Combat grey market goods in the US

Case law surrounding grey market goods is still developing in the United States, but Ronald Dove and Hope Hamilton suggest some practical strategies for successfully preventing their importation and distribution.

Grey market goods, also known as parallel imports, are genuine products protected by copyright, trade mark or patent rights that are imported into a country without the authority of the IP rights owner in that country. It is estimated that tens of billions of dollars are lost annually to grey market sales. The problem is exacerbated by the expanding and borderless internet marketplace and will almost certainly worsen as the global economy slips into recession.

Notwithstanding this growing problem, a broad base of IP owners, including in the fields of luxury goods, information technology, publishing, software and pharmaceuticals, persist in their efforts to tackle the grey market, with notable success.

No grey skies for copyright

The past few months have yielded a series of decisions that have solidified the principle that the so-called first sale doctrine is not a defence to unauthorised importation and distribution of copyrighted grey market goods that are manufactured and first sold abroad.

In September 2008, the US Court of Appeals for the Ninth Circuit affirmed its long standing precedent in this respect (Omega SA v Costco Wholesale Corp [9th Cir 2008]). This was the Ninth Circuit’s first copyright case concerning grey market goods since the Supreme Court decided Quality King Distributors, Inc v L’anza Research International, Inc (1998). In that case, the Supreme Court held that the first sale defence under §109(a) of the Copyright Act applied to copyrighted goods made in the United States, exported abroad, then imported back into the United States, and that the US copyright owner could not stop the sale of grey market goods under those circumstances. The Supreme Court did not reach the issue of whether the first sale defence would apply where the goods were manufactured abroad and then imported into the United States, a point that Justice Ginsberg took great care to emphasise in her concurring opinion.

The Omega decision is the first US federal appellate court opinion to directly address this issue left open by the Supreme Court in Quality King. Omega, a well-known watch manufacturer, filed suit against discount store Costco for infringing its distribution and importation rights under §§106(3) and 602(a) of the Copyright Act. Omega alleged that Costco was selling unauthorised, genuine Omega watches bearing Omega’s US-copyrighted “Omega Globe Design”. Costco responded that such sales were permitted under the first sale doctrine of §109(a), which generally limits §§106(3) and 602(a) and states that once a copyright owner has sold a lawfully made copy, the purchaser “is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy”.

After carefully analysing the Supreme Court’s decision in Quality King, including Justice Ginsberg’s concurrence, the Ninth Circuit concluded that the Supreme Court “did not address the effect of § 109(a) on claims involving unauthorised importation of copies made abroad”. The Ninth Circuit went on to parse the language of the Copyright Act and to conclude that “the application of § 109(a) to foreign-made copies would impermissibly apply the Copyright Act extraterritorially in a way that the application of the statute after foreign sales does not”. Thus, the Ninth Circuit upheld its established precedent, concluding that “the first sale doctrine is unavailable as a defense” and that Costco could be held liable for its unauthorised importation and sale of copyrighted Omega watches manufactured and first sold abroad. Costco has petitioned for rehearing en banc.

Microsoft Corporation has also had significant success in the past year combating grey market goods. Courts ruled in Microsoft’s favour in at least three separate cases involving claims of unlawful importation and distribution of Microsoft’s Student Media software that was manufactured abroad and not authorised for sale.
or use in the United States. Most recently, in *Microsoft Corporation v Intrax Group, Inc*, No (ND Cal, 2008), the US District Court for the Northern District of California granted summary judgment in favour of Microsoft, the exclusive distributor of new Korean manufactured Hyundai heavy construction equipment in the United States and Canada. Hyundai sought an injunction prohibiting Johnson, the defendant, from selling in the United States Hyundai equipment that was manufactured for sale in the Korean and Chinese markets. Johnson argued that Hyundai lacked standing because it did not own the Hyundai trade mark in the United States. He also asserted that there was no evidence of actual consumer confusion, because his buyers were sophisticated and knew that the equipment they were purchasing differed from that authorised for sale in the United States.

The court held that Hyundai had standing under § 43(a) of the Lanham Act, even though its parent owned the Hyundai trade mark in the United States, because it had a reasonable interest to protect against false advertising and the likelihood of consumer confusion, particularly where Johnson was benefiting from Hyundai’s promotion of its products in the United States. The court went on to conclude that Johnson had infringed the Hyundai trade mark due to the likelihood of confusion caused by numerous “material differences” in the equipment, including that the unlawfully imported equipment had altered or defaced serial numbers, was sold without the standard warranty available in the US, had Korean language safety, operation, and maintenance instructions, and had non-EPA compliant engines.

