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INTELLECTUAL PROPERTY, FREE TRADE AND THE FREE FLOW OF GOODS:

A STUDY OF THE "EXHAUSTION" ISSUE IN INTERNATIONAL TRADE

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EDITORIAL NOTE

There are certain inconsistencies, which are deliberate, throughout this work with respect to spelling. The latest official consolidation exercise of the Federal Canadian statutes as of 1985 has decreed that the term "trade mark" (as historically used in Canada in Canadian statutes and the common law) will now be spelled as "trade-mark". The U.S.A. and the World Intellectual Property Organization (WIPO) generally use the spelling "trademark". The EC and the UK both use the spelling "trade mark". Canada's current spelling does have the virtue of being unusual, if not unique amongst major English speaking jurisdictions. Where I am quoting from a foreign source, the foreign spelling will be used. Where I am quoting from, or directly referring to, Canadian material that predates the recent consolidation, I will use the former spelling. It should be noted that the Patent and Trademark Institute of Canada (PTIC) continues and intends to continue to use the spelling "trademark".

The word "grey" is, of course, spelled as "gray" in the U.S.A. (and sometimes in Canada). Likewise, in quotes of American material, I will use the American spelling.

Where the spelling does not lead to confusion, the terminology may do so. For this reason, I have included, as "Appendix I", a Glossary of key terms, such as "grey market goods", "parallel import", "exhaustion", "first sale", "market segmentation", "implied license", "universality", "territoriality", and, above all, the term "confusion" itself as a term of art in intellectual property law.

INTRODUCTION

The major economies of the world are presently striving towards free or freer trade and higher levels of intellectual property protection. These are eminently laudable goals. However, we are now also seeing an increasing tendency to use intellectual property laws as a barrier to trade. The free flow of goods can be restricted, and indeed completely prevented in many cases, by the exercise of intellectual property rights. These rights have typically been conferred by governments and enforced by the courts[1] in an effort to encourage the successful activity of inventors, creators, producers and distributors of products ranging from books to ketchup and computers. However, with the advent of regional and even global freer trade, these rights are being used more and more as privately enforced non-tariff barriers to international trade.

There is also a simultaneous trend towards the creation of three major trading blocs that would entail presumably even freer trade within each of them, and more intense rivalry as between them. Moreover, many of the major players in this extremely important series of developments have been until very recently, or arguably still are, very much protectionist in approach. Accordingly, there are important tensions and ambiguities as to what is meant by "free trade". One of the main areas of doubt arises in intellectual property law where higher levels of protection are generally viewed as desirable but have the potential to become barriers themselves to free trade.

There are major forces at play in this drama. From the "Age of Enlightenment" (i.e. late 18th Century) until the advent of the Chicago School of economics in the late 1970's, intellectual property had traditionally been viewed to a varying degree as a necessary but limited exception to the principle that monopolies were bad for public policy. The conferral of new intellectual property rights was often matched by a corresponding increase in antitrust enforcement. However, this has changed greatly in the last ten to fifteen years. We have seen a trend to far higher levels of intellectual property protection and a greater official tolerance of vertical restraints under antitrust doctrines, as efficiency enhancing, according to the "New Learning" of the Chicago School. In fact, we have seen vertical integration in the entertainment industry that would have been unimaginable only a few years ago.[2]

Higher levels of intellectual property protection are justified and useful if the result is a cost/beneficial increment in investment, progress, innovation and creativity. There is no doubt that this can and does happen. However, unless such higher protection is carefully conferred and is not abused, it can lead to increased monopoly power, abuse of dominance, stifling of competitive innovation, outflows of revenue on a national basis, and a decrease in competitiveness (e.g. due to comparatively higher costs of education, or higher wholesale costs for consumer goods resulting in "cross-border shopping"). These conflicting results lead to great tensions that are now manifest both domestically and internationally.

It is a principal thesis of this work that one of the most significant intersections of these conflicting principles occurs with respect to the issue variously referred to as "exhaustion"[3], "implied license", "grey marketing" or "parallel importation". The opposite doctrine is usually referred to as "market segmentation". The doctrine of exhaustion, stated as simply as possible, and in its broadest exposition, holds that goods that have been legitimately sold into a market anywhere in

the world should thereafter be capable of being exported and imported across borders without any intellectual property restrictions.

The exhaustion issue is an exceptionally difficult one because, even within intellectual property law as such, it involves a multitude of difficult legal and economic principles that sometimes conflict. The three main intellectual property disciplines have different histories and functions.

Patent law encourages manufacturing and is essentially territorial in nature. Historically, it has encouraged local manufacturing. Market segmentation has been part of the *quid pro quo* for disclosure and either local manufacturing or efficient supply. Exhaustion clearly could threaten this policy balance. To complicate matters, the proposed GATT text would do away with patent incentives to local manufacturing. Is it then advisable to retain market segmentation, without the other half of the *quid pro quo*?

Copyright law, apart from recent developments having to do with the protection of computer programmes and other essentially functional forms of expression, has historically been rooted in the protection of authors and cultural matters. It has always been recognized that efficient economic principles may need to give way to the need to protect a country's culture, which is a precious and fragile commodity. Historically, copyright law has also been used by some countries (such as the U.S.A. until the mid 1980's) to encourage local manufacturing.

Trade-marks law is mainly concerned with trade. Trade-marks are exploited more and more on a world-wide basis. However, registration and enforcement is still essentially territorial. It is not the product or service that is protected by trade-mark law, but the good will of the provider (which is often a multinational enterprise, with or without related entities in the territory for which protection is sought). Is market segmentation as provided by trade-marks law necessary to protect this good will? Given that few persons would condone the use by a trade-mark owner or licensee of trade-marks law within Canada to segment markets and prevent trade in its own product as between provinces or cities, does it make sense for a multinational trade-mark owner to do this as between countries? As well, trade-marks law, unlike patent or copyright law, has never had as its purpose the encouragement of manufacturing or invention or creativity.

The exhaustion doctrine is objected to by many intellectual property rights owners for stated reasons such as the following, which will be elaborated in due course:

I. Exhaustion can lead to "free-riding" on the local goodwill and infrastructure that may have been established by or under the authority of the intellectual property right owner.

II. Exhaustion can lead to the substitution of different and even inferior goods (even if manufactured by the owner or one of its affiliates). This situation can lead to the confusion and harm of consumers and the depreciation of the goodwill of the intellectual property right owner.

However, there is considerable evidence that many intellectual property rights owners object to exhaustion for unstated reasons that include a desire to price discriminate[4] and to effect resale price maintenance.

Not surprisingly, the principal arguments in favour of exhaustion are that:

I. It is pro-competitive

II. It allows consumers more breadth and depth of choice

III. It is essential to the free flow of goods, which is in turn a prerequisite of free trade.

IV. True exhaustion in North America would lead to uniform wholesale prices, thereby eliminating a possibly major contributing factor to the "cross-border shopping" syndrome.

V. Exhaustion works. The European Community has been a laboratory for experimentation on this and related issues for thirty years and the experiment has succeeded.

The exhaustion issue entails the use of intellectual property laws by private litigants to block international trade in articles for which importation is sought other than by the "authorized" distributor for the territory in question. When these private remedies succeed, they are a type of "private tariff". Moreover, they are more effective at blocking trade than a normal tariff because entry into the country of importation is in the absolute discretion of the rights holder. As well, there is no public policy element, especially in interlocutory (i.e "temporary") injunction proceedings, in the determination as to whether the goods should be denied entry or distribution in any particular case. Since the underlying statutes that enable this result, most notably the Patent Act[5], the Trade-marks Act[6], and the Copyright Act[7] are widely recognized as infrastructurally important "framework" laws that require a balance of public policy interests, it falls to be determined whether parliament ought to clarify whether they should be used as "private tariffs". That is true, of course, unless parliament intended that they be used to serve purely private interest without public policy parameters.

The problem with exhaustion is to ascertain to what extent can -- or in turn should --intellectual property laws be used to influence the otherwise free flow of genuinely made articles across international borders. In the view of the author, there is a significant potential for the private sector in Canada and the U.S.A. to utilize the legal state of play consisting of existing statutory mechanisms and case law to effect very real impediments to international free trade in goods protected by intellectual property laws in apparent conflict with the stated policies of both jurisdictions with respect to the free flow of goods, particulary within North America. The proposed GATT agreement could tend to perpetuate and endorse the concept of market segmentation, especially with respect to those countries that are subject to bilateral pressure from the U.S.A.

This development contrasts sharply with the *de facto* and *de jure* position within the European Community (EC), under the auspices of which almost all intellectual property barriers to the free flow of goods within the community have been or are about to be rendered inoperable. It is not easy to explain to the "average Canadian" that, notwithstanding the *Canada-U.S.A. Free Trade Agreement* (FTA) with the U.S.A., it is not possible to purchase American-made Heinz ketchup in Canada, even though it is half the price of Canadian-made Heinz ketchup, all because of an interpretation of the Canadian *Trade-marks Act.*

As is explained at greater length elsewhere in this study, the present state of the laws of the most important jurisdictions is as follows:

CANADA:

* Market segmentation available in theory under patent law. Difficult to achieve for many reasons, most notably the exceptions that flow from the "implied license" doctrine and the declaratory provisions of the current Patent Act and Competition Act [8].

* Market segmentation is being increasingly permitted by the courts in trade-marks law in some cases (Heinz[9]), though the courts will not be persuaded in every case (Nestlé[10]).

* Copyright law ineffective to prevent exhaustion except for books.

U.S.A.:

* Similar to Canada re patents but with added gloss of misuse defences available pursuant to antitrust law cases. As well, U.S. rights owners have at their disposal the very potent and much criticized weapon of "s. 337", which enables the use of the U.S. Customs Service to block allegedly infringing goods at the border.[11]

* Trade-marks: related company exemption permits large degree of exhaustion. Legislation pending.

* Copyright: the law is confused, but generally copyright law problematic in blocking parallel imports.

* Generally, the U.S.A. allows more exhaustion for itself than does Canada. Yet, the U.S.A. argues against the exhaustion principle in international negotiations.

EC:

* Subject to certain minor exceptions, there is free flow of goods within the community (not from outside). The doctrine of exhaustion is integrated with competition law and is, apparently, very successful. Of course,

> it should be noted that facile analogies between the EC and North America may not be appropriate. The EC is well on the way to being a unified state (i.e. single country) for many purposes, especially including, from the point of view of the present analysis, intellectual property and competition law.[12]

Thus, it would seem that Canada currently may actually have less exhaustion (i.e. more market segmentation) than the U.S.A. and the EC in many respects. Since Canada is by far a net importer of intellectual property from these traders, it is important to examine whether this situation is in Canada's national interest.

The state of the law and policy in North America is not entirely a reasoned or consistent position but rather one of partially adventitious result based upon a lack of transparency and certainty in domestic laws and partly upon the interests of multinational enterprises (MNEs) that favour the retention of tools that enable market segmentation. While there are a complex set of policy considerations both for and against the use of intellectual property laws to influence the otherwise free flow of goods, this study argues that intellectual property laws, unless circumscribed in a balanced fashion, have the potential to work in this respect at direct cross-purposes with sound free-trade and competition policy principles. From an economic and political standpoint, the European experience would suggest that intellectual property laws should not be so used **within** an economic union, customs union, or free trade zone as variously defined by the GATT and other contexts so as to impede the free flow of legitimate goods. In other words, the European result is one that is deserving of very careful scrutiny in the Canadian context, especially vis à vis our own free trade "area" -- North America -- and the presumably ideal free trade area-- the world.

Whether such a result should be sought in whole or in part within the North American Free Trade Agreement (NAFTA) context is a crucial question. If a European Community (EC) approach is not embraced within North America with respect to this issue, it is at least arguable that Canada might wish to consider unilateral steps towards increasing the level of exhaustion overall, but particularly with respect to trade-marks law. The main reasons to do so, subject to confirmation by economic data, would be to increase competitiveness, to lower costs to Canadian consumers and intellectual property users, and to prevent the outflow of economic rents deriving from unproductive price discrimination.

The exhaustion issue is also looming large in at least two World Intellectual Property Organization ("WIPO") fronts, namely those of patent harmonization and the proposed "Protocol" to the Berne copyright convention.

In any case, the Canadian position should reflect Canadian interests. The particular challenge will be to ascertain those interests in a multilateral context featuring two major sets of trade negotiations, both of which are heavily influenced by the United States, with which Canada already has a Free Trade Agreement.

American thinkers may also wish to reexamine their country's views on the exhaustion issue in the light of clear signs in international trade that competitiveness will be the most crucial element of success, or even survival.

Thus, the main conclusion of this study is that the issue of exhaustion is so crucial to the purposes of intellectual property, competition and international trade law that the policy and legal framework should be very carefully and systematically developed by governments, and not in a haphazard and self-interested manner by private litigants through the courts.

This study will attempt to take a balanced approach to the many complex and interrelated facets of the exhaustion puzzle. This balance necessitates some lengthy analysis and background. It also necessitates some repetition of issues that transect several disciplines. Accordingly, the reader is forewarned that the issues are difficult. However, the author believes that they must be examined by those who are concerned with efficient trade and appropriate levels of intellectual property protection.

CHAPTER I THE LAW OF EXHAUSTION IN CANADA

The following recent examples illustrate the types of situations that have resulted in adjudicated decisions in the courts or other steps aimed at excluding parallel imports:

* KETCHUP: American Heinz ketchup at half the price of Canadian Heinz ketchup denied to Canadian consumers pending trial

* NESCAFÉ MOUNTAIN BLEND COFFEE: American blend with chicory allowed into Canada pending trial

* NINTENDO: American versions of Nintendo games denied to Canadian consumers pending trial

* SEIKO WATCHES: Consumers' Distributing requires Supreme Court of Canada ruling for the right to sell "grey market" Seiko watches as a non-authorized dealer

* Canadian PUBLISHERS AND AUTHORS strive to prevent the importation of "remaindered", or even simply foreign printings, of books to which they have "Canadian" rights.

* JAPANESE CONSUMER ELECTRONICS firms attempt to prevent parallel imports

All of these examples will be documented in this study. This chapter will outline the main line of law that deals with the exhaustion issue in Canada. As will be seen, the results are neither conclusive nor consistent. Moreover, the results do not reflect any systematic policy-driven approach and are largely the result of interlocutory injunctions decided, as such matters often are, in haste. There is very little evidence of any legislative attention to the issue.[13] In fact, the courts have, by default, been forced to deal with policy issues,[14] and have done so, not surprisingly, in a sometimes unsatisfactory manner.

Despite the lack of precision in Canadian law concerning this issue, there is, nonetheless, a fairly clear trend emerging that shows that intellectual property owners are using the litigation system in Canada with some success to achieve market segmentation, and that the result may be a significant contributing factor to the phenomenon of higher prices in Canada for some goods, the cross-border shopping phenomenon, and concern with the nature of the Canada - U.S.A. Free Trade Agreement.

PATENT LAW IN CANADA

The Patent Act confers upon the patentee *the exclusive right, privilege, and liberty of making, constructing, and using the invention and selling it to others to be used...*[15] There is no doubt that these words also encompass "importation", if it is not clear on its face.[16] Despite the plethora of complex cases dealing with importation of patented articles, the law in an overall sense is fairly simple.

There are certain basic conclusions that flow from the statute and case law. First and foremost is that, ordinarily, the sale of a patented article by a Canadian patentee abroad without actual notice of restriction on the right to resell implies a license to the purchaser and those deriving title from him to resell and import back into Canada.[17] This flows from the much cited 1871 English case of Betts v. Wilmott.[18] The facts of that case were very simple and sound remarkably familiar today. The plaintiff in England owned a patent on a certain medicinal capsule product in England and manufactured that product both in England and in France. The English defendant raised the defence that the product he was selling may have originated from the defendant's own "manufactory" in France. The plaintiff could not disprove this. Lord Hatherley stated that:

> *But where a man carries on two manufactories himself and himself disposes of the article abroad, unless it can be shewn, not that there is some clear injunction to his agents, but that there is some clear communication to the party to who the article is sold, I apprehend that, inasmuch as he has the right of vending the goods in France or Belgium or England, or in any other quarter of the globe, he transfers with the goods necessarily the license to use them wherever the purchaser pleases. 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 purchase his license to sell the article, or to use it whenever he pleases as against himself*[19]

A similar principle, often cited in the law of contracts, is that conditions, such as resale price maintenance, do not "run with the goods".[20] Interestingly, Betts v. Wilmott was recently cited by the Alberta Court as upholding the proposition that shrink-wrap license conditions are not necessarily enforceable as against normal purchasers who cannot be taken to have agreed to them.[21] This refers to the licenses that are contained inside a package, or partially on the outside of a package, to which the purchaser is supposedly deemed to agree once the purchaser opens the package. They are consistently viewed by courts in a similar manner as "small print" in consumer contract cases.[22] Thus, they are generally unenforceable because there is no meeting of the minds, and no bargaining of any kind.

However, it is not too difficult under patent law, as apparently in contrast to copyright law, to fix the purchaser with sufficient notice to impose certain conditions, such as a requirement not to resell except in the original unopened package with the label intact. "*....Unless an estoppel or waiver can be raised against the patentee it seems that anyone who acquires an article from a licensee gets no better rights than the licensee has.*"[23] Thus, curiously enough, one who purchases from a mere licensee in the U.S. who does not have the right to sell into Canada, cannot thereupon resell the goods into Canada.[24] This is simply an instance of the venerable rule that *nemo dat quod non habet* -- "one cannot give that which one does not own".

But Betts v. Wilmott is also cited for the proposition that:

> *Where a patentee owns corresponding patents in countries A and B, and assigns to another the patent in country A, retaining the patent in country B, the assignee's subsequent sale of a patented article in country A confers no right to import the article in country B.*[25]

Thus, a patentee can arrange for segmentation of markets by well planned assignments and licenses of patent rights in other countries. Hayhurst sums up the situation for patents as follows:

> *......sale by a licensee does not imply that greater rights are conferred than the licensee has. Sale of an article by a patentee implies that no restriction is imposed, and the patentee cannot avoid the implication save by ensuring that notice is given to each purchaser down the line; otherwise, purchasers are entitled to assume that the patentee's rights are exhausted. One would expect, similarly, that a licensee who wishes to sell subject to a condition narrower than is prescribed by his or her license, and who is free to do so under that license, must ensure that the narrower condition is made known to purchasers.*[26]

A distinction should be drawn, especially in patent law, between the doctrines of "exhaustion" and "implied license". This is explained more fully in Appendix I. The former term is a more continental European one and is widely understood within the EC. It basically entails the notion that the intellectual property right owner's interest in the distribution of goods stops with the first sale of those goods. On the other hand, the UK and Canadian tradition, which derives from the rule in Betts v. Wilmott, is a narrower one and is more properly described as the doctrine of "implied license", i.e. that a purchaser will normally have an implied license to resell goods and to use them for the purposes for which they would reasonably be intended.[27] Nonetheless, terminological precision is giving way to uniformity and the term "exhaustion" is widely used in North America to describe the phenomenon that really is one of implied license.[28]

Now, as it happens, patent rights are not often used to block parallel imports in Canada. The reason for this may be quite simply that the normal channels of distribution of most goods, both commercial and consumer goods, would preclude the imposition of notice on subsequent purchasers that would be required for certainty of success in a court action. If the condition were imposed, for example by prominent wording on the product itself, many purchasers might be reluctant to buy the product if it were at all valuable. After all, how could the product ever be resold as "used"? Who would buy a car or a camera or a VCR that was prominently and indelibly stamped with a message to the effect that the goods were "NOT FOR RESALE WITHOUT THE WRITTEN CONSENT OF THE PATENTEE"? If the wording is only on the packaging, it may be quite easy to simply repackage the goods.

One learned author believes that it is simply sufficient to provide for exclusion of parallel imports in a license:

> *Clearly, it can be more practical for a patentee to impose an express condition in a license, thereby affecting all articles that may be sold under the license, than to attempt to give notice of such a condition to purchasers of individual articles.*[29]

However, the same author also suggests that the cases, largely English, suggest that "it now seems to be established firmly that knowledge of the condition at the time of purchase is essential".[30]

Clearly, there is some ambiguity as to the state of the law in Canada with respect to the parallel importation of patented goods. Moreover, the major risk of any patent action, namely that of a successful defence of invalidity, must be weighed against the possible damage of a shipment of parallel imports.

Moreover, there may be many cases where the real motive for blocking parallel imports would involve, at least in part, intentions that might prove contrary to s. 32 (formerly s. 29) of the Competition Act.[31] This section essentially provides that the Attorney General of Canada can obtain certain remedies where rights otherwise provided by patent, trade-marks, copyright or integrated circuit law are being abused according to the criteria in the section. The section can operate, for example, when patent rights are used so as:

> *to restrain or injure, unduly, trade or commerce in relation to any such article or commodity [s. 32(b)]; or,*
>
> *to prevent or lessen, unduly, competition in the production, manufacture, purchase, barter, sale, transportation, or supply of any such article or commodity. [s. 32(d)]* [32]

Another twist with respect to the potential application of the Competition Act is illustrated, although it arose more in the copyright context, by the interesting interlocutory decision in Pindoff Record Sales v. CBS Music Products.[33] In that instance, the plaintiff, a well known Canadian record wholesaler, placed a large order for records with the defendant, a major branch plant operation in Canada, which demanded assurances that the product would not be exported. The plaintiff refused to give these assurances and the records were not shipped. The plaintiff was at least partially successful in keeping alive a novel civil cause of action under the Competition Act arising out of an alleged conspiracy on the part of the defendant and others in refusing to sell products destined for grey markets outside of Canada.

Another reason that patent law is not more vigorously or obviously used to exclude parallel imports may lie in the rarely used but important provisions of s. 65 of the Patent Act (contained in Appendix III) dealing with deemed abuse by patentees that can lead to sanctions such as compulsory licensing in certain cases. The deemed abuse comprises failure to make or to work the patented invention, importation to the detriment of home manufacture, failure to meet the demand to an adequate extent and on reasonable terms and prejudicing, contrary to public interest, the country's trade or industry, or that of particular concerns, by refusing reasonable licenses to others. The general thrust of s. 65(4) of the Patent Act in this respect is that a patentee who does not work the invention in Canada within three years and who has no satisfactory reason for not so doing may be subject to a compulsory license according to s. 65(2)(a).

These sections clearly contemplate an encouragement towards local manufacturing and, indeed, an admonition to ensure that imports do not interfere with this goal. If this is not absolutely clear, the section expressly declares that:

> *...patents for new inventions are granted not only to encourage invention but to secure that new inventions shall so far as possible be worked on a commercial scale in Canada without undue delay.*

These provisions have had a long and deeply rooted history in Canada and the U.K.[34] This may be about to change, if the Dunkel text of the GATT agreement is signed by Canada. This point is discussed below in Chapter III. The point for present purposes is that these provisions of the Patent Act are known to practitioners and have resulted in an encouragement of both local manufacturing in Canada along with reasonable licensing practices, all of which would tend to militate against the conditions that give rise to the price discrimination that causes grey marketing.[35]

Thus, to summarize the state of patent law in Canada with respect to exhaustion, it would seem to be as follows. A Canadian patentee can, in principle, order its affairs so as to ensure that foreign licensees do not have the right to sell goods into Canada. To the extent that this notice of this limitation can be imposed upon subsequent purchasers, it will be enforceable by the Canadian patentee. However, there will often be a defence available of "implied license". Moreover, Canadian patentees may be reluctant to enforce their apparent rights for fear of a finding of invalidity of the patent or potential difficulties under the Competition Act.

TRADE-MARKS AND PASSING-OFF LAW IN CANADA

The real crux of the grey marketing issue is found in the trade-marks case law. Yet, the state of the Canadian trade-marks law based upon recent cases is such that nobody can be sure of what the law actually is. The questions at large, as will be seen, go to the very nature of what a trade-mark is all about.

The main arena of litigation in Canada and elsewhere with respect to grey marketing has been in trade-marks law. This is probably for three main reasons. The first is that most products sold in the retail market are packaged, marked, and marketed so as to be protected by a trade-mark. Many of these products do not involve a patented invention or any copyrightable material, other than perhaps a label (which will be discussed below). The second is that trade-marks law has shown the most promise to date of affording success to intellectual property rights owners in this arena of litigation. The final reason may be that, at least in the case of Canada, the remedies available under the Trade-marks Act explicitly include border enforcement.[36] On the other hand, there is no explicit border relief available under the Patent Act, and only problematic border relief available under the Copyright Act, and then only in the limited case of books.[37]

Until recently, the economic elements that promoted grey market activity usually coalesced in the case of mass-merchandised and relatively low price, low service requirement, and low freight cost items where a well known trade-mark was involved. Disputes involving Duracell, Heinz, Seiko, etc. (see below) attracted a good measure of publicity. However, there are signs that the remedies available will be used increasingly for more expensive products and for products that are industrial inputs per se, such as computers and computer software.

There are, in turn, three groupings of cases that must be studied in some detail to appreciate what the Canadian law of trade-marks can and cannot do with respect to grey market goods. This analysis, with respect to the earlier cases, is somewhat of an overview.[38]

The first round of cases is that of Remington, Wilkinson, Ulay, and Breck's. The 1961 Remington case[39] allowed interlocutory relief against grey goods that originated both from the plaintiff's parent and an unrelated company in Germany. There was, apparently, no attack on the validity of the plaintiff's trade-mark, according to the reasons.[40] In this interlocutory injunction decision, the plaintiff was able to successfully prevent importation of legitimate goods bearing the Remington trade-mark made by a German company that was unrelated to it, and by its American parent as well. The fact that the injunction also extended, apparently, to goods from the American parent of the plaintiff as imported by the defendant, is usually overlooked in subsequent analyses and judgments of the brief reasons. In his decision, Thurlow, J. indicated that:

> *Here, while a purchaser of one of the defendant's shavers gets a shaver which, in the case of those imported from the United States, is made by the same manufacturer as those sold by the plaintiff, it is not unlikely he will think that the shaver is one sold and warranted by the plaintiff, since it bears one or more of the plaintiff's marks. If so, he will be deceived, and when he examines the warranty card and discovers the true situation the plaintiff's good will is, I think, likely to suffer.*[41]

In the 1967 Wilkinson Sword[42] case, the trade-mark was found to be invalid. In this instance, the plaintiff was a subsidiary of its British parent and had taken an assignment for Canada of the trade-mark in question. In seeking to assert its trade-mark against a third party importing legitimate goods made by the British parent, the plaintiff was no doubt upset to learn that its mark was held not to actually distinguish its product from those of all other parties, including the parent. Hence, it was invalid because the consumer no longer knew who was the source of the goods, since the goodwill was associated with the parent in the mind of the public and the goods were made by the parent. The only connection with the Canadian entity was on paper. There was no actual goodwill in the business and legal sense associated with the Canadian entity.

The 1969 case of Ulay (Canada) v. Calstock Traders[43] is often overlooked in the Canadian literature, which is surprising, considering that it is a much more fully reasoned interlocutory injunction decision than, for example, that of Remington.

The defendant, Calstock, imported a product from Europe called "Oil of Ulay", which was made by an entity related to the plaintiff. The plaintiff had set up business in Canada and independently obtained a trade-mark registration for a similar product called "Oil of Olay". The plaintiff's registration predated the defendants' importation by about two and half years.[44] Both were facial creams, and there is reference to evidence that the Canadian formula differed from the European one, for climatological reasons.[45] Walsh, J., in denying the injunction application, made a thorough survey of the then existing case law in Canada, consisting principally of <u>Remington</u> and <u>Wilkinson</u>. He distinguished <u>Remington</u> on the basis that there had been no attack in that case on the validity of the registration, and that in the instant case, there had been a serious attack.[46] Interestingly, the nature of the attack involved the fact that the Canadian company stressed the international nature of the product. Indeed, the plaintiff's packages had the words "London, Sydney, Durban, Amsterdam" printed thereon.

The defendant alleged that the plaintiff's trade-marks were not distinctive of the plaintiff but rather a group of companies. Although Walsh, J. held that the plaintiff could not be held responsible for the effects of spill-over advertising, he did find that "a serious attack could be made on the distinctiveness of the trade-marks under the provisions of s. 18 (1)(b) of the Act."[47] Interestingly, there is a fairly lengthy but inconclusive discussion of the potential monopoly effects that might result if the injunction would have been granted, including the point about whether or not it was material to the corporate entity as to what channel of distribution resulted in the sale of a legitimate product.[48] The judgment, as reported in the Canadian Patent Reporter, also features a very prescient editorial note by Gordon F. Henderson that summarized the state of the law at the time when the issue was just emerging as an important one in the U.S.A. and EC, and indicates the real difficulty of maintaining distinctiveness in this type of action. Curiously, this judgment does not appear to have been mentioned in any subsequent Canadian decisions dealing with the exhaustion issue.[49]

On its face, the facts of the Ulay case are quite similar to the recent and much better known Heinz case which is discussed below. The main significant difference would appear to be in the length of time that the plaintiff had maintained independent good will in Canada. In Ulay, the Canadian trade-mark was registered about two and a half years before the defendants' importation. The independent good will in Heinz was alleged to have existed for about 50 years.

Finally, Breck's Sporting Goods v. Magder[50] further illustrates the difficulties of an assignee attempting to assert distinctiveness in Canada where the mark is owned and used outside of Canada by another entity. This case involved an attempt by a Canadian distributor who was the assignee of a duly registered Canadian trade-mark to prevent the parallel importation of the goods in question which had been legally made in France by a non-affiliated company who had originally developed the good will in the trade-mark. On the facts of the matter, the Supreme Court of Canada determined that the Canadian entity, although it had an assignment of the trade-mark and was seeking to benefit as a trade-mark owner, was essentially acting only as a distributor for the French company that was identified by the public as the source of the goods.[51] Although the Canadian company had made advertising references to the French origin of the goods in question (fishing tackle), it went to some length to add certain manufacturing steps so as to distinguish its goods from those of the French company. The actual tackle was marked "Made in France". The Supreme Court of Canada found the mark to be invalid because it was not distinctive of the Canadian company's goods.

