

Exhaustion of Trademark Rights and Parallel Importation

May 26, 1999

Sponsoring Committee: Exhaustion of Trademark Rights and Parallel Importation
Subcommittee of the Issues and Policy Committee

Resolution

WHEREAS, trademark owners often design their products, packaging, and sales and distribution networks to meet specific cultural, environmental, and other conditions in specific countries; and

WHEREAS, the value of a trademark depends in large part on the goodwill generated by providing the consumer with a consistent level of quality and service; and

WHEREAS, the value of a trademark can therefore be undermined if a standard of international exhaustion of trademark rights and free parallel importation is followed;

BE IT RESOLVED that the International Trademark Association favors national exhaustion of trademark rights in relation to the parallel importation of goods.

Background

The debate over parallel importation focuses on the extent to which a trademark owner should be allowed to maintain control over its own brands by using its trademark rights in a country (or group of countries as we have defined “national”) [1] to restrict the importation of goods into that country after the goods have been put on the market somewhere else by the trademark owner or with its consent.

Prior INTA Positions

INTA has taken positions on the issue in the past. On September 9, 1986, the Board of Directors approved a Resolution stating:

BE IT RESOLVED that the United States Trademark Association (USTA) disapproves parallel imports when such imports are likely to deceive consumers as to the origin, characteristics,

qualities, warranties or other similar elements of the imported goods; and

BE IT FURTHER RESOLVED that at the present time, USTA neither approves or disapproves parallel imports when such imports are not likely to deceive consumers as to the origin, characteristics, qualities, warranties or other similar elements of the imported goods.

This Resolution was reaffirmed by the Board on September 18, 1996, with the following amendment:

BE IT FURTHER RESOLVED, that it is the position of INTA that the foregoing Resolution has worldwide applicability regardless of country of origin or destination.

In 1987, the Board of Directors approved the following Resolution:

WHEREAS consumers rely upon trademarks to identify products and services with specific characteristics they desire and expect; and

WHEREAS businesses rely upon trademarks to establish good will for themselves and the goods and services they produce, market and sell; and

WHEREAS trademarks designate the source of, affix responsibility for and assure the quality of goods and services sold in the marketplace; and

WHEREAS trademark rights are recognized and created under disparate national laws which establish and govern the scope of their protection in each respective national jurisdiction;

BE IT RESOLVED, that the USTA believes the concept of the territoriality of trademark rights to be vital to protect consumers from confusion, mistake or deception; to safeguard the good will businesses build and maintain in their marks; provided, however, that the exercise of such rights shall be consistent with the established principles of trademark law and shall not adversely affect fair competition; and

BE IT FURTHER RESOLVED, that USTA disapproves in principle Senate Bill S.1097 (Chafee), which would provide for the continuation of parallel imports under section 526 of the Tariff Act of 1930, as that section is currently interpreted by the Customs Service; and approves in principle Senate Bill S. 1671 (Hatch), which would provide that any owner of a registered trademark may request that certain goods be excluded, if such goods are imported into the United States or sold without authorization of the trademark owner.

The Parallel Importation Subcommittee of the Issues and Policy Committee was asked to re-evaluate these past resolutions and determine if a stronger position was appropriate. In the past year, several events have occurred in Europe and the U.S. which reflect an increasingly negative attitude toward the concept of national exhaustion, and INTA has found its ability to

speak out in defense of the rights of trademark owners hampered by the limited nature of its previous resolutions.

Recent Government Actions Impacting the Issue

In July 1998, the European Court of Justice (ECJ) rendered its decision in the case of *Silhouette v. Hartlauer* [2]. The ECJ found in favor of Silhouette, reaffirming the standard of national exhaustion as it is defined in this resolution. The Court reasoned that, based on the European Trademarks Directive, [3] Member States of the European Community should not be permitted to adopt a standard of international exhaustion. This was affirmed by the opinion of the ECJ's Advocate-General in March 1999 in *Sebago Inc. v. GB-Unic SA*. [4]

In response to the ECJ's decision in the Silhouette case, however, supporters of international exhaustion encouraged the governments of several countries to request that the European Commission revisit the exhaustion issue and adopt an international exhaustion regime. A Commission-ordered study, released in February of 1999, considered the economic consequences of such a change. The study did not make any recommendations as to which exhaustion regime would be preferable but focused instead on anticipated changes in price and trade volumes, employment, and other macroeconomic effects. However, the study did survey trademark owners as to the anticipated effect of a change to international exhaustion. In general, the trademark owners surveyed indicated that their businesses would be adversely affected by the increase in parallel imports likely to result from a change to international exhaustion.

