only lessens the problem of affordable access, but also reduces the volume of trade in counterfeit drugs because consumers will tend to buy genuine parallel imported drugs over fake versions. In addition, the parallel imports of drugs do not destroy the patent owner's goodwill if all drugs are produce under the same standard with the same quality. If the produce is not different, it is no risk of damage to the patent owner's reputation.

⁷⁰¹ See CORREA, *supra* note 143, at 36; Regarding humanitarian concerns, drugs are not like other products since medications are considered a necessary thing for all humans. Indeed, increasing access to essential medicines, such as the drugs for treatment of HIV/AIDS, benefits the entire global community. Many diseases are contagious and fatally dangerous, such as malaria, tuberculosis and HIV/AIDS. The more available affordable drug treatments are the less risk of infection world-wide. Arguments for liberalizing parallel imports of drugs focus on the consumers, social welfare and health policy concerns.

developing countries in part, because the present provision provides many conditions that must be satisfied before a compulsory licensing can be issued. It was not until after the Doha Conference that developing countries began utilizing compulsory licensing and parallel imports without fear of the U.S. trade sanction. The Doha Ministerial Declaration and Special Declaration on Public Health stated that in cases of a public health crisis, developing countries can issue compulsory licensing or/and allow parallel imports.

Although after Doha, the use of compulsory licensing became more possible, it is not a good solution for countries with low production technology because they do not have the infrastructure to actually make drugs. In such countries, parallel imports are considered a better scheme to fulfill the need of domestic patients. Developing countries may choose to allow parallel imports under the international exhaustion doctrine and obtain low price drugs from outside sources. Drug prices may be cheap in some countries as the result of a compulsory licensing or relaxing patent law. It must be stressed that compulsory licensing or parallel imports standing alone would not be enough to address the problem, but the two schemes together provide a workable solution.

This section will first explain the strengthening of patent protection under the TRIPs Agreement and its affect on developing countries. Also addressed is how compulsory licensing and parallel imports can solve the problem of high prices and low availability of essential drugs. The section ends with enumerating issues that should be solved by the TRIPs council in the near future.

B. Strengthening Patent Protection and the Effects on Developing Countries

The pharmaceutical industries require strong patent protection on global scale because these industries need to secure sufficient revenue from market sale to offset their research and development costs.⁷⁰² The patent protection allows them to capture royalty revenues from their innovation.⁷⁰³ The strong global patent protection enables pharmaceutical industries to maintain a profit. Seventy-five percent of the world's pharmaceutical market is dominated by the United States, the European Union, and Japan.⁷⁰⁴ Developing countries have balked at patent protection for drugs because the patent protection would increase drugs prices for consumers in their countries. The greater increase in price, the less access citizens in developing countries will have to pharmaceutical drugs. Consumers in low-income countries might not have enough income to afford the patent drugs. The issue of affordable access to drugs and treatment constitutes a matter of life or death.⁷⁰⁵ Developing countries take the position that

⁷⁰² See Gerald J. Mossinghoff, Endnote, *Research-Based Pharmaceutical Companies: The Need for Improved Patent Protection Worldwide*, 2 J.L. & TECH. 307, 308-10 (1987)(explaining that pharmaceutical research is extremely costly and time consuming. Inadequate patent protection not only affects the pharmaceutical industry's research efforts, but also has a negative effect on the U.S. trade.)

⁷⁰³ See Stuart R. Walker, Symposium, *Global Responses: The Search for Cures in the Development of Pharmaceuticals*, 5 IND. J. GLOBAL LEG. STUD. 65, 65-78 (1997).; and also see Rosemarie Kanusky, Symposium, *Intellectual Property: Comment: Pharmaceutical Harmonization: Standardizing Regulations Among The United States, The European Economic Community, and Japan*, 16 HOUS. J. INT'L L 665, 667 (1994); see William Davis, Comment, *The Medicine Equity and Drug Safety Act of 2000: Releasing Gray Market Pharmaceuticals*, 9 TUL. J. INT'L & COMP. L. 483, 506 (2001) (pointing out that public authorities cause pharmaceutical price distortion and there are differences among national regulatory policies and health care systems.); and also see MASKUS, *supra* note 38, at 53-54. (mentioning that the national policy and regulation affects on the price of products.)

⁷⁰⁴ The EC, U.S. and Japan Sign Commitment to Standardize Pharmaceutical Tests, 8 INT'L TRADE REP. (BNA) 1702, 1702 (Nov. 20, 1991).

⁷⁰⁵ See Correa, *Public Health*, *supra* note 162, at 3; see MASKUS, *supra* note 38, at 6; and also see Jayashree Watal, *Pharmaceutical Patents, Prices, and Welfare Losses: A Simulation Study of Policy Options for India under the WTO TRIPs Agreement*, 23 THE WORLD ECONOMY 733-52 (2000).

increased drug prices from providing patent protection will have a considerable impact on the access to drugs, which will negatively affect public health.

Developed countries have attempted to encourage and force developing countries to provide sufficient patent protection for drugs. Before the emergence of the TRIPs Agreement, many developing countries had excluded drugs from patent protection.⁷⁰⁶ The U.S. has played a particularly important role in pushing many developing countries to strengthen their patent protection, through the U.S. threat and the use of trade sanctions.⁷⁰⁷ The Pharmaceutical Manufacturers Association (PhRMA) brought the issue of inadequate patent protection for pharmaceutical products in developing countries to the USTR's attention in order to have trade sanction section 301 imposed.⁷⁰⁸ As the

⁷⁰⁶ For example, before 1992, drugs were not protected under the Thai Patent Act of 1979 because under the Act drugs could not be patented. In 1988, under the passage of the Omnibus Trade and Competitiveness Act, Thailand was subjected to U.S. pressure to provide the patent protection for drugs. In 1991, the USTR moved Thailand from a priority watch list to a priority foreign country, as an egregious violation of U.S. intellectual property rights. As the result of international pressure, the Thai government amended its domestic patent law in 1992. The Patent Act of 1992 was passed on February 27, 1992, under which drugs are protected. See Thomas N. O'Neill, *Intellectual Property Protection in Thailand: Asia's Young Tiger and America's "Growing" Concern*, 11 U.P.A.J. INT'L BUS. L. 603, 616 (1990); In Brazil, from 1969 to 1994, Brazil did not provide patent protection for drugs. The Brazilian government believed "that the elimination of patent protection would create a strong domestic pharmaceutical industry in the face of the dominant foreign multinational competitors." See Christopher S. Mayer, Notes & Comments, *The Brazilian Pharmaceutical Industry Goes Walking from Ipanema to Prosperity: Will the New Intellectual Property Law Spur Domestic Investment?*, 12 TEMP. INT'L & COMP. L.J. 377, 378-79 (1998); Prior to TRIPs Agreement, some countries, particularly India, only provided the patent protection for the pharmaceutical process, but not for the product. This allowed domestic pharmaceutical industry to legally produce generic drugs by using similar substances as patent drugs, but utilizing a different process. This helped make essential drugs more accessible and affordable for domestic patients. Many countries denied patent protection for pharmaceuticals. Argentina only provided the process patent, but not the product patent for pharmaceuticals. Mexico denied both product and process patent for pharmaceuticals. However, after the TRIPs Agreement, all members are obligated to provide patent protection for pharmaceutical products. See Mossinghoff, *supra* note 702, at 312-14.

⁷⁰⁷ See Robert Weissman, *A Long Strange TRIPS: The Pharmaceutical Industry Drive to Harmonize Global Intellectual Property Rules, and the Remaining WTO Legal Alternatives Available to Third World Countries*, 17 U. PA.J. INT'L ECON. L. 1069, 1083 (1996). [hereinafter Weissman, *A Long Strange TRIPS*]

⁷⁰⁸ See PhRMA Special 301 Submission 2001, available at <http://www.phrma.org>. (visited Aug. 12, 2002); see Stefan Kirchanski, *Protection of U.S. Patent Right in developing Countries: U.S. Efforts to Enforce Pharmaceutical Patents in Thailand*, 16 LOY. L.A. INT'L & COMP. L.J. 569 (1994) (mentioning that on April 26, 1991, the USTR cited India, the People's Republic of China, and Thailand for their failure to provide the adequate intellectual property protection.)

result of the strong pressure of developed countries, the TRIPs Agreement makes it clear that WTO members have to provide patent protection for any fields of invention, including pharmaceutical products. Consequently, each member is obligated to protect pharmaceutical products under its domestic patent law in accordance with the TRIPs standard.

Recently under the TRIPs Agreement Article 27.1, all WTO members are obligated to provide patent protection in all fields of technology, which includes pharmaceuticals. Members cannot make exclusions or exceptions to the patent protection even for the “essential medicines” listed by the World Health Organization (WHO).⁷⁰⁹ The TRIPs Agreement essentially gives drug patent owner the exclusive rights on a worldwide scale. In particular, distribution and importation rights allows the patent owner to segregate the market based on territory, and to ultimately control the availability of those patent goods in each market. Such control enables a monopoly in each national market segment to effectively increase the drug price.⁷¹⁰ Providing patent protection for pharmaceuticals causes price increases and limits access to essential drugs on consumers in developing countries.⁷¹¹ Without a shred of doubt, the TRIPs Agreement has resulted

⁷⁰⁹ See Correa, *Public Health*, *supra* note 162, at 9.

⁷¹⁰ See F. Michael Scherer & Jayashree Watal, Post Trips Options for Access to Patented Medicines in Developing Countries 11 (WHO Jan 2001), available at http://www.cmhealth.org/docs/wg4_paper1.pdf. (visited Aug. 15, 2002) (pointing out that increased patent protection leads to higher drug prices).; See The United Nations, Report of the High Commissioner of the Human Rights Commission on Economic, Social and Cultural Rights, The Impact of the Agreement on Trade-Related Aspects of Intellectual Property Rights on Human Rights, UN Doc E/CN.4/Sub.2/2001/13 at 14, para 44 (2001). (The UN study reports that the HIV treatment “AZT” costs 48 USD per month in India, where the drug is not protected under patent law, as compared to 239 USD in the United States, where patent protection is provided for drugs. In addition, the cost of 150 mg of the HIV drug fluconazole is 55 USD in India, as compared to 697 USD in Malaysia, 703 USD in Indonesia, and 817 USD in the Philippines.)

⁷¹¹ A number of economic studies presented that, in area of pharmaceuticals, patent protection in developing nations would lead to price increases, higher royalty, profit payments abroad and greater market control by foreign firms. See The TRIPs Agreement and Pharmaceuticals: The Report of an ASEAN Workshop on the TRIPs Agreement and its Impact on Pharmaceuticals, Jakarta, 2-4 May 2000. [hereinafter

in increased drug prices, limited access to essential drugs, and monopolies in domestic market, which developing nations perceive as dangerous and unacceptable.⁷¹²

In the past, developing countries' governments sometimes used a compulsory licensing method to control drug prices and encourage domestic market competition. A compulsory license was issued to local manufacturers to produce essential drugs with affordable prices and more availability for domestic patients.⁷¹³ Before TRIPS, developing countries were more at liberty to issue a compulsory licensing. However after TRIPs, it appears to be more difficult for developing countries to rely on compulsory licensing because under Article 31 of TRIPS requires a number of conditions and restrictions that must be met before issuing a compulsory licensing. The following section discusses the restrictions on compulsory licensing.

C. WTO/TRIPS Safeguards for Public Health

As a result of the concerns over affordable pricing and access of medicinal drugs, the TRIPs Agreement provides some safeguards to aid developing countries in dealing

ASEAN Workshop on TRIPS and Pharmaceuticals]; see World Health Organization, available at <http://www.who.int> (visited Aug. 15, 2002) (clarifying that in accordance with WHO, access to essential drugs entails three elements: (1) therapeutic access (the discovery and development of proper treatments), (2) physical access, and (3) financial access.); see World Health Organization, *Globalization, TRIPS and Access to Pharmaceuticals* 4 WHO Policy Perspective on Medicines No. 3 (March 2001), available at http://www.who.int/medicines/library/edm_general/6paggers/PPM03%20ENG.pdf (visited Oct. 7, 2002) [hereinafter *TRIPS and Access to Pharmaceuticals*] (pointing out that the enforcement of WTO rules on patent protection will have a negative effect on local manufacturing of generic drugs and TRIPS does not seem to encourage adequate research and development in developing countries for diseases such as tuberculosis and malaria. Developed countries may be pressuring developing countries to implement patent law that go further than the TRIPs obligations.)

⁷¹² See Willem A. Hoyng & Florika Fink-Hooijer, *The Patent Term of Pharmaceuticals and the Legal Possibilities of Its Extension*, 21 IIC 161, 162 (1990); and also see Scherer & Watal, *supra* note 710.

⁷¹³ See JAYASHREE WATAL, *INTELLECTUAL PROPERTY RIGHTS IN THE WTO AND DEVELOPING COUNTRIES* 317 (2001).

with public health concerns. The safeguards include the exclusion of patentability, a compulsory licensing and parallel imports.

1. The Exclusion of Patentability

There are two approaches under TRIPs, which pharmaceuticals might feasibly be excluded from patent protection within limited circumstances and justification. These exceptions allow developing countries to maintain their previous stances on pharmaceutical patents. The first exception is *ordre public* under TRIPS Article 27.2, which permits exclusion from patentability when necessary to protect human health.⁷¹⁴ It is possible for WTO members, particularly developing countries, to deny a drug patent in order to produce and market the drug through a non-commercial entity. However, the developing country is required to demonstrate that its actions were “necessary” to protect public health.⁷¹⁵ The second exception is Article 8.1, which potentially authorizes the exclusion of pharmaceuticals from patent protection for public health reasons. Nevertheless, any application of an exception to protect rights is subjected to a necessity technology and consistency test and must be consistent with other obligations under the TRIPs Agreement.⁷¹⁶

⁷¹⁴ See TRIPs Art. 27.2, *supra* note 2.; see CORREA, *supra* note 143, at 62. (pointing out that the text of the TRIPS Agreement utilizes the concept of *ordre public* as one of the grounds for providing an exception to patent rights. This concept may be interpreted as being narrower than “public order” or “public interest.” However, WTO Member countries flexibly define which situations are covered under their own public value perception because there is no generally accepted notion of *ordre public*.)

⁷¹⁵ See Weissman, *A Long Strange TRIPS*, *supra* note 707, at 1100-01.; and also see CORREA, *supra* note 143, at 9.

⁷¹⁶ See TRIPs, *supra* note 3, art. 8.1; see Correa, *Public Health*, *supra* note 162, at 10-11 (pointing out that the issue is whether an exception to patentability may be justified under the general GATT exception to trade disciplines, article XX(b), when the exception is necessary to protect public health. Currently the article XX(b) has been interpreted and applied rather narrowly in GATT/WTO case law and it is doubtful whether GATT article XX(b) would apply in the TRIPS context.); see ERNST-ULRICH PETERSMANN, *THE*

2. Compulsory Licensing and Parallel Imports

Besides the exclusion of patentability exception, there are other alternative approaches: compulsory licensing and parallel imports. In order to grant a compulsory licensing, Article 31 of the TRIPs Agreement provides some conditions that members have to meet before a compulsory licensing is issued.⁷¹⁷ Even though the TRIPs Agreement allows developing countries to use a compulsory licensing, it limits the nation's power to issue a compulsory license.⁷¹⁸ For example, the compulsory license should not unreasonably conflict with the normal exploitation and not unreasonably prejudice the interests of patentee. Additionally, a product made under compulsory licensing is supplied predominantly to domestic market under Article 31(f). In limited circumstance, members may issue a compulsory license to produce product without the patent holder's consent in some situations.