These are the main "first wave" cases in the modern era in Canada (i.e post 1953, when the major revision of the Trade-marks Act took place) that illustrate the conundrum facing Canadian practitioners where a registered trade-mark is involved. It will be rare that there is no corporate affiliation between the plaintiff-importer of the so-called legitimate goods and the foreign source of the so-called grey goods, i.e. Remington. Where there is a lack of affiliation, there is also quite often on the facts a substantial risk that the mark will be declared invalid because the public does not really know with whom the goods are associated, if the mark is very well known world-wide. The more the multi-national enterprise (MNE) attempts to take advantage of a worldwide reputation and marketing strategy, the greater is the risk that the public cannot distinguish the origin of the goods, which is the basic purpose of trade-marks law.

The issue of well known foreign marks and how to ensure their continuing protection in Canada is quite complex and not directly germane to the core of this study. There is extensive and complex Canadian case law on this subject.[52] However, some of the issues that arise in these cases do bear on the present issues. Many enterprises actively seek a worldwide reputation, for obvious reasons. However, trade-marks law is, we are constantly reminded, essentially territorial in nature.[53] The domestic owner, or licensee, or assignee of a trade-mark will tend to want the mark to be distinctive of the domestic enterprise for some purposes, such as warranty entitlement or market segmentation. However, at the same time, the same domestic entity wishes to be associated with the international entity, which may be located elsewhere in a geographic sense, and may not even be related in a corporate sense (the Breck's case). One is tempted to refer to this natural desire to have the best of both worlds as the "have your cake and eat it too" theory of trade-marks.

We now see two trends in marketing. One is towards a clear differentiation of domestic good-will; the other is towards uniform advertising and one message worldwide. For example, if it is the corporate strategy of a MNE to use the same, or virtually the same, advertising message and trade-mark throughout the world, how is the consumer to be expected to associate the trade-mark with a local or national entity? "Global advertising", for example in the case of Coca-Cola, is said to be "a trend that will explode in the next couple of years."[54] Of course, a company such as Coca-Cola may not be unduly worried about grey marketing.[55]

The basic result of these earlier cases was that, for approximately 20 years, trade-mark owners in Canada were extremely reluctant to bring infringement actions involving parallel imports of goods made by related companies for fear of a finding of invalidity of the registration. Even in the case of non-related companies, there was still great danger to the Canadian trade-marks owner if there was any possibility of confusion in the commercial message being conveyed. The only hope was in the sparsely reasoned interlocutory decision in Remington, which as noted, involved, in part, completely separate enterprises. The Breck's case showed the danger that still lurked where any attempt was made to take advantage of an internationally known trade-mark.

This takes us to the second wave of jurisprudence, which culminated in the Seiko case in the Supreme Court of Canada.[56] This judgment was the final conclusion of, essentially, a "passing off" action commenced against Consumers (the appellant) by Seiko who was the exclusive Canadian distributor, and indirect subsidiary, of the Japanese manufacturer of Seiko watches (Hattori). Consumers Distributing had been importing Seiko watches from a mysterious and never disclosed source other than the plaintiff, and was advertising and selling them to the public as Seiko watches. At the opening of the trial, Consumers agreed:

> 1) Not to hold itself out as an authorized Seiko dealer by advertising and selling Seiko watches as internationally guaranteed;
>
> 2) To post a notice to customers disclaiming authorized dealer status and to the effect that the watches being sold were not internationally guaranteed; and
>
> 3) Not to issue or distribute any Seiko warranty booklets.

The sole issue before the Supreme Court of Canada was simply whether the appellant could advertise and sell Seiko watches subject to the first two of the above constraints. (The third point did not form part of the permanent injunction issued at trial). If the Supreme Court of Canada had held otherwise than in favour of the appellant, it would have extended the law of passing off to realms heretofore never contemplated in Canadian law, except by the courts below in the particular case. The *locus classicus* of "passing off" actions had just been decided in 1979 by the House of Lords in the celebrated Advocaat case.[57] Ultimately, the only argument put to the Supreme Court of Canada was that the watches being sold by the appellant were not Seiko watches, because they lacked certain attributes of Seiko watches, such as an international guarantee and the provision of knowledgeable point of sale service; in other words, they were being "passed off" as Seiko watches. This was NOT presented as a trade-marks action. Thus, with some hindsight, the outcome seems perhaps inevitable, although the lower courts plainly concluded otherwise.

Perhaps the only binding conclusion of the Court was that this was not a case of passing off, or even of "extended passing off". The Court stated that "only a moment's consideration is required to recognize that none of this 'extended doctrine' has even a remote connection to the conduct complained of here".[58]

The "moment's consideration" referred to is devoted to a very brief discussion as to whether the public was misled in fact as to their entitlement to warranty service from the manufacturer or, in this case, its wholly owned Canadian distributor/subsidiary.[59] This issue was in fact somewhat moot because the appellant had agreed at trial to post a disclaimer regarding warranty entitlement.

The holding of the court, in its most simple form, was that there is no passing off when a genuine good is sold in Canada, even in the absence of an "international warranty", so long as the consumer is advised that this warranty entitlement is in fact not available. This is not to say that a passing off action could never be available in a grey market case. Indeed, as will be seen below, it was attempted, although unsuccessfully, under the provisions of s. 7 of the Trade-marks Act, in the Nestlé case in 1991. However, it seems quite clear that there would need to be some significant element of misrepresentation to the consumer, which is evidently very difficult if not impossible to prove in the case of genuine and properly labelled goods. If the goods are not properly labelled, the fault may lie with the manufacturer itself, or may be corrected by the importer with additional labelling. As well, the posting of a disclaimer in a store and in advertising brochures may negate any possible deception with respect to such issues as warranty entitlement. Moreover, it is also fairly clear that Canadian courts will not likely be impressed with non-tangible attributes of the goods (such as servicing, warranty entitlement, etc.) unless these attributes are truly important.[60]

A number of "consumer policy" issues arise in and from the Seiko case that are not, of course, thoroughly dealt with in the Supreme Court of Canada judgment, which perforce confined itself to a relatively narrow ratio. Some of these issues are discussed below in Chapter III. Instead, the Court appears to have deliberately opened up a Pandora's box of other questions, the resolution of which may well have undermined the Court's otherwise clear conclusions on the Seiko case. For example, the Court noted that the manufacturer might well have been a plaintiff in an action under the Trade Marks Act[61] as a registered user in Canada of the trade-mark owned by the Japanese parent.[62] Even if the parent-manufacturer refused to join in the resulting action, the Trade Marks Act provides the distributor/registered user with a remedy in such a situation whereby it can proceed without the trade mark owner's consent.[63]

Lurking in the background of some grey market litigation is the touchy issue of price-fixing, or, as it is more politely called, resale price maintenance. It was briefly alluded to but summarily discarded as an issue in the trial court decision in the Seiko case.[64] It is also, perhaps, hinted at in an even more perfunctory way in the Supreme Court judgment:

> *Presumably, the appellant is able to offer a watch in such condition at a lower price than some or all of the authorized Seiko dealers, and this is one possible source of anxiety on the part of the respondent.*[65]

Resale price maintenance, as a policy issue, is related to the more often discussed issue of price discrimination. Both are dealt with in Chapter III below. Suffice it to note at this point that, in theory, neither resale price maintenance nor price discrimination should be a problem if, but only if, there is vigourous interbrand competition. The problem, which will be discussed below, is that there may not always be such interbrand competition.

I have dwelt upon the Seiko case in some detail because the Supreme Court used the judgment therein to issue a coy but clear invitation to trade-mark owners to so arrange their affairs that a properly constituted action under the Trade-marks Act might succeed. We are now beginning to see how this might occur, with the next group of cases.

The third wave of cases is the recent group of Federal Court Trial Division decisions involving Mattel, Heinz, Nestlé, and the slightly earlier British Columbia judgment in Sharp Electronics.[66] With the exception of Nestlé, these cases have all resulted in interlocutory decisions favouring the exclusion of grey market goods. The parties involved appear to be following the hints of Estey, J. in Seiko and their counsel may have carefully studied the articles by Barrigar and Hayhurst (see below), which detail some of the necessary strategies that need to be followed if a plaintiff is to succeed at excluding grey goods.

The first of these cases is Sharp Electronics of Canada Ltd. v. Continental Electronic Info. Inc.[67] In this instance, the plaintiff was a registered user of the Sharp trade-mark and exclusive distributor of Sharp facsimile machines in

Canada. It is not clear whether the plaintiff was affiliated with Sharp of Japan, nor is there any discussion of this issue. The action was framed as a passing off action on the basis that the machines imported by the defendant were not the same as those imported by the plaintiff, allegedly insofar as certain electrical standards were concerned. There were allegations of possible safety problems and apparently much material was filed on the regimes of CSA, UL, DOC, FCC, and ESB (Electrical Safety Branch under B.C. law) electrical approvals. On the key factual issue, Melnick L.J.S.C. states:

> *Sharp Electronics contends that the Fax machines are not identical and that certain modifications are made by the manufacturer to conform to Canadian standards. Continental, on the other hand, maintains that the machines are the same. Neither side offers any hard evidence in the form of an actual analysis of a given machine by an expert. The conflict in the evidence is clearly an important and fundamental issue. It should be settled at trial. However, from the material before me, I am prepared for the purpose of this application to take inference that the Fax machines manufactured by Sharp (Japan) for sale in Canada may be modified in some way to conform with CSA standards and DOC requirements.*[68]

Now, one can question why there was apparently little or no technical evidence submitted by either party on such an important matter. One can question whether the traditional tests of whether an injunction should be granted as stated in <u>Turbo Resources</u> and <u>American Cyanamid</u> and other judgments[69] were properly followed. One can question the weight given to the Judge's finding that Continental's on-going business operations would be jeopardized if the injunction were granted. One can question whether there was sufficiently detailed analysis of the extremely complex questions potentially arising out of the safety standards approval system. One can wonder about whether it is conceivable that a prominent multinational manufacturer would actually put potentially dangerous equipment on the market, given that it is so clearly foreseeable that it will be plugged into a Canadian electrical outlet and that Canadian electricity is not presumably very much different than that of U.S. electricity. A court might even, conceivably, take judicial notice of the last point.

In the end, because there are so many unanswered questions with respect to this case, and it is, after all, only an interlocutory decision, it may not have very persuasive precedential value. But, it could open the door for more law suits based upon electrical standards and other safety or certification based issues.

Apparently, the Court left an open invitation for Sharp to avoid the injunction by finding that ESB approval with a disclaimer of warranty entitlement would suffice to put the defendant outside of the scope of a passing off action.[70]

Such certification or safety and standards programs[71] have tremendous potential for being used as non-tariff trade barriers.[72] However, this is largely not an intellectual property issue and is beyond the scope of this study. Such standards are sometimes outside of direct governmental control and are a type of delegated responsibility of government. The case is valuable for raising some of these issues and in its brief but useful discussion of the role of standards. Because of the complexity of the issues raised in this case that go beyond intellectual property law, one would hope that they are resolved someday in a full trial with adequate evidence.[73]

The next case is Mattel Canada Inc. v. GTS Acquisitions and Nintendo of America Inc.,[74] which was an interlocutory injunction case decided by Joyal, J. of the Federal Court Trial Division. The reasoning in this case is much more detailed than in Sharp. There is fairly considerable reference to some of the classic cases mentioned earlier, including Remington. The facts would appear to be that Nintendo (America) was the owner of the Nintendo trade-mark in Canada and the exclusive distributor in North America for Nintendo products, which came from its parent, Nintendo, in Japan. Nintendo (America) entered into an exclusive distributorship deal with Mattel for Canada, under which Mattel was obliged to purchase a guaranteed minimum of quantity. The sale of Nintendo products by Mattel constituted 60% of the plaintiff's revenues. The minimum sale requirement was for $50 million dollars U.S. in 1989-1990.

Apart from some evidence that the imported product lacks French labelling and French instructions and does not bear the Mattel name as does the product officially earmarked for Canada, there is little issue made of the difference in the products. In fact, Joyal, J. states quite plainly:

> *If the action before me were by the owner of the NINTENDO marks and if the only evidence be that the defendant is selling a Nintendo product covered by the trade mark (sic), there would be no case for the owner. It would be somewhat ridiculous to assert infringement or passing off when the defendant is dealing the owners own wares. There cannot be in such circumstances, any deception. The owner might have some cause of action against the defendant based on contract on the grounds that the defendant is selling in a territory prohibited to him, , but such an action could not, in my view, be founded on deceit or deception.*[75]

And yet, a few pages later, Joyal, J. states that:

> *This review of case law indicates to me the lack of any deception on the public by the sale of any trade mark*

> *(sic) owner's own goods is not conclusive of the kind of issue before me.*[76]

What of the reasoning of the Supreme Court of Canada in Seiko with respect to deception? Moreover, one cannot help but wonder whether the court was so struck with the fact that Mattel had a minimum sales obligation of $50 million (U.S) in Canada for the year ending March 31, 1990 and had spent $20 million dollars on advertising and marketing by the end of 1989.[77] Certainly, such reasoning by the court is not explicit. Moreover, this is an argument that is commonly heard in policy circles -- that a licensee must have the means necessary to recoup the investment made. However, one might ask in the context of this particular judgment whether such a principle should extend to a profit predicated upon rights that are not clearly established under the law but are only speculative. It is surely not an all or nothing situation with respect to such a product as Nintendo games. There could be an exclusive Canadian distributor who could operate quite profitably, in principle, even with the possibility of parallel imports. The reasons do not deal with an analysis of why it is apparently the case that U.S. Nintendo games are so much cheaper than the identical games in Canada, and why it is profitable for third parties to import and resell them. This is, of course, understandable since judges are not expected to determine Canadian trade policy. The Supreme Court of Canada has in fact declined an invitation to speculate on such matters in the Breck's case.[78] There is also no evidence of any "value added" by the Canadian distribution channel, other than minor language labelling aspects which Joyal, J. finds to be trivial.[79]

An important exception to the "exhaustion" theory -- that is that goods legitimately sold anywhere should be capable of being freely traded -- is that which arises in the recent English Colgate case[80] and the earlier Castrol case.[81] These decisions both concerned products -- toothpaste and automotive oil respectively -- that were legitimate and made by related companies, but said to be suited only for local conditions and not suitable in England. A similar fact situation has not arisen to my knowledge in Canada. In any case, the English law may not be directly applicable, given a different statutory base and the Treaty of Rome.[82]

In the Colgate case, the defendant was enjoined from importing Colgate toothpaste into the UK from Brazil that was said to be of inferior quality. It is interesting to speculate whether the judgment would have been the same if the imported toothpaste were labelled clearly as "Brazilian Formulation" with an overlay sticker. It is also interesting to speculate about the policy rationale that supports the marketing of lower quality goods in developing countries, as opposed to differing formulations for legitimate reasons, as was the case in the classic Champagne judgment.[83]

The other broad theory (discussed by Bereskin) is the **"territorial theory".** This holds that trade-mark owners can segment markets just as copyright and patent owners can.[84] However, I am not as sanguine as Mr. Bereskin about the efficacy of patent and copyright owners real power to segment, for reasons stated elsewhere in this study.

Mr. Bereskin seems concerned about the policy implications of Mattel. He asks "Why does appointment of Mattel Canada as exclusive registered user make any difference? Why should a registered user be in a better position than the trade-mark owner to control gray goods?"[85] He should find some comfort, at least, in the reasons given by Strayer, J. in Nestlé (see below).

Another unsatisfactory aspect of this decision in my view is its failure to address the critical issue of invalidity of the registration raised in the Wilkinson and Breck's cases. While I have no evidence other than intuition, I would guess that most Canadians regard Nintendo products as originating from an entity in Japan. Therefore, there may well have been an invalidity issue here but it is simply not dealt with. Such an issue can arise in any case where there is a very well known mark that originates (in the layperson's sense) in another country.

We come now to the Heinz ketchup case.[86] This was decided on February 13, 1991 by Cullen, J. of the Federal Court Trial Division. The defendant, Edan Foods managed to find several truckloads of Heinz ketchup available at about half the Canadian wholesale price from Heinz (U.S.), which is the parent of Heinz (Canada). So, Edan brought in this ketchup and sold it to Knob Hill Farms, a discount supermarket chain in Ontario. Edan apparently labelled the ketchup as imported by them and added labelling information to comply with Canadian language laws. There is nothing in the reasons that indicates that the labelling contained information that went so far as to indicate a different formulation. Perhaps this would have led to a different result. Conceivably, such labelling could have been applied, if not by the plaintiff, then by the defendant itself.

Heinz Canada apparently introduced a lot of evidence to the effect that Heinz ketchup as made in the United States of America is different from that made in Canada. They do not allege that it is worse in quality, only different. Unfortunately, there are no details in the judgment as to the difference, only evidence that Heinz Canada spends a lot of money to keep abreast of changes in the tastes of the Canadian ketchup market. There is no discussion, however, of the effect of spillover advertising on television, or in other media.

Mr. Justice Cullen is also clearly struck by the fact the Heinz Canada is the major buyer of Canadian-grown tomatoes, and that a lot of Canadian third parties, such as tomato farmers, could suffer irreparable harm if the injunction were not granted. While this may be a very important matter in terms of Canada's trade strategy and agricultural policy, it is respectfully submitted that it is completely legally irrelevant to the determination of an injunction application under the current Trade-marks Act.

Mr. Justice Cullen says that this case is on all fours with Remington Rand. However, the imported products in Remington Rand came from both a non-related German company and a related American company.[87] This is not discussed in Cullen, J.'s reasons. There is not a hint of discussion of the invalidity issue.

Notwithstanding these concerns with the fairly sparse reasons in this case, it is not at all clear that the result in the case is wrong under current law. But the case raises a number of very problematic legal and policy issues.

First, the legal issues. The Heinz case apparently involves trade-marks that have been assigned. Hence, there is no registered user issue. Therefore, there is no issue of policing the quality. If U.S. product never was imported by either U.S. or Canadian Heinz, and appropriate active steps were taken to prevent such importation, then there should be no great problem for Heinz Canada to prevent the parallel importation of U.S. ketchup. But the formulation is said to be different. Different, but not inferior, as in the Colgate case. Because Heinz Canada and Heinz U.S. are different entities selling somewhat different products, Heinz' case cannot be summarily dismissed as Joyal, J. made clear in Mattel he would do if it were the trade-mark owner bringing the suit selling identical goods. These are not identical goods.

But, Heinz is in a potentially difficult legal position here. The more they lead evidence as to different products, the more they help their case on the issue of infringement. The "guarantee" theory -- which is oriented toward protection of the public -- helps their case. This holds that the function of trade-marks law is to ensure that an accustomed standard or quality of the product is satisfied for the consumer. This is most recently expounded in the important Heintzman case (see below). On the other hand, Wilkinson and Breck's support the "source theory" whereby the purpose of trade-marks law is held to be the identification of the article with the actual source of the product. This is more in the nature of a private right that stakes out the owner's "property" in the mark, although it is also useful for purposes of product liability. The risk of invalidity is based upon the Wilkinson and Breck's cases, where the commercial message tended to identify the goods with the assignor rather than the assignee. In a nutshell, what is the Canadian public to make of a situation where ketchup bottles that look essentially the same (the shape is a famous distinguishing guise and registered as such), both emanating from companies called "Heinz" that are clearly related, are advertised heavily in both jurisdictions with ads that inevitably and perhaps even deliberately "spill over" in both print and electronic media? True, the effects of spill-over advertising will not necessarily be held against a party who cannot control such advertising (although such control is not analyzed in this instance). [88] Thus, the more there is evidence of a different product as between Heinz Canada and Heinz U.S. with the same name and bottle, the stronger is Heinz Canada's case on the "guarantee" theory. However, the weaker it is on the source theory. This is because the public sees the same name and same bottle and may tend to assume that the same corporate source is behind all products that have the name "Heinz" which are sold in bottles that are surely a "distinguishing guise".

Could the public be confused as to the source of the goods? Is there any possibility that the differing formulation may be motivated by a desire to segment markets? Is the tail wagging the dog? Unfortunately, many of these questions are not answered as yet in this case, which the defendant is trying to present as a "David and Goliath" situation.[89]

Some of these questions and other related technical ones go right to the heart of what trade-marks law is all about and how the Trade-marks Act works. For example:

I. Can a plaintiff, in a situation such as this, rely on the provisions of s. 19 of the Trade-marks Act, in which the question is, essentially, "Is there an infringement? If so, is there a defence of invalidity?" This does not require proof by the plaintiff of a misrepresentation made by or confusion caused by the defendant. The plaintiff would appear to need prove only "use" in the trade-mark sense.[90]

II. Are we still, even after the 1953 amendments, bound up in the difference between a manufacturer's good will and a seller's good will? This distinction used to hold that a mere purveyor or seller of goods did not need the trade-mark owner's licence to sell the goods; however, a manufacturer who wished to use the same or similar trade-mark did need a license. With the advent of the registered user system in 1953, the obtaining and filing of a registered user agreement appeared to solve all of the problems of the old distinction. These provisions were intended to ensure that "modern" commercial practises which involved licensing could be carried on without any risk of deception to consumers or of loss of distinctiveness to trade-mark owners, provided that registered user agreements were filed on the public record and that the control and supervision of these agreements were complied with.

III. Note that s. 4 of the Trade-marks Act[91] clearly would seem to make the acts of the defendant here constitute "use". Could the defendant argue that this exercise in parallel importation was not "in the normal course of trade" and hence did not constitute use? Or, would this, in effect, amount to *"ex turpe causa non oritur actio?*

IV. Could the defendant in this case argue that any confusion, as defined in s. 6 of the Trade-marks Act, is caused by the plaintiff failing to mark its products in a way that would differentiate them to a reasonable consumer? Thus, any "confusion" (as per s. 6 (2) of the Trade-marks Act) on the part of the consumer or misapprehension by the consumer that the U.S. and Canadian made ketchup are made by the same legal entity is really the fault of the one or the other or both of Heinz U.S. and Heinz Canada for using virtually identical labels and bottles, for a product that they themselves say is different. Or does small print that states the place of manufacture suffice to avail the importer (Edan)?

V. What is the legal interrelationship between the loss of distinctiveness under s. 18 needed to be proven by the defendant to succeed in its defence and confusion in the sense of s. 6(2) as arguably caused by the plaintiff?

VI. Of what effect on the construction of ss. 19 and 20 of the Trade-marks Act are the provisions of s. 51 (see Appendix IV). These provisions essentially provide that the use of a mark by related pharmaceutical companies or use of confusing marks by such related companies has the same effect as use by the owner. While at first glance this would appear to be a helpful provision for drug companies, it may have been intended to be quite the opposite. This is because it would prevent them from using the Trade-marks Act to achieve market segmentation. It is believed that s. 51 was inserted as an adjunct to the 1969 compulsory licensing provisions in the Patent Act. The question for the present context is whether it can be argued that *expressio unius est exclusio alterius* -- that is by stating the principle of related company exhaustion in one context, is it thereby precluded everywhere else.

Another aspect of the evidence of differing quality is the potential impact of the recent Heintzman case.[92] This is a potentially very important trade-marks case which holds, essentially, that where the quality of the goods is substantially changed (i.e. inexpensive and inferior Korean pianos were substituted for handmade Canadian pianos bearing the venerable "Heintzman" mark) without due notice to the public, the mark can become invalid. Now, if the concern for the protection of the consumer interest shown in Heintzman is followed, it is possible that Heinz could be hoisted on its own petard. By deliberately having different products standards in Canada and the U.S.A. bearing the same trade-mark, could it thus be argued that the danger of confusion may in part be created by Heinz itself?

Another aspect of Cullen, J.'s reasoning in Heintzman seems to be that "It is not clear the Heinz products constitute a significant proportion of its [the defendant's] sales."[93] Similar findings were made in the Sharp and Mattel cases. Does this mean that the larger the discrepancy in size between the plaintiff and the defendant and the less reliant the defendant is upon the product and the more reliant the plaintiff is, the more chance there will be for the balance of convenience test to be met in favour of the plaintiff in these cases? It is suggested that interlocutory judgments should not only consider the balance of convenience but give due and perhaps superior weight to the apparent merits of a case. This should especially apply in intellectual property cases, because of the *in rem* aspect of these cases.[94] The relative size of the litigants should not be a major factor in most instances, unless the granting or withholding of the injunction is likely to put one or the other party out of business on the spot.[95]

It is understood that this decision is being appealed. This is good for jurisprudence, because it is clearly less than ideal to have major public policy issues decided solely at the level of interlocutory injunctions, where evidence is sparse and time is short.

It is very difficult to reconcile this decision with that of Ulay, discussed above. It is not known whether Ulay was cited in argument, but it is not mentioned in the reasons. The possible difference might lie in the evidence that Heinz had some 50 years of independent good-will in Canada, which is far longer than the independent good will in the Ulay case. It will be recalled that Ulay also dealt with a somewhat different product emanating from a related company. However, it would be useful to see a reconciliation, or at least a judicial consideration, of the Ulay case in the Heinz matter, if the latter proceeds.

It is interesting to ask some questions, for which there are no quick answers or conclusions, about the Heinz case from a policy standpoint more than a legal one. We have just finished implementing a free trade agreement with the U.S.A.. The public presumably thinks that this means that goods should flow freely back and forth. Everyone knows that Heinz ketchup sometimes doesn't flow freely from the bottle, but would the public not expect that it should flow freely across the border if there is "free trade" in place? Is it not somewhat incongruous that Canadian ketchup prices should be apparently twice that of U.S. ketchup, and that U.S. ketchup cannot be imported into Canada due to the Trade-marks Act? From an economic standpoint, who is benefitting from the court's judgment?

The filed documentation in the Heinz case suggests some interesting points which might tend to suggest, if proven, that there could be an issue of "dominance" in the competition sense. It should be noted that this information is based upon material filed by the respondent at the injunction stage and not yet proven at trial.[96]

THE NESTLÉ CASE

Another highly important recent decision is that of Nestlé v. Edan.[97] The defendant is the same as that in Heinz and the facts are superficially similar.

Nestlé Canada is a subsidiary of Nestlé Switzerland and a sister company of Nestlé U.S.A. Nestlé Canada is the registered user of several trade-marks such as "Taster's Choice", "Nescafé", "Mountain Blend", etc. owned by Nestlé Switzerland.

Nestlé U.S. makes coffee and sells it in similar packages under the trade-mark "Mountain Blend" in the U.S.A. The U.S. "Mountain Blend" is said by the plaintiff to differ "markedly in composition, taste, appearance, and quality" from the "Mountain Blend" brand sold in Canada.

It should be noted at this point that many multinational companies have at least two tiers of trade-marks that are used in their marketing. For example, "Nestlé" appears to refer to the corporate source of many types of goods, but not to specific products themselves. The second tier in this case includes trade-marks such as "Taster's Choice", "Nescafé", "Mountain Blend", etc. which are applied to specific products made and sold by Nestlé. Another example might be that of General Motors, which makes "Pontiac" automobiles, which in turn comprise "Trans Am", "Bonneville", "Grand Am", etc. models. It is often (but not invariably) at the second or third tier that the alleged infringement takes place, when there is an allegation that the actual product differs in quality or nature. In the present case, the dispute does not involve an allegation that the coffee in question does not come from Nestlé, but rather that "Mountain Blend" is a different product in the U.S.A. than in Canada.

This lawsuit was somewhat novel and potentially quite interesting because it claimed not for infringement but for causing confusion contrary to s. 7(b), passing off, contrary to s. 7(c), and doing acts contrary to honest industrial usage (contrary to s. 7(e)) of the Trade-marks Act. Apparently, at the hearing which took place on July 31, 1991, the latter two issues were not seriously argued. Strayer, J. held, essentially, that there was no confusion because the labelling was sufficiently explicit that a consumer would not be misinformed as to the nature of the product being purchased. A last-minute attempt to amend the cause of action to encompass infringement as in the Heinz case was understandably rejected by the Court.

Of some note is the fact that Edan invoked Article 1808 of the FTA which deals with referrals of matters from judicial decisions. Edan was, presumably, either attempting to construe the Canada-U.S. Free Trade Agreement in its favour, which would have been difficult, since it is completely silent on this issue or, attempting to get the Government to explain why the agreement is silent. Edan may have made some technical flaws in attempting to involve the Government of Canada. Not the least of these is the fact that s. 5 of the Canada-United States Free Trade Agreement Implementation Act, C-10.6 , states that:

> *No person has any cause of action and no proceedings of any kind shall be taken, without the consent of the Attorney General of Canada, to enforce or determine any right or obligation that is claimed or arises solely under or by virtue of Part I, or any regulation made under Part I, or the Agreement.*

Edan was apparently seeking to force the Canadian and U.S. Governments to state their views as to the meaning of the FTA on the matters in question. Notwithstanding the fact that the FTA is silent on the matters in question and that the Government would have been likely to win the procedural skirmishes here, there remain certain interesting questions. For example, if the FTA is silent about matters such as this, why is it silent? It might have been argued that the FTA does not have provisions analogous to those of the Treaty of Rome (ss. 36, 85 and 86) which result in the overruling of domestic law.

In the result, the Free Trade issue appears to be moot at the present time and was adjourned _sine die_. This would appear to be because the motion was dealt with on its merits rather than on procedural matters. It is understood that the disposition of this motion will not be appealed, and that the matter will proceed to trial.

Several questions remain unclear from the filed record. Why is Nestlé of Switzerland, the parent company, not joined? Should the action be proceeding without them?[98] Why are the defendants not clearly labelling the product as "American Blend" or some other words, to inform Canadian consumers of the different taste?

It appears to be particularly significant that the lawsuit was brought as a "passing-off" case rather than an infringement action as in _Heinz_. Apparently, a late effort to amend the statement of claim was not successful (reasons, p.2). This may relate to the question of why the parent was not joined, although this is not alluded to in the reasons. However, the court does allude to the "uncertainty of the jurisprudence concerning the rights of registered users." (Reasons, p. 6)

A key strategic point may lie in the fact that this type of statutory passing-off action does not provide for a defence of invalidity as is the case under a s. 19 infringement action. Thus, the risk of a finding of invalidity as in Wilkinson is reduced if not eliminated. Thus, it may be that the parent did not want to participate in the action or that there was concern of the vulnerability of the trade-mark registration.

