

Summary Report

Question Q 156

International Exhaustion of Industrial Property Rights

I Introduction

The question considers the issues surrounding international exhaustion of industrial property rights (patents, trademarks, designs and plant breeders' rights). The question does not concern copyright and related rights. It gives AIPPI an opportunity to build on the resolution on Q101 (Exhaustion of Patent Rights) (Yearbook 1991/1, 298).

The Reporter General received 29 Reports from the following groups: Argentina, Australia, Belgium, Brazil, Bulgaria, Canada, Czech Republic, Denmark, Egypt, Finland, France, Germany, Hungary, Italy, Japan, Korea, Mexico, the Netherlands, Paraguay, Portugal, Romania, Singapore, Spain, Sweden, Switzerland, the United Kingdom, the United States, Venezuela and Yugoslavia. The Reports give an excellent overview of the law in the reporting countries.

II Questions

Question 1.

Is there international exhaustion of (i) patents; (ii) trade marks; and (iii) other industrial property rights? That is, can an industrial property right owner use industrial property rights against parallel imports from another country, when the imported products have been put on the market in that country by the industrial property owner or with consent?

A number of groups noted that international exhaustion is not solely a legal issue - there are **economic** and **political** aspects which must be balanced.

(i) **Patents:** AIPPI resolved in Q101:

"The AIPPI resolves that a patentee be able to invoke its patent against parallel import of a patented product, notwithstanding the circumstances under which such product has been put on the market in country B, subject to exception by contractual agreement authorizing import of the product in country A.

"The ability to invoke the patent against parallel import of patented products is a logical consequence of the fundamental principle of territoriality of patent rights. The inability to prevent parallel import diminishes the value of patents and the benefits deriving therefrom.

"The AIPPI observes that arrangements may exist where a number of countries decide to form a single regional market, in effect defining a single regional territory. In such an arrangement, a requirement for freedom of movement of goods within a single market may lead to acceptance of the legitimacy of parallel imports between countries which are party to the arrangement, provided that those countries together

agree among themselves that such a restriction of the rights of a patentee is necessary in the realization of such a single market."

The following states do not apply a rule of international exhaustion of patents: Australia, Belgium, Brazil, Bulgaria, Czech Republic, Denmark, Egypt, Finland, France, Germany, Hungary, Italy, Japan, Korea, Mexico, the Netherlands, Paraguay, Portugal, Republic of Korea, Romania, Spain, Sweden, the United Kingdom, United States and Yugoslavia. In contrast, Argentina, Canada, Singapore and Venezuela do apply a rule of international exhaustion to patents. The Canadian group noted the "stream of commerce" by which genuine goods of an IPR owner might be free to move.

Some countries which have a common law heritage (including Australia, Canada and the UK) noted English case law to the effect that a sale by a patentee without restriction allows the purchaser to re-sell patented goods in any country, by reason of an implied licence. In contrast, a licensee of a patent may only import into another country if permission is given in the licence. The Australian group reported that sale by an Australian patentee without any conditions attached, in any other country of a patented product would confer on the purchaser a licence to import the product into Australia. The US group noted that a licence to import was required. The Canadian group noted that while there was a regional economic arrangement under NAFTA, this does not deal with the question of parallel imports or provide for regional exhaustion. The Brazilian Group noted that where the patentee is exploiting his patent by means of importation then third parties may also import. This may, however, not conform with Article 27.1 of TRIPS under which "... patents shall be available and patent rights enjoyable without discrimination ... whether products are imported or locally produced.". Further if a compulsory licence is granted on the grounds of abuse of economic power, the licensee may parallel import for one year, as may any other third party.

Some groups described regional Exhaustion of Patents within the EEA, following the decisions of the ECJ in *Centrapharm v Sterling Drug* (C-15/74, 31 October 1974) and *Merck v Stephar* (C-187/80, 14 July 1981), as occurring when a product covered by a patent is marketed within the EEA by the patent owner or with consent.