GATT/WTO DISPUTE SETTLEMENT SYSTEM: INTERNATIONAL LAW, INTERNATIONAL ORGANIZATIONS AND DISPUTE SETTLEMENT (1997); and also see MICHAEL TREBILCOCK & ROBERT HOWSE, *THE REGULATION OF INTERNATIONAL LAW* 155-65 (2nd ed. 1999).

⁷¹⁷ Compulsory licensing is based on the balancing of conflicting interest between intellectual property owners and consumers. Consumers have to pay higher prices for patented goods due to patent royalty and it is illegal to access new technology without paying royalty. Compulsory licensing is the only legal way to access new patents with a reasonable patent royalty and without constituting a patent infringement.

⁷¹⁸ See TRIPs art. 31, *supra* note 2; see Verma, *supra* note 86, at 344-355.(mentioning that the exception should not unreasonably conflict with the normal exploitation and not unreasonably prejudice the interests of the patentee. The TRIPs exception is open to interpretation and is applied differently by each nation. For example, a nation must determine whether the proposed user has made efforts to obtain authorization from the right holder on reasonable commercial terms and conditions, and such efforts have been unsuccessful within a reasonable period of time under Article 31 (b). Under Article 31(h), the patent holder is to be paid adequate remuneration. However, it is difficult to determine the economic value of authorization. One means of calculation is to determine the economic value received by the grantee. Article 31 (h) provides that " the right holder shall be paid adequate remuneration of each case, taking into account the economic value of the authorization." The scope and duration must be limited to the purpose of the compulsory license and the license must be non-exclusive and non-assignable, and terminated upon certain circumstances.); and also see Weissman, *A Long Strange TRIPS*, *supra* note 707, at 1114.

For pharmaceuticals, a compulsory license has been used to stimulate price-lowering competition and to ensure availability of needed medicines for developing countries.⁷¹⁹ However, the conditions mentioned earlier must be met before issuing a compulsory license, which may impede a government's ability to stimulate or encourage affordable pharmaceutical production.⁷²⁰ Moreover, the subject matter in relation to a compulsory license can be brought to the WTO dispute settlement system in case that a nation issues a compulsory license without complying with requirements under Article 31 of the TRIPs Agreement.

In pharmaceuticals, there are two types of technology capacities: innovation of a new drug and manufacturing of drugs. A country's capacity to develop pharmaceuticals is directly related to its degree of economic development.⁷²¹ In many cases, developing countries allowed to issue compulsory licensing to produce patent drugs do not have

⁷¹⁹ For example, Zimbabwe could issue a license to a local company for an HIV/AIDS drug made by Bristol-Myers Squibb. The Zimbabwe manufacture would produce the drug for sale in Zimbabwe under a generic name and pay a reasonable royalty to Bristol-Squibb. See Robert Weissman, *Aids and Developing Countries: Democratizing Access to Essential Medicines*, *Foreign Policy in Focus* Vol. 4, No.23, Aug. 1999 at 1, available at <http://www.foreignpolicy-infocus.org/briefs/vol4/v4n23aids.html>. (visited Oct. 7, 2002). [hereinafter Weissman, *Aids and Developing Countries*]

⁷²⁰ In stances where parallel imports are not available, the government may not concur with a party's request for a compulsory license. Issuance of a license depends on the government's deliberation that local consumers need such drugs and evidence supporting the necessity for issuing a compulsory license. This may cause uncertain outcomes.

⁷²¹ See P. Challu, *The Consequences of Pharmaceutical Product Patenting*, 15 *WORLD COMPETITION* 77 (1991); see J. Davidson Frame, *National Commitment to Intellectual Property Protection: An Empirical Investigation*, 2 *J.L. & TECH.* 209, 219, 223 (1987) (clarifying that the industrial countries with a strong commitment to intellectual property protection have the technological capacity to compete effectively in global market. Developing countries with a weak intellectual property protection desire to develop the technological capacity, but must support intellectual property protections in order receive technology transfers from developed countries.); Developing countries considered patent protection as an impediment to accessing new technology at low cost. The protection and enforcement of IPRs should contribute to the transfer and dissemination of technology and support technological innovation, to the mutual advantage of producers and users. IPRs protection should also be carried out in manner conducive to social and economic welfare by striking a balance between the rights and obligations of producers and users. See Agreement on Trade-Related Aspects of Intellectual Property Rights, pmbl.; and also see Howard A. Kwon, Article, *Patent Protection and Technology Transfer in The Developing World: The Thailand Experience*, 28 *GW J. INT'L L. & ECON.* 567, 570 (1995).

sufficient technology to produce the drugs. Technology for innovating and producing pharmaceutical products is almost exclusively available in developed countries, not developing countries.⁷²² However, some particular developing countries such as India and Brazil who may currently have ability to produce pharmaceuticals, and to innovate some new drugs but not have ability to innovate all essential drugs. Thus, compulsory licensing that permits patent use does not adequately assist developing countries due to limited technology and the inability to obtain the necessary raw materials.⁷²³ Due to such circumstances, parallel imports may be a better alternative.

Parallel imports provide an alternative means for improving access to essential drugs because Article 6 of the TRIPs Agreement states that members are free to decide whether parallel imports are allowable.⁷²⁴ Although Article 28 grants the exclusive right of import to the patent owner, Article 6 enables member to limit the patent holder's right

⁷²² See ASEAN Workshop on TRIPS and Pharmaceuticals, *supra* note 711, at 20. (Based on the degree of development of pharmaceutical technology and industrial production, the United Nation Industrial Development Organization (UNIDO) has categorized 190 nations into 5 groups regarding the world's pharmaceutical industrial. 10 industrial countries have a sophisticated pharmaceutical industry with a significant research base. 12 industrial countries and 5 developing nations have a pharmaceutical industry with some innovative capabilities. 6 industrial countries and 8 developing countries have a pharmaceutical industry capable of producing both therapeutic ingredients and finished products. 2 industrial countries and 87 developing countries have a pharmaceutical industry that can formulate finished products only -from imported therapeutic ingredients. Finally, 1 industrial country and 59 developing countries are without a pharmaceutical industry.); and also see Robert Balance, Janos Pogany & Helmet Forsteiner, *The World's Pharmaceutical Industries: An International Perspective on Innovation, Competition and Policy*, UNIDO (1992).

⁷²³ See Tina Rosenberg, Look at Brazil: Patent Laws are Malleable. Patients are Educable. Drug Companies are Vincible. The World's AIDS Crisis is Solvable, *The New York Times Magazine*, Jan. 28, 2001, available at <http://www.nytimes.com/library/magazine/home/20010128mag-aids.html>. (visited Oct. 16, 2002).; In this case, compulsory license to import might be more useful for developing nations. TRIPs Agreement provides for non-discrimination between locally produced and imported products under article 27:1 and a compulsory license may be granted for importation to satisfy local needs under article 3.1 See TRIPs and Access to Pharmaceuticals, *supra* note 711, at 4.

⁷²⁴ See CORREA, *supra* note 143, at 75-88. (mentioning that according to the interpretation of Article 6 with Article 30, parallel imports in patent drugs are obviously permitted under the TRIPs Agreement. This provision is considerably open to members to define the types of exceptions within the scope of Article 30. For example, the experimental exception, the 'Bolar' exception, and parallel import are reasonably fall within the scope of Article 30.)

under the principles of the exhaustion doctrine.⁷²⁵ Therefore, the determination regarding whether an intellectual property owner can bar parallel imports is a matter of national discretion.⁷²⁶ The nation discretion ruling regarding parallel imports are valid because TRIPs members cannot submit a complaint to the WTO Dispute settlement system. Under Article 6, members are free to adopt either national or international exhaustion and the WTO Dispute Settlement system will not address exhaustion doctrine disputes.⁷²⁷

In brief, based on article 6, members are free to legalize parallel imports without any conditions, which is in contrast to compulsory licensing. Compared to compulsory licensing, parallel imports may be a better solution for developing countries with low drug production technology in order to reduce drug prices and increase access to drugs in domestic market. Allowing parallel imports can effectively increase access to essential drugs for combating the HIV/AIDs epidemic and other essential diseases such as malaria, tuberculosis, and leishmaniasis. The example of AIDs will be used for further analysis and discussion. Certainly, the discussion and analysis in AIDs example can apply to the analysis on other essential drugs as well.

⁷²⁵ See WATAL, *supra* note 713, at 296.(explaining the relation between Articles 28 and 6. The right of importation under article 28, like all other rights of use, sale, importation or other distribution of goods conferred under TRIPS, is subject to the provisions of Article 6. However, Article 6 only removes the issue from arbitration under WTO dispute settlement rules and it does not take away from the absolute right of patent owners to prevent importation by third parties, whether of counterfeit or parallel import goods.)

⁷²⁶ See TRIPS and Access to Pharmaceuticals, *supra* note 711, at 4.

⁷²⁷ See World Health Organization, Globalization and Access to Drug, 24 (1999), available at <http://www.who.int/medicines/library/dap/who-dap-98-9-rev/who-dap-98-9-rev.pdf>. (visited Oct. 7, 2002) [hereinafter Globalization and Access to Drug] (mentioning that to improve the accessibility though parallel importation, members may establish that the exclusive rights of the patent holder may not be claimed in cases where products marketed with that patent holder's consent in any other country are imported. No state may complain of a breach of the agreement on this ground.)

D. HIV/AIDS

The devastation of the HIV/AIDS pandemic has become a serious health issue in many developing countries. Fortunately, HIV/AIDS drugs are available because of innovations by pharmaceutical companies in developed countries. Enforceable patent protection acts as an incentive for developing new medicines.⁷²⁸ People in both developed and developing countries have been infected this disease. However, unfortunately, a number of HIV infected patients in developing countries cannot afford the cost of drugs. Poor patients in developing countries should not be expected to pay the same price that people in developed countries could do. Hence, access to HIV/AIDS drugs has turned out to be a hottest issue regarding to the tensions between global health concerns and patent protection.

High HIV drug prices have resulted from strong patent protections, causing limited access to HIV drugs in many developing nations.⁷²⁹ The AIDS pandemic has

⁷²⁸ See Keith E. Maskus, *Proceedings of The 2002 Conference Access to Medicines in the Developing World: International Facilitation or Hindrance?: Panel #4: Access to Essential Medicines and Affordable Drugs: Ensuring Access to Essential Medicines: Some Economic Considerations*, 20 WIS. INT'L. L.J. 563, 564 and 590 (2002). [hereinafter Maskus, *Access to Essential Medicines*] (pointing out that for the "neglected diseases," such as malaria and leishmaniasis, pharmaceutical companies may allocate very few resources to develop those drugs since incomes in poor countries are excessively low to expect a positive return on their R&D investment. In this case, governments in poor countries should undertake research for their own by asking for funding from rich countries, organization, and NGOs.)

⁷²⁹ For example, in Thailand, there are more than 1 million people infected with AIDS, and less than 5% of the Thai HIV/AIDS patients can afford double antiretroviral therapy. The U.S. pressure on Thailand to provide the patent protection for drugs has made it hard for HIV patients in access to AIDS drugs. See ASEN Workshop on TRIPs and Pharmaceutical, *supra* note 711, at 37; see Rosemary Sweeney, *Comment, The U.S. Push for Worldwide Patent Protection for Drugs Meets the AIDS Crisis in Thailand: A Devastating Collision*, 9 PAC. RIM L. & POL'Y 445, 447(2000).; Africa has the highest explosion of AIDS and the Caribbean has the second-highest rate of AIDS infection. In Eastern Europe and the former Soviet Union, the number of AIDS infected patients increase almost double. See Rosenberg, *supra* note 749, at 1.; and also see Margaret Duckett, *Compulsory Licensing and Parallel Importing: What Do They Mean? Will They Improve Access to Essential Drugs for People Living With HIV/Aids?*, International Council of Aids Serviced Organization (ICASCO) (July 1999), available at http://icaso.org/compulsory_english.htm. (mentioning that eighty-nine percent of the world's HIV infected population lives in the poorest ten percent of countries.)

challenge both developing countries' governments and international organizations. The governments have to help poor to get access to safe medicine at an affordable price by means public health management.⁷³⁰ International organizations also assist developing countries in treating HIV/AIDS.⁷³¹ At present, many people die, particularly in poor countries, because of a lack access to essential drugs.⁷³² WHO asserts that access to essential drugs is a human right and medicines are not simple commodities.⁷³³ The issue of insufficient access to HIV drugs has been a concern of developing countries and international organizations, particularly the WHO.

The WHO supports its members in the use of WTO/TRIPs-related safeguard such as a compulsory licensing and parallel imports to enhance affordability and availability of existing medicines.⁷³⁴ By addressing many aspects, including public health, TRIPs attempts to balance on the conflicting interests of developed and developing countries.⁷³⁵

⁷³⁰ See Maskus, *Access to Essential Medicines*, *supra* note 728, at 571-78. (mentioning that governments may either negotiate with drug companies or use bulk purchases for price discount. Governments may force drug companies to negotiate in terms of price by using both voluntary and compulsory license. Governments in poor countries should support appropriate research for their own needs and funding may come from donors such as developed country governments, multilateral organizations, and NGOs.)

⁷³¹ There are a number of international organizations and UN agencies (for example The World Health Organization, The United Nations Development Program, The UN Sub-Commission for the Protection and Promotion of Human Rights, UNAIDS, and the World Bank, ect.) debating the issue of access to drugs and the effects of strong intellectual property protection in developing countries.

⁷³² WHO estimates that more than one third of world's population lacks regular access to the medicines they need. In developing countries, 10.3 million children under five years of age died last year; 8.6 million of these deaths could have been prevented if those at risk would have had access to essential drugs. See ASEAN Workshop on TRIPs and Pharmaceuticals, *supra* note 711, at 9.

⁷³³ See TRIPs and Access to Pharmaceuticals, *supra* note 711, at 5. (explaining that in order to determine whether a nation has enough access to essential drugs, it relies on: (1) the rational selection and use of medicines (2) sustainable adequate financing (3) affordable prices, and (4) reliable health and supply systems.)

⁷³⁴ *Id.* at 5; For example, Zimbabwe could issue a license to a local company for an HIV/AIDS drug made by Bristol-Myers Squibb. The Zimbabwe manufacturer would produce the drug for sale in Zimbabwe under a generic name and pay a reasonable royalty to Bristol-Squibb. See Weissman, *Aids and Developing Countries*, *supra* note 719, at 1.

⁷³⁵ See TRIPs, *supra* note 3, art. 7 and 8.

Article 7 Objective

Thus, members are free to incorporate TRIPs obligations with their own nation law. This allows flexibility for developing nations to use compulsory licensing and parallel imports to respond to public health concerns.⁷³⁶

Although in the area of public health, TRIPs provides some safeguards (compulsory licenses and parallel imports) for developing nations, the U.S. Government and pharmaceutical companies strongly oppose developing countries' efforts to make HIV/AIDS drugs more available and affordable to their people via TRIPs safeguards, particularly with compulsory licensing.⁷³⁷ The U.S. Government has put pressure to developing nations by means of political, economic, and legal mechanisms, especially trade sanction section 301.⁷³⁸ Developing countries have been threatened with U.S. trade

"The Protection and enforcement of intellectual property rights should contribute to the promotion of technological innovation and to the transfer and dissemination of technology, to the mutual advantage of producers and users of technological knowledge and in a manner conducive to social and economic welfare, and to a balance of rights and obligations." (emphasis added)

Article 8 Principles

"1. Members may, in formulating or amending their laws and regulations, adopt measures necessary to protect public health and nutrition, and to promote the public interest in sectors of vital importance to their socio-economic and technological development, provided that such measures are consistent with the provisions of this Agreement." (emphasis added)

⁷³⁶ *Id.* art. 1. Article 1 Nature and Scope of Obligations

"Members shall give effect to the provisions of this Agreement. Members may, but shall not be obliged to, implement in their law more extensive protection than is required by this Agreement, provided that such protection does not contravene the provisions of this Agreement. Members shall be free to determine the appropriate method of implementing the provisions of this Agreement within their own legal system and practice." (emphasis added)

⁷³⁷ See Weissman, *Aids and Developing Countries*, *supra* note 719, at 2; and also see The Associated Press, Brazil is Planning to Request License for AIDS Viracept, June 27, 2001, available at <http://www.aegis.com/news/ap/2001/AP010688.html>. (visited on Oct. 7, 2002). (commenting that Brazil continued to issue compulsory licenses for an AIDS drug due to the high price of the AIDS drug. The U.S. filed a complaint with the World Trade Organization over Brazil law; however, this case was dropped under immense international pressure.); see MASKUS, *supra* note 707, at 211-12. (pointing out that in the perspective of developing and least-developed countries, the restrictions on parallel import amount to non-tariff barriers to goods that have legitimately been released from the control of IPRs owners. Actually parallel imports play an important role in countering "abusive price discrimination and collusive behavior based on private territorial restraints.")