Strayer, J. briefly, but clearly, distinguishes this case from that of Heinz. He states:

> *I believe that the cases are distinguishable in that the plaintiff there sought an injunction to prevent infringement and it was the registered owner in Canada of the trade mark (sic). Further, the packaging of the U.S. product was virtually indistinguishable from the plaintiff's Canadian-made products, yet the taste was substantially different (reasons, p. 8).*

Strayer, J. had previously made a finding of fact that the labels in the Neslté case were sufficiently different and contained enough information that a shopper who had a "serious interest in the kind of coffee he is buying" could tell the difference (reasons, p. 5).

This raises a rather interesting question. Does it mean that the more the confusion is caused by the manufacturer (i.e. identical package, different goods), the more the manufacturer (or its related companies) can take advantage of this situation?

This case is far from the last word on the issue in Canada. However, it goes a long way towards delineating the actual "black letter" legal issues that need to be dealt with in such types of cases. It will stop an immediate avalanche of similar injunction applications, but may reinforce the apparent Heinz formula for success in these situations, which now appears to be fairly clear (unless, of course, it is overruled).

It is interesting that Edan was also recently sued by Kraft General Foods Canada, Inc., another multinational food giant, in another case involving parallel importation of coffee.[99] The statement of claim alleges that coffee bearing the well-known trade-mark "Chase and Sanborn's" was imported without the plaintiff's authorization from the USA, where it was made by a company related to Nestlé, and that Kraft and Nestlé are unrelated competitors. Thus, according to the statement of claim, the identical or very similar trade-mark is being used by two completely unrelated companies in Canada and the U.S.A. respectively, presumably due to a different history of assignments. The plaintiff alleges infringement under ss. 19 and 20 of the Trade-marks Act, passing off under s. 7(b) of the Act, and depreciation of goodwill contrary to s. 22 of the Act.

It should be noted that the fact situation alleged in the Kraft action, if accurate, is one that is likely to be fairly rare. It would be unusual that the same trade-mark would have a long and separate history in two neighbouring countries in the hands of unrelated competitors. On its face, this is a similar situation to that of Hag II in Europe (see below), except that the Hag II case resulted from a forced separation due to wartime confiscation.

Since there has been no judicial consideration of this matter, it has no precedential value. However, it is interesting to note two facts. The same defendant, Edan, has attracted the attention of at least three multinational food giants in one year, and at least three law suits in the federal court. The second fact is that these three cases, two of which have already resulted in important decisions, all involve food and free trade issues.

OVERALL ASSESSMENT OF THE CANADIAN TRADE-MARK AND PASSING OFF CASES

The current state of the law in Canada is very inconclusive at best. It is always difficult to predict the state of the law based upon injunction cases. However, very often an interlocutory injunction is the end of the matter in Canadian intellectual property actions. Such matters may never go to trial and therefore often do not receive a fully reasoned and fully considered decision. Interlocutory injunctions are decided quickly, on affidavit evidence alone, and on a different onus and balance of probabilities basis than would be applied at trial.[100]

However, an interlocutory injunction can set an immensely important precedent if it is the last and only word on a particular issue. For example, the current group of cases relies upon (or ought to at least consider if properly argued and reasoned) the Remington case which was itself an injunction decision.

Recent injunction activity involving trade-marks has not been confined to the Federal Court. There are two Quebec

Superior Court cases worthy of note. The first is that of Bergeron v. Babin.[101] In this instance, an injunction to prevent the parallel importation of "Rap-Tou" food processors from France against the wishes of the exclusive distributor for the U.S.A. and Quebec was refused on the basis that a trade-mark does not confer the same type of monopoly as does a patent. This judgment does not seem to advert to questions of trade-mark ownership or registration. These factors may explain why it has not, apparently, been cited elsewhere.

As well, note should be made of Sony du Canada v. 173968 Canada Inc (Impact Electronique).[102] This case involved the importation of refurbished products from the U.S.A. and cannot therefore be regarded as germane to the mainstream line of cases.

Therefore, these recent cases cannot be ignored merely because they are injunctions. Those responsible for policy, if they are concerned with the result of these cases, must not passively allow businesses to acquire vested rights and behaviour based upon this line of reasoning. Otherwise, it will become almost impossible to change the law at a later date. A good instance of this phenomenon can be seen with respect to the problems with official marks under s. 9(1)(n) of the Trade-marks Act. In that instance, the Federal Court gave a ruling in 1980 that opened the door to the use by "public authorities" of the official marks provision in a virtually unlimited manner.[103] This decision opened the door to commercial exploitation, as sanctioned reluctantly time after time by the courts, of the provisions that were intended to be of non-commercial benefit to such organizations as universities and charities. Now, 12 years later, and after powerful interests that have been qualified as "public authorities" such as the Olympic Trust of Canada have come to rely on the provisions of s. 9 for their commercial existence, it is proving difficult to change these provisions.[104]

What is the current state of play and the likely outcome of the recent trade-mark injunctions cases in Canada? To summarize, it would seem that there are the following types of actions which have been brought:

I. **Passing off:** the action is brought by a Canadian entity claiming a contractual or statutory interest in the trade-mark, but the action does not invoke the provisions of the Trade-marks Act. The trade-mark registration is not put at stake, but such actions would appear to have little prospect of success, absent serious misrepresentation (Seiko).

II. **Ownership of a Canadian registered trade-mark where the assignee is related to the assignor.** Such cases appeared until recently to have little likelihood of success and put the validity of the registration at great risk. (Wilkinson Sword). However, in Heinz, there was a successful injunction application based upon an alleged 40 year separation of goodwill from the U.S. parent and a different product using the same trade-mark.

However, a Canadian trade-mark owner may be able to succeed in preventing the importation of grey market goods into Canada, without having its own trade-mark declared invalid if, in the case of related companies:

A. There are separate corporate entities in Canada and abroad.

B. There is a genuine assignment. The trade-mark rights in Canada belong to the Canadian subsidiary or related company.

C. There can be shown to be separate goodwill in Canada from that of the foreign related company.

D. The product can be differentiated to the appropriate extent, based upon differences in Canadian tastes, needs, climates, etc.

E. The packaging and labelling as much as possible are identical.

III. **Ownership of the registered trade-mark in Canada by an assignee that is at arm's length from the original trade-mark owner.** Such a case has some possibilities of success, based upon the precedent of <u>Remington</u>. However, if any attempt is made by the Canadian owner to capitalize upon the goodwill of the foreign owner, the trade-mark registration is likely to be found invalid (<u>Breck's</u>).

IV. **Appointment of arms length Canadian distributor as an exclusive registered user.** This method was successful in the case of <u>Mattel</u> involving the Nintendo mark.

The prevailing opinion is that, on the basis of the present statute law, a case of infringement can be established in principle, given the right facts, without necessarily a finding of invalidity. That depends, it would seem, on the plaintiff being the owner of the mark in Canada. The Heinz case may be the case in point. If this theory is correct, then labelling will not avail the defendant because, as noted above, the question of "use" that leads to the finding of infringement is not related under the Trade-marks Act to the issue of confusion.

On the other hand, confusion, as is being argued in the Nestlé case, may be rebutted by the use of labelling (whether applied by the importer or the multinational manufacturer itself -- although this point is not discussed) to dispel any misapprehension on the part of consumers (as was done in Seiko).

According to Mattel, an arm's length registered user can also succeed. However, this author agrees with others, as noted above, that it is at the very least anomalous that a mere registered user (who is by definition subject to control by the owner -- see s. 50 of the Trade-marks Act in Appendix 4) is in a better position to enforce than an assignee. Moreover, the basic theory of the registered user provisions of the Trade-marks Act is that a trade-mark can be licensed by means of a registered user agreement without the loss of distinctiveness because the goodwill of the licensee is deemed to enure to the owner. However, this is exactly why it is difficult to see how Nintendo and Mattel are entitled to have separate goodwill for purposes of market segmentation but merged goodwill for purposes of trade-mark validity.

Without unduly anticipating the policy discussion in Chapters III and IV below, it is respectfully suggested that these types of distinctions are noted far more by commentators than by the courts themselves, in an effort to rationalize an otherwise inexplicable and unsatisfactory state of the law. In other words, it makes very little sense to most observers, whether average consumers, sophisticated business persons, or even specialist intellectual property lawyers, that the ability to import "genuine" goods should depend upon whether or not the plaintiff is an owner or a registered user, whether a "passing off" action is brought at common law or under s. 7 of the Trade-marks Act, whether or not the Canadian plaintiff is or ever was related to the foreign owner or predecessor in title of the trade-mark, whether there is a difference in the nature or the quality or both or neither of the wares, etc. From a public policy standpoint, these are relatively meaningless distinctions because they are largely artificial, and incomprehensible to all but a very few specialized counsel in the country. Even these counsel in turn disagree with each other as to the significance of the nuances. Moreover, these distinctions are truly artificial because well-advised enterprises can readily fit themselves into a particular category, even if this involves the potentially minor inconvenience of establishing a slightly different product for the Canadian market.

From a practical economic standpoint and an international trade standpoint, the resulting levels of uncertainty could form significant barriers to entry and activity on the part of small, medium, and even large Canadian businesses who cannot afford to litigate to the Supreme Court of Canada to determine whether or not they can import a particular shipment of genuine goods.

To conclude this assessment, it is fairly apparent that the Canadian courts are going in the direction of market segmentation. Even if some leeway with respect to exhaustion is left at the end of the day, businesses will doubtless rearrange their affairs to come within the narrower rules (i.e. by assigning trade-marks to their subsidiaries and creating slight differences in the "Canadian" product) and hence achieve market segmentation. This is difficult to reconcile with the general spirit of free trade and the FTA in particular.

COPYRIGHT LAW IN CANADA

At the outset, it should be stated that many countries, including Canada, have used or attempted to use copyright legislation as a means to achieve cultural ends, not the least or most unworthy of which is the establishment of a healthy national independent book and news media publication industry. Whether or not copyright law is an appropriate tool to achieve this worthy end is highly debatable, but will not be debated here. It is noted above that Canada got off to a very shaky start in its legislative program on intellectual property on this very issue over 100 years ago and that the issue is still not resolved.[105]

The purpose of this chapter is to examine how and to what extent the copyright law can be used to block parallel importation of products that embody copyrighted material. The most obvious case would be a book. The least obvious would be a bottle containing a product, the label of which may or may not include copyrightable subject matter. A mid-way case would involve a product such as a camera or a computer that comes in a box with an instruction booklet inside. Another interesting example would be a sound recording with liner notes on the jacket or inside in the form of a pamphlet.

Again, it must be stated at the outset that there are some rather complex issues involved in the question of parallel importation of copyright material that are somewhat beyond the scope of the present exercise. These questions entail the interrelation of ss. 44 and 45 of the Copyright Act and why, in the final analysis, these sections (which establish a border enforcement scheme in conjunction with the Customs Tariff[106]) are only useful in situations involving "books". These very important issues will not be dealt with in detail at this time.

WHY IS THE COPYRIGHT ACT NOT USED MORE OFTEN TO BLOCK PARALLEL IMPORTS?

The Copyright Act, through the provisions of ss. 27(4), 44 and 45 makes it reasonably apparent that a copyrighted work that is made outside of Canada by someone other than the Canadian copyright owner can be found to infringe in Canada, even if it is lawfully made in the other territory.

The most important provision is found in s. 27(4) which states:

> *Copyright in a work shall be deemed to be infringed by any person who:*
>
> > *(a) sells or lets for hire, or by way of trade exposes or offers for sale or hire,*
> >
> > *(b) distributes whether for the purposes of trade or to such an extent as to affect prejudicially the owner of the copyright,*
> >
> > *(c) by way of trade exhibits in public, or*
> >
> > *(d) imports for sale or hire into Canada.*
>
> *any work that to the knowledge of that person infringes copyright or would infringe copyright if it had been made in Canada.*[107]

The immensely inscrutable ss. 44 and 45 of the Copyright Act provide, in conjunction with the Customs Tariff, that Revenue Canada Customs can be enlisted to block imports at the border. However, there is a long standing interpretation by Revenue Canada known as the "Varcoe Ruling"[108], to the effect that once a book (and the sections apply only to books) are put on Schedule "C", all copies of the book will be blocked, even those which the so-called legitimate importer may wish to bring in itself. As will be presently seen, the Copyright Act simply does not work well to block parallel importation of anything but books.[109]

As noted, border enforcement (through the help of Canada Customs) is only available for books and even then can be a two-edged sword that can hurt its holder. This is one of the main factors that leads to the *de facto* result that there is a fair degree of parallel importing of books and other products protected by copyright law into Canada.

Once the goods have been distributed into stores, it is extremely impractical to stop their sale, since any given outlet will usually have only a small quantity, and the knowledge requirement under s. 27 of the Copyright Act would not normally be provable until after that damage has been done. Practitioners generally agree that a registered letter to the proprietor of a store is the sine qua non before liability can arise. If such a letter is ill-advised and threatens sham litigation, then it is becoming increasingly possible that there can be adverse consequences under Canadian law for such a practice.[110]

There are other reasons that may explain why the Copyright Act is largely, if not completely, ineffective in blocking the parallel importation of anything but books.

One obvious explanation is that many labels and packages for products would not qualify for copyright protection. For a label or package to qualify for copyright protection, it must contain either copyrightable literary or artistic material. A mere listing of ingredients and basic factual information together with the trade-mark in alphanumeric form would not readily qualify as copyrightable material. It should be noted that the law on this point is in a state of great flux as well, given the recent Feist[111] case in the U.S., and the not quite so recent Exxon [112] case in the U.K. The Feist judgment denied copyright to mere factual data on the basis of lack of originality. Anglo-Canadian jurisprudence is slightly more generous to those who toil by the "sweat of the brow" to put together race track forms, etc.

Another reason that copyright in a label or on a package will not likely avail in obtaining an interlocutory injunction is this. When the label is on a product or the package contains the sought-after product, it is the product that is the object of the commercial transaction. A company such as Heinz is in the business of selling ketchup, not labels for ketchup bottles. Therefore, it would seem incredulous for them to argue that there is irreparable harm being done by the importation of copyrighted labels. Moreover, labels and packaging usually are of nominal monetary value compared to the product itself. Perhaps Heinz can make a case sufficient for an injunction on the basis of irreparable harm based on the difference in the product itself; however, it is difficult to see how irreparable harm can be done by alleged copyright infringement in a label.

Of course, the same would not hold true for a book.

The literary work, namely the book, is the very object of the transaction and not a mere slim technical thread[113] upon which to seek an injunction. Irreparable harm can more easily be established in litigation involving books.

It is submitted that this lack of efficacy on the part of the Copyright Act to be useful in barring the importation of grey market ketchup, cameras, or computers is essentially proper as public policy. (See the discussion of the U.S. Sebastian case in Chapter II). The Copyright Act has been stretched beyond credibility on many occasions in recent years, but it was surely never intended to serve as a replacement for prohibitive tariffs on table top condiments or most of the other items that have been the subject of grey market litigation.

An interesting example of where an attempt to use the Copyright Act in a clearly inappropriate situation can be found in Dennison Manufacturing v. MNR [114] wherein the plaintiff sought to exclude the importation of certain "attachment tags" or "cavity attachment moulds" used to affix labels and tags to clothes on sale in stores. Dubé, J. found that entitlement to copyright in this situation was far from clear and that *mandamus* of the Minister of Revenue to enforce exclusion at the border would not lie.

The lack of strength in the Copyright Act to deal with anything but books is also illustrated, inferentially, in the recent case of Mattel v. GTS Acquisitions and Nintendo of America.[115] That case, discussed earlier in this study, involved the importation of computer games and it would appear from the reasons given by Joyal, J. (allowing an interlocutory injunction) that copyright law was not even argued. The case was dealt with strictly on trade-marks law principles, although computer programs were clearly protected by copyright at the time the cause of action in this case arose. This might be contrasted with the recent decision of Jerome, A.C.J. in Beamscope Canada Inc. v. 2439-0692 Quebec Ltd.[116] in which an injunction sought under the Copyright Act for the importation of Nintendo computer games was declined basically because the court found the cause of action as framed to be far from clear, and the legal issues surrounding ownership of the artwork, timing of the ownership and the timing and production of the assignments raised a "vigourous and comprehensive" defence.

The older classic cases of remaindered books should be mentioned for the sake of completeness.[117] These show that the parallel import remedy in the case of books can sometimes be problematic as well.

CURRENT DOMESTIC POLICY INITIATIVE

At the time of writing, the Minister of Communications has announced a policy that would, *inter alia*, strengthen the right of Canadian publishers who act as exclusive distributors for foreign publications, to restrain imports of books printed abroad.[118] The practice of book stores or libraries of buying books from channels outside of Canada (usually for reasons of price or service) is called "buying around". The policy seeks to inhibit or prevent "buying around". Canadian publishers are said to depend on the income from the distribution of foreign books. According to the Minister:

> *....we will give exclusive distributors greater protection of their distribution rights in the Canadian market. Nothing in this amendment will*

create an absolute right either to distribute or import books, nor will it require that all imported books be subject to exclusive distribution agreements.

Simply put, where such agreements exist, stronger protection will be provided. At the same time, publishers/distributors and book sellers, librarians and wholesalers will be given sufficient time to reach an agreement on their relationship in such areas as pricing and service. This agreement will be reflected in the regulations under the Copyright Act. These amendments will not be proclaimed until the regulations are in place.[119]

This is a very controversial policy that pits booksellers and libraries against Canadian publishers. The latter are placed in the invidious position of having to ask for protectionist exclusive rights to deal exclusively with foreign titles in order to cross-subsidize Canadian publishing (which is said to be inevitably money losing). This raises a host of policy concerns (some of which are discussed in Chapters III and IV of this work) as to whether relief measures, if any, should come from direct or indirect subsidies, or special status under the Copyright Act. Given the fact that this matter continues to be before Cabinet and is thus highly sensitive, the author cannot explore it in detail at this time. Rather, the point is simply made that this is a controversial direction currently espoused by the Minister of Communications.[120]

CHAPTER II EXHAUSTION LAW IN THE GLOBAL CONTEXT

This chapter will examine the law of exhaustion in certain major fora outside of Canada. This analysis will, perforce, be much less detailed than that in the preceding chapter dealing with Canada. The laws of the U.S.A., and EC will be examined overall. References will be made as well to certain relevant aspects of Australian law, since this is a relevant jurisdiction for Canada from a policy and/or trade standpoint. Finally, the chapter will conclude with a treatment of the issue in the treaty context.

The emphasis in this analysis will be on where the law is headed in these jurisdictions and the overall policy trends, rather than on detailed case law examination. In any event, the sheer volume of case law in the U.S.A. and the EC on this particular issue is enough to fill several volumes with detailed analysis. In contrast, the quantity of case law in Canada is vary sparse.

PART "A" -- THE U.S.A.

Overall, it will be seen that the U.S.A., despite its official protestations favouring market segmentation, has evolved so as to achieve a policy that tends to favour exhaustion with respect to goods that originate from a source that is related in a corporate sense to the U.S. entity claiming exclusive territorial rights. This is not particularly transparent under U.S. law; indeed, it requires a review of the last seven decades of litigation to come to this conclusion. However, U.S. interests, and indeed many Canadian interests, are strongly in favour of Canada providing stronger rights of market segmentation that will inevitably favour U.S. companies than U.S. law itself does, when examined with reasonable closeness.

PATENTS

When goods are purchased abroad from the holder of a U.S. patent, in the absence of an express condition of sale to the contrary, the purchaser can then import those goods into the U.S.A.[121]

> *The principle that the first sale of a product by a patent owner or his licensee exhausts that patent monopoly, and deprives the holder of any further control over resale of the product, applies to an authorized first sale abroad by a patent owner or licensee that also has the right to sell in the United States.*[122]

Purchases made abroad from a mere licensee, however, do not give the right to resell in the U.S.A., even when the U.S. patentee holds a corresponding patent in the country of purchase.[123] Thus, the technique of ensuring that goods made abroad are made only under license has the potential to ensure that the U.S. patentee can exclude the parallel importation of such goods into the U.S.A.. The basic theory for this is simply the old maxim that *nemo dat quod non habet* - a licensee cannot give what he does not own. Naturally, there may be corporate, tax or marketing considerations which militate against such licensing. These factors must all be weighed and balanced together.

A patentee/licensor's right to control a patented product once it is sold is thus severely limited by the "exhaustion doctrine". However, where the purchaser has notice of the restriction, the purchaser may be liable along with the licensee.[124]

Thus, it can be seen that the U.S. law of exhaustion under patents is quite similar in its theoretical basis to that of Canada, and really amounts to the venerable theory of "implied license".

Under section 261 of the Patent Code, there can be geographical limitations on patent licenses even within the U.S., but there are complex antitrust doctrines and case law to contend with.[125]

The U.S. law, however, differs from that of Canada in some major respects. Firstly, there is a well developed jurisprudence in antitrust law that creates a potential minefield for territorial restraints "downstream". At one time, such restraints were viewed as a *per se* violations of s. 1 of the *Sherman Act*. Today, such acts might be viewed more under the rule of reason approach of *Continental TV v. GTE Sylvania*.[126] However, horizontal restraints, which are generally dealt with by s. 1 of the *Sherman Act*, are still "per se" illegal in the U.S.A. in the grey market or other contexts.[127]

The complexity and flexibility of the U.S. antitrust law is illustrated by the plausible theory that a grey marketeer could be guilty of a s. 1 or s. 2 *Sherman Act* antitrust violation because of an unlawful attempt to monopolize.[128]

Moreover, the U.S. has available the formidable and discriminatory (as so found by a GATT panel) remedies of s. 337 of the (Smoot-Hawley) Tariff Act of 1930.[129] This can result in double royalties to U.S. patent owners in certain cases.[130]

Thus, great care must be taken in comparing the law of exhaustion in Canada and other countries to that of the U.S.A. The law of the latter jurisdiction is not particularly transparent. Much of it is contained in jurisprudence that is superficially unrelated to intellectual property law directly. It must also be remembered that, at least presumptively, judicial attempts to enforce an intellectual property right are sheltered by the Noerr-Pennington doctrine, pursuant to which requests for administrative, judicial or legislative relief, even by organized trade associations are generally immunized from illegality.[131]

It is probably the case that the Americans have more exhaustion under patent law than they care to admit. This proposition requires considerable further study. It is, in all its potential detail, quite beyond the scope of this work. An example of the myriad complexities of the U.S. case law and interrelationship between intellectual property and antitrust doctrines can be seen in the proceedings of a conference held on "Gray Markets" in 1986, prior to the major Supreme Court Judgment in Copiat.[132]

TRADE-MARKS

The issue of grey marketing under American law goes back a very long time, and has received some very copious and distinguished judicial consideration. As will presently be seen, the U.S.A. has generally permitted far more grey marketing activity within its own confines -- through the less than transparent aegis of case law -- than has Canada and many other jurisdictions. Before examining the modern statutory framework and the recent jurisprudence including the celebrated 1988 COPIAT[133] decision before the U.S. Supreme Court, it is necessary to examine some early jurisprudence.

The first major grey (the Americans use the spelling "gray") marketing case to arise in the U.S.A. was that of Appolinaris v. Scherer.[134] In that case, the plaintiff was the exclusive U.S. distributor of a brand of mineral water marketed in Europe with a label warning that importation into the U.S.A. and Britain was forbidden. Nonetheless, the defendant obtained the product with the label and imported it into the U.S.A. The Court refused to enjoin the importation because the product was genuine. The Court stated that:

> *It is not possible by any contract ...to create a territorial title to the products of this spring; no such title is known to the law of personal property. No analogy can be drawn from the law of patents, because title to this species of property is purely statutory; and it is by force of arbitrary law alone that the title in the incorporeal property can be subdivided into territorial parts.*[135]

This is the famous passage that is often cited as delineating the **"universality"** theory of trade-marks law. However, that theory is sometimes said to be abandoned.[136] Others, however, see the universality theory as far from dead.[137]

The reason why the universality theory (roughly equivalent to the term "exhaustion") is thought by some to be dead in the U.S.A. is that it was apparently overruled by no less than Justice Oliver Wendell Holmes in the celebrated decision in Bourjois v. Katzel.[138] In Bourjois, the plaintiff had not only purchased exclusive distribution rights but also the entire U.S. goodwill, trademarks, trade names, etc. The product was perfume. It is interesting that many of the key cases on exhaustion concern perfume and coffee. The reasoning of Justice Holmes is basically predicated upon the observation that the French owner of the perfume could not have competed with the U.S. assignee subsequent to the deal and thus, a third party not privy to the contract should not be in any better position. He recognized an exclusive territorial right in the U.S.A.[139] This case is often cited for the modern notion of "territoriality" and rejection of the "universality" theory.[140]

Another very important U.S. case dealing with grey marketing is that of Guerlain. This was another perfume case that also raised major and as yet unresolved antitrust issues.[141] In this case, the U.S. Department of Justice prosecuted three exclusive U.S. distributors along with the foreign manufacturers of their products for monopolizing trade in these products in the U.S.A. by attempting to exclude grey market imports. District Judge Edelstein was satisfied that such a monopoly enterprise existed. Judge Edelstein also considered questions raised by s. 526 of the Tariff Act, which is discussed below.

In a very controversial move, the Justice Department, in an apparent policy dispute over s. 526 of the Tariff Act and its relevance to grey marketing, successfully petitioned the U.S. Supreme Court to have the decision vacated about one and a half years after Judge Edelstein's decision and their initial victory, and Judge Edelstein rather bitterly complied.[142]

The U.S. government has clearly had a long and vacillating viewpoint of the interconnection between grey marketing and antitrust activity. This interconnection is just now being seen in Canada. The competition implications for Canada are elaborated below in Chapter III.

The modern statutory framework dealing with exhaustion under U.S. trademark law can be found under sections 32, 42 and 43 of the Lanham Act[143] and section 526 of the Tariff Act, 1930.

If the impugned goods are already within the territorial United States, the action will proceed under sections 32 and 43 of the Lanham Act. Section 32 protects against use of a trademark which is a reproduction, counterfeit, copy or colourable imitation of a registered trademark without the consent of the registrant. Section 43(a) protects against the use, in connection with the marketing of goods, of a false designation of origin, false description or false representation.

If the goods have yet to be imported into the United States, Section 42 of the Lanham Act and section 526 of the Tariff Act, together with Customs Regulations [144] are, in principle, available to the holder of a registered U.S. trademark to prevent the importation of such goods. Clearly, border enforcement is normally much more effective than enforcement against goods that have already been dispersed throughout the country.

Section 42[145] of the Lanham Act allows a trademark owner to record its registered mark with Customs to prevent the importation of goods bearing a copy or simulation of the registered mark. It is worth reading s. 42 in its entirety:

> *Except as provided in subsection (d) of section 1526 of Title 19, no article of imported merchandise which shall copy or simulate the name of the any domestic manufacture, or manufacturer, or trader, or of any manufacturer or trader located in any foreign country which, by treaty, convention, or law affords similar privileges to citizens of the United States, or which shall copy or simulate a trademark registered in accordance with the provisions of this chapter or shall bear a name or mark calculated to induce the public to believe that the article is manufactured in the United States, or that it is manufactured in any foreign country or locality other than the country or locality in which it is in fact manufactured, shall be admitted to entry at any customhouse of the United States; and, in order to aid the officers of the customs in enforcing this prohibition, any domestic manufacturer or trader, and any foreign manufacturer or trader, who is entitled under the provisions of a treaty, convention, declaration, or agreement between the United States and any foreign country to the advantages afforded by law to citizens of the United States in respect to trade-marks and commercial names, may require his name and residence, and the name of the locality in which his goods are manufactured, and a copy of the certificate of registration of his trademark, issued in accordance with the provisions of this chapter, to be recorded in books which shall be kept for this purpose in the Department of the Treasury, under such regulations as the Secretary of the Treasury shall prescribe, and may furnish to the Department facsimiles of his name, the name of the locality in which his goods are manufactured, or of his registered trademark, and thereupon the Secretary of the Treasury shall cause one or more copies of the same to be transmitted to each collector or other proper officer of customs.*

This provision is, for the most part, similar to section 526 of the Tariff Act and Customs regulations made pursuant thereto.

Under section 526 of the U.S. Tariff Act the United States trade-mark owner must be a United States domiciliary. A plaintiff that is the owner of a United States registration, if domiciled in the United States, will normally seek relief under both section 42 of the Lanham Act and section 526 of the Tariff Act.

Section 526 essentially states that it is unlawful to import merchandise manufactured outside the United States bearing a trade-mark **owned** by a U.S. citizen or corporation unless the goods fall within **exemptions** set out by regulation or are specifically listed as exempt goods in the Federal Register. It is important to note that, pursuant to section 526(d), goods exempted under the regulations pursuant thereto are also exempted from the application of section 42 of the Lanham Act.

Section 526(a) of the U.S. Tariff Act 1930 [146] provides:

Merchandise bearing American trademark

(a) Importation prohibited

> *Except as provided in subsection (d) of this section, it shall be unlawful to import into the United States any merchandise of foreign manufacture if such merchandise, or the label, sign, print, package, wrapper, or receptacle, bears a trademark* ***owned*** *by a citizen of, or by a corporation or association created or organized within, the United States, and registered in the Patent and Trademark Office by a person*

> *domiciled in the United States, under the provisions of sections 81 to 109 of Title 15, and if a copy of the certificate of registration of such trademark is filed with the Secretary of the Treasury, in the manner provided in section 106 of said Title 15, unless written consent of the owner of such trademark is produced at the time of making entry.*
>
> (emphasis added)

The plain language of section 526 gives the United States trademark owner the absolute right to prohibit all imports bearing its trademark. On the other hand 19 CFR 133.21 allows a number of exemptions including:

> *s. 133.21 (c) Restrictions not applicable.*
>
> *The restrictions set forth in paragraphs (a) and (b) of this section do not apply to imported articles when:*
>
> *(1) Both the foreign and the U.S. trademark or trade name are owned by the same person or business entity;*
>
> *(2) The foreign and domestic trademark or trade name owners are parent and subsidiary companies or are otherwise subject to common ownership or control*

The meaning of "owned" and the scope of the exemptions under s. 526 had been dealt with in a number of conflicting cases brought by several trademark owners, including Cartier, Vivitar, and Olympus. Accordingly, an organization of trade-mark owners called the Coalition to Preserve the Integrity of American Trademarks (COPIAT) sought a declaratory judgment that Customs must exclude all imports bearing the plaintiff owners' trademarks entering the United States without the consent of the plaintiffs.