The UK group noted that Article 10 of the Biotechnology Directive (98/44/EC) establishes EEA regional exhaustion for biological material obtained from the propagation or multiplication of material placed on the market in one Member State.

(ii) **Trade Marks:** the answer for trademarks is different to that for patents. Countries including the Member States of the EEA, Bulgaria, Czechoslovakia, Hungary, Romania, the US and Yugoslavia do not apply a rule of international exhaustion for trademarks. In contrast, Argentina, Australia, Brazil, Canada, Japan, Paraguay, Mexico, Singapore, Switzerland, Venezuela and Yugoslavia all allow international exhaustion. It is noted that this list is longer than the list of countries applying a rule of international exhaustion to patents. The Canadian group noted that there would be no "deception as to origin" in such cases. The Australian group noted that the approach that is based on the fact that trademarked goods are put on to "the billowing sea of trade" and should thus be free to move. In Japan, trademark owners are generally precluded from using their rights against parallel imports of "genuine" goods, although the report observes that under Japanese law it is not clear what "genuine" goods are. In Korea the answer depends on where the goods are manu-

factured. If manufacture takes place in Korea then parallel imports can be prevented. If not then they cannot.

Member States of the EEA noted the decision of the ECJ in *Silhouette v Hartlauer* (C-355/96, 16 July 1998) and *Sebago v GB Unic* (C-133/98, 1 July 1999) which precludes Member States of the EEA from applying a rule of international exhaustion - there is, of course, regional exhaustion within the EEA. Until that decision Denmark had a rule of international exhaustion. Recent case law development in the UK has shown differing judicial approaches to the ECJ's position. In England *Zino Davidoff v A&G Imports* (Case C-414/99) has been referred to the ECJ: it contradicts *Silhouette*. The English court suggested that there may be implied consent to importation by marketing outside the EEA where there was a failure to take sufficient steps to prevent the importation. The Scottish courts have taken the opposite view. The UK group believes that consent should *not* be implied. The US group explained that relief against importation was limited where goods not materially and physically different are marketed by the trademark owner or by companies with certain relations to the trademark owner.

Some groups described regional exhaustion of trade marks within the EEA established in the ECJ decisions *Centrapharm v Winthrop* (C-16/74, 31 October 1974) and *Terrapin/Terranova* (C-119/75, 22 June 1976) as being the same as that for patents.

(iii) **Other rights:** Groups reviewed a number of other industrial property rights showing that there are various approaches and a lack of uniformity to international exhaustion. Singapore has international exhaustion for designs. Hungary and Finland allow exhaustion for semi-conductor chips and integrated circuits; the US for mask works; Venezuela for plant breeders' rights. Just under half the groups reported that there are no rules of international exhaustion; but rules seem to vary from rights to right. In Australia an IPR owner can prevent parallel imports of circuit layout designs and plant varieties if there is no licence given to the importer. The Spanish group noted that the draft EU Utility Model Directive (12 December 1997) specifically states that there will be no international exhaustion. The UK Group noted that the EU 1998 Design Directive (to be implemented by October 2001), the proposed Utility Model Directive and the proposed Community Design Regulation both follow the EEA position for trade marks and preclude member states of the EEA from applying a rule of international exhaustion.

Question 2.

(a) Can contractual restrictions imposed by an industrial property right owner be used to limit the effect of international exhaustion? (b) What is the effect of breach of contractual restriction by a purchaser - does exhaustion occur?