⁷³⁸ See Myles Getlan, Comment, *TRIPs and the Future of Section 301: A Comparative Study in Trade Dispute Resolution*, 34 COLUM. J. TRANSNAT'L L. 173, 173 (1995). (pointing out that that improving IPRs protection in other countries by the section 301 approach has failed and suggest that the most effective way to strengthen IPRs protection abroad should be to improve the GATT dispute resolution process.); see

sanctions if they do not strengthen their patent laws, even though such laws benefit the U.S. pharmaceutical companies and not developing countries' own citizens. Some countries such as Thailand may be afraid of this pressure and discontinue their projects to help their poor. On the other hand, some countries such as India, and Brazil may be brave enough to carry on their projects and effectively achieve. It is true that because of compulsory licensing or parallel imports, the pharmaceutical industry will have to accept less profit. However, the cost is small when weighted against the interest of all patients in having increased access to essential drugs.

In the case of parallel imports, developing countries may possibly expect the less intimidating action under trade sanction section 301 from the U.S. for the following reasons. First, developing countries that are TRIPs member are free to allow parallel imports by applying an international exhaustion doctrine. Second, compared to compulsory licensing, there is less government involvement in parallel imports because there is no need of government approval of the importation. Third, unlike compulsory licensing, under parallel importation the IPRs owners receive a benefit from the first sale of their products at price they set. It seems that the IPRs owners are more voluntary in parallel imports than compulsory licensing. Finally, the U.S. also allows parallel imports of parallel imports of pharmaceutical products from Canada and Mexico⁷³⁹ as a result of

Adam Smith, *A High Price to Pay: The Costs of the U.S. Economic Sanctions and the Need for Process Oriented Reform*, 4 UCLA J. Int'l L. & Foreign Aff. 325, 325-46(1999). (suggesting that the U.S. should limit its use of trade sanction as an instrument of foreign policy because the trade sanctions can harm the U.S.'s short-term and long-term economic interest such as reducing in the U.S. export sector.; and also see American Association for World Health, Executive Summary, Denial of Food and Medicine: The Impact of the U.S. Embargo on Health and Nutrition in Cuba 6-14 (1997).

⁷³⁹ See The Medicine Equity and Drug Safety Act of 2000 (MEDSA) H.R. Rep. No. 106-948, at 38 (2000). MEDSA was passed as section 745 of Public Law 106-387.; see William Davis, Comment, *The Medicine Equity and Drug Safety Act of 2000: Releasing Gray Market Pharmaceuticals*, 9 TUL. J. INT'L & COMP. L. 483 (2001) (pointing out that The MEDSA was a piecemeal compromise aimed at lowering pharmaceutical

the U.S. consumer pressure and governmental health care policy.⁷⁴⁰ Therefore, it is improper for the U.S. to force other countries to restrict parallel imports, if the U.S. itself allows gray market pharmaceuticals.

Therefore, the following section will explain and analyze the controversial disagreements between the U.S. and developing countries by selecting some actual cases taking place in Thailand, Brazil, India, and South Africa. The situations of these developing countries will illustrate the adverse effects of the U.S. pressure on developing countries, such as a high price of medicines and a delay in the issuance of compulsory licensing. Moreover, due to difficulties on compulsory licensing, parallel imports may be considered a proper solution for increasing access to drugs rather than compulsory licensing.

1. Thailand

Thailand is faced with the AIDS pandemic as the result of the high number of prostitutes, the low education in safe sex, the HIV transmission through injection drug and the high-price of HIV drugs. Due to high price in HIV drugs, most HIV infected

prices by allowing wholesalers and pharmacists to buy U.S. approved drugs abroad and resell them in the United States, passing the discounted foreign prices along to the consumer. Before issuing the MEDSA, the United States expressly banned the resale or parallel imports of foreign-purchased pharmaceuticals under the Prescription Drug Marketing Act of 1987.); see Prescription Drug Marketing Act of 1987, Pub. L. No. 100-293, 21 U.S.C. 381(d) (2000); see JOHN F. CALFEE, PRICE, MARKETS AND THE PHARMACEUTICAL REVOLUTION 1-3 (2000); and also see *infra* note 777.

⁷⁴⁰See Melody Petersen, *Drug-Cost Bill May Not Dent Industry Profit*, N.Y. TIMES, Sept. 28, 2000, at C1.; and also see Robert Pear, *For Price Break on Drugs, Congress Looks to Canada*, N.Y. TIMES, Sept. 9, 2001, at 22.; In the case of parallel imports, the U.S. government and pharmaceutical companies have been faced with both internal pressure from the U.S. consumer when dealing this issue in the U.S. territory and external pressure from the international organizations and the governments and consumers of developing countries when dealing with the parallel imports situation in other countries.

patients cannot afford the antiretroviral drug.⁷⁴¹ In order to reduce the price of HIV drugs, the Thai Government has attempted to grant limited patent protection rights and support an active generic industry.⁷⁴² The Thai Government has tried to grant compulsory licensing for essential drugs, which is consistent with the text of TRIPs Agreement.

Unfortunately, the U.S. has opposed such action, for example, the Thai Government attempted to grant a compulsory licensing for the drug didanosine (ddl), owned by Bristol-Myers-Squibb (U.S. multinational pharmaceutical company). In return, the U.S. imposed a strong trade pressure in order to prevent the issuance of the compulsory license. Finally on January 16, 2000, the Thai government involuntarily rejected the issuance of the ddl compulsory license because of the U.S trade pressures.⁷⁴³

Needless to say, the threats of the U.S. Government and pharmaceutical companies has caused hesitation and delay by the Thai Government in issuing compulsory licenses and has impeded access to HIV/AIDS drugs in Thailand.

⁷⁴¹ See HIV & AIDS in Thailand, available at <http://www.avert.org/aids/thia.htm> (visited July 31, 2003); Johns Hopkins, Bloomberg School of Public Health, Condoms and Education Dramatically Reduce HIV Spread in Thailand-Drug Use Still Major Transmission Source, Jan. 24, 2002, available at http://www.jhsph.edu/Press_Room/Press_Release/Thailand.html (visited July 31, 2003); Judy Rein, Article, *International Governance through Trade Agreements: Patent Protection for Essential Medicines*, 21 NW. J. INT'L L. & BUS. 379, 402 (2001), cited in Global Trade and Access to Medicine: AIDS Treatments in Thailand, 354 Lancet 1893, 1984 Nov. 27, 1999. (the cost of triple therapy is USD 675 per month, while the average monthly salary of an office worker is only USD 120. The high price certainly reduces access to HIV drugs because HIV infected patients cannot afford to the price of therapy.)

⁷⁴² For example, Thailand Government Pharmaceutical Organization (GPO) has been producing generic AZT for a quarter of the price of the brand name version for several years. See Sutin Wannabovorn, Thais Protest U.S. Firm's AIDS Drug Monopoly, available at <http://biz.yahoo.com/rf/991222/bg/html> (visited Oct. 28, 2002)

⁷⁴³ See Thailand: Government Rejects Compulsory Licensing for ddl, Kaiser Daily HIV/AIDS Report, Thursday, Jan. 20, 2000, available at <http://report.kff.org/achive/aids/2000/01/kh00120.3.htm> (visited Oct. 28, 2002).; Thailand: U.S. and 'Gig Pharma' Orchestrate Pressure, Access to Essential Medicines Report, Jan. 11, 2001, available at <http://www.msf.org/countries/page.cfm?articleid=CACADFA1-C511-43ED-ADE7...> (visited Oct. 28, 2002); and also see The Letter from James Love, Consumer Project on Technology, available at <http://www.cptech.org/ip/health/Thailand/tmr-jan22-2000.html>. (visited Oct. 28, 2002).; To increase access to drugs besides a compulsory license, Thailand allows parallel imports of drugs from other countries in Asia. The U.S. pharmaceutical companies have argued strongly against Thailand allowing parallel imports. The information is available at www.phrma.org/issues/int/thailand.html (visited Oct. 28, 2002)

Nevertheless, the current Thai Patent Act, adopting an international exhaustion doctrine, allows parallel imports that may solve the issue of obtaining access to essential drugs and diminish the adverse effect of U.S. pressure on Thailand.

2. Brazil

Like Thailand, Brazil also faced a HIV/AIDS crisis. However, the Government of Brazil has successfully launched many programs to help AIDS patients in terms of prices and access to drugs.⁷⁴⁴ Regardless of the U.S. pressure, the Brazil Government has used both a compulsory licensing and parallel imports strategies.⁷⁴⁵ In other words, the Government is brave enough to step forward to protect its own people against the U.S. Government and pharmaceutical companies by playing an important role to support the accessibility of drugs and technology transfer in the pharmaceutical industry.

In order to improve access to drugs with affordable price and encourage the transfer of technology, the Brazil patent law provides patents for pharmaceuticals, but subject to a working requirement. As a result of a “working requirement” under Article

⁷⁴⁴ See Rosenberg, *supra* note 723, at 1. (“In 1998, the government began making copies of brand-name drugs, and the price of those medicines has fallen by an average of 79 percent. Brazil now produces some triple therapy for \$ 3,000 a year and expects to do much better, and the price could potentially drop to \$ 700 a year or even less. Brazil is showing that no one who dies of AIDS dies of natural causes. Those who die have been failed—by feckless leaders who see weapons as more alluring purchases than medicines, by wealthy countries (notably the United States) that have threatened the livelihood of poor nations who seek to manufacture cheap medicine and by the multinational drug companies who have kept the price of antiretroviral drugs needlessly out of reach of the vast majority of the world’s population.”); and also see Brazil Fights for Affordable Drugs Against HIV/AIDS, *Rev Panam Salud Publica/Pan Am J Public Health* 9(5), 2001, at 332-33, available at <http://www.paho.org/English/DBI/ES/v9n5-TEMA-Brazil.pdf>. (visited Oct. 16, 2002). [hereinafter Brazil Fights for Affordable Drugs] (explaining that Brazil’s policy of providing patient with free antiretroviral (ARV) drugs has played a significant role in the country’s achievements. A key to the broad public access to ARVs has been the local manufacturing of cheaper generic equivalents of the medicines developed and patented in wealthier countries. By 1999 this approach had cut treatment costs in Brazil by 70%.)

⁷⁴⁵ See Article 68 and 71 of Brazil patent law (compulsory licenses), translated into English by the World Intellectual Property Organization, available at <http://www.cptech.org/ip/health/cl/brazil1.html>. (visited Oct 18, 2002)

68, it permits the issuance of compulsory licenses in case where patent holders choose to supply the market through imports rather than local production.⁷⁴⁶ The Government put pressure on multinational pharmaceutical companies to produce patented drugs in Brazil instead of importing the drugs into Brazil.

In response to this regulation, the U.S. requested a WTO dispute settlement panel in February 2001. The U.S. Government claimed that Article 68 of the Brazilian Industrial Property Law 1996 violated the TRIPs Agreement because the 'local working' requirement discriminated against imported products. Brazil argued that the provision allowing compulsory licensing or parallel imports complied with the TRIPs Agreement because it was intended to address "abuse of rights or economic power" by the patent holder.⁷⁴⁷ During the time of dispute, many international NGOs, and developing and least-developed countries put intense opposition to the U.S. position. If the U.S. were to succeed in its case, it would not only exterminate the Brazil's successful AIDS program,

⁷⁴⁶ Article 68 provides that if a patent holder fails to manufacture a patented product in Brazil within 3 years of patent registration (either in its own factory or by granting a license to a local firm), the Government may suspend the patented product's right to "market exclusivity" and may authorize another company to manufacture the drug through the issuance of a compulsory license or allow the importation of patented products. If a patent holder does not manufacture the patented product in Brazil, the Government may allow the import of the patented products from the cheapest source. However, if the company manufactures the drug locally, the firm is protected from parallel imports. The pharmaceutical companies have to choose between getting the exclusive right for marketing their drugs by producing those drugs in Brazil or losing their rights.

⁷⁴⁷ See *Brazil Fights for Affordable Drugs*, *supra* note 744, at 334-36. (explaining that PhRMA also claimed that a decree on compulsory licensing issued by Brazil's President in October 1999 to regulate Article 71 of Patent Act could be a violation of the TRIPs Agreement. Unlike Article 68, Article 71 allows compulsory licensing on grounds of public interest and national emergence, rather than abuse of right and 'local working' requirement.); Article 8.2 of the TRIPs Agreement provides "Appropriate measures, provided that they are consistent with the provisions of this Agreement, may be needed to prevent the abuse of intellectual property rights by right holders or the resort to practices which unreasonably restrain trade or adversely affect the international transfer of technology."; and also see Paul Champ & Amir Attaran, *Patent Rights and Local Working Under the WTO-TRIPs Agreement: An Analysis of the U.S.-Brazil Patent Dispute*, 27 *Yale J. Int'l L.* 365, 367 (2002). (pointing out that local working requirement is generally permissible based on the broad reading of a whole context of TRIPs)

but would also obstruct others from using the same approach as Brazil to solve the issues of inaccessibility and non-affordability of essential medicines.⁷⁴⁸

As the result of powerful global pressures and a change in U.S. policy under the Bush Administration, the U.S. announced on June 25, 2001 that it would withdraw the case against Brazil in a joint statement with Brazil.⁷⁴⁹ The U.S. and Brazil have set up the U.S.-Brazil Consultative Mechanism to find mutually agreeable "creative solutions."⁷⁵⁰ In return for the U.S. withdrawing the case, Brazil agreed to consult with the U.S. prior to issuing a compulsory license for patents held by U.S. companies, based on a case-by-case decision.⁷⁵¹ The U.S. action of withdrawing the case was joyfully acclaimed by developing and least-developed countries and NGOs.⁷⁵² This event not only demonstrated a pleasant compromising solution between a developing and developed country, but also mitigated other confrontations between the U.S. and other developing countries who opposed the U.S. position, particularly South Africa.

Due to a strong political commitment by Brazil to solve the HIV/AIDS crisis without fear of U.S. pressure, Brazil is one developing country that has successfully

⁷⁴⁸ See Ellen 't Hoen, Article, *Public Health and International Law: TRIPS, Pharmaceutical Patents, and Access to Essential Medicines: A Long Way From Seattle to Doha*, 3 CHI. J. INT'L L. 27, 33 (2002).; and also see Brazil Fights for Affordable Drugs, *supra* note 744, at 336.

⁷⁴⁹ See Helene Cooper, U.S. Drops WTO Complaint Against Brazilian Patent Law, Wall St J. Eur A2 (June 26, 2001).; and also see USTR Press Release, United States and Brazil Agree to Use Newly Created Consultative Mechanism to Promote Cooperation on HIV/AIDS and Address WTO Patent Dispute, June 25, 2001, available at <http://www.ustr.gov/release/2001/06/01-46.htm> (visited Oct. 18, 2002). (The Bush Administration has stated that the United States is committed to a flexible approach that is sensitive to health crises, but also protective of intellectual property rights. Under this policy, the Administration has informed WTO Members that should member nations take steps to address major health crises, such as the HIV/AIDS crisis in sub-Saharan Africa, the United States would raise no objection if Members availed themselves of the flexibility afforded by the WTO/TRIPS Agreement. This agreement allows Brazil to receive important pharmaceutical support for its HIV/AIDS program.)