The U.S. Supreme Court chose COPIAT and two related cases[147] to resolve the issue. Two renowned retailers, 47th Street photo and K Mart intervened as defendants. The Appeals Court had reversed[148] the Circuit Court decision[149] which upheld the regulations stating:

> *The construction of section 526 of the Tariff Act by the Customs Service, as embodied in the challenged regulations, is sufficiently reasonable. This construction is supported by the legislative history, judicial decisions, legislative acquiescence, and the long-standing consistent policy of the Customs Service. The regulations clearly implement the limited purpose for which section 526 was enacted and are consistent with and effectuate the intent of Congress to permit entry of trademarked goods not involving the Katzel situation.*[150]

Justice Kennedy of the Supreme Court of the United States in its reasoning divided grey marketing into three categories:

> *The gray market arises in any of three general contexts. The prototypical gray-market victim (case 1) is a domestic firm that purchases from an independent foreign firm the rights to register and use the latter's trademark as a U.S. trademark and to sell its foreign-manufactured products here. Especially where the foreign firm has already registered the trademark in the United States or where the product has already earned a reputation for quality, the right to use that trademark can be very valuable. If the foreign manufacturer could import the trademarked goods and distribute them here, despite having sold the trademark to a domestic firm, the domestic firm would be forced into sharp intrabrand competition involving the very trademark it purchased. Similar intrabrand competition could arise if the foreign manufacturer markets its wares outside the United States, as is often the case, and a third party who purchases them abroad could legally import them. In either event, the parallel importation, if permitted to proceed, would create a gray market that could jeopardize the trademark holder's investment.*
>
> *The second context (case 2) is a situation in which a domestic firm registers the U.S. trademark for goods*

> *that are manufactured abroad by an affiliated manufacturer. In its most common variation (case 2a), a foreign firm wishes to control distribution of its wares in this country by incorporating a subsidiary here. The subsidiary then registers under its own name (or the manufacturer assigns to the subsidiary's name) a U.S. trademark that is identical to its parent's foreign trademark. The parallel importation by a third party who buys the goods abroad (or conceivably even by the affiliated foreign manufacturer itself) creates a gray market. Two other variations on this theme occur when an American-based firm establishes abroad a manufacturing subsidiary corporation (case 2b) or its own unincorporated manufacturing division (case 2c) to produce its U.S. trademarked goods, and then imports them for domestic distribution. If the trademark holder or its foreign subsidiary sells the trademarked goods abroad, the parallel importation of the goods competes on the gray market with the holder's domestic sales.*
>
> *In the third context (case 3), the domestic holder of a U.S. trademark authorizes an independent foreign manufacturer to use it. Usually the holder sells to the foreign manufacturer an exclusive right to use the trademark in a particular foreign location, but conditions the right on the foreign manufacturer's promise not to import its trademarked goods into the United States. Once again, if the foreign manufacturer or a third party imports into the United States, the foreign-manufactured goods will compete on the gray market with the holder's domestic goods.* [151]

The majority of the court, as reflected in Justice Kennedy's opinion, held as follows with respect to the three case scenario outlined above:

> *All Members of the Court are in agreement that the agency may interpret the statute to bar importation of gray-market goods in what we have denoted case 1 and to permit the imports under case 2a. ..... As these writings state, "owned by" is sufficiently ambiguous, in the context of the statute, that it applies to situations involving a foreign parent, which is case*

> *2a. This ambiguity arises from the inability to discern, from the statutory language, which of the two entities involved in case 2a can be said to "own" the U.S. trademark if, as in some instances, the domestic subsidiary is wholly owned by its foreign parent. A further statutory ambiguity contained in the phrase "merchandise of foreign manufacture," suffices to sustain the regulations as they apply to cases 2b and 2c. This ambiguity parallels that of "owned by," which sustained case 2a, because it is possible to interpret "merchandise of foreign manufacture" to mean (1) goods manufactured in a foreign country, (2) goods manufactured by a foreign company, or (3) goods manufactured in a foreign country by a foreign company. Given the imprecision in the statute, the agency is entitled to choose any reasonable definition and to interpret the statute to say that goods manufactured by a foreign subsidiary or division of a domestic company are not goods "of foreign manufacture."* [152]

The basis of the court's majority opinion is that any ambiguity in the words "owned by" should be resolved in favour of allowing the importation of goods originating from a foreign parent or a foreign subsidiary of the U.S. plaintiff. As well, the ambiguity of the words "foreign manufacture" sustains the regulations in cases 2 (b) and 2 (c) so as to allow importation in those instances (see above).

As this decision clearly demonstrates, the issue has become highly technical and dependent on corporate structuring and intellectual property portfolio management - more analogous to tax jurisprudence than intellectual property.

The judgment is exceptionally complex. Justice Brennan and Justice Scalia each wrote separate decisions in which they partly concur and partly dissent. A detailed analysis of this decision is entirely beyond the scope of this work.[153]

However, the decision does provide at least some guidance to both trade-mark owners and importers who require some certainty in their planning. Although the decision may raise as many questions if not more than it answers, it provides far more certainty than we have in Canadian law. From an overall policy standpoint, it clearly favours the concept of parallel imports to a great extent.

The COPIAT decision has been much scrutinized by those of all views on grey marketing in the U.S.A. *"Unfortunately, the case was decided on narrow technical grounds. The Court did not address the intellectual property or consumer issues surrounding the gray market and left the gray market situation just as unclear as it had been before the decision."* [154] Many commentators in the U.S.A. are calling for legislation to deal with this issue. [155] One such attempt was Bill S. 626 in 1990.[156]

There has been no shortage of jurisprudence since the COPIAT decision in the U.S.A. Evidently, there is little satisfaction amongst some litigants with the state of the law. However, the appellate courts are not apparently eager to clarify it, much less to change it.

For example, in Lever Brothers v. United States[157], the Court of Appeals for the District of Columbia held in principle that importation of goods that are physically different but bear an identical trade-mark can be barred by Customs, even if originating from an affiliated company. However, the court stopped just short of granting relief to Lever Brothers:

We think the natural, virtually inevitable reading of s

42 is that it bars foreign goods bearing a trademark identical to a valid U.S. trademark but physically different, regardless of the trademarks' genuine character abroad or affiliation between the producing firms. On its face the section appears to aim at deceit and consumer confusion; when identical trademarks have acquired different meanings in different countries, one who imports the foreign version to sell it under that trademark will (in the absence of some specially differentiating feature) cause the confusion Congress sought to avoid. The fact of affiliation between the producers in no way reduces the probability of that confusion; it is certainly not a constructive consent to the importation. The cases are entirely congruent with this view. Customs' assertion of administrative difficulties appears overdrawn, and in any event would seem to justify no more than inaction in those cases that are close on the factual issue of product identity. Thus, despite the deference we owe Customs under Chevron, we believe that the affiliate exception does not square with s 42.

For now, however, our conclusion must remain provisional. Neither party has briefed the legislative history nor administrative practice in any detail.[158]

As this work is being completed, a potentially very significant decision has been handed down by the Judge Greene of the District Court of the District of Columbia on April 15, 1992, further to the previously mentioned appellate judgment. Judge Greene held that:

Neither the legislative history of the statute nor the administrative practice of the Customs Service clearly contradicts the plain meaning of section 42. The Court therefore concludes that section 42 of the Lanham Act prohibits the importation of foreign goods that bear a trademark identical to a valid United States trademark but which are physically different, regardless of the validity of the foreign trademark or the existence of an affiliation between the U.S. and foreign markholders.[159]

This appears to mean that the U.S. Customs Service cannot apply its "affiliate exception" to block imports of foreign goods that bear a trademark identical to a valid U.S. trademark but which are materially, physically different. Thus, related company goods that are materially different can be blocked by U.S. Customs. In fact, U.S. Customs Service, on June 26, 1992, has issued a notice inviting requests for such orders, noting that Judge Greene's order is under appeal and the new practice is thus temporary.[160]

This is a potentially major development that could erode, if not undo, the result of the COPIAT decision of the U.S. Supreme Court, discussed above. It is, of course, a similar result to that of the recent Heinz decision in Canada, discussed at length in the previous chapter. At the time of writing, it is too early to assess fully the impact of Judge Greene's ruling, other than to predict that the issue must once again be dealt with by the U.S. Supreme Court or by definitive legislation.

A few weeks before the 1991 appellate decision in Lever Brothers decision discussed above, the Court of Appeals for the Third Circuit in the case of Weil Ceramics v. Bernard Dash [161] declined to prohibit importation where their goods were purchased abroad from the parent of the U.S. rights holder. The trial court had not made any finding that the goods were materially different and this was relevant on appeal.[162] This point was also expressly cited by the Court in the Lever Brothers case.[163]

Finally, there is an important appellate judgment in Yamaha v. United States.[164] This judgment is mostly about "issue preclusion" or "collateral estoppel" -- i.e. whether or not the law is settled. The D.C. Circuit believes that it is. [165] After inconclusive discussion of the "physical differences" doctrine, the court offered some interesting policy commentary about Yamaha's marketing strategy:

> *But if Yamaha-America is undersold by the gray market, it is because its own parent has chosen to sell the same goods abroad at a lower cost. It is true that the decision not to issue a genuine goods exclusion order has an impact on Yamaha-America's ability completely to control the market, but ABC determined that Yamaha-America has no right to such control. Yamaha-America is precluded from rearguing this same issue in the guise of a takings claim.*[166]

Yamaha is also seeking certiorari in another grey marketing matter to the U.S. Supreme Court.[167]

COPYRIGHT

The law in the U.S.A. with respect to the parallel importation of copyrighted works is even more ambiguous. On the one hand, the U.S. Copyright Act[168] contains provisions that purport to grant rights and bar imports (ss. 106 and 602).[169] On the other hand, there is a statutory statement of the "first sale doctrine" (roughly equivalent to exhaustion but normally used in the domestic context) in s. 109 of the U.S. Copyright Act.[170]

There is authority that parallel imports of books purchased abroad wholesale can be stopped.[171] Moreover, there is also authority that parallel imports of records can be prevented because the first sale doctrine was held to apply only to domestically produced records.[172]

However, an important case that needs to be considered in the present context, and one of the highest and most recent authorities, is that of Sebastian International v. Consumer Contacts[173] This case concerned an attempt by a manufacturer of personal care products to prevent the parallel importation of those products. The plaintiff relied upon copyright in the labels on the products, since the labels had been printed by the plaintiff in the U.S.A. and sold in the U.S.A..

The Court's judgment belies a certain scepticism about the nature of this lawsuit:[174]

> *This case comes to us in the guise of an alleged copyright infringement but, in reality, is an attempt by a domestic manufacturer to prevent the* ***importation*** *of its own products by the "gray market." We conclude that, having sold its goods with copyrighted labels to foreign distributors, the manufacturer is barred by the FIRST SALE doctrine from establishing infringement through an unauthorized importation. Consequently, we will vacate a preliminary injunction enjoining defendants from distributing within the United States, products that plaintiff had manufactured in this country and then exported.*

(emphasis added)

The Court considers at some length the legislative history and purpose of the importation provisions, the decisions in CBS v. Scorpio[175] (although not binding on the Sebastian court) and finds, after concluding that the copyright owner does not require additional reward beyond that of the first sale, that the provisions must be so read as to conclude that "a first sale by the copyright owner extinguishes any right later to control importation of those copies."[176]

Finally, and as an object lesson to policy makers, the Court states bluntly:

> *Because contractual remedies have proved inadequate, see Johnson & Johnson Products v. DAL Int'l Trading Co., 798 F.2d 100 (3d Cir.1986), domestic manufacturers now invoke the copyright law to advance their economic interests. This twist has created the anomalous situation in which the dispute at hand superficially targets a product's label, but in reality rages over the product itself. We think that the controversy over "gray market" goods, or "parallel importing," should be resolved directly on its merits by Congress, not by judicial extension of the Copyright Act's limited monopoly.* [177]

Congress was thus explicitly invited to intervene. This case was followed in another frequently cited judgment involving copyright in labels and computer programs. See Red-Barron v. Taito.[178]

Thus, as in the case of patents and trade-marks, it appears that actual U.S. law is not nearly so inimical to parallel importation and is far more ambiguous with respect to this subject than many U.S. based interests would wish one to believe.

Those in Canada who may wish to point out inconsistencies in U.S. foreign and trade policy with respect to the exhaustion issue should be aware of the Duracell[179] matter. In the early 1980's, Duracell Inc., one of the world's two main manufactures of alkaline batteries for the consumer market, went to great and mostly unsuccessful lengths to prevent the grey marketing of their products. This effort included litigation and lobbying for both enforcement and legislation. One of the most notable examples of litigation involved a proceeding in the

U.S.A. against a Canadian enterprise that specialized in grey marketing.

Duracell used the aegis of the U.S. International Trade Commission ("ITC") to stop the activities of one Dr. Mark Nussbaum, a Canadian dentist and celebrated grey marketeer who was bringing Duracell batteries from Belgium into the U.S.A. at a considerable saving to consumers. The ITC rendered an extensive and learned opinion under the notorious s. 337 of the Trade and Tariff Act in which it found that injury (one of its statutory requirements) must be tested as against the domestic entity rather than the multinational enterprise as a whole and found in favour of Duracell. [180] Dr. Nussbaum successfully appealed, pursuant to the statute, to the President of the United States (Ronald Reagan at that time) and he won.[181] The extraordinary nature of the appeal procedure in this type of case clearly shows that Congress views matters such as this as very important to U.S. policy. Duracell attempted to overturn the decision of the President in the courts and they lost.[182] The Court's review of the matter is replete with references to its finding that the President had, pursuant to the requirements of 19 USC 1337, overturned the finding of the ITC "for policy reasons".[183] Thus, President Reagan's policy finding that favoured parallel imports into the U.S.A. from a Canadian grey marketeer of products made by an American multinational was upheld.

This is a useful decision to cite to those representing American interests who claim that strict market segmentation is a sound policy. It is common wisdom that President Reagan was responsible in large part for the incorporation, for a time, of the "Chicago School" of antitrust analysis -- the "New Learning" -- into U.S. government policy. If President Reagan -- the ultimate exponent of "laissez faire" -- favoured exhaustion, then one cannot but wonder why there has been an apparent reversal in

U.S. policy since then. Or, is the reversal primarily intended for the perception of foreign countries such as Canada? It is possible that the U.S.A. prefers to maintain a relatively high degree of exhaustion in its domestic forum for purposes of competition, efficiency and consumer choice, but wishes its trading partners to provide clear market segmentation.

PART "B" -- THE EC

In essence, there is almost complete exhaustion within the European Community with respect to any goods put on the market inside or imported into the Community by or with the consent of the intellectual property right holder. There are only a few clear qualifications to this principle. One is that legitimate goods originating from abroad can be denied importation into the EC.[184] However, it is to be noted that the EC rules only set forth minimum standards with respect to exhaustion.[185] Another is that goods produced under a compulsory license cannot be imported into a country that does not have such a license.[186] The situation of goods bearing a trade-mark having a "common origin", where the goodwill is now separate, is in a state of some evolution at the present time.[187] Thirty years of Treaty of Rome case law that supports the exhaustion principle has, to a large extent, been codified in a Council directive relating to trade-marks law.[188]

As will presently be seen, the EC (viewed as a unit) probably has a stronger basis to exclude genuine goods from outside the Community than do either the U.S. or Canada, but there is almost complete exhaustion with respect to the flow of goods inside the Community. This state of affairs has come to pass over the past thirty years by virtue of decisions of the European Court of Justice (E.C.J) that interpreted broad pro-competition principles in the Treaty of Rome. These provisions are essentially those of Articles 30 - 36 (quantitative restrictions), Article 85 (illegal agreements) and Article 86 (abuse of dominance). See Appendix VII for the text of these provisions.

Generally, there appears to be satisfaction with this state of play. There is certainly no evidence of any legislative momentum to retreat to the *status quo ante*. Thus, although it can be argued that the developments in Europe were not entirely deliberate on the part of governments, they have nonetheless been welcomed and endorsed by national governments and the European Commission. The incremental nature of those developments was based upon extensive case law and Commission policy that deals explicitly with legal and economic considerations. The acquiescence and sometimes outright design of various governments show that the present policy is a reasoned one overall.

On the one hand, the case law and literature on the subject of exhaustion in the European Community (EC) is so vast and complex that it almost defies analysis.[189] It is certainly beyond the scope of this paper to undertake this analysis in detail.[190] Indeed,this would require several volumes. On the other hand the situation 30 years after the Treaty of Rome and in the year of "1992" is in certain respects extraordinarily simple. It resolves to this.

Generally, the competition provisions of the Treaty of Rome have been so interpreted by the European Court of Justice (E.C.J) as to override any provisions of member state intellectual property laws that would otherwise serve as a barrier to the free movement of goods originating from within the community from one member state to another.

The most decisive factor in all of the decisions of the E.C.J would seem to be the issue of "consent". If the goods were first placed on the market inside the EC or imported into the EC with the consent of the intellectual property claimant, then the right of distribution would seem to be exhausted.[191] Indeed, this distillation of the case law takes into account such disparate situations as goods made under a compulsory license (where no exhaustion is permitted)[192] and would also appear to take into account the recent ruling in Hag II[193], discussed below, which concerned forced divestiture. It is an interesting rule because it appears to work rather well and has the virtue of extraordinary simplicity at the end of the day. This point will be returned to in Chapter IV.

Some claim that this is subject to a recent exception with respect to trade-marked goods originating from separate entities, or a "common origin". This is the situation where trade-marks in different member states were once owned by the same or related entity, but are now owned by completely unrelated companies with no connection by way of relationship or control through licensing. This is referred to as "common origin".

The recent decision in Hag II has called into question the extent of the application of the exhaustion doctrine in the case of trade-marks having a common origin. In this particular instance, the separation of the corporate entities was completely involuntary. It was a consequence of wartime confiscation during World War II in the Benelux countries of the celebrated coffee business of Hag, which was a German company. The current owners of the Belgian trade-mark are completely unrelated to the current German owners and trace their title from the wartime legislation. The divestiture was completely involuntary.

However, the Hag II case has attracted considerable attention because it, in effect, overrules a much earlier important decision involving the same parties, known as Hag I.[194] In Hag I, the Belgian company was unable to prevent the importation of "Café Hag" from Germany into Belgium. Hag II was basically a replay of Hag I, with the German defendant in the former case now the plaintiff, and the successor of the former plaintiff, now the defendant. This time, the German company was trying to keep the Belgian coffee out of Germany. In Hag II, the plaintiff succeeded. The implications of this case are not clear at the time of writing. For example, does the case apply to voluntary separations of goodwill? This author believes that it does not and that the case is limited to its rather special facts. The "consent" of the original owner to the marketing of goods in another country seems to be crucial. Does a voluntary assignment of goodwill, etc. constitute "consent" per se? Hag II may be limited to its fairly unusual facts. However, the dissolution of the "common origin" doctrine may be broader and may mark a reversal in the EC trend. There is very lively debate over this dilemma, which is much too complex to pursue in this study.[195] Moreover, the implications for situations involving assignments by way of bankruptcy and liquidation, and arising when new counties join the EC may not yet be clear.

Generally speaking, the official position, as stated in 1989 by the EC Commission [196] in contemplating "1992" is this:

The following general rules are important to bear in mind when dealing with industrial property rights:

(i) *The principle of free movement of goods. Once goods protected by industrial property rights have been legitimately marketed in Member State A, by the owner or someone authorized by him to do so (for example, a licensee), the importation of those goods into Member State B cannot be prevented on the basis of the parallel property rights existing under the national legislation of Member state B. For example, a manufacturer registers a trademark for his products in each Member State where the products are sold, for example France and Germany. Once the goods in question have been marketed in Germany, the importation of those goods into France cannot be stopped by invoking the same trademark it is registered under in France.*

Of course, where a third party unlawfully uses a registered trademark, the manufacturer can take the necessary steps, but this is a normal case of trademark infringement, not a matter of illegally partitioning of the common market.

(ii) *If an undertaking is in a dominant position in the common market or a substantial part thereof, the improper exploitation of an industrial property right may be in violation of Article 86 (abuse of dominant position). There must, of course, be an actual or potential effect on trade between Member States.*

(iii) *The owner of an industrial property right may decide to confer upon an enterprise the benefit of that right; for example, he may let another firm use his registered trademark, or if he is the owner of a patent, he may confer a license to manufacture and sell the goods to another. In return, the other party will normally be asked to pay a royalty. In itself, such authorization of third party to exploit the patent or any other industrial property right is not caught by Article 85 (1). Problems, may, however, arise when the authorization is accompanied*

> *by clauses which restrict competition without being justified in that they protect the industrial property right.*
>
> *In general the tests for application of Article 85 (1) or exemption under Article 85 (3) are the same in the area of industrial property rights as in other areas.*

The jurisprudence, national legislation and bureaucratic thinking on the interrelationship between intellectual property and competition principles are at a very advanced state in Europe at the present time. The Europeans have clearly accepted the principle that a "common market" means full economic integration[197], based upon vigourous competition and that competition concerns are paramount even over intellectual property rights and national laws when necessary to achieve this objective.

North American policy makers may wish to examine whether the success of the EC and the astonishing prosperity of many of its members in the first three decades is not due, in part at least, to the vigorous interplay of high levels of intellectual property protection and high levels of antitrust enforcement, with the latter having the last word in most cases.

It is to be noted that the free flow of goods within Europe has been achieved notwithstanding a great diversity in national intellectual property laws. This is because there is the political will to ensure the free flow of goods and because the <u>Treaty of Rome</u> overrides national laws to the extent necessary to give it effect, which is probably an essential aspect of a true common market.[198]

Matters for further study in regard to harmonization and the free flow of goods in Europe include Directive 89/104/E.EC on Approximation of Member States' Laws Relating to Trade Marks and the Proposed Regulation on a Community Trade Mark. However, these are beyond the scope of the current exercise.

Interestingly, it seems that Canada and the U.S.A. have not devoted a great deal of effort to learning possible lessons from the Europeans, at least with respect to intellectual property. One respected commentator has put it this way:

> *Initial fears that the provisions of the Community law on competition and the free movement of goods and services might spell the end of national intellectual and industrial property laws have been proved unfounded...Indeed, the solutions achieved by the Community and its Court would appear so well balanced and felicitous that the United States and Canada would do well to adopt them, even if they could not agree upon full economic integration in other respects.*[199]

PART "C" -- RECENT DEVELOPMENTS IN AUSTRALIA

Australia is a jurisdiction that used to be watched very closely by Canadian public policy makers. It shared a common heritage of British law; it has a roughly similar constitution based upon a federal structure[200]; and it holds an influence well beyond that which would be suggested by economic statistics alone. The relationship of Australia and Canada is now diverging. This divergence is beyond the scope of the present enquiry. It may have to do with the *de facto* division of the principal world economic units into European, North American, and East Asian blocs. Clearly , Australia would tend towards the latter and Canada would tend towards the middle group, for obvious geographical and historical reasons.

Australia has recently confronted the issue of exhaustion with respect to books and come to precisely the opposite conclusion as Canada.[201] As was noted in Chapter I, Canada has announced the intention to strengthen its Copyright Act in order to make it more difficult to bring in parallel imports. Australia, on the other hand, has recently decided that the price of books in that country was far too high because it was the victim of price discrimination. Accordingly, it has decided that copyright law provisions were the cause of this price discrimination; and it has amended its copyright law after considerable study, consultation, controversy and debate in such a way that exhaustion will be encouraged, unless, in effect, there is local manufacturing and prompt and effective distribution at world prices.

The new legislation came into effect December 23, 1991.[202] This amendment to their Copyright Act would enable parallel importation of books not first published in Australia (meaning more than 30 days after publication elsewhere) or unavailable for more than 90 days in Australia. The Australian Minister responsible for this rather bold and internationally controversial piece of legislation stated:

> *We belong to a world community, and we are entitled to access, at the earliest possible opportunity, to world literature whether one is talking in terms of cultural, social and recreational reading, or access to textbooks and major publications of intellectual, academic, and scientific significance which would help Australia to become a cleverer and more competitive country internationally.*[203]

In fact, as bold as this seems, there is a suggestion in the book trade literature that the Australian Government is prepared to go even further and extend such measures to sound recordings.[204] The groundwork for possibly similar legislation with respect to sound recordings is laid out in the Report of the Prices Surveillance Authority dated December 14, 1990 which concludes that sound recording prices in Australia were too high and these high prices "have not been used to support any significant development of the local recording industry." It is quite possible that the subject of parallel importation of sound recordings will be dealt with in 1992.[205]

Whether this legislation is consistent with the Berne Convention may be an interesting question.[206] The Berne Convention provides in Article 3 that publication in any Berne country will suffice for full protection to the author and Article 5 provides for full national treatment. Provisions that, in effect, require local manufacturing are no longer tolerated by the Berne Convention. The Australian policy certainly appears to encourage local manufacturing. It does so by requiring that if a work is not first or simultaneously published in Australia, and the copyright owner does not permit parallel importation within 30 days of overseas publication, the copyright in Australia can be lost!

This would also be problematic with respect to the currently proposed GATT TRIPs text (Article 9), which incorporates by reference the aforesaid articles of the Berne Convention.

PART "D" -- TREATY DEVELOPMENTS: GATT, WIPO, NAFTA, and FTA

GATT TEXT:

The following is a brief analysis current to December 20, 1991 concerning the proposed GATT TRIPs text put forth by Arthur Dunkel on December 20, 1991. This is the latest official document publicly available.

Article 6 provides, essentially, that the TRIPs agreement does not apply to exhaustion but that a country is free to retaliate against another if it does not like the latter's laws regarding exhaustion, such retaliation being outside of the scope of the GATT agreement. This is reinforced by the reference in the patent section, article 28.1

Article 6 states:

Exhaustion: For the purposes of dispute settlement under this Agreement, subject to the provisions of article 3 and 4 above nothing in this Agreement shall be used to address the issue of the exhaustion of intellectual property rights.

Articles 3 and 4 refer to National Treatment and Most Favoured Nations provisions, respectively. Article 28.1 refers to the patent right of importation and contains a footnote cross-referencing this right to Article 6 provisions.

NAFTA:

At the time of writing, the official Canadian Government policy is to keep the NAFTA text secret. However, one might surmise, for reasons mentioned elsewhere in this work, that Mexico would tend to favour exhaustion and the U.S. would tend to oppose it. On this assumption, the following is noted.

ANALYSIS OF GATT AND NAFTA POSITIONS:

GATT:

The virtue of the GATT Dunkel text with respect to exhaustion is that it leaves open the possibility for particular countries to enact or utilize exhaustion doctrines without fear of sanctions per se under the GATT. On the other hand, it would appear to allow countries such as the U.S.A. to retaliate against such measures with reprisals that are, in turn, not necessarily subject to GATT disciplines. Given the U.S. propensity for bilateral actions, whether "legal" or otherwise under the GATT, it can only be assumed that the U.S. may react with reprisals against countries choosing to go the exhaustion route. Thus, in this author's view, the proposed GATT text is not really neutral about exhaustion. It is potentially opposed to it, because it leaves countries that espouse it very vulnerable to bilateral pressure.

On the other hand, it is likely unthinkable that the U.S.A. would agree to endorse the principle of exhaustion within GATT, broadly speaking. They are actively fighting it on the patent front in the Patent Law Harmonization effort in WIPO as well.

A reasonable possibility for compromise would be a recognition that the U.S. does practice a certain degree of exhaustion as matters presently stand, especially under trade-marks and copyright law, and that such a degree of exhaustion should be open to any countries without fear of bilateral reprisal. This would involve drafting a rule that keeps in harmony with, perhaps with some minor modifications, the rule in the Copiat case and the various copyright cases, such as Sebastian and Red Barron (supra).

Another compromise position would entail a rule that exhaustion may apply, at the option of any member state, with respect to goods emanating from a company related to that which seeks to enforce the domestic right but not when the relevant level of protection in the country of origin of the goods is substantially lower than in the country of destination (i.e. produced under a compulsory license) or from a country outside of the GATT agreement. This is roughly the situation within the EC.

This option should be unobjectionable, in principle, since the GATT TRIPs provisions are designed to ensure relatively high and uniform levels of protection within the GATT. Any objections to this principle must be viewed with serious suspicion as to the real motives, in all probability that of market segmentation. However, since the GATT exercise is clearly a long way from the type of free trade that exists within the EC, this option is probably not likely to achieve significant consensus at this time.

It should also be remembered that the EC and U.S. -- especially the former with its larger internal market -- have economies of scale and buying power that enable them to purchase goods at world prices and ensure free flow of those goods within their own borders. Thus, they are both in a position to strive for market segmentation by other countries, while enjoying the best of both possible worlds themselves, i.e. lowest world prices for importation and market segmentation for exports.

Thus, the options for Canada with respect to the GATT (assuming that there is any room to negotiate) are as follows:

I. Sign the present text.

II. Insist on exhaustion being purely a domestic consideration, without any possibility of reprisals. (not likely of success).

III. Insist that current mid-ground of exhaustion as defined by U.S. and European law be the rule within the GATT (possible and reasonable compromise).

In any case, it should be noted that market segmentation is something that the U.S.A. wants to see in other countries such as Canada. In the language of trade negotiators, it is something that they are probably willing to "pay for". Therefore, if countries such as Canada are willing to accept market segmentation, such a regime must clearly be in our national interest, or bargained away only for something that is actually and clearly worth the cost.

NAFTA

On the assumption that the U.S.A. will generally oppose exhaustion and the Mexicans will espouse it, the main options in the NAFTA context are:

I. Complete Exhaustion (EC Style) within North America.

II. Freedom of NAFTA members to enact exhaustion as a matter of national legislation without possibility of reprisal.

III. Freedom to enact exhaustion as a matter of national legislation, but subject to reprisal.

IV. A prohibition on exhaustion.

Note that the above options do not differentiate as between patent, trade-mark and copyright. Variations might include a cultural exemption for copyright. Nonetheless, these are the major principles available as options. These principles would apply to goods first put on the market from within North America or imported into North America with the consent of the rights owner. Refinements could be made, such as a related company exemption for trade-mark goods (i.e. full exhaustion for goods coming from related companies), and strong market segmentation with respect to books but **only** books.