The U.S. has also witnessed a recent challenge to trademark owners' rights to control their brands. In 1998, the U.S. Customs Service proposed regulations that would allow the importation of goods that are physically and materially different from those authorized for sale with the same trademark in the U.S. as long as the goods carry a label identifying them as such. Despite INTA's stated opposition, these regulations came into effect March 26, 1999.

Current Debate over Parallel Imports

Proponents of international exhaustion favor lower prices regardless of any potential adverse effect on brands. Given these developments, the Subcommittee concluded that it was important for INTA to speak out more clearly and definitively in support of national exhaustion. INTA's 1986 resolution, reaffirmed in 1996, focused too narrowly on deception of the consumer as the sole detriment to the brand caused by unrestricted parallel imports. The 1987 resolution focused too narrowly on a specific piece of U.S. legislation, thereby preventing INTA from using it to take positions in other countries.

A standard of national exhaustion appropriately takes into account many brand protection concerns that are not addressed under a standard of international exhaustion. The prices at which products are sold can vary from country to country for a great variety of legitimate reasons, among them differences in regulatory requirements, environmental standards, labor and material costs, and government subsidies and taxes. Parallel importers exploit these

conditions by buying products in a market where they are relatively cheap and selling them where the price is higher. They argue that parallel trade enhances competition and benefits consumers by providing for a larger distribution of branded products at lower prices. However, parallel importers have little or no incentive to maintain the goodwill of the mark and its ability to attract customers in the future. The parallel importer spends less time and effort to ensure the quality of the product and may provide little, if any, warranty or service.

Further, given the wide diversity of personal preferences among consumers and of environmental standards and conditions in unrelated cultures and economies, products with the same trademark often vary when produced for sale in different markets. For example, personal care or cleaning products sold for use in some countries are formulated to meet hard water conditions which do not exist in other countries. A brand of toothpaste in one country may taste different from the same brand sold in another country because the brand owner has researched local flavor preferences and tailored the product accordingly. Ingredients in motor oils need to be adjusted according to the climate in which they are intended to be sold.

Price alone is not a consumer's only concern when buying a product. The consumer relies on the trademark to identify specific goods or services that will meet certain expectations about the quality and characteristics of the product and the level of after-sales service. If these expectations are not met because a consumer receives a product intended for sale in another market, even if he or she has not been deceived in any way about the product, the consumer will be disappointed and will usually blame the trademark owner. Thus the trademark owner's reputation is damaged and the brand value diminished.

Brand value may also be damaged by virtue of the impact fluctuation in currency exchange rates has on the availability of parallel imports. The trademark owner has no control over currency fluctuations, yet they may be very damaging to its ability to command a reasonable price for an exclusive license in a particular jurisdiction if there is no protection against parallel importation from countries with weak currencies. A standard of international exhaustion could well reduce the value of a brand by reducing the amount a licensee would be willing to pay for an exclusive license.

A standard of international exhaustion fails to take into account any of the above considerations relevant to maintaining and enhancing trademark rights through brand recognition.

No International Consensus on Exhaustion of Rights

There is currently no international treaty in the field of trademarks dictating a standard of national or international exhaustion. The Paris Convention does not address the issue. The Agreement on Trade Related Aspects of Intellectual Property (TRIPs) is deliberately neutral on the subject. Article 6 of TRIPs states:

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.

In order to get an overview of the worldwide situation regarding parallel imports, the Subcommittee researched legislation and case law in various jurisdictions as well as treaties in certain regional groupings. In general, it was found that most countries favor some concept of national exhaustion.

Conclusion

Based on its analysis and deliberations, the Subcommittee recommends that the Board adopt a resolution supporting the principle of national exhaustion of trademark rights.

Notes

[1] “National” in this resolution refers to an independent country or group of countries which have adopted a single, common market with an overriding governmental authority, which operates rules and regulations in the field of intellectual property for the common market, and which operates a court system which has the ultimate authority on the interpretation and enforcement of those rules and regulations. The European Community (or by special treaty the European Economic Area) and the United States of America are examples of such single markets. Treaties ruling free trade in a given area may not fall under this definition.

[2] Case C-355/96, [1998] CEC 676

[3] Article 7 of the First Council Directive 89/104/EEC of 21 December 1988 to approximate the laws of the Member States relating to trade marks provides as follows: 1) The trade mark 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 trade mark by the proprietor or with his consent. 2) Paragraph 1 shall not apply where there exist legitimate reasons for the proprietor to oppose further commercialisation of the goods, especially where the condition of the goods is changed or impaired after they have been put on the market.

[4] Case C-173/98, [1999]. In *Sebago*, the Advocate-General rejected an argument that a trademark owner impliedly consents to the marketing within the EEA of its full line of products where it has only consented to the marketing of a batch of identical products, reasoning that to rule otherwise would recognize a standard of international exhaustion that is inconsistent with the Harmonization Directive as discussed in the *Silhouette* case.