⁷⁵⁰ *Id.*

⁷⁵¹ See Chakravarthi Raghavan, US. Beats a (Tactical) Retreat over Brazil's Patent Law, available at <http://www.twinside.org.sg/title/tactical.htm> (visited on Oct. 16, 2002).

⁷⁵² See *Id.* The NGOs welcomed the US action such as Elen 't Hoen of Medicins sans Frontier (MSF), Oxfam, and Jame Love of the US Consumer Project on Technology.

achieved improved accessibility to affordable AIDS drugs. Brazil's achievement provides a good example for other developing countries to solve AIDS issues by following Brazil's footsteps. In addition, by obtaining an adequate amount of manufacturing capacity, Brazil also assists other developing countries to increase manufacturing capacity through a transfer of technology.⁷⁵³

3. India

Similar to other developing countries, India was threatened by U.S. trade sanction with support of PhRMA for inadequate patent protection for pharmaceuticals.⁷⁵⁴ The U.S. pharmaceutical companies claim that the India Patents Act of 1970 essentially provided no patent protection for pharmaceuticals. The drug companies asserted that (1) the term of patent protection was too short to provide protection and the examination and opposition procedure caused too much delay and decreased the available duration of protection; (2) the royalty for compulsory licenses was artificially low; and (3) product patents were not available for pharmaceuticals.⁷⁵⁵ However, India has an obligation to amend its patent law to provide the patent product for pharmaceuticals by 2005.⁷⁵⁶ Like

⁷⁵³ See Hoen, *supra* note 748, at 33.

⁷⁵⁴ PhRMA urged the US. Government to identify India as a Priority Foreign Country (PFC) through the 2001 "Special 301" review process and to initiate a dispute settlement action in the WTO on ground of failure to comply with TRIPs obligation. See Pharmaceutical Research and Manufactures of America, PhRMA Special 301 Submission Priority Foreign Countries, 8 (2001), available at <http://www.phrma.org/intnat/all.phtml?prefix=reg>. (visited on Dec. 2, 2001)

⁷⁵⁵ See Shodeep Baneriji, *The Indian Intellectual Property Rights Regime and the TRIPs Agreement*, in INTELLECTUAL PROPERTY RIGHTS IN EMERGING MARKETS (Clarisa Long, ed.) at 58-59.; see ASEN Workshop on TRIPs and Pharmaceuticals, *supra* note 711, at 7. (pointing out that before the emergence of the TRIPs Agreement, patents were granted either for a product or for a process of production. A product patent grants monopoly right over the product, regardless of the production method. A process patent grants right over the process and over the products directly produced by that process. Thus production of the same product by means of different production method does not infringe a process patent and it is allowed.)

⁷⁵⁶ See Suresh Koshy, *The Effect of TRIPs on Indian Patent Law: A Pharmaceutical Industry Perspective*, 1 B.U. J. SCI. & TECH. L. 4, 9-10 (1995); and also see Carsten Fink, How Strong Patent Protection in India

Brazil, the Indian Patent Act of 1970 states that importation of a patented product is not equivalent to a working patent in India.⁷⁵⁷ Multinational pharmaceutical companies argue that this working requirement is not consistent with the TRIPs Agreement.

The Patent Act of 1970 has produced considerable advantages for the Indian pharmaceutical industry by producing inexpensive drugs for the market, and maintaining the trade balance in the pharmaceutical sector.⁷⁵⁸ Although India is classified as a developing country, India has a successful pharmaceutical industry with innovative capacities of drug development.⁷⁵⁹ Pharmaceutical prices in India are considered among the lowest price in the world. India has become a source of parallel imports to other developing and least-developed countries, providing low price drugs for poor populations.⁷⁶⁰ However, India has enacted legislation granting patent protection, effective 2005. In other words, this favorable factor of a weak patent protection will no

Might Affect the Behavior of Transnational Pharmaceutical Industries, Development Research Group, The World Bank, at3.

⁷⁵⁷ See Baneriji, *supra* note 755, at 67-68, and 80. (explaining that section 83(a) states “patents are granted to encourage inventions and to secure that the inventions are worked in India on a commercial scale” and section 33(b) provides “they are not granted merely to enable patentees to enjoy a monopoly for the importation of the patented article.” Before the enactment of the Patent Act of 1970, the Patent Act of 1911 obviously states that importing a patented product was equivalent to working the patent. As the result of this provision, MNCs only established trading centers based in India by importing products from other countries. There was no technology transfer and no dissemination of the information and knowledge regarding the patents. Therefore, the Government enacted the Patent Act of 1970 to correct this problem by no longer considering importation equivalent to a working patent. The 1970 Act favors domestic firms, reverses the MNCs domination, and supports the Indian pharmaceutical industries. Currently, Indian manufactures produce drugs not only for the Indian market, but also for an international market. India stays competitive in the global market because Indian drugs are priced more cheaply. Indian has become a major player in international generic drug markets.)

⁷⁵⁸ See Koshy, *supra* note 756, at para.23.

⁷⁵⁹ See Carlos M. Correa, Implications of the Doha Declaration on the TRIPS Agreement and Public Health, June 2002, WHO/EDM/PAR/2002.3, (Health Economics and Drugs EDM Series No.12, WHO) at Annex 2 Table of Levels of Development of Pharmaceutical Industry, by Country (Source: Balance R, Pogany J, Forstner H. The World's Pharmaceutical Industry. An International Perspective on Innovation, Competition and Policy. Vienna, United Nations Industrial Development Organization, 1992) [hereinafter Correa, *Implications of Doha Declaration on TRIPS and Public Health*]

⁷⁶⁰ See Shubha Ghosh, *Pills, Patents, and Power: State Creation of Gray Markets as a Limit on Patent Rights*, 53 FLA. L. REV. 789, 814 (2001). (pointing out that the main source of the parallel imports in South Africa is from India, which until recently did not recognize patents on medicine.)

longer continue to exist in the near future (2005) as a result of the TRIPs Agreement. This change will affect the Indian pharmaceutical by increasing drug prices, which may make India's drugs unaffordable and inaccessible for the poor.⁷⁶¹ Nevertheless, the strong support by Indian Government, the innovative capacities in pharmaceutical industry, and the long-term benefits of a weak patent protection should facilitate the Indian pharmaceutical industries to continually maintain their competitive position in global market in terms of low price and more availability. That would benefit all poor patients not only in India but also in other developing and least-developed countries by improving access to essential drugs, particularly HIV drugs.

4. South Africa

South Africa has experienced the highest increase of HIV in the world, with 2.4 million people infected, or 6.3 % of the population. Due to the high prices of HIV drugs, the South Africa Government has attempted to reduce the cost of medicines and increase access to HIV drug.⁷⁶² The government passed the Medicines and Related Substances Control Amendment Act of 1997 to improve access to essential drugs. The 1997 Amendment permits both the development of generic AIDS drugs under compulsory licensing and the parallel importation of low-priced AIDS drugs into South Africa.⁷⁶³

⁷⁶¹ *Id.* 82-86.; see Jayashree Watal, *Introducing Product Patents in the Indian Pharmaceutical Sector: Implications for Prices and Welfare*, 20 *World Competition: Review of Law and Economic*, 1, 5-21(1996).; and also see Watal, *supra* note 705, at 733-52. (pointing out that if the patent protection raised the drug price in India, India might take advantage of cheaper drugs from Bangladesh.)

⁷⁶² See David Benjamin Snyder, Comment, *South Africa's Medicines and Related Substances Control Amendment Act: A Spoonful of Sugar or a Bitter Pill to Swallow?*, 18 *DICK. J. INT'L L.* 175 (1999).

⁷⁶³ *Id.* at 180-4. (pointing out that allowing parallel imports under the exhaustion doctrine have obvious potential benefits for consumers because of the increase in competition created. Section 15(C) (b) clearly permits parallel imports by allowing people to import a manufacturer's patented pharmaceuticals sold in other countries into South Africa.)

Allowing parallel imports has definitely given poor HIV patients increased access to drugs in terms of low price and more availability. With inadequate capability for pharmaceutical manufacturing,⁷⁶⁴ it is difficult for South Africa to produce patented drugs in South Africa under compulsory licensing. Thus, parallel imports are a more useful means to gain access to affordable HIV drugs than compulsory licensing in South Africa.⁷⁶⁵

Responding to the 1997 Amendment, both the U.S. Government and pharmaceutical companies strongly opposed South Africa's efforts to undertake compulsory licensing or parallel imports to make HIV/AIDS drugs or other essential medicines more available and affordable to its people.⁷⁶⁶ The U.S. had withheld certain trade benefits from South Africa and had threatened trade sanctions by placing South Africa on the Special 301 Watch List.⁷⁶⁷ The issue became increasingly debated because of a South Africa court case, with the South Africa government against the 39 largest pharmaceutical companies in the world.⁷⁶⁸ They took South Africa to a court by claiming that South Africa's 1997 Medicines and Related Substances Control Amendment Act

⁷⁶⁴ See Correa, *Implications of Doha Declaration on TRIPS and Public Health*, *supra* note 759, at Annex 2. (stating that South Africa only has the capacities to produce finished products from imported ingredients.)

⁷⁶⁵ The main source of the parallel imports is from India, which until recently did not recognize patents on medicine (but has enacted legislation granting patent protection that will be effective in 2005). See Ghosh, *supra* note 760, at 814.

⁷⁶⁶ See Robert Weissman, *Aids and Developing Countries*, *supra* note 719, at 2.; and also see The Associated Press, Brazil is Planning to Request License for AIDS Viracept, June 27, 2001, available at <http://www.aegis.com/news/ap/2001/AP010688.html>. (visited Oct. 7, 2002). (explaining that Brazil continued to consider issuing a compulsory licenses for an AIDS drug. The U.S. had filed a complaint with the World Trade Organization over Brazil law; however, this case was dropped under immense international pressure.)

⁷⁶⁷ Press Release, Office of the U.S. Trade Representative, U.S.T.R. Announces Results of Special 301 Annual Review (Apr. 30, 1999), available at <http://www.ustr.gov/release/1999/04/99-41.html>. (visited May 14, 2002).

⁷⁶⁸ See Pharmaceutical Manufacturers Association of South Africa and 41 others v. President of the Republic of South Africa and 9 Others, The High Court of South Africa (Transvaal Provincial Division) Case No. 4183/98. (field Feb 18, 1998)

section 15C, allowing a compulsory licensing and parallel imports, violated the TRIPS Agreement.⁷⁶⁹

The three-year court case ended on April 23, 2001. The South Africa government agreed to abide with TRIPs obligation and to set up a joint working committee with the pharmaceutical companies to draw up regulations governing the 1997 Medicines Act.⁷⁷⁰

In return, the pharmaceutical companies agreed to supply drugs to South Africa at drastically reduced prices to help poor patients.⁷⁷¹ The U.S. government recently acknowledged the importance of providing affordable AIDS drugs in South Africa⁷⁷² and

⁷⁶⁹ *Id.*; and see South Africa Medicines and Related Substances Control Act No. 101 of 1965, Amendment No. 70, Section 15 (C) (1997), available at <http://lists.essential.org/pipermail/pharm-plicy/2001-January/000607.html>; There are two schemes under section 15 (C) to make drugs more available and cheaper: parallel importation and compulsory licensing schemes. Its parallel import provision is obviously valid under TRIPS since article 6 of TRIPS allows Members to freely decide regarding application of the exhaustion doctrine. But the compulsory licensing provision is questionable since the textual provision is ambiguous and overly broad and possibly inconsistent with the requirements under Article 31 of the TRIPS Agreement. See Duane Nash, *Berkeley Technology Law Journal Annual Review of Law and Technology: VI. Foreign & International Law South Africa's Medicines and Related Substances Control Amendment Act of 1997*, 15 BERKELEY TECH. L.J. 485 (2000); see Winston P. Nagan, *International Intellectual Property, Access to Health Care, and Human Rights: South Africa v. United States*, 14 FLA. J. INT'L L. 155 (2002) (pointing out that both compulsory licensing and parallel import schemes are permissible under the TRIPS Agreement. The Minister's broad power to authorize either parallel imports or compulsory licensing of essential drugs would not violate international law when the Minister of Health reasonably acts under public international law. Public policy may trump the normal operation of a private international law rule. When the right to life is involved, the exceptions under Article 30 and 31 of TRIPs are strengthened. The right to life is an important indicator to consider for determining reasonable and unreasonable conduct under TRIPS.); and also see Frederick M. Abbott, II, *Discontinuities in the Intellectual Property Regime: The TRIPS-Legality of Measures Taken to Address Public Health Crisis: A Synopsis*, 7 WID. L. SYMP. J. 71, 82-84 (2001). [hereinafter, Abbott, *TRIPS and Public Health Crisis*] (noting that section 15 (C) is not overbroad or ambiguous and entirely consistent with the acceptance for authorizing international exhaustion and parallel imports. As pharmaceutical industries claimed that the statute granted the Minister of Health discretionary powers that might possibly be used inconsistently with WTO rules, such discretion does not in itself constitute a violation of WTO law since a discretionary measure is WTO-inconsistent only when it is invoked in a WTO-inconsistent manner.)

⁷⁷⁰ See Steven Lee Myers, *South Africa and U.S. End Dispute Over Drugs*, N.Y. TIMES, Sept. 18, 1999, at A8. (explaining that South Africa had pleaded to apply this law by abiding with WTO obligation since the U.S. government had worried that law was written too broad and might violate the WTO rules.)

⁷⁷¹ See HIV and AIDS Drugs in Africa, available at <http://www.avert.org/aidsdrugsafrika.htm>. (visited on Oct. 16, 2002).

⁷⁷² See Vice President Gore's June 25, 1999 Letter to James E. Clyburn, Endorsing the Use of Compulsory Licensing and Parallel Imports of Pharmaceutical Drugs in South Africa, available at <http://www.cptech.org/ip/health/sa/vp-feb-25-99.html>. (visited Sept. 27, 2002) (Vice President Gore wrote "I support South Africa's effort to provide AIDS drugs at reduced prices through compulsory licensing and

subsequently lessened its pressure on South Africa, which should be a good sign for other developing countries.

E. The Current Support From WTO Doha Ministerial Conference

In November 2001, the WTO Ministerial Conference met in Doha in Qatar. Compared to the 1999 WTO Ministerial meeting in Seattle, developing countries participated more equally in the Doha Conference.⁷⁷³ The outcome of the Doha Ministerial Conference was important in terms of public health, as presented in the Doha Ministerial Declaration and the specific Declaration on Public Health.⁷⁷⁴ In fact, the Doha declarations were successfully achieved because of the strong participation of developing and least-developed countries with the support of developed countries.⁷⁷⁵ The U.S. has

parallel importing, so long as they are carried out in a way that is consistent with international agreements.”); On July 26, 1999, the Treatment Action Campaign (TAC) met with the U.S. representatives to discuss the use of compulsory licensing and parallel imports to make HIV/AIDS drugs available at affordable prices in South Africa. This information is available at <http://www.hri.ca/partners/alp/press/gore-press.shtml>. (visited Sept. 27, 2002).