CHAPTER III ANALYTICAL PERSPECTIVES

The controversy over exhaustion arises because many intellectual property rights owners wish to use their rights so as to effect international market segmentation. Such a practice entails the creation of separate markets according to national boundaries. While such activity may be based upon benign intentions in some cases (as discussed below), the real reason is often rooted in a desire to price discriminate. In plain language, the intellectual property right owner may wish to charge what the local market will bear. In its most extended form, market segmentation can prevent the importation of goods into a country when those goods are absolutely identical in all respects to those for which the intellectual property owner or even licensee claims a right in that country and the goods were made by the same intellectual property rights owner, or a related company. In fact, the goods might even have been originally made in the country where importation is sought, having earlier been exported. The problem would arise when a third party seeks to re-import them.[207]

The controversy, for better or worse, has become something of a lightning rod for larger issues that have to do with the very purpose of intellectual property law and international trade. The controversy is exacerbated by the fact that some multinationals are inconsistent or ambiguous in their own attitude.[208] Even some of the most balanced and scholarly of writers on this subject tend to view it in a normative manner; that is, they examine the state of the law from the perspective of what they believe that the state of the law ought to be. The very same Seiko watch can be "legitimate" in one lawyer's eyes and little better than a counterfeit in another lawyer's view. For example, one of Canada's most highly respected scholars in intellectual property characterizes the controversy as follows, in a manner that tends to suggest a particular point of view:

> *Controversy arises when imported goods have been made or acquired abroad by* ***freeloaders*** *who seek by importation to* ***cash in on the creativity and investment of others****. ....The argument is made by some that an article legitimately sold abroad should be free to travel anywhere, in the interest of encouraging competition aud the production of goods in the most economic location, particularly when someone who seeks to restrain the importation has allowed the article to be sold abroad and has presumably benefitted in some way from the original sale.* ***This rather utopian idea might have greater appeal if all countries would eliminate trade barriers -- but that will be the day!*** [209] (emphasis added)

The grey market issue was estimated to be worth $7 to $10 billion dollars a year in the U.S.A. alone in 1988. At that time, the writers of an often cited article in the Harvard Business Review did not know whether to characterize this as a problem or an opportunity. It was noted in the article that many companies were very ambivalent about the issue.[210] It is probably the case that there is a far greater dollar value to this figure than may be evident, because of the nature of the economic "demonstration effect", namely that many firms will order their affairs to conform with the perceived states of the law based upon reported examples. Their behaviour will, however, not be easily captured in statistics.

Why would an intellectual property rights owner wish to effect market segmentation? The answers can be complex and varied, or sometimes quite simple. The motives can include apparently legitimate ones ranging from consumer protection, regulatory compliance, and a desire to sustain local manufacturing on the one hand. On the other hand, the motive can be a thinly veiled attempt at resale price maintenance, international price discrimination, and interbrand horizontal collusion. The range of debate is very intense. Some will say that the former apparently legitimate concerns are not valid, and that "laissez-faire" principles would dictate that consumers can make informed choices, so long as there is no actual deception and no attempt to circumvent valid safety regulations. On the other hand, some will say that even the latter goals which would result in significant imposition of vertical and even horizontal restraints are entirely justifiable and even efficiency enhancing from an economic standpoint.

Free trade is said to be in pursuit of the goal of the elimination of barriers to trade in goods and services in order to promote economic efficiency through international competitiveness.[211] It is important to realize that one highly effective impediment to the achievement of this goal may lie in the actual or potential exercise of certain intellectual property rights that enable the control of importation of genuine goods. These rights are privately held and their exercise is, essentially, beyond the control of government policy makers.

There is a strong trend in North America to use intellectual property rights as a "private tariff" to segment markets for various purposes. Businesses will seek to avail themselves of such private tariffs, if traditional public tariff and non-tariff barriers are reduced or eliminated.[212]

The are significant differences between this type of intellectual property "private tariff" and traditional tariffs. In the case of the use of an intellectual property right to control importation, the rights owner can either bar importation or directly or otherwise[213] collect a royalty for the privilege of importing. With a traditional tariff, the revenues raised by the tariff go directly to the state. The economic benefit to the protected industry consists of increased revenues from sales that would otherwise be lost to foreign competitor. The other main difference is that there is virtually no capacity of the state to start, stop, raise, lower, adjust, or eliminate the "private tariff" in the public interest. Thus, the government could arguably lose control over a very important aspect -- some would be more blunt and call it a barrier -- in relation to international trade. Moreover, it is a barrier that can be invoked, in principle at least, from abroad and against Canada's interest.

This is not a new issue. It dates back to the nineteenth century in Canada and elsewhere. What is new is the awareness that this issue strikes at the very root of free trade, common market theory, competition law and competitiveness doctrines, and consumer protection doctrines.

The exhaustion issue cuts a broad path across several disciplines, quite apart from intellectual property law. These are mainly the fields of **competition policy, trade law, marketing law, consumer law, and both micro and macro economics**. Of course, all of these fields are in turn interrelated. This study cannot pursue all of these lines of inquiry, because such an analysis of the exhaustion issue would require several book-length studies to detail all of the ramifications.

Rather, the author will assess some of the observations in the previous chapters about the state of the law in light of policy goals of these various related disciplines. It should be stated at the outset that there is no clear answer to the problem of exhaustion, other than that it is an understated issue in Canada and North America. It is the author's belief that, in all probability, both the private and public sector in North America have failed to consider all of the ramifications of the issue.

The most important debate and tension probably exists between those who espouse an intellectual property viewpoint on the one hand and those who espouse a competition policy viewpoint on the other. Traditionally, these perspectives were diverging. This was based upon the apparently simple notion that intellectual property constituted a degree of monopoly and competition authorities were mandated to control excessive monopoly.

However, the debate is now considerably complicated by the fact that there are sharply diverging views within each discipline that tend to embrace positions traditionally held by proponents of the other perspective. Generally, those who believe that intellectual property laws should primarily serve the interests of the owners (which is not necessarily the same as that of the creators) of intellectual property do not like the exhaustion doctrine. They prefer the notion of market segmentation. On the other hand, those who believe that intellectual property law entails a balance of conflicting interests tend to favour the exhaustion doctrine. There is, in turn, a similar debate with respect to the correct perspective of competition policy on the issue. And, in turn, there is a debate as to the proper mode of interplay between intellectual property and competition laws. Should the latter act as a discipline on the former? Or, if the former set of laws is inherently balanced, is any discipline necessary? On the other extreme, should we have powerful market segmentation oriented intellectual property laws with no discipline or meddling whatsoever by competition authorities, except in egregious cases? All of these possibilities have articulate defenders.

The following analysis does not purport to definitively answer these questions. Rather, it will examine each perspective separately in order to see where it leads, and will attempt to synthesize the results.

A. Intellectual Property Perspective

The correct intellectual property perspective from which to examine the exhaustion issue is far from settled.

For example, Horner begins his book on the subject of parallel importation in Europe with a discussion of why such a practice occurs, and the first case he cites is that of Distillers v. Commission (1980)[214] which concerned an attempt by Distillers to prevent the parallel importation of their whisky within Europe in order to achieve price discrimination.[215] A constant theme in his work is that of the antitrust aspect to the exhaustion issue. He devotes an entire chapter to the linkage.

Likewise, Lippner, author of a book on parallel imports under U.S. law also has a chapter on antitrust law enigmatically entitled "Antitrust and the Gray Market: An Issue Lost but not Forgotten".[216] He states that, despite the recent easing of antitrust enforcement in the U.S.A. (which has probably reversed in direction since he published his book), "*... the development of gray market law and the development of antitrust law are inextricably intertwined, and consideration of the former requires an understanding of the latter.*"[217]

Those who view intellectual property rights as derived from "natural law" and as a tool to achieve maximum exploitation of the underlying subject matter tend to view the exhaustion doctrine as a diminishment, if not a confiscation, of what is otherwise their property.[218] On the other extreme, those who see intellectual property law purely as an indulgence by the state to grant limited monopolies as a necessary tool in order to provide incentives to invent and create see the exhaustion doctrine as an essential limitation on the power of right owners to earn monopolistic returns. In the middle, there are a large number of rights owners and their advisors who simply do not understand the doctrine. It has been of very little interest in Canada to date except to those directly affected by it in litigation. These parties have tended to be large and sophisticated. However, the recent round of litigation in Canada has taken on somewhat of a "Goliath v. David" aura, with several large multinational food conglomerates suing a relatively small importer who is driven by fundamentalist biblical belief in free trade and vigorous competition.[219]

Moreover, it is quite possible and indeed quite logical to argue that there are different considerations in the various disciplines of intellectual property. For example, patent law has historically been intended in Canada to encourage local manufacturing as a "quid pro quo" of rewarding foreign patentees who have always dominated Canada and hold over 90% of the patents on file in this country. If a product is locally manufactured, there can be some obvious benefit to Canada in permitting the exclusion of parallel imports from abroad. Even if this results in higher prices to consumers, there may be corresponding benefits such as employment, transfer of technology, better service, and Canadian value-added improvements. One could argue that it makes sense to exclude parallel imports even in the absence of local manufacturing. However, this is more of a political and economic argument and will be dealt with below.

At the time of writing, the proposed GATT agreement on intellectual property would effectively bring an end to local manufacturing requirements in Canada and elsewhere, based upon patents at least.[220] Thus, if Canada adheres to this text, the possibility of allowing for market segmentation as a tool in concert with local manufacturing to encourage employment and research and development in Canada would appear to be no longer available in the case of patents. Another justification for market segmentation would need to be found.

In the case of trade-marks, it should be remembered that trade-marks are all about trade. The trade-mark system was meant to prevent counterfeiting, "free-riding" on another's goodwill, and to promote consumer protection and efficiency through identification of the source, and, to a lesser but important extent, protection of the quality of the wares or services and serving the function of a "guarantee".

B. Competition Policy Perspective

The competition policy viewpoint on the exhaustion issue is a moving target in many jurisdictions. The 1980's have featured a marked tendency towards the "Chicago School" of analysis. Some of the tenets of this school are:

* let the market place rule,

* use the rule of reason and case by case approach,

* consider "vertical restraints" with an open mind

as to their effects on efficiency and incentives to invest

* only "naked, horizontal collusion" is wrong

* some types of price discrimination are efficiency enhancing.

In this light, it is not surprising that some commentators in the competition field are not strongly opposed to market segmentation, and even argue in favour of it. In fact, it is not without irony that a recent working paper (that does not reflect official policy) prepared by some officials (Anderson, Khosla, et al) in the Canadian Bureau of Competition Policy actually seems to endorse the principle of market segmentation as being in Canada's interest based upon Chicago School thinking.[221] The reader is referred to this paper for a detailed explanation of the Chicago School of the "New Learning".

However, it must be recognized that the notion of price discrimination -- charging different prices to customers other than for cost-based reasons such as freight or volume discounts -- is very much a factor in the discussion of grey marketing and market segmentation.[222]

There are many arguments that can be mounted against the Chicago School. Herewith are some that pertain to the present discussion and the analysis of the experts in the Bureau of Competition Policy ("BCP") in the above-mentioned paper:

I. ECONOMIC EFFECTS:

The Chicago analysis typically suffers from a fundamental flaw in reasoning. Its apparent premise, which is highly conclusory, is that private restraints and vertical restraints in an international context can actually enhance the competitive and efficient operation of markets in a number of ways. There is little apparent evidence or few examples to support this conclusion.

II. RELEVANT ASPECTS OF EC EXPERIENCE

As is widely known, the EC provides virtually complete exhaustion within the community and a strong measure of segmentation as against the rest of the world. However, what the Khosla, Anderson et al paper does not adequately address is that the policy actually works very well for Europe, that there is no market failure in terms of distribution networks or service, and that there has been no indication that this policy will be reviewed in the foreseeable future. The paper does not analyze how Europe functions with four powerful G-7 countries and nine far weaker economies. The paper does not address the fact that there is a considerable lack of harmonization within Europe as to substantive law. Yet, the policy does work. Where are the analogies to North America? Where are the disanalogies? For example, could a smaller country with no hope of redressing a huge IP imbalance still benefit from exhaustion, because of lower prices and greater efficiency? Clearly most of the European countries would say, "yes".

There is have an interesting recent study by P. Leslie commissioned by and available from the Federal Provincial Relations Office of the Government of Canada that analyzes in some detail possible analogies between the EC and Canada itself in terms of a re-made system of government in this country. Intellectual property is specifically mentioned.[223] There is no published Government study as to whether the EC model might be useful in terms of intellectual property or competition law in the GATT or, particulary, the NAFTA context. Such a study would be very informative.

III. COMPETITION POLICY INTERFACE

The case of Continental v. GTE Sylvania[224] in the U.S.A. is often still cited by the Chicago School for a case by case or, in effect, "laissez-faire" approach. The U.S. is quickly retrenching from its non-enforcement days of the early 80's. For example, note the Borland merger matter referred to below. Canadian analysis at the present time should, arguably, take its cues from the NutraSweet[225] case, and its more interventionist results in terms of vertical restraints involving patents and trade-marks. This is arguably the wave of the future for Canada, not the GTE case.

IV. UNDERLYING ASSUMPTIONS

As discussed elsewhere in this work, the Chicago School approach assumes that there is interbrand price competition in the cases in which market segmentation is advocated. The problem is that there is often probably not full price competition, especially as amongst off-shore suppliers. In fact, there is probably often active collusion. (see the statement of Sir Leon Brittan in Appendix II). Moreover, where such collusion does not actively exist, vertical restraints such as market segmentation may facilitate tacit collusion.[226] Note the comments of Sir Leon Brittan referred to elsewhere in this work (see Appendix II). The assumption of interbrand price competition in goods emanating off-shore (which, by definition, will be the source of most goods wherein grey marketing is an issue) is not justified in all cases; in fact, it may be somewhat naive.

In the author's view, many of the competition economists ignore the potentially most obvious aspect of the exhaustion issue. Companies can and probably frequently do collude in the case of export trade. In fact, many governments, including that of Canada, explicitly sanction such collusion in their domestic laws, while taking as long an extraterritorial reach as possible with respect of foreign activities that impinge on domestic interests. This delicate fencing match or dance has been called one of "lunge, parry and riposte." [227] The relevant provisions that exempt export cartels form the provisions of Canada's <u>Competition Act</u> are included in Appendix VI. [228]

The enforcement level of antitrust or competition law is a cyclical phenomenon (to a great extent in the USA and to a thusfar lesser extent in Canada) that depends upon many complex economic and political factors. The level of enforcement is very germane to this discussion. If there is a lower level of antitrust enforcement, there will likely be a high degree of market segmentation.

It was earlier noted how the U.S. Justice Department successfully prosecuted a conspiracy in the Guerlain matter[229], and later went to some deliberate lengths to undo their victory. There are some significant signs that the level of antitrust enforcement in the U.S.A. and Canada is taking a strong tack back towards vigour with such recent decisions as the following examples which involve intellectual property and related matters.

A very interesting industry realignment phenomenon in the U.S.A. is that of the Borland acquisition of Ashton-Tate. Borland was, initially, something of a David in a field of Goliaths. It has now become a major member of the software establishment. The recent merger may set an important precedent in the involvement of antitrust authorities to prevent the full exercise of otherwise available copyright rights. The facts and the history of this matter are rather complex.[230] In a nutshell, when Borland decided to buy Ashton-Tate, the U.S. Department of Justice became concerned that the two of them held some 60% of the relational data base (e.g. "D-Base") market. Both Ashton-Tate and Borland were involved in some high profile "look and feel" litigation as plaintiff in the case of Ashton-Tate (Ashton-Tate v. Fox) and as defendant in the case of Borland (Lotus v. Borland). Interestingly, the proposed antitrust consent decree which has just been published in the U.S. Federal Register[231] would, among other things, oblige Borland to take certain courses of action in the event of certain outcomes of these lawsuits. But above all, the proposed decree would prevent the full exercise of the copyright rights otherwise available, although it would still recognize copyright in the underlying code, including its structure, sequence and organization.

The significance of this antitrust event has yet to be fully evaluated. It may signal, at the very least, another indication of the reassertion of enforcement of antitrust law in the U.S.A. with respect to intellectual property, and may in some respects go far beyond previous notions of such enforcement. To the best of my knowledge, this is the first time that the antitrust authorities have attempted to limit the assertion of otherwise available copyright rights as a fundamental condition of the approval of a merger. This event may also signify a particular sensitivity on the part of U.S. antitrust authorities to the market for computer software, and how it is affected by intellectual property law.

In Canada, we have the example of the NutraSweet[232] case, mentioned elsewhere, which has held that "levering" a U.S.A. patent in Canada and the overly zealous use of a trade-mark to exact exclusive arrangements can constitute abuse of dominance.

Moreover, a possibly very significant event, although it does not directly involve intellectual property, is the recent Laidlaw decision.[233] In this case, the use of threats with respect to litigation was held to constitute abuse of dominance. The relevance for the present purposes is that some multinationals are quick to "threaten" litigation against grey marketeers, who are usually much smaller entities. There are various degrees of "colour of right" involved in such threats. *Quaere* whether a company that has won a controversial interlocutory decision that is under appeal in a matter such as a grey marketing case should be able to use such a decision to represent the law of the land in threats against small and unsophisticated defendants?

Moreover, one need not look to hypothetical off-shore conspiracies for collusion involving attempts to prevent grey marketing. The notorious Guerlain case in the U.S.A., which was successfully prosecuted, and subsequently vacated at the behest of the Department of Justice, illustrates the sometime propensity of multinationals to conspire in order to price discriminate.[234]

It seems that there is clearly the potential for enormous economic damage to be rendered to an importing country such as Canada if a group of foreign manufacturers were to agree to do their best to prevent parallel imports into Canada with a view to resale price maintenance (See Appendix II). There would be very little practical or legal recourse available to this country in such an event, unless sufficient evidence of the conspiracy can be found in Canada. Even then, either culpable individuals or exigible assets would need to be available within Canadian jurisdiction in order to achieve meaningful enforcement. This would normally be extremely unlikely, since virtually all components of the conspiracy could take place off-shore. The transfer price to Canadian subsidiaries of licensees would be sufficiently high amongst all of the interbrand "competitors" that the object of resale price maintenance at or above a certain level could be achieved even with apparent competition inside Canada, and with no provable "mens rea" on the part of any persons inside Canada sufficient to sustain a conviction under s. 45 of the Competition Act.[235] The only remedy might be to not hand such a cartel the ammunition they need in the form of laws that encourage the market segmentation of Canada.

It is no answer to suggest that Canadian law can deal with the issue of collusion in this context. It has historically been hard enough to prosecute criminal conspiracies in Canada, even where every element and every party is domestic.

For the above reasons, it would be even harder, if not impossible, to deal with foreign cartels.

If and when a proper economic data study is done on this issue, one of the factors that might be studied is the demand elasticity of goods that are subject to grey marketing.[236] Demand elasticity is a measurable economic concept that states to what extent the price of a good can rise without a corresponding drop in demand. Demand is said to be "inelastic" when a given degree of price increase is not matched by an equivalent degree of decrease in demand.[237]

Clearly, efforts at resale price maintenance and price discrimination are likely to focus on goods that are at least somewhat demand inelastic, in economic terms. It would also seem reasonably clear that demand inelasticity is more likely to occur in the case of goods that are more rather than less protected by intellectual property, since the existence of a strong intellectual property right is a major, if not insurmountable barrier to entry for potential competition. This is most obvious and most true in the case of a patent. For example, no one other than The NutraSweet Company can manufacture or import aspartame in the USA, because aspartame is currently protected by a product patent in that jurisdiction. In Canada in 1987 and elsewhere, when the patent expired at or around that date, there were attempts at competition.[238] The NutraSweet case in Canada is a good illustration of how patents and trade-marks can be used as barriers to entry.

In the case of a patent, the barrier can be essentially insurmountable. Even a company such as Kodak, with all of its might and resources, simply could not legally and successfully market an instant film without infringing the immensely successful subsisting pioneer patents held by Polaroid.[239]

In the case of a strong and pioneering patent for a good that is in high demand, there may be little or no interbrand competition. In the case of aspartame, the Canadian Competition Tribunal found that aspartame constituted a separate market for competition purposes; there were no satisfactory substitutes sufficient to negate the Director's position that there was a separate market for aspartame. Thus, while the patent subsisted, there was obviously no interbrand competition in the market for high intensity sweeteners. Even after the patent expired in Canada, aspartame still constituted a separate market because no other satisfactory substitute had yet appeared at the time of the proceedings before the Competition Tribunal.

When there is a separate market in the competition sense for a product, and there is a patent subsisting, there will by definition be no interbrand competition unless the patent owner decides this will be the case. It may be in the patentee's interest to do so, as was vividly illustrated in the famous VHS v. BETA war. Although Sony had the first and by all accounts best patent, they refused, by and large, to license it (with only a few exceptions, such as licenses to Sanyo and Toshiba). The owners of competing VHS patent, which was a close substitute, widely licensed it. The resulting competition and lower prices have resulted in the almost complete demise of the Beta market.

The point with respect to patent protection and price maintenance or price discrimination is simply this. Interbrand competition, which is said to be a safeguard against international price discrimination and resale price maintenance, does not exist in certain markets where a pioneer patent may be in effect. The VHS/Beta case study shows that the owner of a pioneering patent can be disciplined (and perhaps can only be disciplined) by the owner of a patent for a close substitute. To the extent that patent law gives enforceable territorial rights, the patentee would thus, in such a case, have a very high ability and incentive to price discriminate. This does not appear to have been taken into account in Globerman's 1987 study on patent exhaustion in the context of a bilateral FTA.[240] Globerman cites several other factors that tend to mitigate the potential of price discrimination by patentees and concludes his study with the rather enigmatic double negative statement as follows:

> *In summary, the limited available evidence suggests that the absence of exhaustion does not significantly enhance the potential for price discrimination in most industrial sectors.*[241]

In the case of trade-marks, the barrier can be overcome in principle, because the trade-mark does not protect the product as such. It protects only the trade-mark owner's goodwill associated with the product. However, the right conferred by a trade-mark may amount to a high barrier in some cases. The abuse of a trade-mark for the purpose of abuse of a dominant position was also vividly illustrated in the recent Canadian decision involving <u>NutraSweet</u>,[242] which dealt with the giving of substantial rebates to customers of aspartame for use of the NutraSweet logo on packaged goods. This was the so-called "branded ingredient" strategy. It was found by the Competition Tribunal to be a significant barrier to entry to would-be rivals. Another classic example is that of the trademark "Realemon", which has been subject to much antitrust and intellectual property litigation in the U.S.A. and England. The product consisting of concentrated lemon juice is not susceptible of patent protection, but the Borden company has gone to great lengths through the use of their lemon-shaped squeeze bottle to attempt to monopolize the market through trade-mark related means and have recently proven to be successful in the House of Lords.[243]

The doctrine of abuse of dominance plays a particular role from the competition standpoint in an examination of exhaustion.[244] It would seem fairly obvious that a firm will not even bother to attempt market segmentation for price discrimination purposes unless the firm has some market power,[245] at the least, and possibly a dominant position (or colludes with others who in the aggregate have such power). Otherwise, consumers will simply buy substitutes.

For example, suppose that there are a dozen or so manufacturers or high quality widgets of a certain type with worldwide markets. It is tempting to consider examples such as fine watches or cameras. However, such examples must be treated with great care, because the manufacturers tend to come from one country. If Sir Leon Brittan is correct (see Appendix II), such manufactures may indeed be tempted to collude with respect to off-shore markets.

Dominance is an elusive concept in competition law. It is defined somewhat cryptically in s. 79(1)(5) of the Competition Act as existing when *"one or more persons substantially or completely control throughout Canada or any area thereof, a class or species of business"*. A player can come to dominate a market by virtue of its size, barriers to entry, licensing practises, etc. The use of an intellectual property right pursuant only to an intellectual property right is not an abuse of dominance per se.[246] Likewise, "superior competitive performance" is, in effect, a defence to abuse of dominance.[247] Needless to say, these defences were raised but were unsuccessful in the NutraSweet case.

A possible hypothetical example for present purposes might be the market for ball point pens, which in turn comprises several markets ranging from the disposable give-away type of pen to the ultra-luxurious jewelled types of pens sold in luxury boutiques in Geneva and on Fifth Avenue. In any of these markets, there are several manufactures from several countries.

Suppose that there is a market, in industrial economic (i.e. competition law) terms, for gold plated high quality refillable "snob appeal" pens for executives. Suppose that the average selling price of such instruments is about $100. However, an astute Canadian arbitrager finds a container load of these instruments -- enough to supply a major Canadian discount retailer with years' worth of inventory -- in an off-shore location such as Hong Kong. These lower priced pens emanate from several competing grey market sources and are what the economists would call perfect substitutes for each other (i.e. quality, finish, design, "snob appeal", longevity, etc. are all about equal). None of the pens are protected by patents; however, they are all marketed under well-known international trade-marks. Now, if only one of the Canadian intellectual property rights owners seeks to enjoin the importation of these pens, that owner will gain nothing. This is because a competing product which is a perfect substitute in every way will be available at a lower price, and consumers will likely buy it, if they can overcome their distaste at shopping at the discount store (which seems to be more and more the case). Of course, if all of the Canadian rights holders in ball point pen trade-marks decide jointly to seek prohibition of parallel imports, there would be a clear-cut offence under the Competition Act.

But let us change the example. Suppose the market involved is that of professional quality bassoons, the lowest pitched woodwind instrument in the standard symphony orchestra configuration.[248] Suppose that there are only two manufacturers in the world of these instruments at a professional quality level and that one (bassoon maker "A") is by far the preferred choice, and is dominant in any sense of the word. In fact, there is a long waiting list of customers for new "A" bassoons. Bassoon maker "B" exists to service those in a hurry to buy a bassoon, or students on the way up, or professionals on the way down, or those who have had their "A" bassoon stolen. Normally, "A" bassoons are priced twice as high as "B" bassoons. "A" has an extraordinarily valuable trade-mark based upon two hundred years of good will, and has the endorsement of the worlds' top dozen bassoonists. There are no patents involved. Actually, "A" and "B" are more or less indistinguishable in quality. However, because of long standing reputation and the endorsement factor, "A" is dominant in the bassoon market, accounting for 80% of the total sales transactions. There are significant barriers to entry, based upon such matters as having an inventory of 50 year old cured maple ("B" has only a small supply), certain technical expertise, skills, and "know- how." Thus, "A" and "B" bassoons overlap in the market for professional quality bassoons. "A" bassoons normally sell for $10,000 each and "B" bassoons for $5,000 each. Each are imported into Canada by separate and competing Canadian exclusive distributors.

Clearly, either of the exclusive distributors would have an interest in preventing the importation of grey market bassoons involving their own product, and even those of their rival. For example, if "A" bassoons become available for $6,000 each, some of the "B" clientele might move "upscale" in the market, because they can afford an extra $1,000 in some cases, although rarely an extra $5,000. This is because the bassoon industry is clearly an oligopoly with a dominant player, possibly not an uncommon pattern in today's world.

Any serious empirical economic study of the grey market (which has never been done in Canada) should consider the role of dominance in the market. This is difficult because economists do not always agree on when a firm is dominant. In certain cases, such as NutraSweet,[249] where the firm had a 95% market share and was the only firm with a large enough capacity to satisfy major customers' requirements, there was fairly clear dominance. In other cases, it will seldom be so obvious. For this reason, the precedential effect of NutraSweet may be somewhat limited.

In Heinz,[250] it is alleged that Heinz has 70% of the Canadian ketchup market and intuition would suggest that this trade-mark is far better known than that of any of its competitors. Does that constitute dominance? We do not yet know in Canada. No competition issue has been raised on the record in the Heinz case to date. It would seem intuitively obvious that questions of market definition would be much more complex in the case of tabletop ketchup as compared to high intensity sweeteners. There are many condiments available for table top use that are not ketchup at all, such as mustard and relish, and various sauces. For some persons, these are more than acceptable substitutes. This would undoubtedly complicate any attempt at market definition for purposes of Competition Act proceedings.

In Europe, the concept of abuse of dominance goes to the very heart of many of the decisions of the European Court of Justice that have interpreted article 86 of the Treaty of Rome. Related case law also exists in abundance in the U.S.A. with respect to misuse and abuse of patent rights.

If this leads to a different standard of behaviour for large and dominant firms, this is what modern competition law is all about. This is certainly what the Canadian NutraSweet case is about. Had the smaller complainant engaged in such activities as quantity rebates, trade-mark usage rebates, minimum purchase requirements, etc., it would have been viewed merely as aggressive competition.

Finally, it is suggested that many of the examples of attempts to affect and in turn prevent grey marketing may show that the product involved, if not marketed under the umbrella of a very strong patent or a dominant firm holding a well-known trade-mark, will be a product in an oligopolistic market. This is a market that, while not subject to a monopoly, has very few competitors, and a great deal of interdependence, actual and perceived, among them.[251] With few competitors, there is always a danger of conscious parallelism in pricing and less than perfect competition. Classic examples in Canada of oligopoly are the downstream petroleum industry, the airline industry, and the beer industry.

It is very dangerous to speculate on industry analysis in the absence of industrial economic data. It would be most interesting and useful to attempt, based upon publicly filed and available information, to ascertain whether the reported court cases in Canada involving exhaustion tend to involve industries that meet the competition economists' criteria for oligopoly, demand inelasticity, and perhaps even dominance.

Some may say that it is easy to find counter examples, such as the market for watches in the <u>Seiko</u>[252] case. However, although there is no discussion of dominance and very little discussion of resale price maintenance[253] in that case, it could be plausibly argued that Seiko enjoys, or at least did so at the time, an unusual position in the market for mid-priced feature-laden quartz watches that compete with and are a functional substitute for, in terms of fit, finish, and features, their much more expensive Swiss competitors. Seiko is the largest watchmaker in Japan.[254]

This leads to the question of whether there a role for the Director of Investigation and Research in some of these cases. It would seem that the <u>NutraSweet</u> decision may have set a potentially important precedent with respect to the use of intellectual property to effect abuse of dominance, although the facts of that case were unusual (i.e. the 95% market share and the recently expired patent) and not directly related to the present issue.