**Quality control**

Employing strict quality control measures also has proven to be an effective tool in combating grey market goods. Although US courts have been inconsistent in their approach to considering quality control measures – some treat such measures as a factor in the “material difference” test, others treat them as

**Look to the Lanham Act**

Trade mark owners continue to find success in appealing to the US Lanham Act to fight grey market goods. In *Hyundai Construction Equipment USA, Inc v Chris Johnson Equipment, Inc*, (ND Ill, 2008), a federal court in Illinois granted summary judgment in favour of Hyundai, the exclusive distributor of new Korean manufactured Hyundai heavy construction equipment in the United States and Canada. Hyundai sought an injunction prohibiting Johnson, the defendant, from selling in the United States Hyundai equipment that was manufactured for sale in the Korean and Chinese markets. Johnson argued that Hyundai lacked standing because it did not own the Hyundai trade mark in the United States. He also asserted that there was no evidence of actual consumer confusion, because his buyers were sophisticated and knew that the equipment they were purchasing differed from that authorised for sale in the United States.

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Chase the grey away

It is important to develop a strategy for combating grey market goods that is most suitable for your needs. Factors that influence such strategies include the scope of the problem, budget, business relationships and the type of IP right underlying any claim. Specific considerations and strategies include:

- **Positioning your business for the greatest enforcement potential.** Maintaining trade mark registrations and properly registering copyrights is critical. Consideration should also be given to business relationships. The ability to enforce rights in the United States may be lost if licences and distribution agreements in other countries do not make clear that right owners, licensees and distributors in those countries are not authorised to export to or sell those products in the United States. Likewise, the US trade mark or copyright holder or its licensees must unambiguously have exclusive rights to sell in the United States.

- **Positioning your products for the greatest enforcement potential.** In the case of trade mark rights, consider instituting quality control standards and anti-counterfeiting systems that will allow trade mark owners to identify and distinguish between non-authorised goods (for example UPCs, serial numbers, batch codes, expiration dates, unique packaging for different markets, and use of secondary trade marks). Trade mark owners should also bear in mind that the threshold for “material” differences between authorised and non-authorised products is relatively low. In the case of copyrights, copyright owners will be most successful combating grey market goods where the goods are manufactured abroad and intended for sale abroad. But copyright claims only work where the products themselves are protected by copyright or contain packaging or labelling protected by copyright. If the design is not placed on the product or the packaging or other material important to the consumer, an importer may evade liability by simply bringing the goods into the US without the copyrighted elements or removing the copyrighted element prior to resale.

- **Utilising notice-and-take-down procedures.** Most established marketplace websites, including eBay and Amazon, have procedures in place through which IP owners can submit notice-and-take down requests to remove infringing grey market listings from such websites.

- **Identifying the target.** Identifying and tackling repeat infringers often yields the greatest success in short order. In some instances, however, companies may wish to investigate suppliers, wholesalers, foreign distributors, Internet ISPs, and other entities in the chain in an attempt to tackle the problem at its source.

Practicing tips

While US law concerning grey market goods is continuing to develop, particularly with respect to internet-related sales, the strategies available to IP owners are relatively clear. First, it is important to understand the scope of the problem. Regular due diligence and investigation is central to protecting any IP right. Investigative firms can assist with storefront counterfeit and grey market goods sales. In recent years, a few companies and law firms have developed sophisticated internet investigation groups, which employ both human resources and technical tools to crawl the internet in search of counterfeit and grey market goods.

It is also imperative to be aware of your enforcement options. In addition to notice-and-take down procedures, cease-and-desist letters and pursuing claims in federal courts, trade mark owners can under certain circumstances register their marks with Customs to prevent the unlawful importation of grey market goods or litigate their claims before the International Trade Commission, seeking an exclusion order directing Customs to prevent the unlawful importation of such goods.

Another option is to consider building coalitions. The struggle to combat grey market goods is common to many, and the particular interests and challenges facing businesses in similar markets can be identical.

Finally, educate consumers and potential infringers about what constitutes illegal conduct, including by publicising successful enforcement efforts. Such publicity may affect infringers as they weigh the risks and benefits of their activities. Stay informed of developments in the case law and of the new and evolving tools to combat the importation and sale of grey market goods.

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