⁷⁷³ See Peter Lichtenbaum, Article, *Reflections on The WTO Doha Ministerial: “Special Treatment” vs. “Equal Participation:” Striking A Balance in The Doha Negotiations*, 17 AM. U. INT’L L.REV. 1003, 1021 (2002). (discussing the special treatment for developing countries in the Doha Declaration and arguing that the negotiations have an opportunity to move toward a more complicated amalgamation of the special treatment approach with the equal participation model. This combination should result in a higher degree of market liberalization than has occurred in the past.); and also see Peter M. Gerhart, Article, *Reflections on The WTO Doha Ministerial: Slow Transformations: The WTO As A Distributive Organization*, 17 AM. U. INT’L L.REV. 1045, 1090-92 and 1094 (2002).

⁷⁷⁴ See Doha Ministerial Declaration (Nov. 14, 2001), WT/MIN(01)/DEC/W/1, available at http://www.wto.org/english/thewto_e/minist_e/min01_e.htm. [hereinafter Doha Ministerial Declaration]; and also see Declaration on The TRIPs Agreement and Public Health (Nov. 14, 2001), available at http://www.wto.org/english/thewto_e/minist_e/min01_e/minidecl_trips_e.htm. [hereinafter Doha TRIPs and Public Health Declaration]

⁷⁷⁵ During the draft of Ministerial Declaration on TRIPs and Public Health, there are three proposals from (1) a group of developed countries (the United States, Australia, Canada, Japan, and Switzerland); (2) a group of developing countries (the Africa Group and 19 countries); and (3) the EU. Those text drafts are respectively available at http://www.wto.org/english/tratop_e/trips_e/minidecdraft_w313_e.htm; http://www.wto.org/english/tratop_e/trips_e/paper_develop_w296_e.htm; and http://www.wto.org/english/tradtop_e/trips_e/paper_eu_w280_e.htm. (visited Oct. 8, 2002); see TRIPs and

changed its domestic and foreign policy in an area of public health. The U.S. foreign policy has become more liberal regarding the utilization of compulsory licensing and parallel imports.⁷⁷⁶ Its domestic policy also changed from prohibiting parallel imports to allowing parallel imports in to the U.S. of pharmaceuticals that meet the U.S. standard in order to reduce the domestic drug price.⁷⁷⁷ Moreover, the Bush Administration has indicated concern about the HIV/AIDS crisis, and the individuals, families and communities affected by the disease.⁷⁷⁸

Public Health vs TRIPs and Pandemics?, BRIDGES Monthly Vol. 5, No. 7 Sept. 2001, available at <http://www.ictsd.org/ministerial/doha/bridgesmonthly5-7.htm> (visited Oct. 18, 2002).

⁷⁷⁶ See Exec. Order No 13, 155, 65 Fed Reg 30, 521 (2000); and also see Hoen, *supra* note 748, at 34-35. (illustrating that the US President Clinton chose Seattle as the spot to declare a change in U.S. policy on intellectual property rights and access to medicines. In May 2000, President Clinton confirmed the change in U.S. policy by issuing an Executive Order on Access to HIV/AIDS Pharmaceuticals and Medical Technologies, supporting the use of compulsory license to increase access to HIV/AIDS medication in sub-Saharan Africa.); see A Press Release from the Office of the USTR, dated Sept. 17, 1999, available at <http://www.ustr.gov/release/1999/09/00-76.html> (reporting that the U.S. promised to drop threats of trade sanction against South Africa); and also see John A. Harrelson, *IV Note: TRIPS, Pharmaceutical Patents, and The HIV/AIDS Crisis: Finding the Proper Balance Between Intellectual Property Rights and Compassion*, 7 WID. L. SYMP. J. 175 (2001) (recommending that the United States should no longer pressure other countries to prohibit compulsory licensing. Instead, the U.S. should more focus on whether such countries provide adequate compensation to patent owner for compulsory licensing as entailed under the TRIPs Agreement.); and also see John R. Thomas, *HIV/AIDS Drugs, Patents and the TRIPs Agreement: Issues and Options*, CRS Report for Congress (RL31066), July 27, 2001, at 19-21.

⁷⁷⁷ Before issuing the Medicine Equity and Drug Safety Act of 2000 (MEDSA), the United States expressly banned the resale or parallel imports of foreign-purchased pharmaceuticals under the Prescription Drug Marketing Act of 1987. The MEDSA was a piecemeal compromise aimed at lowering pharmaceutical prices by allowing wholesalers and pharmacists to buy U.S. approved drugs abroad and resell them in the United States, passing the discounted foreign prices along to the consumer. See Prescription Drug Marketing Act of 1987, Pub. L. No. 100-293. See 21 U.S.C. 381(d) (2000) [hereinafter called PDMA]; see Davis, *supra* note 739, at 483. (pointing out that there is an opportunity for arbitrage in the pharmaceutical industry among the U.S. foreign neighbors because of price differential.); and also see Ghosh, *supra* note 760, at 789. (comparing between the parallel imports (re-importation) of drugs from Canada to the U.S. and the parallel imports in South Africa and pointing out that there is a difference between both cases.); In October 2000, the US Congress passed legislation as part of a general appropriation bill for agriculture, that allowed re-importation of patented pharmaceuticals from Canada into the U.S, subject to the approval of the Department of Health and Human Services.; and also see H.R. Conf. Rep. No. 106-948m at 39 (2001)

⁷⁷⁸ See USTR Press Release, United States and Brazil Agree to Use Newly Created Consultative Mechanism to Promote Cooperation on HIV/AIDS and Address WTO Patent Dispute, June 25, 2001, available at <http://www.ustr.gov/release/2001/06/01-46.htm> (visited Oct. 18, 2002).

By recognizing the gravity of the public health problem in many developing and least-developed countries,⁷⁷⁹ Members agreed that the WTO Agreement on TRIPS “does not and should not prevent Members from taking measures to protect public health,” and “affirm that the agreement can should be interpreted and implemented in a manner supportive of WTO Members’ right to protect public health and, in particular, to promote access to medicines for all.”⁷⁸⁰ The declaration also affirms “the right of WTO members to use, to the full, the provisions in the TRIPS Agreement, which provide flexibility for this purpose.”⁷⁸¹ The flexibilities include “the right to grant compulsory licenses and the freedom to determine the grounds upon which such license are granted”, “the right to determine what constitutes a national emergency” (including HIV/AIDS crisis as public health emergency), and the freedom to implement the exhaustion doctrine. The Doha declaration reaffirms use of the exhaustion doctrine under Article 6 of TRIPs by stating that the purpose is “to leave each Member free to establish its own regime for such exhaustion without challenge, subject to the MFN and national treatment provisions of Article 3 and 4.”⁷⁸²

This statement from the Doha Declaration means that developing countries can issue compulsory licensing or/and allow parallel imports (by implementing the international exhaustion doctrine) for public health reason, without fear of invoking legal challenges from other WTO members, particularly the U.S.⁷⁸³ Moreover, under Doha all

⁷⁷⁹ See Doha TRIPs and Public Health Declaration, *supra* note 774, at para 1.

⁷⁸⁰ *Id.* at para 4.

⁷⁸¹ *Id.* at para 4 and para 5.

⁷⁸² *Id.* at para 5 and 5 (d).

⁷⁸³ To answer the question whether the declaration are bound in the dispute process. See Alan O. Sykes, Article, *Public Health and International Law: TRIPS, Pharmaceuticals, Developing Countries, and the Doha “Solution,”* 3 CHI. J. INT’L L. 47 (2002). (answering the question whether the declaration are bound

least-developed countries have an additional ten years transition period, until 2016, to comply with pharmaceutical patents.⁷⁸⁴

Nevertheless, although WTO Members recognized the issue of the limited pharmaceutical production capacities in developing countries, there has been no real resolution of this issue over whether developing countries, which cannot produce generic medicine by themselves, can issue a compulsory license to a company in another country to produce drugs for import into the developing countries. This situation is called a 'third party compulsory licensing.'⁷⁸⁵ Indeed, in order to ultimately make compulsory licensing more effective, the Doha Declaration should specify that members are able to grant compulsory licensing to foreign manufactures to provide medicines in the domestic market. If Article 31(f) is interpreted to allow compulsory licensing only of domestic manufacturers serving the domestic market, the compulsory licensing would prove to be of limited use due to insufficient pharmaceutical production capacity in the developing

in the dispute process. Although ministerial declarations within WTO are not legally binding in the dispute resolution process, the Doha Declaration is likely to influence interpretation of the TRIPs Agreement.)

⁷⁸⁴ See Doha TRIPs and Public Health Declaration, *supra* note 774, at para. 7

⁷⁸⁵ *Id.* at para. 6. Paragraph 6 states "We recognize that WTO members with insufficient or no manufacturing capacities in the pharmaceutical sector could face difficulties in making effective use of compulsory licensing under the TRIPs Agreement. We instruct the Council for TRIPs to find an expeditious solution to this problem and to report to the General Council before the end of 2002."; This problem occurs because Article 31(f) of the TRIPs Agreement states that a product made under a compulsory license is supplied predominantly to the licensee's domestic market. Many developing countries lack or have an insufficient capacity to manufacture medicines on their own. This problem had been raised by developing countries. Developing countries argued "nothing in this TRIPs Agreement prevents Members from granting compulsory licenses for foreign suppliers to provide medicines in the domestic market... In this respect, the reading of Article 31 (f) should confirm that nothing in the TRIPs Agreement will prevent Members from granting compulsory licenses to supply foreign market." See the Developing Country Group's Paper, *supra* note 775, at para.34; In this matter, the EU supports developing countries by suggesting that it should allow developing countries that cannot produce drugs themselves to license a company in another country to manufacture a given drug for export to the Member granting the compulsory license. See The EU's Paper, *supra* note 775, at para.13.; see Implications of Doha Declaration on TRIPs and Public Health, *supra* note, at 19-22; and also see TRIPs, *supra* note 3, art.31(f). Article 31 (f) states "(f) any such use shall be authorized predominantly for the supply of the domestic market of the Member authorizing such use."

nation. Therefore, developing and least-developed countries with low technology may be better off utilizing parallel imports instead of the compulsory licensing to increase access to essential drugs. Developing countries may be more secure from other countries' complaint against parallel imports because issues over international exhaustion doctrine cannot be brought to the WTO dispute settlement.

F. The Unresolved or Remaining Problems after The Doha Conference and

Conclusion

As the result of the Doha Conference, developing countries can issue a compulsory license or/and allow parallel imports (by implementing the international exhaustion doctrine) for public health reasons without fear of legal challenges from other WTO members. In practice, however, the U.S. still exerts pressure on developing countries to strengthen their patent protection on drugs because the U.S. pharmaceutical industry has a strong lobby. The volume of trade and profits from pharmaceutical sectors are large enough to get a close attention from both private and government agencies. Nevertheless, in comparison to compulsory licensing, parallel imports may be a better solution for developing countries, particular countries with low capacity to produce drugs.

However, parallel importation still presents the problem of how to find a source of low-priced drugs. The low-priced drugs may be available in countries that provide a relaxed patent protection or use compulsory licensing. Currently, developing countries with production capacity such as India and Brazil have liberalized or relaxed their patent

laws in order to produce the low cost drugs. Nevertheless, by the TRIPs deadline of 2005, these countries will have to raise their patent law standard to meet TRIPs obligation and may no longer be a source of parallel imports. In the case of compulsory licensing, developing countries with production capacity may issue compulsory licensing to produce essential drugs, but Article 31(f) of TRIPs Agreement only allows compulsory licensing of domestic manufactures serving the domestic market. So drugs made under compulsory licensing technically could not be imported for the need of a foreign country. The TRIPs council should allow parallel importation of compulsory licensed drugs. By relaxing on the interpretation of Article 31(f), the TRIPs Council should allow the strategy of the combination between compulsory licensing following by parallel imports (which is making a drugs under compulsory licensing in one country and then import to another).⁷⁸⁶

Also under Article 31(f) the countries with insufficient technology to manufacture drugs are not able to grant compulsory licensing to a foreign manufacture to produce and only provide medicines for the developing country's domestic market (known as a 'third party compulsory licensing'). WTO Members recognized this problem and instructed the

⁷⁸⁶ This strategy can be work if the TRIPs Council agrees that the drugs made under compulsory licensing can be used not only for domestic market but also for potential foreign markets. The combination of compulsory licensing in one country and then parallel imports in another country would work in a way to get inexpensive drugs where they are needed.; *see* WATAL, *supra* note 713, at 325. (pointing out that Article 31(f) does not rule out exports. However, exports will be permissible only to countries where the product is not patented or where a compulsory license has been issued to a local entity to import the product. Moreover, in relation to parallel imports, it is dubious whether exports can be allowed to countries that allow parallel imports. This argument applies also to the use of compulsory license to import the patented product because the TRIPs Agreement does not prohibit this.); and also *see* Carlos M. Correa, Patent Rights, in *INTELLECTUAL PROPERTY AND INTERNATIONAL TRADE: THE TRIPs AGREEMENT* 214-15 (Carlos M. Correa & Abdulqawi A. Yusuf, eds. 1998) (mentioning that the text of Article 31(f) does not completely ban exports of products covered under the compulsory licensing. In relation to the export market, the partial limitation may not be applied in connection with compulsory licenses on the grounds of anti-competitive practices under Article 31(k). This notion is consistent with the U.S. practices because exports by a compulsory licensee have been expressly permitted in the cases of license granted in the U.S. to remedy anti-competitive practices.)

TRIPs Council to find an expeditious solution before the end of 2002. Nevertheless, as of 2003, there has been no satisfying solution because of intense disagreement among members on this issue.

In my opinion, in the long-run TRIPs Agreement should allow members to use a 'third party compulsory licensing' which grants compulsory licensing to a foreign manufacture to produce and provide drug for the need of domestic consumers.⁷⁸⁷ This approach appears to be the best way to get a low-prices drug because, in the near future, it will be hard to find sources of low-priced drugs for parallel importation. Unfortunately, at present, 'third party compulsory licensing' is not allowed under the TRIPs Agreement. Therefore, parallel imports should help developing countries with insufficient technology to access to affordable essential drugs. In the short term, the combination of a relaxed patent law and liberalization of parallel imports under TRIPs may help to provide accessible low-priced drugs. Allowing parallel imports as a temporary solution may help to fill the need of developing countries in the intermediate term while the TRIPs Council works on providing a long-term solution to the issue.

⁷⁸⁷ In my opinion, a third party compulsory licensing approach differs from the combination of compulsory licensing and parallel imports since the former used no intermediary importers, thus avoiding price arbitrage. The later requires parallel importers and results in price arbitrage. The third party compulsory licensing approach is based on a straight pact between government and a foreign manufacturer and the goods produced under this licensing are directly exported from foreign country and import to the country issuing the compulsory licensing.

CHAPTER FOUR

RECOMMENDATIONS: THE HARMONIZING SOLUTION TO THE QUESTION OF PARALLEL IMPORTS

I. INTRODUCTION

As mentioned in the previous chapters, the question of parallel imports reflects the non-harmonized perspective between the developed and developing countries within the scope of the exhaustion doctrine, to which there is currently no global harmonizing solution. Historically, most developed countries have had a policy of restricting parallel imports by applying the national exhaustion doctrine in order to protect the benefits of intellectual property rights (IPRs) owners. Developed countries are mainly the producers or creators of intellectual property products and engage in international price differential. Up to now some developed countries have made some modifications toward the international exhaustion doctrine, but the United States continues to restrict parallel imports. Most other developing countries, however, allow parallel imports by applying the international exhaustion doctrine in order to support the consumer welfare and the free movement of goods. Developing countries are mainly considered the consumers or users of intellectual property products rather than the creators of those products.