It might also be noted that the recent decisions in <u>Chrysler</u>[255] and <u>Xerox</u>,[256] while not involving intellectual property per se, did involve parallel dealing of sorts and have been brought, thus far, to sympathetic conclusions along with the <u>Nutrasweet</u> case, pending appeals in these various matters. NutraSweet's appeal has now been abandoned.

In principle, a distributor or retailer could mount an argument that the refusal of a party to supply it on terms comparable with available grey market product could be a reviewable practice under s. 75 of the Competition Act.[257] It is interesting to note that s. 75 contains several indirect references to trade related issues. Note that for some purposes the "market" is not limited. For other purposes, the "market" appears to be confined to Canada. Could an aggrieved distributor or retailer argue that it should be supplied product on North American terms, especially given the existence of a Free Trade Agreement with the USA? If the often cited argument that Canadian retailers are charged higher prices than their American competitors is true, this might be an avenue worthy of pursuit.

However, it should be noted that distributors have an excuse not to deal with cut-price discounters in situations where it can plausibly be argued that service and image are important. This excuse is built into the resale price maintenance provisions of the Competition Act, and it essentially consists of the notion that a supplier need not deal with a retailer that cannot adequately service its product or might compromise its image. The resale price maintenance provisions of the Competition Act contain a host of provisions that could avail a defendant in an action of this type, and there have been few prosecutions recently with respect to the "RPM" offences.[258]

C. Trade Perspective

The tension between "Free Trade" on the one hand and "protectionism" on the other, and the linkage of both doctrines to the exhaustion issue has been noted by others.[259] In a nutshell, the dilemma is simply this. Market segmentation is a type of protectionism. Exhaustion is the ultimate expression of free trade. However, the question is increasingly being asked whether the espousal of the exhaustion doctrine unilaterally by an importing country might not have some efficiency related benefits (which are not necessarily obvious) as well as lower consumer and input prices (which are quite obvious).

More and more, the debate over free trade is realizing that partial free trade is rather reminiscent of the venerable cliché about being half-pregnant. It is an oxymoron and it is not an inherently desirable condition. Protectionism can be justified, as can real free trade. The mid-way state is very problematic. However, it seems to be the best compromise that can be reached to date in North America. Nonetheless, it must not be forgotten for present purposes that the Treaty of Rome allows a far greater degree of exhaustion than does the Canada U.S. Free Trade Agreement.

For example, both the U.S.A. and Japan have, until fairly recently, been very protectionist with respect to intellectual property (Japan still, arguably) and at the same time provided relatively low levels of protection. Both went to some lengths to encourage market segmentation in various ways. The U.S. used intellectual property laws, customs laws, and border measures. The Japanese have used standards, procurement and other means.[260]

Now that both countries are heavy exporters of intellectual property, they find it in their self-interest to encourage other countries to pay as much as possible for U.S. and Japanese exports of intellectual property. They would probably like to see current patterns frozen, since the historical trend has indicated that developing countries will catch up with them, just as the Japanese did with the USA. Korea and India will eventually catch up with Japan, by using cheaper labour and aggressive cross-licensing.

The exhaustion issue is highly sensitive because it challenges the very raison d'être of free trade discussions. The USA, which is the prime "demandeur" of the GATT negotiations, is also the prime opponent on the exhaustion issue. Why could this be?

Until the Punta del Este ministerial meeting which launched the current GATT round, there was very little evident interest on the part of politicians and senior bureaucrats in the connection between international trade and intellectual property. Indeed, there are only "en passant" references to it in the GATT text itself and the leading treatise on the subject of the 1969 Tokyo Round text.[261] However, all that has now changed with the text of the Punta del Este declaration regarding intellectual property, which reads as follows:

> *Negotiating Objective:*
>
> *In order to reduce the distortions and impediments to international trade, and taking into account the need to promote effective and adequate protection of intellectual property rights, and to ensure that measures and procedures to enforce intellectual property rights do not themselves become barriers to legitimate trade, the negotiations shall aim to clarify GATT provisions and elaborate as appropriate new rules and disciplines.*
>
> *Negotiations shall aim to develop a multilateral framework of principles, rules and disciplines dealing with international trade in counterfeit goods, taking into account work already undertaken in the GATT.*
>
> *The negotiations shall be without prejudice to other complementary initiatives that may be taken in the World Intellectual Property Organization and elsewhere to deal with these matters.*

Since these now familiar words were written in 1986, the GATT negotiations overall together with the subset negotiations dealing with intellectual property (known as Trade Related Aspects of Intellectual Property or "TRIPs") have ground, essentially, to a standstill at the time of writing. While the "game" is far from over, it is very difficult to predict what will become of this exercise. At the time of writing, there is very little evidence of any indication that Canada will not accept the "TRIPs" text, unlike the widespread evidence of dissatisfaction with the text that deals with agriculture.

It was recognized at the outset, although the goal became fuzzy as time went on, that intellectual property rights were "not themselves to become barriers to trade". The exhaustion issue was never really on the table in the GATT context, other than in an essentially redundant footnote in certain earlier draft texts. In the latest text, the subject is expressly excluded but in such a way that powerful countries may feel free to retaliate against less powerful countries that espouse exhaustion, under the rubric of the door apparently left open to them by Article 6 of the draft Dunkel Text.

Article 6 of the Dunkel text provides, essentially, that the TRIPs agreement does not apply to exhaustion <u>but</u> that a country is free to retaliate against another if it does not like the latter's laws regarding exhaustion, such retaliation being outside of the scope of the GATT agreement. This is reinforced by the reference in the patent section, article 28.1 Given the U.S.A.'s predilection to bilateral action even in breach of the GATT (i.e. the "s. 337" matter), this clause is potentially worrisome. It might have been better from the viewpoint of countries with less bilateral muscle than the U.S.A if the text had provided that exhaustion is a matter for national legislation, except in certain cases such as integrated circuits where it is required. This would not stop the U.S.A. from encouraging market segmentation on a bilateral basis. It would, however, stop them, in principle, from requiring it by means of bilateral reprisal.

The North American Free Trade Agreement (NAFTA) negotiations provides, at least in theory, an opportunity for a more explicit and bolder result. At the time of writing, the draft NAFTA Text is considered secret by the Canadian Government. One could readily surmise that Mexico will be very interested in the exhaustion issue. The following analysis speculates upon possible Mexican motivations on this issue.

Clearly, Mexico will want to do as much manufacturing as possible and to enjoy the lowest possible consumer and industrial input costs. It will be a long time before Mexico is a net exporter of intellectual property rights. While there already is an incentive for intellectual property rights owners to manufacture in Mexico, due to the low wage costs, there is also a certain disincentive at present to do so because of the grey market "problem", as many manufacturers see it.

The "problem" would occur in the case where the savings realized from lower labour costs may be more than offset by the loss of economic rents associated with price discrimination. This would potentially be the result if the Mexican factory operating under license from a U.S.A. or Canadian intellectual property rights owner were to be permitted to supply the Mexican market at prices that reflect the lower Mexican production costs, and these lower priced goods were to find their way into the U.S.A.

and Canadian market. The manufacturer would thus lose the opportunity to reap economic rents chargeable on account of the more inelastic demand for certain products in Canada and the U.S.A. as compared to Mexico. In other words, a manufacturer might be able to maximize profits in the short term by manufacturing goods in Mexico for a low cost, and selling the articles into separate Canadian and U.S.A. markets at high prices based upon price discrimination. In this scenario, the manufacture might charge relatively high prices in Mexico, knowing full well that some demand would be lost, if only to ensure that there is no arbitrage of those products into Canada and the U.S.A. Clearly, the ideal situation for Mexico in the foreseeable future would be to achieve the maximum production of manufactured goods, which can only occur from the greatest possible demand. Mexico will not directly enjoy the intellectual property royalties to anywhere near the extent of Canada or the U.S.A. that may be achievable from price discrimination within the North American market and the rents that may be achievable in some cases from saved labour costs. Indeed, if there were perfect interbrand competition within North America and no barriers to the free flow of goods, there would be no rents achieved from saved labour costs. They would be "competed away".

It is no complete answer to the above conundrum facing a manufacturer who is contemplating setting up a production facility in Mexico to suggest that, in the absence of strong market segmentation tools, the operation be structured as a branch plant, and that the plant be forbidden from supplying the "export" market from Mexico. In many industries such as electronics and the sound recording business, branch plants and distributors of MNEs are notoriously competitive with each other and will not hesitate to service export markets.[262] Moreover, there may be Mexican antitrust laws that would interfere with such planning, but that is beyond the scope of this paper. Thus, the logical Mexican goal of maximum unit production at lowest cost can only be achieved, from their point of view, in a no-barrier and truly "free trade" zone comparable to the EC. On the other hand, the U.S.A. might want to actually toughen intellectual property barriers to this free flow, in order to ensure that the relatively inelastic demand in the U.S.A. and Canada is not weakened by a Mexican-generated supply of cheaper grey market goods.

Of course, an argument could be made that market segmentation within North America might benefit Mexico in the sense that it would be an incentive for U.S. firms to promote manufacturing in Mexico, based upon the vertical restraints that would facilitate a segmented and profit-maximized marketing approach to North America. Acceptance of this point of view really requires acceptance of the "less is more" aspect of Chicago School thinking, discussed previously in this chapter.

The real crux of the exhaustion issue from the Mexican standpoint as it relates to a North America Free Trade Agreement might ultimately resolve to this. If barriers are reduced and manufacturing shifts to Mexico, there will be potentially enormous cost savings to U.S.A. and Canadian based manufactures in certain sectors. Mexico will want to share the results of increased efficiency, welfare and potential economic surplus. Mexico will want to do so in a more substantial manner than simply seeing an increase in low wage factory employment. Whether they view market segmentation as a tool to extract surplus from Mexico or to shift it there, at least in part, will colour the result. On balance, they will probably wish to see more rather than less exhaustion within North America.

For all these reasons, Mexico will likely be very interested in the exhaustion issue and will likely ensure that it is "on the table" and vigorously negotiated. The options, broadly stated, range from mandatory exhaustion within North America (EC model), mandatory market segmentation for each of he North American partners (the probable U.S.A. preference), and an understanding to permit each country to do whatever it wishes with respect to this issue. Whether Canada's interest in this context lies closer to Mexico or to that of the U.S.A. is an interesting and important question, for which there is probably no obvious answer.

If, however, free trade talks break down in North America, would Mexico still want to espouse the exhaustion principle domestically? In all likelihood, as an emerging economy, they probably would do so, although not quite so vigorously. For example, like the U.S.A. in the past and Canada today, they might want to use market segmentation to protect their cultural industries. On the other hand, since English is not the native language in Mexico, they may not need to be protectionist with respect to cultural industries. With respect to trade-marks, unless there is evidence that trade-mark owners are prepared to do a substantial amount of manufacturing in Mexico, it would seem that there would be little advantage to Mexico to segment the Mexican market, perhaps even less so than in a country such as Canada which does have fairly good per capita buying power.

<u>TRILATERAL EXHAUSTION:</u>

An argument often raised against exhaustion is that it cannot work well in the absence of standardization of intellectual property laws. Some suggest that trilateral exhaustion in North America would result in less transfer of technology, lower standards of intellectual property, and the likelihood that Canada would need to amend key provision of its law such as that relating to the first to file under the patent system in order to harmonize with the intransigent position of the U.S.A. who continues to stick with the "first to invent" system", although there are at last strong indications that this may change. Some of the facts and reasoning behind such an assertion here are simply incorrect. For example, Mexico's recently effected a major overhaul of its intellectual property system in 1991,[263] in apparent anticipation of the NAFTA negotiations. With these changes, there will be very little difference in patentability within North America. As well, Mexico recently abolished its trade and transfer of technology law. Moreover, even in Europe, the substantial differences in patent systems are taken into account in the exhaustion policy. The notion that we should not undermine the recent DOC book policy is not based upon any analysis. That policy (though approved by Cabinet) has not been implemented, may not be implemented, and is contrary to recent developments in other jurisdictions such as Australia. To be chained to that particular initiative is a bit like the tail wagging the dog. Moreover, in the unlikely event that this policy should result in actual legislation, there could always be a "cultural" exemption. Finally, this analysis completely ignores the fact that the local working requirements of Canadian law (for example, under s. 65 of the Patent Act) are about to vanish if Dunkel's GATT text is adopted (as discussed elsewhere in this work). Absent such incentives, is it seriously believed that market segmentation will result in transfer of technology? It will only likely result in price discrimination.

Also, on the subject of transfer of technology, some economists ignore the important point often made about distribution channels and how market segmentation supports the existence of separate channels in Canada. It has been suggested[264] that about 50% of the costs of retail items in Canada is attributable to distribution. Maybe this cost is too high, for the benefits received. Maybe there is inefficient and unproductive distribution activity in Canada due in part to the lack of exhaustion. In any case, mere passive distribution (i.e. warehouse, delivery, even local service facilities) have nothing whatsoever to do with transfer of technology. They may create jobs, but at what welfare cost?

D. Consumer Perspective

The Canadian judgements, apart from Seiko, pay little attention to consumer policy issues. This is probably as it should be, because such issues are, for better or worse, not clearly a part of our relevant positive (i.e. statutory) law. For example, in Seiko,[265] the Court leaves unresolved the question of what would have happened had the appellant refused to post a disclaimer as to entitlement to the international guarantee. This is an important point in the context of consumer and marketing law because many consumer products are sold with a printed manufacturer's warranty included inside or indeed on the package, and many consumers no doubt rely upon these warranties (or the expectation based upon advertisements that they are enclosed) when making their purchase. If the product comes in a sealed package and requires no dealer set-up, is there any reason why the consumer should be denied warranty entitlement?[266]

It should be noted that warranty practices of multinational enterprises vary a great deal. Some offer worldwide warranties. However, entitlement may depend upon proof of purchase from an authorized dealer.[267] Notwithstanding such a stated policy, some companies honour such warranties even though they may not be legally obliged to do so.

Other companies are very explicit that their warranty is valid only in a given territory. The consumer may not be aware of any of these aspects until the package is opened and the warranty is examined. One could argue that such essential information should be on the outside of the package, if the company is seeking to limit liability. One could also argue, as was successfully done in the Canadian Seiko [268] case, that the provision of sufficient information to the consumer to avoid deception will suffice to dispel any legal wrong.

New York State has an interesting law called the Warranty Disclosure Act.[269] This consumer protection legislation requires retailers to inform consumers of such facts as a manufacturer's warranty, lack of English language instructions, etc. The statute suffers from certain defects which include the anomaly that a retailer need not post any sign if it offers a warranty that is equal to or better than that of the manufacturer.[270] California has similar legislation as well.[271] Given the ruling of the Supreme Court of Canada in Seiko,[272] it would seem that such legislation would be redundant in Canada.

If dealer expertise or "set up" is an important element in consumer warranty entitlement, at what point ought this to become legally significant? Most would probably agree that this should be important with an automobile which purportedly requires considerable dealer preparation and adjustment. In fact, a separate and substantial charge is normally levied for this "pre-delivery inspection" or "dealer preparation". Few would likely agree that it matters with the example of a quartz watch which requires no dealer service. Other watches, however, may require some dealer adjustment, or explanation. On the other hand, it can be argued that consumers are free to choose the level of service that they need and are willing to pay for.

The more difficult argument to rebut is really that of the "free-rider" retailer. For example, a consumer may shop for a camera or VCR at a full service outlet that takes great time and care to explain the product. However, the actual sale may be lost to a grey marketeer across the street who can charge lower prices because he has a lower overhead. The rebuttal to this argument in turn may be very simple. If there is sufficient demand for full service, then there ought to be enough consumers who wish such service that some full service retailers will continue to stay in business, for example, those that can offer a full international manufacturer's warranty. This is intuitively obvious in such centres as New York where grey market emporiums coexist around the corner from some of the most posh shops on Fifth Avenue, selling the same products. This is simply competition and market differentiation.

Perhaps the manufacturer should be required to print conspicuously on the outside of all packages and in all other advertising alluding to warranties that no warranty is provided unless the product is purchased from an "authorized" dealer. While this might create a greater degree of legal certitude, it would no doubt cause some marketing problems. Many manufacturers may be understandably reluctant to take such steps since consumers could balk at buying products so labelled.

Consumers want the lowest possible prices, a wide selection of goods, the best possible warranties, and the best possible service.

A commonly postulated compromise (given that this utopia may not be obtainable in Canada) is said to be that of the old maxim "caveat emptor". If the consumer wishes to buy grey market goods and thereby save money but forgo free warranty service or some other benefit, should the consumer not have the choice? Is there any harm as long as the consumer knows exactly what is being purchased?

The answer may not be as simple as it appears. Some companies, such as Toshiba, claim that they would not have their network of service outlets in Canada in the absence of market segmentation.[273] However, one can postulate that, if Toshiba's competitors were to operate excellent service networks, Toshiba would need to follow. Or, a third party might fill the void.

However, experience illustrates that in a very large, dense, and competitive geographical retail consumer market such as New York City, there is the widest possible range of options for consumers of products protected by intellectual property, ranging from outright counterfeit goods sold openly on Fifth Avenue directly in front of some of the world's most expensive and service-oriented fine retail stores.

Counterfeit goods admittedly represent an extreme, and would appear initially to be irrelevant to the analysis of grey market goods. However, they are not completely irrelevant because, from a competition economist's standpoint, all possible substitutes should be considered. There may be some marginal cases where counterfeit goods do represent a substitute, even if inadvertent on the part of the consumer, for grey market goods or even authorized goods.

Note, in turn, that there are really two types of counterfeit markets. The obvious example is that of the street corner sale in New York. Nobody is under the illusion that the goods are genuine. The $20 watch that looks on the surface like the real $20,000 model does not fool anyone at the point of sale. However, there is another counterfeit market which is sometimes not so obvious. In this case, perfectly reputable retailers may be duped into purchasing counterfeit goods for resale at legitimate good prices or less reputable retailers may sell such goods, knowing that they are not legitimate. Ironically, the goods are not necessarily inferior in quality in some low technology instances. Clearly, in the latter cases, there can be a significant amount of economic harm and free-riding as far as the legitimate rights owner is concerned.

For example, imagine an astute shopper looking for a particular type of wrist watch in New York City. The shopper is shown the watch at one of the finest jewellery salons on Fifth Avenue, and receives a lengthy explanation of its many features. She is offered the watch for $2,000, complete with an internationally valid 10 year warranty. Around the corner, the shopper sees the same watch in a discount store for $1,000. However, the only warranty offered is from the store itself. There is an express disclaimer posted that the store is not an authorized dealer for this type of watch. There is no service. The watch comes in a box -- take it or leave it -- and all sales are final. Outside on the street at the corner, a couple of enterprising young persons have set up a highly portable table, with dozens of watches laid out. The astute shopper sees what looks to be the very watch she was looking at in the other places. The asking price is $30. A little bargaining results in the vendor lowering the price to $20. This watch bears a forged trade-mark and is, of course, counterfeit by any definition. (It may be, however, a perfectly good watch and a real bargain at the price). The shopper pauses, and then goes home to ponder which of the products to buy.

The real potential for economic harm is probably not so much from the grey market product as from the counterfeit product, but even in this situation, one must be very wary of the figures professed as to actual harm. The sale of a counterfeit watch will rarely be in substitution for the real watch. Therefore, it is not a lost sale. The real harm may lie in the possible devaluation of the real watch through its mass imitation. However, it is open to designers of watches to take advantage of the trade-marks and design laws to combat such harm, including the use of the distinguishing guise provisions of the Trade-marks Act. That is what those laws are intended to protect.

On the other hand, an example such as that given above for New York and the U.S.A. market may not be that useful because the U.S.A. has such enormous internal economies of scale due to its large market that it can have some benefits of market segmentation without some of the costs (such as higher prices). If this is in fact the case, Canada and Mexico might wish to become part of this large market and augment it even further in size and capacity, both in terms of production and demand. At least this is worthy of further study.

E. Competitiveness and "Cross-Border Shopping"

The cross-border shopping issue is, of course, closely related to that of the trade perspective discussed above. However, it is a subset of that discussion. At the time of writing, there is considerable concern and much news about plant closings, cross-border shopping, and the relationship of these phenomenon to employment and prosperity in Canada. Moreover, the Department of Finance has announced tariff cuts on items ranging from VCR's to tennis rackets aimed at eliminating price differentials between Canada and the USA.[274] These are items that are not manufactured in Canada. One could, of course, quaere why these tariffs were not removed a long time ago, since the items are not manufactured in Canada. However, the answer to this conundrum is not apparent. It may have to do with a need for revenue or the need to retain a trade bargaining chip.

Cross-border shopping, of course, is nothing other than a collective and widespread exercise in individual parallel importation for personal use. It is common knowledge that many types of consumer goods are much cheaper in the U.S.A. than in Canada, and Canadian shoppers are apparently prepared by the millions to incur the transaction costs of travel time, transportation expense, border and bridge tolls, some remaining customs duties, PST and GST in many cases, and other costs and inconvenience to purchase clothing, groceries, consumer electronics, etc. in or from the U.S.A. Lest one discount the potential role of intellectual property as a factor in why this situation exists, it should be noted that grocery shopping is widely reported to be one of the main activities of Canadian cross-border shoppers. As noted earlier, the two most important law suits in the last year in Canada dealing with exhaustion have involved ketchup and coffee respectively.

The possible connection of intellectual property and the cross-border phenomenon has also been suggested in an influential study done by Ernst and Young in 1991,[275] apparently prior to the Heinz case. The study does not go into the issue of grey marketing in detail. Indeed, there is a pressing need for an economic study based upon actual data to examine the question. Such a study would be very difficult, or very expensive, or both, to undertake on a scientific basis, because of the vast array of factors that can affect cost and price of items in Canada and abroad. If the study were to focus on instances where there has been litigation, it would not necessarily be representative of the norm.

It is often said that Canada's intellectual property laws, to the extent that they enable a certain degree of market segmentation, encourage investment in Canada through branch plants.[276] However, there is very little documentation of this. This is something that a proper economic study could substantiate one way or another.

The main point for the issue of competitiveness -- which entails the ability of a sector to compete on a global basis without artificial protection[277] -- is this. Canadian retailers will obviously be at a competitive disadvantage as compared to American retailers if their wholesale cost is higher (apart from legitimate freight and service charges). Canadian manufactures will likewise be at a disadvantage if their input costs are higher, for no reason other than price discrimination. In fact, quite apart from the inherent and obvious harmful effects of price discrimination that serves no "rule of reason" purpose, there is a potentially much more insidious and dangerous effect. A large and powerful economy such as that of the U.S.A., Japan, or Europe could use systematic price discrimination as a tool to weaken the manufacturing and retail infrastructure of a potentially competitive but currently weaker economy. This could result in factory closings, unemployment, higher consumer prices, and overall world inefficiency -- in other words, a recession. Unfortunately, short term thinking sometimes leads to the type of greed that can cause such a result.

This is not for a moment to say that market segmentation is responsible for all of the world's current economic malaise, or even that of Canada. However, the harmful effects of market segmentation are only now being understood and require much more study from an economic standpoint.

If it is intrinsically cheaper to build a widget in Wyoming, why would it be built in Winnipeg? Even if Canada had strong market segmentation laws, the manufacturer would simply ship from Wyoming to Winnipeg and charge a higher price to recover the freight differentiation costs.[278] This , of course assumes that there are no "manufacturing clause" aspects of the applicable Canadian law. Given that it is probably unthinkable to have compulsory license or local manufacturing requirements under trade-marks law, it must therefore be seriously reconsidered whether market segmentation under trade-marks law, especially, serves a net benefit to Canada.

F. The "Unilateral/Bilateral/Multilateral" Issue"

Some, including Globerman, and Anderson and Khosla, et al[279] have looked at whether Canada should act "unilaterally" on the exhaustion issue. This could arise in the event that our major trading partners do not wish to increase the degree of exhaustion with respect to goods entering their countries. Would it still be in Canada's interest to increase levels of exhaustion on a unilateral basis?

This is difficult to analyze, given the virtually complete lack of any empirical data upon which useful economic verification of different options can be undertaken. Such an examination has been called for in the Ernst and Young study on cross-border shopping.[280]

Subject to further potentially expensive research, it would appear, however, that, on this issue, Canada and other countries might conceivably find it beneficial to act unilaterally. This is because significant increases in efficiency and competitiveness could result from increased domestic competition and lower prices not only for consumers but for beleaguered Canadian industrialists and retailers. Moreover, it makes little sense to use intellectual property laws to encourage the domestic production of goods that can be imported more cheaply form the U.S.A., especially if we presumably have a free trade deal with the U.S.A.[281]

A net importer such as Canada should, arguably, provide higher levels of intellectual property protection on a national treatment basis only if we get something back in return. Our goal as a country is not to simply remit royalties to those countries who export more intellectual property than we do. If we decide to do so, it should be because there is clearly a net benefit to Canada, in spite of the deficit in intellectual property royalty payments.

In fact, some of those nations, such as the U.S.A. and Japan attained their preeminent exporting status, in part, by paying as little as possible for intellectual property for as long as they could not only to their own nationals but especially to those of others. As well, they used protectionist measures of various types as long as they could. For example, the U.S.A. only joined the Berne Convention that deals with copyright in 1988, just a very few years after abolishing its notorious manufacturing requirement for books. It was only in 1972 that the U.S. accorded copyright protection to international producers of sound recordings. The U.S.A. still maintains its requirement for reduction to practice in that country as a necessary requirement of patent protection.

Canadians have never, as a nation, been pirates. In fact, we have consistently provided higher levels of protection, for example, under copyright law, to American citizens than their own country does (i.e. moral rights, duration of term, absence of formalities, fewer compulsory licenses, and a longer term). However, there is a limit to which we need pay for matters of principle alone. For example, numerous valuable American films, books and songs have long since gone into the public domain in the U.S.A. but are still producing large royalties in Canada for U.S. interests. An example is the music of Irving Berlin, whose early works were public domain in the U.S.A. 56 years after they were composed. Those works will be protected in Canada for 50 years following Mr. Berlin's recent death at the age of 100.

It is essential to protect the intellectual property of Canadians and others (according to the national treatment principle) for two main reasons. The selfish reason is that Canadians see themselves as producers and exporters of intellectual property. Some Canadians, such as Bryan Adams and Northern Telecom, are already major exporters of intellectual property. On the whole, however, we are importers of intellectual property by a ratio of 20 to one in patents and somewhat less in copyright. The amelioration of the balance of payments figures in copyright are no doubt directly related to the CRTC Canadian content rules for radio and television.

The unselfish reason that we should accord high levels of protection to our own nationals and hence to others is that, to a point, "it is the right thing to do". Society, quite properly, values intellectual property. However, when intellectual property law is used for abusive purposes according to competition policy doctrine, or unwarranted price discrimination, or unwarranted resale price maintenance, or other goals that would lessen healthy competition that should otherwise occur, it is necessary to ask whether we have gone too far in protection. Perhaps this should be the acid test of a proper balance.

If exhaustion is of benefit to Canada, it may be that we simply cannot expect another country to "pay" for it. That is simply not logical. If anything, other countries should "pay" (in the language of trade negotiators) for Canada to go the market segmentation route. Otherwise, why is there so much pressure on us to do so?

G. Perspectives Based Upon National Interests

It has been suggested, although it would be difficult to document, that the existence of s. 65 of the Patent Act (quoted in Appendix III) has encouraged manufacturing in Canada. This provision provides for the granting of a compulsory license in the event of non-working for more than three years of a patent in Canada. The section is problematical in its wording (e.g. "no satisfactory reason can be given for that non-working"). It has been used a handful of times over the years. But, like s. 32 of the Competition Act, its very existence is said to be an important factor in the existence of branch plant manufacturing in Canada.

Indeed, Hayhurst notes the existence of the compulsory licensing sections of the Patent Act, and the fact that s. 66(1)(a)[282] thereof provides that "*the Commissioner may include in the license a term requiring the compulsory licensee, the patentee, and the persons claiming under the patentee to refrain from importing.*"[283] This would seem to confirm that there was a notion of coherent policy in the Canadian Patent Act, namely that of a quid pro quo. This would suggest that the patent holder or exclusive licensee in Canada should be, at the very least, encouraged to manufacture in Canada, and thus provide Canadian employment.

If this is true, it is probably sound from a policy standpoint. If the Government is prepared to allow for market segmentation under patent law, it would only seem logical to encourage, if not require, local manufacturing. Ironically, at the time of writing, it would seem that such local manufacturing provisions may become a thing of the past based upon the proposed

GATT agreement.[284]

One could readily argue that it makes sense for a country such as Canada, in which approximately 95% of patents are held by foreigners[285] to have the maximum reasonable degree of incentive for local manufacturing. Clearly, we would otherwise be deprived of access to technology and perhaps even many important products and processes themselves. Moreover, it is also possible that local manufacturing cannot be seriously fostered without some degree of market segmentation, since Canadian manufacturing would otherwise be at the mercy of goods imported from abroad that are cheaper at any given time than the Canadian-patented product. Of course, if multinational organizations were to develop truly distinct world product mandates that were assigned upon the basis of genuine competitive advantage, this would no longer be an issue. It would also not be an issue if there were to be truly uniform pricing throughout the world (except for legitimate differential costs such as freight). For better or worse, this is frequently not the case.

It would seem fairly obvious that different countries might have different approaches to the issue of exhaustion. We have analyzed how, on the one extreme, a country such as Mexico would actively want to encourage exhaustion within a free trade zone or common market so as to garner the largest possible share of manufacturing.

The USA, on the other hand, seems actively opposed to permitting other countries to embrace the exhaustion principle. Moreover, representatives of U.S. based multinationals are fairly consistent in taking this approach in the Canada context as well. Why is this so?

It is suggested that the answer lies in the fact that exports of intellectual property based goods and services, such as films, records, computer programs, and high technology products based upon integrated circuits are the only real areas of trade surplus and preeminence left to the USA. The 1970's and 1980's saw the USA, in effect, "trade places" with Japan.[286] The U.S.A. now realizes that the high levels of intellectual property protection with respect to the economic rights accorded to producers and the maximum power to exploit these rights are not only essential but in the interest of the USA. Moreover, the USA, because of its large size and relatively high per capita income constitutes the second largest internal market in the world (after the EC). Thus, the U.S. can produce certain types of goods with great economies of scale, and can buy goods abroad at world prices because of the enormous buying power and potential market within. Moreover, U.S. antitrust law, even in the nadir of enforcement in the Reagan years, was arguably still reasonably vigourous as compared to countries such as Japan.