(a) and (b). This question raises the distinction between the common law approach to exhaustion and the approach of other countries. The common law approach is that a sale of goods is a contractual matter, and that treatment of IPR may be affected by the contract. In other countries, the treatment of IPR cannot be limited by contract. In a majority of countries, exhaustion is considered to be a matter governed by the legal effect of IPR, which are property rights having effect against all third parties. It is thus not possible for a contract between individuals to have any effect on the position. This is the legal theory, for example, in Brazil, Czech Republic, Paraguay and Yugoslavia. In contrast, in Japan (for patents at least) international exhaustion may be limited by contract and where there is a

breach of contract, no exhaustion takes place. The Japanese position for patents is that if a patent owner fails to impose a contractual restriction on sale outside Japan then, irrespective of whether there is a parallel patent in the country of sale, the patentee is deemed to have waived his rights to prevent importation into Japan. In contrast, for trade-marks, the law is not clear. In Australia contracts may be effective in the case of patents, but not in the case of trademarks. In Canada it is necessary to bring a contractual restriction to the attention of a purchaser if it is to be effective. In Singapore contractual restrictions cannot be imposed to limit the effect of international exhaustion. In Japan the law differs for patents and trademarks.

A number of groups drew attention to the role of anti-trust and competition laws in attempts to limit exhaustion (Australia, countries of the EEA and Venezuela). The Venezuelan group noted that any contractual restrictions on the effects of international exhaustions is considered null.

Question 3.

(a) If contractual restrictions can be used to limit importation, does it matter whether they are express or implied?

(b) If contractual limitations are express, are there any particular marking requirements?

(c) If protected products are marked to indicate some marketing restriction, what are the consequences of removal or loss of any marking?

(a) For some groups (Hungary, Finland, France and Venezuela) this question was irrelevant, as it is not possible for contractual restrictions to have an effect on exhaustion. The majority of countries required that contracts be express. In Japan they should usually be express for patents. All groups thought that it would be easier to deal with express terms rather than implied terms. In the EEA, the pending *Zino Davidoff v A&G Imports* (C-414/99) should answer the question whether consent may be given implicitly. The Canadian group noted that the test was whether a purchaser had actual knowledge of a restriction, not whether the restriction was express or implied.

(b) In Japan there should be a label or the like to place the subsequent purchaser on notice that importation into Japan is prohibited. No other country has any marking requirements, but some groups noted that it should be helpful for goods to be marked (Brazil, Egypt, Korea and Paraguay).

(c) This question is related to question 6, answered below.

Question 4.

Does international exhaustion of industrial property rights apply where a product has been put on the market under a compulsory licence (if applicable)?

Compulsory licences usually only apply to patents. In the great majority of countries international exhaustion does not apply where a product has been put on the market under a compulsory licence. The exceptions are Canada, in which a compulsory licence is treated as equivalent to an ordinary licence, so that exhaustion can arise, and Australia, where the point is not decided and might go either way. The Brazilian Group noted that Article 31 TRIPS ("Other Use Without Authorisation of the Right Holder") starts "Where the law of a

Member allows for other use of the subject matter of a patent *without* authorisation of the right holder ...", (added italics). This suggests a compulsory licence cannot be an authorisation.

The German Group noted that in the EEA following the ECJ decision in *Pharmon v Hoechst* (C- 19/84, 9 July 1985) which provides that a compulsory licence is not to be taken as consent.

Question 5.

Is "consent" which gives rise to exhaustion limited to specific arrangements, (for example a relationship with a subsidiary or affiliated company, or an agreement with a licensee), or a question of fact in each case?

The "consent" giving rise to exhaustion is, in almost every country a question of fact. The Japanese and Finnish groups noted that consent might be presumed in the case of group companies. The Spanish group suggested that this might apply across the EU, where appropriate economic links or control could be established. The Argentinean group noted that certain specific company arrangements (e.g. parent/subsidiary) should give rise to consent. The US Group noted that where goods identical to those of the US trademark owner were manufactured abroad by an affiliate of the US trade mark owner, or by one entity under common control or ownership with the US trade mark owner then importation is allowed. Affiliation exists where either firm is a parent or subsidiary of the other, where the foreign manufacturing firm is merely the domestic firm's own unincorporated manufacturing division, or where there is common control between firms.

Question 6.

Can an IPR owner object to parallel importation where (a) goods or (b) their packaging have been modified?

This question applies mostly to trademarks.