From the free trade standpoint, the rules restricting parallel imports effectively restrain the international trade and cause the non-tariff barriers⁷⁸⁸ The WTO supports the global free trade based on the idea that free trade optimally benefits the whole society.⁷⁸⁹ In the international trading system, where free trade has a high value, it seems that the rule on parallel imports should be viewed favorably and possibly extended, there should have a consistent rule on this issue. Traders should know the rules in order to conduct their business within the rules. Different rules among countries may cause difficulties for traders to adopt the rules in different countries, which may finally decrease the volume of free trade. The inconsistent rule on parallel imports could impede the free movement of goods, which is incompatible with GATT principles. Thus, the international consensus on a uniform standard of the exhaustion doctrine should be conferred.

A realistic approach would be harmonizing the exhaustion doctrine through the TRIPs Agreement because this is a trade-related intellectual property issue and the TRIPs

⁷⁸⁸ See Abbott, *supra* note 7, at 479. (mentioning that referring to the exhaustion/parallel imports question, trade specialists deem that "rules blocking the importation of products are non-tariff barriers to trade, and that non-tariff barriers are fundamentally inconsistent with the principles of WTO, all other things being equal." Trade specialists approach the question with doubt that "rules blocking imports are inherently suspect. How can they be justified? This question will receive serious additional attention over the next few years."; and also see Robert M. Stern, *Introduction: Conflict and Cooperating in International Economic Policy and Law*, 17 U. PA. J. INT'L ECON. L. 539, 540-41(1996)(explaining the concept and benefit of free trade under the comparative advantage theory and the gains from trade.)

⁷⁸⁹ See JACKSON, *supra* note 6, at 436.(analyzing the advantage of free trade); see Michael Reynolds, Comment, *Examining the Foundation for a Free Trade Zone in the Americas*, 3 D.C.L. J. INT'L L. & PRAC. 521, 522 (1994)(explaining that international trade facilitates the producers' access to larger markets and equates to greater consumer consumption.); see JOHN CROOME, GUIDE TO THE URUGUAY ROUND ARGUMENT part V (1999) (mentioning that free trade constitutes economic benefits.); see David A. Gantz, Article, *Thirteenth Annual International Law Symposium "Negotiating the Free Trade Labyrinth: Your Map to the 21st Century": Introduction to the World Trading System and Trade Laws Protecting U.S. Business*, 18 WHITTIER L. REV. 289, 290(1997)(illustrating the increase of global trade); and also see World Trade Organization, A After Two Outstanding Years, World Trade Growth in 1996 Returned to Earlier Levels, available at <http://www.wto.org/wto/intltrad/intlorg.htm>. (visited Apr. 16, 2002).; and also see Abbott, *First Report*, *supra* note 83, at 611. (stating that the rules of WTO proceed from one basic idea: "that the elimination of barriers to the movement of goods and services across and within national boundaries is beneficial to global economic welfare because this encourages specialization and efficiency in production and distribution, and results in an increased output of goods and services.")

Agreement is specifically a trade-related intellectual property agreement.⁷⁹⁰ Additionally, most developed countries and developing countries are members of the TRIPs Agreement.⁷⁹¹ At present, there is no international legal standard in the application of exhaustion doctrine under the TRIPs Agreement. Article 6 of the TRIPs Agreement fails to address this issue and members are free to choose the scope of exhaustion doctrine in accordance with their own interests.⁷⁹² Hence, this dissertation aims to define the harmonizing solution for this matter by proposing the international exhaustion doctrine as an appropriate international standard for all WTO members.

II. THE REASONS TO CONSIDER THE APPLICATION OF INTERNATIONAL EXHAUSTION DOCTRINE AS THE HARMONIZING SOLUTION

Currently, there is a strong trend in national law relating to the exhaustion doctrine toward to the application of international exhaustion. Many developed and developing countries such as Japan, Australia, New Zealand, and Thailand have liberalized parallel imports under the application of the international exhaustion doctrine.

⁷⁹⁰ The TRIPs Agreement has been widely recognized by both developed and developing countries as an important multinational agreement, which reflects both developing and developed perspectives and balances their conflicts of interest. This Agreement provides the minimum standard of IPRs protection and harmonizes the national laws of members. Thus, it is appropriate to incorporate the international exhaustion scheme into the TRIPs Agreement. Moreover, the TRIPs Agreement has the dispute settlement mechanisms, which contain propositions for elaborating, identifying and developing the principle that are announced in this Agreement. *See* TRIPs, *supra* note 3, art. 63 and 64; and also *see* Understanding on Rules and Procedures Governing the Settlement of Disputes, Apr. 15, 1994, WTO Agreement, Annex 2, 33 I.L.M. 112 (1994).

⁷⁹¹ *See* Gantz, *supra* note 789, at 290, citing in U.S. Department of State, Treaties in Force 444 (1996); Currently, there are 146 countries being the WTO member on 4 April 2003. *see* The list of WTO members, available at http://www.wto.org/english/thewto_e/whatis_e/tif_e/org6_e.htm. (visited June 15, 2003)

⁷⁹² *See* Martinez, *supra* note 80, at 2. (pointing out that the exhaustion doctrine is a policy instrument to regulate the international arbitrage of goods incorporating IPRs. Therefore, the decision to choose among three regimes will put weight upon safeguarding competition in distribution and balancing the interests of consumers and producers.)

The European Union has already moved away from national to regional exhaustion and has a possible trend toward the international exhaustion doctrine, particularly in the area of trademark. Thus, it is possible that in the future, other countries would follow those countries' approaches and adopt the international exhaustion doctrine.⁷⁹³ The international exhaustion doctrine should be appropriately considered an international standard.

As aforementioned on the high value of free trade, the general rationale supporting the international exhaustion doctrine is based on the free trade. Adopting the international exhaustion throughout the world could encourage the free trade and free movement of goods.⁷⁹⁴ Hence, the high value of free trade should sufficiently support the justification of the international exhaustion doctrine. Additionally, there are other two specific rationales supporting the international exhaustion doctrine, which are the consumer's benefit and social development. The application of international exhaustion doctrine by allowing parallel imports could bring the most favorable benefit to consumers in terms of lower prices and more availability of products. Consumers in both developed and developing countries benefit from a greater selection of products, and the greater

⁷⁹³ For example, as discussed in Chapter Three, there is a potential trend in the European Union liberalizing parallel imports from outside the Community by changing from the Community-wide exhaustion to the international exhaustion doctrine in the area of trademark.

⁷⁹⁴ The international exhaustion doctrine is consistent with the TRIPs Agreement's purpose to reduce distortions and impediments in international trade. Many commentators suggest that the international exhaustion of IPRs should be incorporated in the future revision of the TRIPs Agreement, so as to bring it into full conformity with the ideals of free trade underpinning the GATT. See CORREA, *supra* note 143, at 82; see Yusuf, *supra* note 52, at 18; and also see MASKUS, *supra* note 38, at 13.; By recognizing the European Union's accomplishment in the application of the Community-wide exhaustion doctrine, it potentially deems that the international exhaustion doctrine should encourage free trade and free movement of goods among WTO members. As mentioned in Chapter Two, the EU has adopted the regional exhaustion doctrine known as the Community-wide exhaustion, which supports the free movement of goods within community. Therefore, if the Community-wide exhaustion efficiently promotes the free movement of goods at the regional level, the international exhaustion doctrine should positively promote the free movement of goods at the global level.

product competition leads to greater price competition.⁷⁹⁵ Parallel imports effectively enhance competition by playing an important role in neutralizing price differential by providing beneficial price competition.⁷⁹⁶ Although consumers in developed countries may get more benefits from the lower price rather than those in developing countries, consumers in developing countries still benefit in terms of availability and selection of needed products at affordable prices. Particularly, in the event that the owners of IPRs decide not to market their products in some developing countries, consumers in such countries can purchase those products from parallel importers.

With regard to the social development rationale, applying the international exhaustion by permitting parallel imports could encourage the dissemination of knowledge and essential products in the global level. Parallel imports support the diffusion of knowledge and information, which is the underlying principle of intellectual

⁷⁹⁵ See Fogel, *supra* note 64, at 333 and 335; see MASKUS, *supra* note 38, at 13. (pointing out that how parallel imports encourage price competition while limiting marketing incentives and concluding that it is not recommended to consider the global policy banning parallel imports.); and also see Abbott, *First Report*, *supra* note 83, at 612-13 and 620.

⁷⁹⁶ See Donnelly, *supra* note 82, at 501-03.; Parallel imports can play an important role in neutralizing price discrimination that benefit to consumers in the developed, developing, and least-developed countries in order to purchase the products at a reasonable price. From capitalism's perspective, the price of product depends on the demand and supply in the market. If one product in some national market is over the domestic demand, parallel imports can reallocate such a product to other national markets that have high demand for such goods. Thus it helps the international resource allocation among nations, reduces the anti-competitive acts of IPRs owner in price-fixing and licensing agreements, and prevents or reduces the counterfeit market or black market since parallel imported goods could fulfill the demand of low income market and consumers would prefer to buy parallel import goods rather than counterfeit goods. see Abbott, *First Report*, *supra* note 83, at 612, 619-624 and 623 (mentioning that the "international price discrimination distorts comparative advantage, and there is not persuasive evidence that it is necessary (or would be helpful) for promoting the interests of developing countries."); see Patricia M. Dazon, *The Economics of Parallel Trade, Pharmacoeconomics*, Mar., 13 (3), 293, 298 (1998), citing in Brittan L. Brittan speech on pharmaceutical pricing (press release) Brussels: European Commission, 1992 Dec. 2. (explaining that there is a common discernment that price differentials imply cost shifting "A pharmaceutical company may only be willing to sell in a low-price country because it can recoup any losses it makes there from sales in higher-priced countries.")

property rights protection, particularly copyright and patent.⁷⁹⁷ Most intellectual property products are considered essential products and implicated the knowledge such as encyclopedias, textbooks, educational software, and pharmaceuticals. Parallel imports increase the volume of a product's global distribution to consumers by either creating an additional distribution channel or facilitating the relocation of oversupplied goods from one country to another country that needs such goods. Therefore, the more channels of product distribution there are, the more diffusion of knowledge and essential products.

This dissertation proposes the international exhaustion doctrine as the international standard. But in reality, this approach needs an elaboration of details. Consequently, the following section will define and suggest the appropriate rule on international exhaustion doctrine.

⁷⁹⁷ The international exhaustion doctrine promotes the transfer and dissemination of technology. In other words, allowing parallel imports by adopting the international exhaustion doctrine supports the concept of free movement of goods and dissemination of intellectual property works. See Carlos A. Primo Braga, Intellectual Property Rights and Economic Development 31 (World Bank Discussion Paper No. 412, 2000)(explaining that granting the exclusive rights to IPRs owners restrict the diffusion of knowledge and information. However, simultaneously, IPRs can play a positive role in diffusion of knowledge and information and influence international transactions. The IPRs may increase the variety of internationally traded goods and services.); see Corlos M. Correa, *Pro-competitive Measures under TRIPS to Promote Technology Diffusion in Developing Countries*, in GLOBAL INTELLECTUAL PROPERTY RIGHTS: KNOWLEDGE, ACCESS AND DEVELOPMENT 41-44 (Peter Drahos & Ruth Mayne ed., 2002); see Gillian K. Hadfield, *The Economic of Copyright: An Historical Perspective*, 38 COPYRIGHT L. SYMP.(ASCAP), 1-46 (1992); see Report of The Register of Copyrights on The General Revision of the U.S. Copyright Law, 3-6 (1961)(stating "the ultimate purpose of copyright legislation is to foster the growth of learning and culture for the public welfare, and the grant of exclusive rights to authors for a limited time is a means to that end."); and also see H. Rep. No. 2222, 60th Cong., 2d Sess. (the legislative report on the Copyright Act of 1909).

III. THE HARMONIZING RULE ON THE INTERNATIONAL EXHAUSTION DOCTRINE

In the light of free trade, ideally every nation should adopt the pure international exhaustion doctrine that applies to all types of intellectual property rights, namely copyright, trademark, and patent. However, in practice there are political and policy rationales to step back from accepting the principle of the international exhaustion doctrine. The policy justification focuses on the purpose of the IPRs protection because the pure international exhaustion doctrine could diminish the main purpose of the IPRs protection. The IPRs protection has a value that should not be undermined by free trade.

The political justification concerns on the power of developed countries in international forum. As mentioned earlier, developed countries with high technology, have dominant political and economic powers that support the national exhaustion doctrine; conversely, developing countries with low technology, have fewer political and economic powers that support the international exhaustion doctrine. Expectedly, developed countries may not accept the concept of pure international exhaustion because the IPRs owners, who mainly reside in developed countries, would completely lose their exclusive right to control the further distribution of goods after the first sale. If developed countries disagree with the application of the international exhaustion doctrine, it would be impossible to establish the international exhaustion doctrine as the international legal standard. The important question is how to compromise the demands of both sides under the application of the international exhaustion doctrine.

Consequently, if the notion of the pure international exhaustion substantially conflicts with the developed countries' interest and the objective of the IPRs protection, the international standard should be the application of the international exhaustion doctrine with some limited exceptions. The limited exceptions are shaped by the concerns of developed countries and the core purpose of the IPRs protection.

As mentioned earlier, the harmonization on the rule of exhaustion doctrine should be done through the TRIPs Agreement. Therefore, this dissertation recommends that in the TRIPs Agreement, regardless of the types of IPRs protection, Article 6 should codify the international exhaustion doctrine as an international legal standard and the WTO dispute settlement should be used to address the issue of exhaustion doctrine. In other word, there should be affirmative norm of exhaustion doctrine in the TRIPs Agreement itself to provide the standard for dispute settlement to proceed.⁷⁹⁸ The international exhaustion doctrine should apply to copyright, patent and trademark with some limited exemptions. The provision of Article 6 should be:

Article 6: Exhaustion of Intellectual Property Rights

“Subject to the provisions of Article 9 ter, Article 11, Article 16bis and Article 28bis, the exclusive rights of an intellectual property owner shall be exhausted after the first sale or transfer of ownership of the goods incorporated intellectual

⁷⁹⁸Providing the affirmative norm and allowing the dispute settlement to address this issue could decrease the future arguments and the inconsistency among members on the issue of exhaustion. Currently, the current Article 6 of TRIPs Agreement exclusion of exhaustion from dispute settlement, except in relation to National Treatment (art.3) and Most-Favoured-Nation (art.4). Theoretically, the decision that country made about exhaustion may be treated as non-violation violation (so-called non-violation nullification or impairment under Article XXIII 1(b) of GATT) despite the fact that there was TRIPs consistency. TRIPs provides the IPRs protection in high level and the exclusion in the dispute settlement of exhaustion doctrine seem to negate the purpose of TRIPs Agreement. At present, the exhaustion doctrine can be brought to dispute settlement only if involving the Nation Treatment and Most-Favoured-Nation (MFN). The Community-wide exhaustion in the EU may cause the issue of MFN because of providing different treatment between goods from EU members and goods from outside the EU. However, it may be allowed under Article 4 (d) of TRIPs Agreement.; Under Article XXIII 1(b) of GATT, a WTO member have the right to raise complaint over measures by another member, although such measures do not violate specific provision or obligations of this Agreement, but these measure nullify or impair any benefit accruing directly or indirectly under the Agreement. See GATT, *supra* note 5, art. XXIII 1(b).

property rights anywhere in the world with the authorization of intellectual property owners.”

Note: Certain specific exemptions are provided in Article 9ter, Article 16bis, and Article 28bis. Article 9ter (Right of Communication) and Article 11 (Rental Right) refers to the specific exemption under copyright; Article 16bis refers to the specific exception under trademark; and Article 28bis refers to the specific exception under patent. Moreover, the authorization of intellectual property owner may be either express or implied for the first sale or transfer of ownership.⁷⁹⁹

Each type of the IPRs is tailored to a different policy, and the underlying purpose of each type of IPRs may vary from one another.⁸⁰⁰ Developed countries may have a different degree of concern depending on the type of IPRs. International exhaustion should be applied somewhat differently, in accordance with the various intellectual property law settings. Therefore, the following parts will clarify the appropriate specific exemption according to the type of IPRs.