Thus, the U.S.A. is in the understandable position of both wanting to and probably being able to "have its cake and eat it too" on this issue. If they can convince the rest of the world to accept market segmentation, they will maximize their profits from the sale of their intellectual property abroad. On the other hand, because of their enormous buying power, strong antitrust enforcement, and relatively weak market segmentation laws at home, their consumers and industrialists have the benefit of world prices on most goods.

Finally, as is sometimes the case, certain U.S. interests both within government and the private sector are urging other governments to take up positions that are inconsistent with present U.S. law and policy. The U.S. tends to do this in the case of intellectual property and antitrust law where their own law is less than transparent. Past examples include border measures (the "s. 337" issue), moral rights, reduction to practice, and compulsory licensing in general. This study has shown in chapter II that the U.S. (by means of court decisions) may permit considerably more exhaustion than is apparent by reference to its statutes. This is evidently the policy of the U.S. Government, because Congress has, in the final analysis, done nothing to change the situation in recent years. Thus, we could very well see a situation in GATT where the U.S. complains that other countries have inadequate laws with respect to the exhaustion issue, while refusing to admit that their own laws are even more "liberal" with respect to free trade.

CHAPTER IV POLICY OPTIONS AND CONCLUSIONS

It is quite easy either to oversimplify with generalities or to obfuscate with details the essence of the exhaustion policy debate. In this chapter, the author will attempt to steer a course down the middle, in order to outline some pertinent questions that need to be asked by both the private sector and the public sector to address the issues. The following table analyzes some of the "pros and cons" of exhaustion on a general basis.

EXHAUSTION

	PROS		CONS
I.	Gives purchasers of IP (both consumers and industrialists) benefit of lowest price within the geographical market (i.e. North America).	I.	Lower prices may result in less service, lower quality, etc.
II.	Gives consumer opportunity of choosing a level of service needed.	II.	May eliminate benefit of international warranties and "goodwill" cf. Seiko case.
III.	The "free rider" problem is omnipresent in intellectual property law. As long as owner/creator is getting an adequate reward, it is not a problem.	III.	Creates "free rider" problem.

IV.	Would reduce or eliminate price differentials on IP embodying goods based solely upon market segmentation.	IV.	Territorial limitation is of the very essence of intellectual property law.
V.	Would not interfere with price differentials based upon legitimate factors such as freight, currency fluctuations, and local servicing where demand warrants.	V.	As long as there is interbrand competition, the market should determine how these costs are allocated.[287]
VI.	Subject to antitrust laws and sound competition policy, would not interfere with contractual licensing vertical restraints.	VI.	This is a non-issue. The "Chicago School" philosophy concludes that business persons always act in their own ultimate self interest, which is to be efficient.
VII.	May relieve cross-border shopping pressure by lowering costs to Canadian retailers and making them more competitive with U.S. retailers (i.e. by giving them the same cost input).	VII.	Cross - border shopping is a very complex phenomenon that derives from many influences, not just intellectual property.
VIII.	Modern technology permits manufactures to trace channels of distribution if they so wish, i.e. though data bases of	VIII.	The state should provide laws that help companies enforce their policies.

	serial numbers, bar codes, etc.		
IX.	A sale is a sale is a sale. Grey market sales do not deprive inventors, authors, etc. of royalties. They deprive them only of the potential for monopoly maximization of royalties.	IX.	A grey market good is not "genuine". A sale at less than maximum profit represents an economic deprivation, even if not as severe as that of piracy.
X.	Differences in products should be the responsibility of the manufacturer/IP owner. i.e. the same trade mark would not be used on inferior products in Brazil and up-market products in England. That is "having your cake and eating it too". Part of the function of a trade-mark is to guarantee consistency and quality. Identical trade-marks should not be used on different products. This is within the control of multinational enterprises.	X.	International trade marks are necessary and desirable. Local conditions will dictate different formulations and even standards.
XI.	Minor and even artificial differences in quality or nature of products could be exploited to achieve	XI.	With interbrand competition, price discrimination and the development of local product differentiation can

	price discrimination.		be efficiency enhancing.
XII.	A manufacturer, with reasonable diligence can determine whether a particular distributor is "overselling" its territory by diverting goods into another territory?	XII.	Contractual restraints are insufficient to achieve enforcement of "quotas".
XIII.	Some manufacturers commonly turn a blind eye to such diverting of goods even when they are aware of it. "A sale is a sale is a sale".	XIII.	This is always an option that is open. however, it should not be forced upon a manufacturer.
XIV.	Renders the issue an "intramural" rather than a public policy issue.	XIV.	This is an issue akin to counterfeiting. Public resources should be deployed to prevent grey marketing.
XV.	Would tend to correct abuse of dominance, which is probably frequently present in grey market litigation but immensely costly to correct through antitrust law.	XV.	There are other tools to correct abuse of dominance. In any case, this is really a European or American concept that does not belong in Canada.[288]
XVI.	Would basically affect only related company transactions, where no "harm" is done.	XVI.	Related company "competition" can be just as vigorous and healthy as that of non-related

	Situations of truly separate goodwill "i.e.the EC "Hag II case" are extremely rare.		companies. MNEs function autonomously with "world product mandates".
XVII.	Grey marketeers, by providing demand in one country for goods that might have otherwise been surplus in another, arguably solve problems created by manufacturers themselves in setting unrealistic sales goals?	XVII.	Who better than a rights owner can determine efficiency and the rights owner's best interest?
XVIII.	Corrects a problem that is largely beyond any country's control, namely that of off-shore export cartels since most countries, including Canada render these immune and prosecution from abroad is virtually impossible.	XVIII.	Antitrust authorities can enforce laws where there is harm domestically and the MNEs have a domestic presence.
XIX.	General exhaustion principle still admits of particular exceptions, such as books of a cultural nature (whatever that may be!).	XIX.	Every case is different. Not just culture. Therefore, leave it to the courts.
XX.	Will encourage manufacturing in the lowest cost, highest efficiency location. This is supposedly	XX.	Not necessarily. Why is this not already taking place?

what free trade and
competitiveness is
all about.

It should be stressed that exhaustion is not an "all or nothing" concept. There are subtleties and degrees. An example of a doctrinal difference is whether exhaustion should apply only to goods made by a related company. Another example would be the question of whether exhaustion should apply if the goods differ in quality or composition (nature). A difference having to do with enforcement would be the question of who should enforce market segmentation laws -- the private sector through injunctions or the public sector at the border. Likewise, another enforcement issue involves the question of whether breach of market segmentation laws ought to give rise to criminal sanctions.[289]

There are several current fora where choices will need to be made. These include, GATT, NAFTA, the FTA, various WIPO initiatives, and possibly unilateral domestic initiatives. Most of the relevant points have been made through the foregoing analysis and will be distilled and simplified in this chapter.

Exhaustion, though not a difficult principle to state, involves a multiple of legal issues, even within the domain of intellectual property. The problems created by it do not admit of simple policy solutions.

This is because the issue must in turn deal with different legal principles i.e.:

* Patent law deals with manufacturing .

* Trade-mark law deals with trade.

* Copyright deals more with cultural issues.

The best policy for each may appear to conflict and be different from the other. Indeed, there may be no single unified policy that is best for Canada or any other country, much less a general agreement or treaty.

Trade-marks law has both an international and a national "dimension". i.e. Coke, Kodak, etc. want their products to be known worldwide by the same trade-mark. But registration is a national concern and the international system requires national registration. It is not always easy to reconcile the national and international nature of trade-marks law.

This runs counter to the international aspect of trade-marks law. Exhaustion depends on the international theory. Segmentation depends on the national theory. Trade-mark law has some territorial aspects and some international ones as well. These sometimes conflict. Trade-marks such as "Coke" or "Kodak" are intended to be recognized world wide. Yet they must be registered in each country. In Canada, for example, it is necessary to get a registration that the mark must have been used or well known in Canada - except under s. 14 where Canadian registration is based upon foreign registration.

On the other hand, consider the case of patents in Canada. S. 67(4) of the Patent Act provides quite explicitly that

> *Sec. 67 (4) For the purpose of determining whether there has been any abuse of the exclusive rights under a patent, it shall be taken, in relation to every paragraph of subsection (2), that patents for new inventions are granted not only to encourage invention but to secure that new inventions shall so far as possible be worked on a commercial scale in Canada without undue delay.*

This provision occurs in the context of a section of the Patent Act that authorizes the granting of compulsory licenses for non-working in Canada.[290] There is no reported jurisprudence on this section and only about eight applications have ever been made. Yet, it is generally considered that the very existence of this section has had a successful effect in encouraging manufacture, or at least efficient distribution, of patented products, taken together with the implied license rule and the "loopholes" associated with Betts v.Wilmott.[291]

Since the purpose of Patent Act and compulsory license scheme is thus clearly declared to be the encouragement of manufacture in Canada without undue delay, then market segmentation historically has made sense in the case of patents. In the past, a patentee in Canada must have either manufactured or have had a good excuse not to do so within three years.

Interestingly, the proposed GATT text (article 27(1) would abolish local manufacturing requirements as currently set forth in s. 65 of the Patent Act. At the most, a country could decide that there is abuse in the case of non-supply at reasonable prices, but a patentee could no longer be encouraged through the patent law to manufacture locally. The rationale for this may be the encouragement of world product mandates and the creation of a more hospitable investment climate in Canada.

However, quaere whether this development ought not call into question the wisdom of preserving the possibility of market segmentation with respect to patents. Market segmentation has been part of the *quid pro quo* for disclosure and either local manufacturing or efficient supply. If it is decided that patentees shall have no pressures under patent law to manufacture locally and that governments are to stop using patent laws to achieve national ends, then does it still make sense to preserve the territorial nature of patents? With relatively high wage costs in Canada, will we reap the benefit of the location of many world product mandates in this country, absent some type of incentive?

The main difference as between patent and trade-mark law is that the former is the embodiment of an idea that constitutes an invention. The patent system encourages utilization of these ideas within a county to a create a productive enterprise that contributes to national economic activity in return for the extraction of royalties as a result of the monopoly conferred. Patent law necessarily entails a degree of monopoly protection, which can be very substantial in some cases. Trade-marks law does not necessarily entail a monopoly, and indeed, ought not do so. For example, anyone can make and sell hamburgers anywhere. These hamburgers may even look like, smell like, and taste just like hamburgers made under the Macdonald's trade-mark. But, nobody can use that famous mark without authorization. Only Macdonald's can call a hamburger a *Big Mac*™.

It is noteworthy that the EC has broadened its concept of patent and trade-mark[292] to embrace a territorial notion, in many respects, that encompasses the community as a whole. They are rapidly moving in this direction with respect to copyright.

Copyright law, apart from recent developments having to do with the protection of computer programmes and other essentially functional forms of expression, has historically been rooted in the protection of authors and cultural matters. It has always been recognized that efficient economic principles may need to give way to the need to protect a country's culture, which is a precious and fragile commodity. Historically, copyright law has also been used by some countries (such as the U.S.A. until the mid 1980's) to encourage local manufacturing. Copyright law does, however, confer a degree of monopoly. This degree has traditionally thought to be considerably less than that of patent. However, this may be changing as a result of the litigation dealing with the "look and feel" issue in the USA. These cases give a very high degree of protection to subjective elements of computer programmes, such as their "structure, sequence and organization" and their command sequences.[293]

The main tension that arises from the exhaustion issue is still that of the inherently differing mandates of intellectual property and competition law. It is timely to look at the exhaustion issue in the context of competition and innovation.

Society has changed and the industrial world has changed, whereby innovation through research and development can enable a country to be competitive. This is essential to the maintenance of adequate prosperity in a country. If this is our policy, then we should encourage innovation and research and development in Canada, as part of an industrial strategy where we stress what we do best and utilize the raw material advantage that we enjoy. This may dictate some degree of market segmentation. But, we must also guard against becoming too much of a "high price" economy that we defeat our purpose. We must not hurt our consumers at the retail level or indeed our industrial and wholesale consumers, or we cannot compete with other countries.

Betts v. Wilmott still defines the law of Canada today with respect to "implied license". But there are "loopholes" in the ratio which are discussed above in Chapter I. S. 32 of the Competition Act,[294] also discussed above, may also have a chilling effect on overly zealous enforcement of market segmentation rights.

Thus, the situation in Canada with respect to patents up until now has been a delicate balance of a qualified right to segment markets in some situations combined with a knowledge on the part of patentees that the Patent Act can provide for compulsory licensing in the event that the product is neither made nor imported into Canada at a reasonable price. Trade-marks law has differing considerations and different purposes than patent law. Copyright law stands somewhere in between, in that it can confer a monopoly, but not as potent a monopoly as patent law. Moreover, the cultural protection aspect of copyright law is historically important.

THE BATTLE LINES OF THE DEBATE

There would appear to be one very simple way to eliminate grey marketing, if this is what intellectual property rights owners and licensees would like to do. That would be to ensure that, apart from unpredictable and uncontrollable currency fluctuations and legitimate freight and local servicing charges, there should be no differential pricing based upon territories (i.e. territorial price discrimination). Indeed, one could look yet again to the EC, where there is a strong trend towards a common currency. The EC has clearly decided that truly free trade within a community ultimately requires a common currency. Differential prices based upon legitimate freight costs or legitimate and essential local servicing costs will not give rise to grey marketing, because these costs will need to be incurred in any event. Moreover, the authorized distributor is likely to be able to deliver the freight and servicing more efficiently than the grey marketeer. Even commentators who view exhaustion in a negative manner implicitly or even explicitly admit that price discrimination is perhaps the major cause and motivation of the phenomenon.[295] In principle, the "free rider" problem can result in the potential consequential market failure resulting in lack of service facilities and marketing investment. This can be rebutted by arguments that market forces will resolve these problems, although neither side of this debate is, as yet convincing. The EC, however, does not appear to be plagued with problems arising as a result of the "free-rider" phenomenon.

There is one overwhelming irony in this debate. The main opponents of the exhaustion doctrine, such as the MNE's and some of the Chicago School followers, hold that market segmentation encourages local investment, manufacturing, and transfer of technology. The irony is that the branch plant MNEs that are making this argument may thus implicitly be admitting that they would have little or no presence in Canada if it were not for externalities in the nature of trade barriers that require or encourage them to be active in Canada. This puts in doubt not only their loyalty as corporate citizens, but the efficacy of any policy intended to keep them here through protectionist measures. It is an implicit admission that, the moment there is either no coercion or comparative advantage to being located in Canada, the MNE will simply "up and leave".

Moreover, it is difficult to know whether Canadian policy makers are hearing the Canadian branch plant view (with its possible bias towards short term survival) or that of the MNE as a whole. It must be remembered that a multinational may tend to maximize profits through price discrimination if it can, and would thus argue in favour of maintaining an inefficient branch in Canada if those inefficiencies could be compensated for by rents from price discrimination. Given the result of the <u>Heinz</u> case, it may make sense to maintain an otherwise inefficient plant in Canada, if such a decision will create a climate that will result in court-sanctioned price discrimination that leads to profits that offset the inefficiencies (no aspersions to Heinz in particular).[296] Much may depend in particular cases upon whether the CEO of the particular is a Canadian who might suffer if the plant were shut down or is a visiting executive from another country who knows his or her future is secure in any event of the maintenance of a presence in Canada.

In principle, if Canada were to embrace more protectionism by entrenching or extending market segmentation, the result could, in theory, backfire rather badly. This would be the case because the moment there is an incentive for a plant to leave the country (such as cheaper production costs elsewhere), they will do so and then still enjoy the ability to price discriminate without the unpleasant necessity (from the MNE's point of view) of local manufacturing. Local manufacturing has been encouraged for decades by provisions such as s. 65 of the Patent Act (which may become an obsolete concept as a result of the GATT negotiations, based upon a reading of the December 20, 1992 Dunkel Text)) and tariffs (which are subject to public policy reviews and are, in principle, very specifically targeted and administered in an overall public policy oriented manner).

Moreover, there is an apparent irony in the position of the Chicago School opponents of exhaustion. The Chicago School is a modern and more sophisticated version of earlier "laissez-faire" schools of economics. This is the notion that the market will take care of itself, and do so most efficiently with the least possible amount of government intervention. If this is the credo, would it then not make sense to allow the market to decide whether it prefers "grey" goods or "legitimate" goods, or an informed choice?[297]

If government gives intellectual property rights owners the means to block importation and distribution of grey goods, this is in itself a very substantial interference in the market place. Moreover, this is why it is essential that government come to grips with this issue as soon as possible. For governments to do nothing about the issue is to make a decision that the issue should be delegated to the private sector and the courts. There is little doubt about what general direction the courts are headed. Moreover, the demonstration effect of a few key court decisions can have a major effect upon trading patterns.

The choices are not as simple as they would at first appear.

* **The first tier of decision making would involve a determination of whether to allow for more or for less exhaustion as a general principle.**

More exhaustion could be accomplished in various degrees. The ultimate form of exhaustion would be to permit any article legally made anywhere to be imported. This is probably more exhaustion than ought to be considered, since it might permit the importation of goods made in jurisdictions without adequate or indeed any intellectual property laws. The more reasonable level would be to permit, generally, the importation of any goods legitimately made within the circle of countries that belong to, let us say, the GATT or NAFTA, if these negotiations fail, to the Paris and Berne Conventions. This would ensure that the goods are legitimately made. A somewhat lower tier of exhaustion could be effected by permitting the unfettered importation of goods made by enterprises related to the Canadian distributor (the U.S.A. trade-mark status, essentially). Canada's (and most other countries') current laws provide adequate rules to ensure that consumers are not misled or confused as to actual differences in the quality or the nature of the goods.[298]

Alternatively, more market segmentation could be effected as well. It must be plainly recognized that such a measure would be protectionist and have certain short term political and even economic benefits. Presumably, this is why such measures are being considered in the book publishing sector.

* **The next decision to be made would involve whether Canada should act unilaterally, bilaterally, or as part of a concerted treaty effort.**

As we have seen, the U.S.A. is currently reluctant to examine the exhaustion issue, and is reluctant to permit other countries to enjoy the same freedom of exhaustion as they themselves do. Therefore, it is unlikely that any progress can be made on this issue in current treaty efforts unless non-U.S.A. trade negotiators take a much tougher stand on this issue than has been apparent in the past. As indicated earlier, it would seem at the very least to make sense that retention of the current status quo or a move towards more market segmentation in Canada should be something that the U.S.A. ought to be willing to "pay for", since such a position would seem to be clearly in the U.S. interest and not so obviously for the benefit of Canada.

* **Then, if a decision is made to move towards more exhaustion, or indeed more market segmentation, it must be considered whether the principle should be broad, or targeted very specifically to patent, trade-mark and copyright laws in different ways.**

In turn, there could be specific targeting, such as at books but not at other copyrighted products. However, the Dunkel draft text of the GATT TRIPs agreement would put an end to patent law differences based upon specific fields of technology.[299]

* **Modalities of implementation must be considered.**

In principle, there could even be a system that would allow for market segmentation, but only for specific types or perhaps indeed specific marks of goods, based upon some sort of administrative determination based upon public policy tests. However, this would likely entail an enormous bureaucracy. In the end, it would closely resemble a tariff system, except that the economic value of the tariff would enure to the private sector rights owner.

In a "*de novo*" situation, it would be interesting to consider a scheme whereby each country could decide which products and services could or could not be prohibited importation via intellectual property law based upon such factors as local employment, subsidies abroad, industrial and trade policy, etc. This would quickly resemble a tariff system, except that the value of the tariffs collected would enure to the benefit of the rights holders directly.

Alternatively, one might consider a perspective that seeks to combine the "exhaustion" (i.e. European) and "implied license " (Anglo/US) approaches as follows. Where the goods have been put on the market by the intellectual property rights owner or his or her licensee, there is a rebuttable presumption of unlimited implied license. *"That rule would cast upon the proponent of the claim of infringement the obligation to produce evidence that the reasonable intent of the transactions was that there should be only a limited license."*[300]

As noted elsewhere in this work, a test or legal rule based upon differences in the quality or the composition or nature of goods is very prone to abuse. Such abuse would consist of the artificial introduction of differences for the purpose of taking advantage of market segmentation. In any case, such differences could readily be brought to the consumer's attention with appropriate labelling, affixed if necessary by the grey marketeer.

* **The choice of legal instrument must be considered**

In an important study for the Bureau of Competition Policy by Nancy Gallini, the learned author concludes, essentially, that intellectual property law should not be the vehicle to solve the problems raised by the exhaustion issue. She believes that there should be free flow of goods under trade-marks law but that contract and tort law should be available to assist intellectual property rights owners in their legitimate exercise of vertical restraints.[301] The problem with Prof. Gallini's conclusion is not so much the result (which is based upon some very thorough abstract economic analysis), but rather the fact that it ultimately begs the fundamental legal question involved with grey marketing and exhaustion. This is simply that contract and tort law are largely ineffective to deal with the issue of exhaustion because they have little effect upon third parties not privy to and legally obliged by the wishes of the intellectual property rights. Moreover, effective attempts to enforce contractual rights will often run afoul of sound antitrust principles.[302] Finally, contract and tort law are largely "property and civil rights" matters that are outside of federal jurisdiction and are outside of the normal legislative activities of provinces, since they are dealt with by the "common law" in most aspects. In any case, one would not wish to see different laws in different provinces bearing on grey marketing, since that would lead to an important lack of harmonization even within Canada.

In this author's view, one cannot avoid the connection between intellectual property laws and the exhaustion issue. The whole point of the intellectual property legal system is that it operates "in rem" on an international basis based upon the national treatment principle. That is, at once, its virtue and its Achilles Heel. Because of the potency of the system and its potential for abuse, vigilant antitrust enforcers should constantly be ready (as in Europe) to check excessive exercise of intellectual property and contractual rights.

*** Examination of the EC Experience**

There has been much rhetoric in both the recent constitutional debate within Canada and the free trade debate in general in the North American context about analogies with the European Community. It is quite beyond the scope of this exercise to analyze in detail whether the linguistic, cultural, political, historical, climatological and myriad other analogies and disanalogies between North America and Europe in this context are valid or not. However, one point alone seems incontrovertible. The EC has been a laboratory for the exhaustion principle and a very high level of internal free flow of goods (although not absolutely free[303]) for about thirty years. It would seem that the experiment has worked well, although it must be noted that Europe is hardly known for being a low price haven. There appears to be little if any serious momentum to reverse the trend.

No less of an authority than Friederich-Karl Beier, Managing Director of the celebrated Max Planck Institute for Foreign and International Patent, Copyright, and Competition Law, seems to be of the opinion that the current state of affairs in

Europe strikes a balance between free trade, the need for incentives to intellectual property rights owners, and the inherent territorial nature of intellectual property, especially in trade-marks law. He is also sensitive to the role of the EC in the world economy. In fact, it would seem that he is not averse to free trade principles extending from the EC to third countries, i.e the "outside world". The following quotation from Dr. Beier is worthy of consideration, in the context of the EC Draft Regulation and Directive on Trade-marks:

> *On the one hand, in the interest of the free movement of goods within the Common Market, the member states are compelled to adopt the principle of EC-wide exhaustion, i.e when the goods are put into circulation within the community. On the other hand, bearing in mind the basic function of trademarks, which is expressly recognized by the ECJ, namely to "guarantee the identity of the origin... of the trademarked product,", they are at liberty to go beyond this minimum requirement , and to retain the principle of international exhaustion. Any other interpretation would appear to me to be contradictory. It can surely not be seriously assumed that the EC legislature, which is so firmly obligated to the principle of free movement of goods, wanted to force the trial courts to give up principles of national law which already took into account the idea of free trade long before the creation of the EEC Treaty. In maintaining these principles, the courts would have to disregard the wishes of industry, which were voiced at the hearings and negotiations and found a willing ear with most government representatives. Nevertheless, I find such a disregard more acceptable than to ignore the fundamental principles of trademark law recognized by the highest courts of most Member States, in favour of a shortsighted protectionist policy of shielding the Common Market from the outside world, to which we are closely linked, from which we Western Europeans live and with which we must live together.*[304]

It is quite true that overly simplistic analogies between North America and Europe are misleading and indeed dangerous. Certain points ought to be considered in the present context. These include the following:

I. The EC includes separate economies ranging from the very weak and small to the very large and powerful. However, even Germany does not "dominate" Europe to the extent that the U.S. dominates North America.

II. Cultural sovereignty does not seem to be nearly so important and emotional issue in Europe as it is in North America.

III. Europe's recent leap forward in prosperity relative to that of North America is not necessarily simply a result of the advent of the EC. The Marshall plan, the rebuilding of key plants after World War II, and other factors quite apart from the Treaty of Rome have doubtless played a major part.

It would seem that Canada could only profit from an in depth analysis of the relevance of the European Community experience with respect to exhaustion for purposes of our own experiment with free trade. Such an examination would not necessarily entail adoption of the European mode. However, it would, at the least, result in a better understanding of our own situation.

CONCLUSIONS

This study may have, although hopefully has not, raised more questions than it has answered. However, the exhaustion issue cannot be adjourned indefinitely. There is far too much at stake in terms of international trade, competitiveness, consumer and overall economic welfare, and the integrity of intellectual property laws together with sound competition principles to allow these issues to be decided at random or by the courts in default of considered parliamentary activity.

The overall conclusions of this study are simply these:

I. There is little evidence of a considered policy with respect to exhaustion in North America. One can see some historical evidence of a reasoned policy that encourages local manufacturing under Canadian patent law, but this is about to become obsolete if the current GATT text is finalized and adopted.

II. There is a great deal of evidence of a considered policy with respect to exhaustion and its related ramifications with respect to competition, consumer and other issues in the context of the EC.

III. Truly free trade without a fairly high degree of exhaustion, especially in the case of trade-marks law, will be very difficult to achieve.

IV. It may be necessary and prudent to distinguish as between patent, trade-mark and copyright law in the formulation of policy. The best case for exhaustion is under trade-marks law. The best economic case for market segmentation is under patent law. The best cultural case for segmentation is under copyright law, in limited circumstances. However, in all cases, market segmentation should be permitted only to the extent necessary to achieve defined trade policy goals and subject always to adequate competition policy disciplines.

V. Canadian policy makers should take a very long and hard look at who really benefits from market segmentation in Canada. It is probably no coincidence that market segmentation is something that is being urged upon us by those countries with whom we have a negative balance of trade in intellectual property.

VI. The importance of price discrimination is only now being realized.

VII. Vigorous antitrust (competition policy) enforcement is needed to curb excessive or abusive exercise of intellectual property rights that lead to non-productive price discrimination, or worse still, cartelization. This may require amendment of the Competition Act, if the "abuse of dominance" provisions are inadequate. This particular point requires much further study.

VIII. This subject requires considerably further economic analysis based upon actual data and not simply conjecture. Though such a study would be difficult and expensive, it is necessary and overdue.

IX. At the present time, the "exhaustion" issue is one of the most complex, least understood, and most economically significant issues in international intellectual property, competition and trade law.

APPENDIX I

GLOSSARY -- TERMINOLOGY

Because this paper is being written to be of use, hopefully, to persons who are not experts in intellectual property law, it is important to explain a few key terms and concepts.

By **grey market goods**, I am referring to goods that are imported into Canada contrary to the wishes of a party that claims on the basis of either intellectual property rights or contract or both to have the exclusive right to be the Canadian importer or distributor. The goods in question are by definition "legitimate" in the sense that they are not counterfeit or pirate, and were sold into the market somewhere with the consent of the intellectual property right owner, who was presumably paid in full for the goods.

The term **"parallel import"** is often used interchangeably with "grey market" goods. As far as I can see, the only real difference in the terms is that the latter is clearly somewhat pejorative and the former is more neutral and descriptive.

The term **"exhaustion"** refers to the legal doctrine that holds that once legitimate goods are sold into the market place and title passes, there can be no further restriction of any kind on their physical alienation, including territorial restrictions. The rights of the original owner in the physical product (save the right to copy it) are said to have been "exhausted", since payment has been made and title has passed.

This term is usually used in the international context, and perhaps should be spelled out in full as "international exhaustion". This is because there is a related term that is sometimes used with respect to intra-national transactions and that is the "first sale" doctrine.

The **"first sale"** doctrine holds that once title to an article has passed, there can be no further restriction on its alienation by the original owner on parties not privy to any valid and enforceable contract affecting such alienation. Thus, I can set up a video rental store and rent video cassettes to the public without the permission of the copyright holder, as long as the video cassettes are legitimate copies. Or, I can sell the video cassettes, or give them away. Once I have bought and paid for them, I can do whatever I want with them, subject only to the copyright law. For example, I cannot copy them or exhibit them in public without permission. [305] The term "first sale" doctrine is usually used to describe the right of distribution within a country. A rental right, as is sought by many copyright holders, would allow the rights holder to segment the type of market (i.e. sale v. rental) but not necessarily the geographical boundaries.

The opposite of exhaustion is **"market segmentation"**, whereby an intellectual property rights owner can carve out territorial markets for products or services and engage in price discrimination if so desired, subject only to applicable antitrust or competition laws. Price discrimination occurs "when the same commodity is sold at more than one price...or , if very similar products are sold at prices that are in different ratios to marginal costs."[306] It is said that price discrimination is a "socially inefficient way of pricing a commodity".[307] An example of price discrimination would be the selling of a shirt with a designer label for $100 at an "up-scale" store and the same shirt for $10 at a bargain store with a low-prestige label. A more invidious example might be the sale of a drug to cure AIDS at a high price in North America and a low price in Africa. Naturally, in these hypothetical examples, the price difference is not legitimately attributable to actual differences in cost.[308]

Another term that is sometimes used and has some theoretical and historical advantages, is that of **"implied license"**, namely that the purchaser of a good has an implied license to resell anywhere to whomsoever the purchaser may wish to resell. This derives from the venerable case of Betts v. Wilmott[309]. The distinction between "exhaustion" and "implied license" is most succinctly pointed out in the Henderson Report.[310]

There is a very learned and more detailed discussion of the difference between the exhaustion and the implied license theory, more in an American context, in a recent article by R. Stern.[311] Stern confirms the European origin of the exhaustion doctrine and the Anglo-American origin of the implied license theory. He has an interesting theory that the recent celebrated UK case of British Leyland v. Armstrong[312] is really a case involving implied license, namely the implied bargain that the owner of a car can buy spare parts and repair it in whatever way he or she chooses.[313] In that case, the House of Lords reluctantly found that there was copyright in a tail pipe but refused to enforce it on public policy grounds.