(a) All groups reported that a change in the goods was sufficient to allow the IPR owner to object to parallel importation. However, different tests apply in different countries. Thus in Australia "notices of prohibition" must be displayed on goods. In the US the goods must be physically and materially different.

(b) There were differences on the question of modification packaging. Within the EU a test has developed that allows the trademark owner to oppose further marketing unless certain conditions arise. The position is currently on referral to the ECJ following an attempt by an English court to limit further the scope of opposition to repackaging *Glaxo v Dowelhurst* (C-193/00). In Bulgaria, in order to object to re-packaging, the modification itself must constitute an infringement and the quality of goods or packaging must be diminished. In some cases removing marks can create liability for an infringer (Egypt and Yugoslavia). In the Benelux countries it is likely that removal of markings which are intended to indicate to the trade that there is no consent to resale within the EEA is unlawful.

The Dutch group noted the EEA position as set out in *Loendersloot v Ballantine* (C-349/95, 11 November 1997). Relabelling will be an infringement unless:

" - it is established that the use of the trade mark rights by the owner to oppose the marketing of the relabelled products under that trade mark would contribute to artificial partitioning of the market between Member States;

- it is shown that the relabelling cannot affect the original condition of the product;

- the presentation of the relabelled product is not such as to be liable to damage the reputation of the trade mark and its owner; and

- the person who relabels the products informs the trademark owner of the relabelling before the relabelled products are put on sale."

Question 7.

As well as from stating the laws in their respective countries, the groups are also invited to (a) make any proposals for changes; and (b) offer any observations of interest on the topics raised above.

The Danish group suggested that the principles of exhaustion and implied licence can be seen as two conceptual responses to the social/economic need that arises in a unified market (however many countries that comprises). Regional (or national) exhaustion is a logical consequence of such a market. On the other hand neither the results of economic research nor legal principle justifies global exhaustion. The Danish group thus opposes mandatory global exhaustion of national rights.

The Danish group suggests that proof of marking should not be mandatory to avoid international exhaustion.

The Spanish group is against international exhaustion for patents, because of their limited duration. However, the Spanish group sees that the absence of international exhaustion for trademarks allows the owner to divide this market and exploit prices.

The Spanish group noted that the intervention of states in fixing prices of pharmaceuticals could lead to problems for patent owners if parallel importation followed.

The Portuguese group noted that the European Community should resolve developments in a homogeneous manner.

The tensions the issue can arouse were highlighted by the Brazilian group which declared that it had not reached a unanimous view on the international exhaustion of trademarks.

The Dutch started from the position that IP rights are national. Use of a right outside the territory cannot be said to be use of that right in the territory. Further, each right needs to be considered on its own merits. Regional exhaustion works within the EEA. But important differences of economics, legal systems, wealth, development, state price control and regulations throughout the world mean that international exhaustion of IPR is not desirable, as it may lead to reductions in R&D, or restrictions in the markets into which an IPR holder will sell his goods. The question is more about trade policy than a legal theory.

The Japanese group believes that trademark and patent owners in one country should be allowed to exercise their rights against parallel imports of goods sold in another with consent. So far as patents are concerned, this allows the patentee freedom to price and to recover R&D costs. Trademark owners should be compensated for the establishment and maintenance of goodwill in a market. Different levels of goodwill in different markets may lead to different prices. As such the trademark owner should be allowed to prevent parallel imports.

Finland, the UK and Yugoslavia noted that patents and trademarks are treated differently in international exhaustion regimes and should not be taken together for convenience.

The Australian group noted that increased IPR protection is very unlikely to be forthcoming in today's political climate. A number of groups noted that there are political aspects to international exhaustion.

The Italian group called for any developments in this field to be reciprocal. The Finnish group suggested that the WTO might be an appropriate organisation to make changes; the Canadian group suggested WIPO.

The UK and Hungarian groups stressed the need to show any economic benefits flowing from international exhaustion before making changes. The Korea group suggested further research on parallel importation on branded goods.

The French group called for a maintenance of the status quo, while the Venezuelan group called for increased international exhaustion.