⁷⁹⁹ As mentioned in Chapter Two in part of the European Union, the issue of consent is complicated and relevant to the application of the exhaustion doctrine. In the *Davidoff* case, the ECJ clearly stated that in the subject matter of whether the IPRs owner give a consent to market the goods in other territories or not, the consent may be either express or implied. However, the mere silence of the IPRs owner could not constitute an implied consent. The implied consent must unequivocally show that the IPRs owners have no intention to exercise their exclusive right in such territory. The ECJ court's interpretation on the issue of consent is useful for other cases when concerning whether the IPRs owners have authorized in the first sale or not. If the IPRs owners have authorized on the initial sale of goods anywhere in the world, either express or implied, they no longer have the right to control further distribution of these goods under the concept of the international exhaustion doctrine. Under the international exhaustion doctrine, it is unnecessary to determine whether IPRs owners have given their consent to import to other countries or have renounced their right thereof since their exclusive rights were already exhausted after the first sale.

⁸⁰⁰ See BRAGA, FINK & SEPULVEDA, *supra* note 795, at 3.(mentioning that the legal instruments for protecting intellectual property, namely patent, copyright, and trademark, differ in their subject matter, the degree of protection, and the field of application, which reflect the objective of society to balance the interest of creators and consumers for different types of intellectual property work.); and also see Abbott, *First Report*, *supra* note 83, at 614. (pointing out that data and conclusion with respect to one form of IPR should not be equally valid with respect to the other forms because the main purpose of each form of IPR is substantially different.)

A. Copyright

In case of copyright, all countries should straightforwardly apply the international exhaustion doctrine without an exception.⁸⁰¹ The object of copyright is to encourage or support the dissemination of information and knowledge, so the movement of copyright works should be free from control. Moreover, in comparison to patent, copyright work has a lower cost of investment than patent, which usually requires a high expenditure on research and development. A long-term protection of copyright, a life plus 70 years should be long enough for copyright owners to recoup their investments. The total income from the first sale of their copyright works in all markets (high-income and low-income markets) should sufficiently offset their investments. In addition, allowing parallel imports under the international exhaustion doctrine could help copyright owners increase their sales because, in terms of product distribution, parallel imports can bring the unneeded copyright works from a low-price market to a high-price market to meet the needs of low-income consumers in the high-price market.⁸⁰²

This proposal is consistent not only with Thailand's and Japan's stand on allowing parallel imports, but is also consistent with the current movements in Australia

⁸⁰¹ In case of a material difference between the imported product and domestic product, it should not affect the application of the international exhaustion doctrine in the area of copyright. For example, the books produced in Thailand have been printed with different materials than those products produced in the United State. In the U.S., books are made with fine paper and hard cover but in Thailand, books are made with thin and low quality paper and soft cover. However, these differences should not affect the application of international exhaustion since the contents of both books are the same and the consumer may expect the knowledge inside the books more important than the substance or material of these books. Nevertheless, at least the consumers should know such differences before making a decision to purchase these books. Actually, customers can see the obvious differences.

⁸⁰² Not all consumers in the high-price market have a high income. In other words, in the high-price market, there are both high-income and low-income consumers. The low-income consumers cannot afford to buy the high price products, but with the support of parallel import, they can buy the parallel imported products at lower prices. Moreover, the application of the international exhaustion doctrine is consistent with the trend of the global marketplace, in both the real world and a borderless marketplace of the Internet world, which facilitate the free movement of goods without boundary restrictions.

and New Zealand to liberalize parallel imports in area of copyright law. In addition, the United States also allows parallel imports of copyright work under the concept of first sale doctrine if such goods are made in the U.S. and are sold to oversea markets and then imported into the U.S. As ruled in the *Quality King Case*, the first sale doctrine is applicable to imported copies of copyright work.

Although the exhaustion doctrine generally applies to the distribution right, there are different aspects of distribution right that should not subject to the application of international exhaustion doctrine, which are the rental right and communication right.⁸⁰³ The rental right is a mode of distribution of the copyright work, but the international exhaustion doctrine should not apply to the rental right. The TRIPs Agreement obviously provides the rental right on computer programs and cinematographic works to copyright owners in Article 11 because the commercial rental of those works had lead to widespread copying. Thus, it is necessary to give an exclusive right to copyright owners to control the rental of their computer programs and cinematographic works.⁸⁰⁴

The communication right has been considered an aspect of the distribution.⁸⁰⁵ More properly, however, the communication right should be treated as a new hybrid

⁸⁰³ The exhaustion doctrine should apply only to the distribution right. Thus, this doctrine should not apply to reproduction right, adaptation right, moral right and performance right. The moral right should not exhaust after the first sale because the moral right is not a commercial right and aims to provide the rights of attribution and integrity to authors. Under Article 9 of TRIPs Agreement, WTO members are not obligated to recognize the moral right. However, they may grant the moral right to copyright owner. If members provide the moral right protection, the moral right naturally should not be subject to the exhaustion doctrine. Regarding performance right, unlike the rental right, the performance right does not involve the distribution of copies of copyright works. The exhaustion doctrine should not apply to the performance right. See Abbott, *First Report*, *supra* note 83, at 636.(pointing out that regarding the distinctive trait of the broadcast and performance market, the performance right of a copyright owner should not exhaust after the first sale.)

⁸⁰⁴ See TRIPs, *supra* note 3, art.11; see GERVAIS, *supra* note 44, at 84-86.

⁸⁰⁵ See Informational Infrastructure Task Force, Intellectual Property and the National Information Infrastructure: The Report of the Working Group on Intellectual Property Rights 215-18 (1995). (proposing that a new "transmission right" should be written into the current definition of "distribution" under section

exclusive right of copyright owner (relating to distribution, reproduction and performance right) that differs from the traditional exclusive rights. The communication right emerges because the existing exclusive rights cannot properly apply to the new digital environment. The communication right has its own characteristic that makes it different from the distribution right and should not be subject to the application of international exhaustion doctrine. Some copyright works can be transformed from tangible into digital form and can be transmitted throughout the Internet. The right of copyright owner should expand to include both carriage of tangible goods and transmission of digital goods. However, these rights may be defined in different types of exclusive rights under copyright law. For example, under the WIPO Copyright Treaty 1996, the right to control the movement of physical goods is called “distribution right,” but the right to control the dissemination of digital goods is called “communication right.” As the result of digital technology, online transmission has become a significant means of exploitation of copyright works.⁸⁰⁶ Actually, the copyright owner could not control the further

106.); There is a question whether the exhaustion doctrine applies to the transmission right. In the United States, the first sale doctrine or exhaustion doctrine in section 109 does not apply to digital transmission of copyright work. However, there was an idea of amendment section 109 in order to expand the first sale doctrine to digital transmission but this idea was heavily debated and finally did not succeed. See The United States Copyright Office, *The DMCA Section 104 Report: A Report of the Register of Copyrights Pursuant to § 104 of the Digital Millennium Copyright Act*, August 2001, available at <http://www.copyright.gov/reports/studies/dmca/sec-104-report-vol-1.pdf>. (visited Jan. 16, 2003) (The DMCA Section 104 Report provides both proponent’s and opponent’s view of revising section 109. This report concludes that to date, there was no convincing evidence to liberalize section 109 to cover digital transmission of a work. Section 109 should actually apply to the transfer of physical copied of works either in form of analog form or a digital format such as CDs or DVDs but does not extend to the transmission of a work.); and also see David L.Hayes, *Advanced Copyright Issues on the Internet*, 7 TEX. INTELL.PROP. L.J. 1, 39-40 (1998) (mentioning that the importation right under section 602(a) does not apply to Internet transmissions because there is no physical copy moved across international boundaries.)

⁸⁰⁶ See JÖRG REINBOTHE & SILKE VON LEWINSKI, *THE WIPO TREATIES 1996: THE WIPO COPYRIGHT TREATY AND THE WIPO PERFORMANCES AND PHONOGRAMS TREATY: COMMENTARY AND LEGAL ANALYSIS* 104 (2001).; Moreover, the transmission or availability of copyright works online allows the global public to copy them easily. Thus, copyright owners should have an exclusive right to control the communication to the public in order to prevent others from unlawfully copying their works.; Peter A.

transmission of digital products because retransmission or multiple transmissions can be easily made. This risk of lost control in digital transmission does not exist in the distribution of physical objects. Thus, the copyright owner should be entitled to control the digital transmission of their works and the international exhaustion doctrine should not apply to the communication right.

However, this dissertation proposes that the international exhaustion doctrine should be applied to the trade of tangible objects, which have come into physical existence as the result of the communication of copyright works to the public. In other words, physical copies either in digital or non-digital version generated as the result of communication to the public should be subject to the international exhaustion doctrine.⁸⁰⁷

Jaszi, *Impact of The TRIPS Agreement on Specific Disciplines: Copyrightable Literary and Artistic Works: Article: Goodbye to All That-A Reluctant (and Perhaps Premature) Adieu to a Constitutionally-Grounded Discourse of Public Interest in Copyright Law*, 29 VAND. J. TRANSNAT'L L. 595, 610 (1996) (pointing out the new vision of copyright in the new technology that "a new understating of the purposes of copyright, which focuses on promoting the well-being of the copyright industries rather than providing incentives to specific acts of creativity (or distribution), will gradually supplant the traditional understanding on which so much of our public interest rhetoric relies."); and also see Perter A. Jaszi, Symposium, *Innovation and the Information Environment: Caught in the Net of Copyright*, 75 OR.L. REV. 299, 300 (1996) (asking the interesting question "Is the Net changing copyright-or the other way around?" The answer is that "copyright is changing or is in the process of changing.")

⁸⁰⁷ In order to consider the application of exhaustion doctrine to the communication right, there are four possible scenarios depending on what purchasers acquire from such transmission. In the first scenario, purchasers experience the work in the real time via streaming audio transmission and they are not allowed to capture or record but are only allowed to listen such work. The exhaustion doctrine certainly does not apply in this scenarios because there is no physical copy neither digital nor non-digital version occurring as the result of such transmission. In the second scenario, purchasers are allowed to download the work but only by connection with the machine. For example, a purchased program has been downloaded in the hard drive of computer. The download has been made in the machine and there is a copy but not portable because it cannot exist apart from computer. In this case, the exhaustion doctrine is applicable and the owner of computer and computer software can legally sell this computer with the software. In the third scenario, purchases receive the digital transmission and are allowed to copy it only in a digital version, such as diskette or CD. The exhaustion doctrine applies in this case because there is a physical copy in digital version emerged as the result of transmission. In the last scenario, purchasers receive the digital transmission and are allowed to copy it both in digital version and non-digital version. The exhaustion doctrine is applicable in this case because there are physical copies in digital and non-digital versions.

In conclusion, the exhaustion doctrine is applicable only if the result of transmission creates a physical copy of copyright work either in digital version or non-digital (analog) version. Both non-digital and digital forms of copyright works should be treated equally under the international exhaustion doctrine. For example, in the case of digital goods, after customers purchase it and such goods are transformed into

Consequently, this dissertation suggests adding Article 9bis and Article 9ter into the TRIPs Agreement to clarify the application of the international exhaustion doctrine and the distinction between distribution right and communication right by following the WIPO Copyright Treaty 1996.⁸⁰⁸

physical copy either non-digital version or digital version - in a temporary form (such as in RAM) or in a permanent form (such as floppy diskettes or CD ROM), the international exhaustion doctrine would start to apply after this stage and the person who purchased would have the right to use, sell, or dispose it without interference by the copyright owner.

⁸⁰⁸ See World Intellectual Property Organization Copyright Treaty, adopted by Diplomatic Conference at Geneva, December 20, 1996, 36 I.L.M. 65 (1997). [hereinafter WIPO Copyright Treaty] The text WIPO Copyright Treaty is also available at <http://www.wipo.int/clea/docs/en/wo/wo033en.htm> (visited Feb. 7, 2003). World Intellectual Property Organization enacted the two treaties (Copyright Treaty and Performances and Phonograms Treaty) in order to bring the Berne Convention into correspondence with the TRIPs Agreement and to update the Berne Convention with the effects of digital technology. The Copyright Treaty 1996 distinguished between distribution right and communication right, which affects the application of the exhaustion doctrine. The distribution right under Article 6 only applies to the tangible object and the distribution right covers only the physical distribution of a work not including digital transmission, which is defined as the right of communication under Article 8. The Official Commentary on this article by the WIPO Drafting Committee clarified in the issue of whether the exhaustion should be national, regional or international, answering that the Copyright Treaty allows the international exhaustion doctrine. The exhaustion doctrine only applies to the distribution right, not the communication right, since the Commentary noted that "no rights are exhausted in connection with communication to the public, explaining that in the cases where communication of a work results in the reproduction of a copy at the recipient end, the work may not be communicated further to the public or distributed to the public without authorization." It means that exhaustion of right is only associated with the distribution of tangible copies. Article 6 provides: Right of Distribution

"(1) Authors of literary and artistic works shall enjoy the exclusive right of authorizing the making available to the public of the original and copies of their works through sale or other transfer of ownership.

(2) Nothing in this Treaty shall affect the freedom of Contracting Parties to determine the conditions, if any, under which the exhaustion of the right in paragraph (1) applies after the first sale or other transfer of ownership of the original or a copy of work with the authorization of the author."

Article 8 provides: Right of Communication to the Public

"Without prejudice to the provisions of Article 11(1)(ii), 11bis(1)(i) and (ii), 11ter(1)(ii), 14(1)(ii) and 14bis(1) of the Berne Convention, authors of literary and artistic works shall enjoy the exclusive right of authorizing any communication to the public of their works, by wire or wireless means, including the making available to the public of their works in such a way that members of the public may access these works from a place and at a time individually chosen by them."

In my opinion, at least after the copy of work is transferred into physical copy, the right of copyright owner should be exhausted after this point. The physical copy should be included the download of such work into either permanent form, such as floppy diskettes or CD ROM or temporary form, such as RAM (volatile memory). The reason to include temporary form such as RAM is that under the copyright law only downloading computer software on RAM may constitute a copyright infringement as the court mentioned in the MAI case. (MAI Systems Corp. v. PEAK Computer, Inc., 991 F.2d 511 (9th Cir. 1993)) Moreover, making a work available on the Internet for users to download from the webpage is considered as a distribution of copies. (see *Playboy Enters. v. Sanfilippo*, 46 U.S.P.Q. 2d 1350 (S.D. Cal. 1998); *Playboy Enters. v. Webbworld, Inc.*, 991 F. Supp. 543 (N.D. Tex. 1997); and *Playboy Enters. v. Frena*, 839

The proposed text of Article 9bis and Article 9 ter should state:

Article 9 bis: Right of Distribution

- (1) Member shall provide authors of literary and artistic works the exclusive right of authorizing the making available to the public of the tangible original and copies of their works through sale or other transfer of ownership.
- (2) The exhaustion of right in paragraph (1) applies after the first sale or other transfer of ownership of the original or a copy of the work with the authorization of the author, which have taken place anywhere in the world.⁸⁰⁹

Article 9 ter: Right of Communication

- (1) Without prejudice to the provisions of Article 11(1)(ii), 11bis(1)(i) and (ii), 11ter(1)(ii), 14(1)(ii) and 14bis(1) of the Berne Convention, Member shall provide authors of literary and artistic works the exclusive right of authorizing any communication to the public of their works, by wire or wireless means, including the marking available to the public of their works in such a way that members of the public may access these works from a place and at a time individually chosen by them.
- (2) The right of communication is not subject to the exhaustion of right, unless the final process of communication is associated with the distribution of tangible copies subject to Article 9 bis.”⁸¹⁰

B. Trademark

In the case of trademark, all countries should apply the international exhaustion doctrine, but subject to a specific exception. The specific exception is the difference in

F. Supp. 1552 (M.D. Fla. 1993.)) Thus, downloading music, electronic books or movies on the volatile memory of computer known as RAM should be sufficiently considered that such digital copyright work is transferred into physical form that may trigger the first sale doctrine.

⁸⁰⁹ The proposed Article 9bis(1) of the TRIPs Agreement is identical to Article 6(1) of the WIPO Copyright Treaty. Unlike Article 6(2) of the WIPO Copyright Treaty, which allows Contracting Parties to apply either international or national exhaustion doctrine, Article 9 bis (2) should be clearly stated that the distribution right is subject to the international exhaustion doctrine not national exhaustion. Reiterating the international exhaustion doctrine in Article 9bis(2) should definitely confirm that the international exhaustion is considered a uniform standard under the TRIPs Agreement.

⁸¹⁰ The proposed Article 9 ter (1) of the TRIPs Agreement is identical to Article 8 of the WIPO Copyright Treaty. Unlike Article 8 the WIPO Copyright Treaty, which does not mention to the application of exhaustion doctrine. Thus, this thesis proposes to add Article 9 bis (2) in order to clarify that the international exhaustion doctrine does not apply to communication right but if the final process of communication constitutes the tangible objects, it should fall back to the scope of Article 9 bis distribution right and be subject to the application of the international exhaustion doctrine.

quality or in characteristic (material) between domestic goods and parallel imported goods. The degree of the difference should be substantial. Based on the policy rationale of protecting the purpose of trademark, this exception should exist because it promotes the goal of trademark, which is to protect consumer from confusion. This specific exception is consistent with the substance of trademark (as an indicator of a source of origin and a guarantee of quality) and with consumer protection. This concept has been applied in many countries' approaches such as the United States, the European Union, Japan, Thailand, and Hong Kong.⁸¹¹ In addition, the international exhaustion should be applied without concern about the issue of control, whether the person who produces the goods is a subsidiary or affiliate company or the same company. By focusing on the product itself, if the goods have the same standard both in quality and material, it would not cause consumer confusion or harm the trademark owner's reputation. It is consistent with the purpose of trademark as the guarantee of quality of products.

However, there is a question on how to decide whether there is substantial difference in quality or material between domestic and imported goods, and who should be authorized to decide on this issue. This dissertation suggests that the national court of each country should have the authority to decide whether the imported goods are

⁸¹¹ The United States allows parallel imports if the goods are initially sold in a foreign country by the same owner or affiliate company since it does not damage the function of trademark as an identification of source. However, if the imported goods differ from the domestic goods, the US trademark owner can stop such importation because it possibly causes consumer confusion and harms the function of trademark as an identification of quality. The European Union also adopted this concept into the EC trademark directive by codifying that in case of there are differences in quality and material between domestic goods and imported goods from other members, the Community-wide exhaustion does not apply in this case. Currently in the EU, there is a possibility of changing from the Community-wide exhaustion to the international exhaustion in area of trademark as the result of consumers' pressure. Generally Japan also allows parallel imports of trademark goods if the imported goods are not different from domestic goods. Based on the concept of the international exhaustion doctrine, Thailand and Hong Kong obviously allow parallel imports in area of trademark law, unless the imported goods are different from domestic goods.

substantially different from the domestic goods or not. Nevertheless, the court in each nation may have a different standard concerning the question of substantial difference and may cause an unsatisfactory outcome.⁸¹² This discrepancy is considered a minor matter because the courts tend to make similar decisions. If they decide differently, the effect of differences in their decisions would not fall within the international trade system, but only have significance in the domestic market. Therefore, this minor matter should not be treated seriously and defeat the whole concept of liberalizing parallel imports and harmonizing the national laws of TRIPs Agreement member countries on the exhaustion doctrine.

Consequently, this dissertation suggests adding Article 16bis into the TRIPs Agreement to clarify the application of the international exhaustion and the specific exception in area of trademark. The proposed text of Article 16bis should provide:

Article 16bis: Exhaustion of Trademark

- (1) The trademark shall not entitle the proprietor to prohibit its use in relation to goods, which have been put on the market anywhere in the world under that trademark by the proprietor or with his consent.
- (2) The provision of paragraph (1) shall not apply where the condition of the imported goods is substantially different from that of the domestic goods, which may cause consumer confusion.⁸¹³

⁸¹² This issue may be solved by providing a guideline under the TRIPs Agreement. This guideline should explain and provide which elements may be concerned and what degree of difference may be considered being the substantial difference.

⁸¹³ This provision follows the EU approach (Article 7 of Trademark Directive). However, the scope of this proposed provision is narrower than that of Article 7 of Trademark Directive. Article 7(2) uses the phrase "where there are exist legitimate reasons for the proprietor to oppose further commercialization of goods, especially where the condition of the goods is changed or impaired after they have been put on the market." The text is too broad and opens room for trademark proprietor to oppose parallel imports if he has an appropriate rationale because the difference between imported and domestic goods is considered as one of legitimate reasons. This thesis proposes to limit the exception only when there is a substantial difference between the imported goods and domestic goods because the broad exception may destroy the spirit of international exhaustion doctrine and free trade.

C. Patent

All members should adopt the international exhaustion doctrine in area of patent, similar to area of copyright and trademark.⁸¹⁴ However, developed countries, particularly the United States, might be seriously concerned about the patent right to control after the first sale because they dominate patent research and development and want to control the further distribution of their products to recoup their investments. The application of the international exhaustion doctrine without the exception may destroy the core purpose of patent as an incentive of innovation. Moreover, the patent inventions, particularly pharmaceuticals and health products, have an important value to society; so the price of products set by patent owners should be reasonable and affordable to consumers. It means that the price on the first sale of products may not enough to secure the patent owner's return-on-investment. Thus, the law should give patent owners the additional right to control the further distribution of patent goods if they choose to do so. In brief, as a result of political concerns and the awareness of the high investment in research and development and the short term of patent protection (20 years), it should have an exception for patent holders to permit them to recoup their investment by prohibiting parallel imports.

Therefore, this dissertation proposes that the patent owners should have the power to control patented products by using a restriction clause.⁸¹⁵ If the patent holder has a

⁸¹⁴ Patent, copyright and trademark should be subject to the same doctrine, which is the international exhaustion doctrine, in order to avoid any discrepancies. The inconsistency may cause a non-harmonization among trademark, copyright and patent.

⁸¹⁵ See Harvey E. Bale, *The Conflicts Between Parallel Trade and Product Access and Innovation: The Case of Pharmaceuticals*, 1 J.INT'L ECON.L.637 (1998) (pointing out that in the case of patented products with high fixed costs, such as pharmaceuticals, parallel trade may decrease global economic welfare and suggesting that rules restricting parallel trade are necessary to facilitate pharmaceutical price discrimination).

restriction clause on the resale or importation, which has been clearly stated in the contract and on the package or label of the products, the right of the patent holder should not exhaust as the result of the first sale.⁸¹⁶ The patent owner can prohibit such parallel imports. This concept is consistent with Japanese approach by assuming that if the patent owner does not provide a restriction clause on resale or import, the purchaser is free to import and the right of patent owner exhausts after the first sale. In addition, in the United States, some courts have decided that if the person, who sells such patent articles either in the U.S. or abroad, has the right to sell in the U.S. and there is no restriction clause on resale or import, the purchaser is free to import them to the U.S. and the right of the patentee exhausts after the first sale.⁸¹⁷ In the case of Thailand, the Thai patent law obviously incorporates the international exhaustion doctrine and allows parallel imports of patent products.⁸¹⁸

Nevertheless, developing countries might worry that the patent owners have too much power to control their products by asserting the restriction clause on resale or import. There should be an exception to the exception that allows developing countries to

in favor of developing countries.); There is a concern that this exception may over take or consume the rule of international exhaustion. However, there is an economic rationale to explain the reason that some patent owners may not use or claim this exception. Patent owners may choose not to control the subsequent sale by not putting the notice on their product, if they believe that the price of products on the first sale is enough to cover their investment and that the product should freely flow from country to country for their long-term benefit. Parallel importers may help patent owners to reallocate the oversupplied goods in one country to another country that needs such goods. In the long run, parallel imports may help to increase the sale of patent products. The more volume of sale, the more return to patent owners.

⁸¹⁶ The statement of restriction clause should be written on the product label of each individual item. In the case that a buyer remove the label and later import to other countries without authorization, the patent owner cannot sue that person due to lack of contract privity. However, the patent owner can sue the authorized distributor who sale those products to the third party, if they neglect to impose the restriction clause an to scrutinize the further action of purchaser.

⁸¹⁷ See *Curtiss Aeroplane & Motor Corp. v. United Aircraft Eng'g Corp.*, 266 F.71 (2d Cir. 1920); *Sanofi, S.A. v. Med. Tech Veterinarian Prod. Inc.*, 565 Supp. 931 (D.N.J. 1983); and for more detail see *supra* note 251 and 253.

⁸¹⁸ See the text of Article 36 (7) of the Patent Act 1999 in *supra* note 502.

import the patent goods under specific circumstances. By considering an exception to the exception, in the case of a national emergency, the public health, or an essential necessary use of the patent, the patent holder cannot prohibit parallel imports, and it should fall back to the application of the international exhaustion even though there is a restriction clause on importation.⁸¹⁹ The concept of an exception to the exception is consistent with the current concern on the issue of access to essential drugs. In the case of essential drugs, under this concept the member country with the health crisis may use an exception to the exception to allow parallel imports of essential drugs to fill the need of domestic consumers, even though there is a restriction clause on resale or importation on the initial sale of these drugs.⁸²⁰ Moreover, using the word “an essential necessary use” should sufficiently cover the use of other important technologies other than the area of drugs.⁸²¹ It may help to ensure that developing countries can use such technologies if such technologies are necessary for their countries. Thus, an exception to the exception should be sufficiently wide in order to limit the effects of the restriction clause on the further distribution or importation.

⁸¹⁹ The reason is that the essential pharmaceuticals are considered as a necessary thing for all humans. The health matter should be taken into account rather than the IPRs protection concern. *See Abbott, TRIPS and Public Health Crisis, supra* note 769, at 85. (stating “For better or worse, we live in an increasingly borderless world. It is a world in which every state must make some reasonable accommodation to global interests. The United States and other OECD countries should reign-in their industry constituencies and consider long-term global security interests. The TRIPS Agreement is not only about protecting pharmaceutical industry profits. It is also about the health of the global economy, and about the health of individuals.”)

⁸²⁰ As mentioned in Chapter Three, in order to increase access to essential drugs, the provision of the TRIPS Agreement Article 31 and 31(f) should be interpreted in the way that permits Members to issue a third party compulsory licensing to a foreign manufacturer in case they do have insufficient technology to produce essential drugs for the needs of domestic consumers. The importation of drugs made by a foreign manufacturer for the needs of a country that issues a third party compulsory licensing should be consistent with the condition under Article 31 (f) “any such use shall be authorized predominantly for the supply of the domestic market of the Member authorizing such use.”

⁸²¹ An exception to the exception is useful to all members that have a necessity to use such patents, for example the medical equipment or the non-polluting automobiles.

Consequently, this dissertation suggests adding Article 28bis into the TRIPs Agreement in order to clarify the application of the international exhaustion and the specific exception in area of patent. The proposed text of Article 28bis should provide:

Article 28bis: Exhaustion of Patent

- (1) The patent holder shall not have the right to prohibit the importation of goods, which have been put on the market anywhere in the world by the patent holder or with his consent.
- (2) The provision of paragraph (1) shall not apply where at the time of first sale, the patent holder clearly stated a restriction clause of further distribution or importation of such goods in the contract and is clearly stated on the package or label of products.
- (3) Notwithstanding of paragraph (2), Members may exclude from obligation in the provision of paragraph (2) in the event of an essential necessary use or a national emergency, when it is necessary to protect order public or morality, including protecting human, animal or plant life or health or environment.”

IV. CONCLUSION

Certainly, the exercise of the intellectual property rights should not impede the notion of free trade. Simultaneously, the notion of free trade should not seriously diminish the concept of the protection of IPRs.⁸²² The application of the international exhaustion doctrine with specific exceptions is considered the appropriate doctrine for balancing the exercise of IPRs and the notion of free trade. The concept of codifying the international exhaustion doctrine into the TRIPs Agreement would not only reduce the discrepancy among WTO members but would also encourage the free movement of goods, which is one of the main purposes of WTO. To make this concept succeed, it

⁸²² A balance is necessary between the exercise of IPRs and the notion of free trade. It is recognized that the TRIPs Agreement, which mainly provides the minimum requirement for the IPRs protection, is a part of WTO, which principally supports the free trade among WTO members by eliminating both tariff and non-tariff barriers. Thus, the exercise of right by IPRs owner under the TRIPs Agreement should not detract from the main function of WTO/GATT. However, the proper exercise of IPRs should support the free trade because the TRIPs Agreement is aimed at reducing distortions and impediments to international trade.

needs a strong support from the WTO members. It seems that most developing and least-developed countries and some developed countries such as Japan, Australia and New Zealand may be the major advocates for the idea of adopting the international exhaustion doctrine into the TRIPs Agreement. Moreover, the current consumers' movements in liberalizing parallel imports in the areas of copyright, trademark and patent are a major motivation for adopting the international exhaustion doctrine as international legal standard under the TRIPs Agreement.

As mentioned in the earlier chapters, this dissertation addresses both the developing countries' perception and the developed countries' perception. The proposed solutions under this dissertation could be considered an intermediate approach by taking into account the perspectives of both developed and developing countries on the issue of parallel imports. The dissertation aims to find a balance between the benefits of the developed and developing countries and between the interests of IPRs owners and consumers. Consequently, this dissertation, advocating the international exhaustion doctrine, should be useful in supporting the concept of adopting the international exhaustion doctrine into the TRIPs Agreement.

The idea of codifying the international exhaustion doctrine emerged at the time of drafting Article 6 of the TRIPs Agreement, but it did not succeed.⁸²³ Finally, Article 6

⁸²³ See WATAL, *supra* note 713, at 295-96, citing in Jacques J. Gorlin, *An Analysis of the Pharmaceutical-Related Provisions of the WTO TRIPS (Intellectual Property) Agreement*, Intellectual Property Institute, London at 15-16 (1999) for the perspective of U.S. on this negotiation. (explaining that the negotiation was led by Hong Kong, Australia, New Zealand, Singapore and India. In the late 1990 and early 1991, the U.S. was not strongly opposed to this provision, the U.S. only wanted to balance the language to ensure that parallel exports from price controlled regimes would not be permitted. In 1991, the focus of U.S. and EC negotiators was to achieve neutral language. The final text does not prohibit the U.S. from using other means, such as unilateral measures, to persuade WTO members to prohibit parallel trade. It is possible that excluding the application of the WTO, DSU also excludes the prohibition on the use of unilateral trade sanctions.); and also see MATTHEWS, *supra* note 143, at 48-49.

leaves it open to Members to apply the exhaustion doctrine at their own discretion. Although the question of parallel imports is currently not included in the Doha Development Agenda, it does not mean that this issue will not be included in the next meeting's agenda. In the future, it is possible that the concept of codifying the international exhaustion doctrine may be revitalized and possibly succeeded if there is a strong support from all WTO Members, particularly from the developing and least-developed countries and international organizations, as occurred at the WTO Doha Conference. Due to the strong movement by the developing countries, their consumers and various international organizations to liberalize parallel imports of patent pharmaceuticals, the Doha conference finally allowed Members to use parallel imports in order to increase access to essential drugs. Hence, with the strong coordinated support of all developing countries and international organizations, the international exhaustion doctrine can become a uniform standard under the TRIPs Agreement. It seems that a small river by itself cannot destroy a strong dam, but the amalgamation of many rivers has the potential to do so.

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