Stern analyses the then recent U.S. cases of Red Baron and Sebastian (which are discussed in Chapter II of this work) against this dichotomy. Interestingly, Stern makes a useful attempt to analyze the merits of these approaches from a policy point of view. He points out that exhaustion is a broader and more certain rule, and implied license is narrower and more dependent on intent. Therefore, he suggests that the analogy is not unlike that of the "per se" and "rule of reason" approach to antitrust law. Stern prefers the former because it is far more precise and less expensive for all parties concerned to administer.[314] Finally, Stern proposes an amalgam of these two approaches which will be discussed from a policy viewpoint in Chapter IV of this work.

Alternative terminology is also used from time to time. One will sometimes see the term **"universality"** used in an apparently synonymous way to the term "exhaustion" as defined above. Likewise the term **"territoriality"** is sometimes used to describe the principle by which markets can be segmented. However, this alternative terminology will not be used in this paper, since it is fairly rare.

"Confusion" is a term of art defined in the Trade-marks Act at some length, based upon a codification of old cases. The definition is important enough to reproduce in its entirety:

Trade-marks Act
T-13

SEC 6.
When mark or name confusing
6. (1) For the purposes of this Act, a trade-mark or trade-name is confusing with another trade-mark or trade-name if the use of the first mentioned trade-mark or trade-name would cause confusion with the last mentioned trade-mark or trade-name in the manner and circumstances described in this section.

Idem

(2) The use of a trade-mark causes confusion with another trade-mark if the use of both trade-marks in the same area would be likely to lead to the inference that the wares or services associated with those trade-marks are manufactured, sold, leased, hired or performed by the same person, whether or not the wares or services are of the same general class.

Idem

(3) The use of a trade-mark causes confusion with a trade-name if the use of both the trade-mark and trade-name in the same area would be likely to lead to the inference that the wares or services associated with the trade-mark and those associated with the business carried on under the trade-name are manufactured, sold, leased, hired or performed by the same person, whether or not the wares or services are of the same general class.

Idem

(4) The use of a trade-name causes confusion with a trade-mark if the use of both the trade-name and trade-mark in the same area would be likely to lead to the inference that the wares or services associated with the business carried on under the trade-name and those associated with the trade-mark are manufactured, sold, leased, hired or performed by the same person, whether or not the wares or services are of the same general class.

What to be considered

(5) In determining whether trade-marks or trade-names are confusing, the court or the Registrar, as the case may be, shall have regard to all the surrounding circumstances including

(a) the inherent distinctiveness of the trade-marks or trade-names and the extent to which they have become known;

(b) the length of time the trade-marks or trade-names have been in use;

(c) the nature of the wares, services or business;

(d) the nature of the trade; and

(e) the degree of resemblance between the trade-marks or trade-names in appearance or sound or in the ideas suggested by them. R.S., c. T-10, s. 6.

APPENDIX II

STATEMENT OF SIR LEON BRITTAN

October 4, 1989

TOKYO

Sir Leon Brittan, the top ranking Commissioner of the EC responsible for competition law made a statement with respect to Japan's distribution system, noting that many of the Japanese practices are illegal in Europe:

"If our consumers had to pay the prices which are brought about by the Japanese system -- particularly for foreign goods and for land -- there would be a popular uprising," he said.

Sir Leon, the European Economic Community commission's vice-president responsible for competition and financial institutions, urged Japan to adopt similar measures to those used by the EEC to combat unfair practices. "Such action would do much to overcome what is felt in Europe to be a major obstacle to genuinely free trade with Japan," he said. Speaking to Japan's powerful Federation of Economic Organizations in Tokyo, he cited cartels, the maintenance of resale prices and captive distribution networks as three common Japanese practices which are illegal in Europe.

Sir Leon noted that Italian glassmakers, plastics producers and steelmakers had recently been fined up to the equivalent of $72 million Cdn for price fixing and quota arrangements. "Price-fixing between competitors is regarded as an extremely serious infringement of the law," he said.

CLOSED MARKET

Maintenance of retail prices, involving producers dictating the price at which goods reach the end user, is forbidden in trade between EEC members and outlawed by most national legislation as well, he said.

"The same goes for attempts by manufacturers or wholesalers to prohibit discounts to consumers. This was one of the offences for which we took action against Dutch and Belgian cigarette producers. "

On the subject of captive distribution networks, one of the main complaints among foreign companies seeking access to the Japanese market, Sir Leon acknowledged that some European networks were exempt from anti-monopoly rules.

"But we are ever watchful of the danger that markets might become closed to potential new entrants," he said.

The community particularly objects to reciprocal exclusive distribution by competing suppliers and efforts by major **importers** to hinder **parallel imports** through cheaper channels, which Sir Leon described as a "cardinal sin."

Japanese electrical machinery maker Fanuc Ltd. and West German industrial conglomerate Siemens AG were each fined $13 million for an agreement marketing each other's tools, he said.

As for hindering **parallel imports**, "Japanese firms have been among the sinners," Sir Leon said, citing as examples camera-maker Konica Corp. and audio equipment manufacturer **Pioneer Electronic Corp.**

(EMPHASIS ADDED) (as reported by AFP)

APPENDIX III

PATENT ACT

R.S. 1985

c. P-4

SEC 65.
Abuse of rights under patents

65. (1) The Attorney General of Canada or any person interested may, at any time after the expiration of three years from the date of the grant of a patent, apply to the Commissioner alleging in the case of that patent that there has been an abuse of the exclusive rights thereunder and asking for relief under this Act.

What amounts to abuse

(2) The exclusive rights under a patent shall be deemed to have been abused in any of the following circumstances:

(a) if the patented invention, being one capable of being worked within Canada, is not being worked within Canada on a commercial scale, and no satisfactory reason can be given for that non-working;

(b) if the working of the invention within Canada on a commercial scale is being prevented or hindered by the importation from abroad of the patented article by the patentee or persons claiming under him, by persons directly or indirectly purchasing from him or by other persons against whom the patentee is not taking or has not taken any proceedings for infringement;

(c) if the demand for the patented article in Canada is not being met to an adequate extent and on reasonable terms;

(d) if, by reason of the refusal of the patentee to grant a licence or licences on reasonable terms, the trade or industry of Canada or the trade of any person or class of persons trading in Canada, or the establishment of any new trade or industry in Canada, is prejudiced, and it is in the public interest that a licence or licences should be granted;

(e) if any trade or industry in Canada, or any person or class of persons engaged therein, is unfairly prejudiced by the conditions attached by the patentee, whether before or after the passing of this Act, to the purchase, hire, licence or use of the patented article or to the using or working of the patented process; or

(f) if it is shown that the existence of the patent, being a patent for an invention relating to a process involving the use of materials not protected by the patent or for an invention relating to a substance produced by such a process, has been utilized by the patentee so as unfairly to prejudice in Canada the manufacture, use or sale of any materials.

Exception

(3) If an application is presented to the Commissioner on the ground described in paragraph (2)(a) and the Commissioner is of opinion that the time that has elapsed since the grant of the patent has by reason of the nature of the invention or for any other cause been insufficient to enable the invention to be worked within Canada on a commercial scale, the Commissioner may make an order adjourning the application for such period as will in his opinion be sufficient for that purpose.

Declaration of basis of grants of patents

(4) For the purpose of determining whether there has been any abuse of the exclusive rights under a patent, it shall be taken, in relation to every paragraph of subsection (2), that patents for new inventions are granted not only to encourage invention but to secure that new inventions shall so far as possible be worked on a commercial scale in Canada without undue delay.

Definition of "patented article"

"patented article"

(5) For the purposes of this section, the expression "patented article" includes articles made by a patented process. R.S., c. P-4, ss. 67, 72.

SEC 66.

Powers of Commissioner in cases of abuse

66. (1) On being satisfied that a case of abuse of the exclusive rights under a patent has been established, the Commissioner may exercise any of the following powers as he may deem expedient in the circumstances:

(a) he may order the grant to the applicant of a licence on such terms as the Commissioner may think expedient, including a term precluding the licensee from importing into Canada any goods the importation of which, if made by persons other than the patentee or persons claiming under him, would be an infringement of the patent, and in that case the patentee and all licensees for the time being shall be deemed to have mutually covenanted against that importation;

(b) if the Commissioner is satisfied that the invention is not being worked on a commercial scale within Canada, and is such that it cannot be so worked without the expenditure of capital for the raising of which it will be necessary to rely on the exclusive rights under the patent, he may, unless the patentee or those claiming under him will undertake to find that capital, order the grant to the applicant, or any other person, or to the applicant and any other person or persons jointly, if able and willing to provide that capital, of an exclusive licence on such terms as the Commissioner may think just, but subject to this Act;

(c) if the Commissioner is satisfied that the exclusive rights have been abused in the circumstances specified in paragraph 65(2)(f), he may order the grant of licences to the applicant and to such of his customers, and containing such terms, as the Commissioner may think expedient;

(d) if the Commissioner is satisfied that the objects of this section and section 65 cannot be attained by the exercise of any of the foregoing powers, the Commissioner shall order the patent to be revoked, either forthwith or after such reasonable interval as may be specified in the order, unless in the meantime such conditions as may be specified in the order with a view to attaining the objects of this section and section 65 are fulfilled, and the Commissioner may, on reasonable cause shown in any case, by subsequent order extend the interval so specified, but the Commissioner shall not make an order for revocation which is at variance with any treaty, convention, arrangement, or engagement with any other country to which Canada is a party; or

(e) if the Commissioner is of opinion that the objects of this section and section 65 will be best attained by not making an order under the provisions of this section, he may make an order refusing the application and dispose of any question as to costs thereon as he thinks just.

Proceedings to prevent infringement

(2) A licensee under paragraph (1)(a) is entitled to call on the patentee to take proceedings to prevent infringement of the patent, and if the patentee refuses or neglects to do so within two months after being so called on, the licensee may institute proceedings for infringement in his own name as though he were the patentee, making the patentee a defendant, but a patentee added as defendant is not liable for any costs unless he enters an appearance and takes part in the proceedings.

Service on patentee

(3) Service on a patentee added as a defendant may be effected by leaving the writ at his address or at the address of his representative for service as appearing in the records of the Patent Office.

Considerations by which Commissioner to be guided

(4) In settling the terms of a licence under paragraph (1)(a), the Commissioner shall be guided as far as possible by the following considerations:

(a) he shall endeavour to secure the widest possible use of the invention in Canada consistent with the patentee deriving a reasonable advantage from his patent rights;

(b) he shall endeavour to secure to the patentee the maximum advantage consistent with the invention being worked by the licensee at a reasonable profit in Canada; and

(c) he shall endeavour to secure equality of advantage among the several licensees, and for this purpose may, on due cause being shown, reduce the royalties or other payments accruing to the patentee under any licence previously granted, and in considering the question of equality of advantage, the Commissioner shall take into account any work done or outlay incurred by any previous licensee with a view to testing the commercial value of the invention or to securing the working thereof on a commercial scale in Canada. R.S., 1985, c. P-4, s. 66; R.S., 1985, c. 33 (3rd Supp.), s. 24.

APPENDIX IV

TRADE-MARKS ACT

R.S. 1985

c. T-10

SEC 4.
When deemed to be used
4. (1) A trade-mark is deemed to be used in association with wares if, at the time of the transfer of the property in or possession of the wares, in the normal course of trade, it is marked on the wares themselves or on the packages in which they are distributed or it is in any other manner so associated with the wares that notice of the association is then given to the person to whom the property or possession is transferred.
Idem
(2) A trade-mark is deemed to be used in association with services if it is used or displayed in the performance or advertising of those services.
Use by export
(3) A trade-mark that is marked in Canada on wares or on the packages in which they are contained is, when the wares are exported from Canada, deemed to be used in Canada in association with those wares. R.S., c. T-10, s. 4.

SEC 6.
When mark or name confusing
6. (1) For the purposes of this Act, a trade-mark or trade-name is confusing with another trade-mark or trade-name if the use of the first mentioned trade-mark or trade-name would cause confusion with the last mentioned trade-mark or trade-name in the manner and circumstances described in this section.
Idem
(2) The use of a trade-mark causes confusion with another trade-mark if the use of both trade-marks in the same area would be likely to lead to the inference that the wares or services associated with those trade-marks are manufactured, sold, leased, hired or performed by the same person, whether or not the wares or services are of the same general class.
Idem
(3) The use of a trade-mark causes confusion with a trade-name if the use of both the trade-mark and trade-name in the same area would be likely to lead to the inference that the wares or services associated with the trade-mark and those associated with the business carried on under the trade-name are manufactured, sold, leased, hired or performed by the same person, whether or not the wares or services are of the same general class.
Idem
(4) The use of a trade-name causes confusion with a trade-mark

if the use of both the trade-name and trade-mark in the same area would be likely to lead to the inference that the wares or services associated with the business carried on under the trade-name and those associated with the trade-mark are manufactured, sold, leased, hired or performed by the same person, whether or not the wares or services are of the same general class.

What to be considered

(5) In determining whether trade-marks or trade-names are confusing, the court or the Registrar, as the case may be, shall have regard to all the surrounding circumstances including

(a) the inherent distinctiveness of the trade-marks or trade-names and the extent to which they have become known;

(b) the length of time the trade-marks or trade-names have been in use;

(c) the nature of the wares, services or business;

(d) the nature of the trade; and

(e) the degree of resemblance between the trade-marks or trade-names in appearance or sound or in the ideas suggested by them. R.S., c. T-10, s. 6.

SEC 7.

UNFAIR COMPETITION AND PROHIBITED MARKS

Prohibitions

7. No person shall

(a) make a false or misleading statement tending to discredit the business, wares or services of a competitor;

(b) direct public attention to his wares, services or business in such a way as to cause or be likely to cause confusion in Canada, at the time he commenced so to direct attention to them, between his wares, services or business and the wares, services or business of another;

(c) pass off other wares or services as and for those ordered or requested;

(d) make use, in association with wares or services, of any description that is false in a material respect and likely to mislead the public as to

(i) the character, quality, quantity or composition,

(ii) the geographical origin, or

(iii) the mode of the manufacture, production or performance of the wares or services; or

(e) do any other act or adopt any other business practice contrary to honest industrial or commercial usage in Canada. R.S., c. T-10, s. 7.

SEC 19.

Rights conferred by registration

19. Subject to sections 21 and 32, the registration of a trade-mark in respect of any wares or services, unless shown to

be invalid, gives to the owner of the trade-mark the exclusive right to the use throughout Canada of the trade-mark in respect of those wares or services. R.S., c. T-10, s. 19.

SEC 20.
Infringement

20. The right of the owner of a registered trade-mark to its exclusive use shall be deemed to be infringed by a person not entitled to its use under this Act who sells, distributes or advertises wares or services in association with a confusing trade-mark or trade-name, but no registration of a trade-mark prevents a person from making

(a) any bona fide use of his personal name as a trade-name, or
(b) any bona fide use, other than as a trade-mark,
(i) of the geographical name of his place of business, or
(ii) of any accurate description of the character or quality of his wares or services,

in such a manner as is not likely to have the effect of depreciating the value of the goodwill attaching to the trade-mark. R.S., c. T-10, s. 20.

SEC 50.

REGISTERED USERS

Registration as user

50. (1) A person other than the owner of a registered trade-mark may be registered as a registered user thereof for all or any of the wares or services for which it is registered.

Definition of "permitted use"
"permitted use"

(2) The use of a registered trade-mark by a registered user thereof in accordance with the terms of his registration as such in association with wares or services manufactured, sold, leased, hired or performed by him, or the use of a proposed trade-mark as provided in subsection 40(2) by a person approved as a registered user thereof, is in this section referred to as the "permitted use" of the trade-mark.

Effect of permitted use

(3) The permitted use of a trade-mark has the same effect for all purposes of this Act as a use thereof by the registered owner.

Owner may be required to take proceedings

(4) Subject to any agreement subsisting between the parties thereto, a registered user of a trade-mark may call on the owner thereof to take proceedings for infringement thereof, and, if the owner refuses or neglects to do so within two months after being so called on, the registered user may institute proceedings for infringement in his own name as if he were the owner, making the owner a defendant, but an owner so added as defendant is not liable for any costs unless he takes part in

the proceedings.

Application

(5) Concurrently with or at any time after the filing of an application for the registration of a trade-mark, an application for the registration of a person as a registered user of the trade-mark may be made to the Registrar in writing by that person and by the owner of the trade-mark, and the applicants shall furnish the Registrar in writing with

(a) particulars of the relationship, existing or proposed, between them, including particulars of the degree of control by the owner over the permitted use that their relationship will confer;

(b) a statement of the wares or services for which registration is proposed;

(c) particulars of any conditions or restrictions proposed with respect to the characteristics of the wares or services, to the mode or place of permitted use or to any other matter;

(d) information as to the proposed duration of the permitted use; and

(e) such further documents, information or evidence as may be required by the Registrar.

Secrecy

(6) The Registrar shall, if so required by an applicant under subsection (5), take steps to ensure that any document, information or evidence furnished for the purpose of that application, other than matter entered in the register, is not disclosed to any other person except by order of a court.

Registration

(7) The Registrar may, pursuant to an application under subsection (5), approve a person as a registered user of the trade-mark for any of the proposed wares or services described in the application, subject to any conditions or restrictions that he considers proper, if he is satisfied that in all the circumstances the use of the trade-mark in association with the wares or services by the proposed registered user would not be contrary to the public interest.

Time of registration

(8) When a person has been approved as a registered user of a trade-mark, the Registrar shall register him as such forthwith if the trade-mark is registered and, if the trade-mark is not registered, then concurrently with its registration, and shall give notice of the registration to any other registered user of the trade-mark.

Variation of registration

(9) The registration of a person as a registered user of a trade-mark may be varied by the Registrar with respect to the wares or services for which, or any conditions or restrictions subject to which, it has effect, on the application in writing of the registered owner of the trade-mark and not less than one month after giving notice of the application to that person and all other registered users, if the Registrar is satisfied that in all the circumstances the variation would not be contrary to

the public interest.

Cancellation

(10) The registration of a person as a registered user of a trade-mark may be cancelled,

(a) by the Registrar on the application in writing of the registered owner or the registered user of the trade-mark;

(b) by the Registrar on his own motion in respect of any wares or services for which the trade-mark is no longer registered; or

(c) by the Federal Court on the application of any person, of which notice is served on the registered owner and all registered users, on any of the following grounds:

(i) that the registered user has used the trade-mark otherwise than by way of the permitted use, or in such a way as to cause, or to be likely to cause, deception or confusion,

(ii) that the owner or the registered user misrepresented or failed to disclose a fact that if accurately represented or disclosed would have justified the Registrar in refusing the application for registration of the registered user,

(iii) that the circumstances have changed since the date of the registration in such a way that at the date of the application for cancellation of the registration they would have justified the Registrar in refusing the application for registration of the registered user, or

(iv) that the registration ought not to have been effected having regard to rights vested in the applicant by virtue of a contract in the performance of which he is interested.

No right to assign

(11) Nothing in this section confers on a registered user of a trade-mark any transferable right to the use of the trade-mark.

Person adversely affected

(12) The Registrar shall not exercise any discretionary power under this section adversely in respect of a person who will be affected by the exercise of the power without giving that person an opportunity to be heard personally or by his agent. R.S., c. T-10, s. 49; R.S., c. 10(2nd Supp.), s. 64.

SEC 51.

Use of trade-mark by related companies

51. (1) Where a company and the owner of a trade-mark that is used in Canada by that owner in association with a pharmaceutical preparation are related companies, the use by the company of the trade-mark, or a trade-mark confusing therewith, in association with a pharmaceutical preparation that at the time of that use or at any time thereafter,

(a) is acquired by a person directly or indirectly from the company, and

(b) is sold, distributed or advertised for sale in Canada in a package bearing the name of the company and the name of that person as the distributor thereof, has the same effect, for all purposes of this Act, as a use of the trade-mark or the confusing trade-mark, as the case may be, by that owner.

Where difference in composition

(2) Subsection (1) does not apply to any use of a trade-mark or a confusing trade-mark by a company referred to in that subsection in association with a pharmaceutical preparation after such time, if any, as that pharmaceutical preparation is declared by the Minister of National Health and Welfare, by notice published in the Canada Gazette, to be sufficiently different in its composition from the pharmaceutical preparation in association with which the trade-mark is used in Canada by the owner referred to in subsection (1) as to be likely to result in a hazard to health.

Definition of "pharmaceutical preparation"

"pharmaceutical preparation"

(3) In this section, "pharmaceutical preparation" includes

(a) any substance or mixture of substances manufactured, sold or represented for use in

(i) the diagnosis, treatment, mitigation or prevention of a disease, disorder or abnormal physical state, or the symptoms thereof, in humans or animals, or

(ii) restoring, correcting or modifying organic functions in humans or animals, and

(b) any substance to be used in the preparation or production of any substance or mixture of substances described in paragraph (a),

but does not include any such substance or mixture of substances that is the same or substantially the same as a substance or mixture of substances that is a proprietary medicine within the meaning from time to time assigned to that expression by regulations made pursuant to the Food and Drugs Act. R.S., c. T-10, s. 50; 1974-75-76, c. 43, s. 2.

SEC 52.

LEGAL PROCEEDINGS

Custody of offending wares

52. (1) Where it is made to appear to a court of competent jurisdiction that any registered trade-mark or any trade-name has been applied to any wares that have been imported into Canada or are about to be distributed in Canada in such a manner that the distribution of the wares would be contrary to this Act, or that any indication of a place of origin has been unlawfully applied to any wares, the court may make an order for the interim custody of the wares, pending a final determination of the legality of their importation or distribution in an action commenced within such time as is prescribed by the order.

Security

(2) Before an order is made under subsection (1), the plaintiff or petitioner shall be required to furnish security, in such amount as the court may fix, to answer any damages that may by reason of the order be sustained by the owner or

consignee of the wares and for any amount that may become chargeable against the wares while they remain in custody under the order.

Lien for charges

(3) Where, by the judgment in any action under this section finally determining the legality of the importation or distribution of the wares, their importation or distribution is forbidden, either absolutely or on condition, any lien for charges against them that arose prior to the date of an order made under this section has effect only so far as may be consistent with the due execution of the judgment.

Prohibition of imports

(4) Where in any action under this section the court finds that the importation is or the distribution would be contrary to this Act, it may make an order prohibiting the future importation of wares to which the trade-mark, trade-name or indication of origin has been applied.

By whom applications made

(5) Any order under subsection (1) may be made on the application of any person interested either in an action or otherwise and either on notice or ex parte. R.S., c. T-10, s. 52.

APPENDIX V

COPYRIGHT ACT

R.S., 1985, C-42

SEC 27.

INFRINGEMENT OF COPYRIGHT

Infringement of copyright

27. (1) Copyright in a work shall be deemed to be infringed by any person who, without the consent of the owner of the copyright, does anything that, by this Act, only the owner of the copyright has the right to do.

Acts not constituting infringement of copyright

(2) The following acts do not constitute an infringement of copyright:

(a) any fair dealing with any work for the purposes of private study, research, criticism, review or newspaper summary;

(b) where the author of an artistic work is not the owner of the copyright therein, the use by the author of any mould, cast, sketch, plan, model or study made by the author for the purpose of the work, if he does not thereby repeat or imitate the main design of that work;

(c) the making or publishing of paintings, drawings, engravings or photographs of a work of sculpture or artistic craftsmanship, if permanently situated in a public place or building, or the making or publishing of paintings, drawings, engravings or photographs that are not in the nature of architectural drawings or plans, of any architectural work of art;

(d) the publication in a collection, mainly composed of non-copyright matter, intended for the use of schools, and so described in the title and in any advertisements issued by the publisher, of short passages from published literary works not themselves published for the use of schools in which copyright subsists, if not more than two of the passages from works by the same author are published by the same publisher within five years, and the source from which the passages are taken is acknowledged;

(e) the publication in a newspaper of a report of a lecture delivered in public, unless the report is prohibited by conspicuous written or printed notice affixed before and maintained during the lecture at or about the main entrance of the building in which the lecture is given, and, except while the building is being used for public worship, in a position near the lecturer, but nothing in this paragraph affects the provisions in paragraph (a), as to newspaper summaries;

(f) the reading or recitation in public by one person of any reasonable extract from any published work;

(g) the performance without motive of gain of any musical work at any agricultural, agricultural-industrial exhibition or fair that receives a grant from or is held under federal, provincial or municipal authority, by the directors thereof;

(h) the reproduction of a manuscript, original document, archive, photographic positive or negative, cinematograph film or sound recording for deposit in an institution pursuant to a direction under section 14 of the Cultural Property Export and Import Act;

(i) the disclosure, pursuant to the Access to Information Act, of a record within the meaning of that Act, or the disclosure, pursuant to any like Act of the legislature of a province, of like material; and

(j) the disclosure, pursuant to the Privacy Act, of personal information within the meaning of that Act, or the disclosure, pursuant to any like Act of the legislature of a province, of like information.

Further exceptions

(3) No church, college or school and no religious, charitable or fraternal organization shall be held liable to pay any compensation to the owner of any musical work or to any person claiming through that author by reason of the public performance of any musical work in furtherance of a religious, educational or charitable object.

Infringement by personal action

(4) Copyright in a work shall be deemed to be infringed by any person who

(a) sells or lets for hire, or by way of trade exposes or offers for sale or hire,

(b) distributes either for the purposes of trade or to such an extent as to affect prejudicially the owner of the copyright,

(c) by way of trade exhibits in public, or

(d) imports for sale or hire into Canada,

any work that to the knowledge of that person infringes copyright or would infringe copyright if it had been made within Canada.

Public performance for private profit without owner's consent

(5) Copyright in a work shall be deemed to be infringed by any person who for his private profit permits a theatre or other place of entertainment to be used for the performance in public of the work without the consent of the owner of the copyright, unless that person was not aware, and had no reasonable ground for suspecting, that the performance would be an infringement of copyright.

Restriction on paragraph (2)(i) or (j)

(6) Nothing in paragraph (2)(i) or (j) authorizes any person to whom a record or information is disclosed to do anything that, by this Act, only the owner of the copyright has a right to do. R.S., c. C-30, s. 17; 1974-75-76, c. 50, s. 47; 1980-81-82-83, c. 111, s. 5; 1984, c. 40, s. 18.

SEC 44.

IMPORTATION OF COPIES

Importation of certain copyright works prohibited

44. Copies made out of Canada of any work in which copyright subsists that if made in Canada would infringe copyright and respecting which the owner of the copyright gives notice in writing to the Department of National Revenue that he desires that the copies not be so imported into Canada, shall not be so imported, and shall be deemed to be included in Schedule IV to the Customs Tariff, and that Schedule applies accordingly. R.S., c. C-30, s. 27.

SEC 45.
No importation where right or licence to reproduce in Canada granted

45. (1) Where the owner of the copyright has by licence or otherwise granted the right to reproduce any book in Canada, or where a licence to reproduce the book has been granted under this Act, it shall not be lawful except as provided in subsections (3) and (4) to import into Canada copies of the book, and the copies shall be deemed to be included in Schedule IV to the Customs Tariff, and that Schedule applies accordingly.

Notice required of intention to import

(2) Except as provided in subsections (3) and (4), it shall be unlawful to import into Canada copies of any book in which copyright subsists until fourteen days after publication thereof and during that period or any extension thereof the copies shall be deemed to be included in Schedule IV to the Customs Tariff, and that Schedule applies accordingly, but if within that period of fourteen days an application for a licence has been made in accordance with the provisions of this Act relating thereto, the Minister may in his discretion extend the period and shall forthwith notify the Department of National Revenue of the extension, and the prohibition against importation shall be continued accordingly.

Exceptions

(3) Notwithstanding anything in this Act, it shall be lawful for any person

(a) to import for his own use not more than two copies of any work published in any country that has adhered to the Convention and the additional Protocol thereto set out in Schedule II;

(b) to import for use by any department of the Government of Canada or any province copies of any work, wherever published;

(c) at any time before a work is printed or made in Canada to import any copies required for the use of any public library or institution of learning; and

(d) to import any book lawfully printed in Great Britain or in a foreign country that has adhered to the Convention and the Additional Protocol thereto set out in Schedule II and published for circulation among, and sale to, the public within either country.

Satisfactory evidence

(4) Any officer of customs may, in his discretion, require any

person seeking to import any work under this section to produce satisfactory evidence of the facts necessary to establish his right so to import.

Application of provisions regarding importation

(5) This section does not apply to any work the author of which is a British subject, other than a Canadian citizen, or the subject or citizen of a country that has adhered to the Convention and the Additional Protocol thereto set out in Schedule II. R.S., c. C-30, s. 28.

APPENDIX VI

COMPETITION ACT

R.S. 1985, C-34

SEC 45.

PART VI
OFFENCES IN RELATION TO COMPETITION

Conspiracy

45. (1) Every one who conspires, combines, agrees or arranges with another person

(a) to limit unduly the facilities for transporting, producing, manufacturing, supplying, storing or dealing in any product,

(b) to prevent, limit or lessen, unduly, the manufacture or production of a product or to enhance unreasonably the price thereof,

(c) to prevent or lessen, unduly, competition in the production, manufacture, purchase, barter, sale, storage, rental, transportation or supply of a product, or in the price of insurance on persons or property, or

(d) to otherwise restrain or injure competition unduly,

is guilty of an indictable offence and liable to imprisonment for a term not exceeding five years or to a fine not exceeding ten million dollars or to both.

Idem

(2) For greater certainty, in establishing that a conspiracy, combination, agreement or arrangement is in contravention of subsection (1), it shall not be necessary to prove that the conspiracy, combination, agreement or arrangement, if carried into effect, would or would be likely to eliminate, completely or virtually, competition in the market to which it relates or that it was the object of any or all of the parties thereto to eliminate, completely or virtually, competition in that market.

Evidence of conspiracy

(2.1) In a prosecution under subsection (1), the court may infer the existence of a conspiracy, combination, agreement or arrangement from circumstantial evidence, with or without direct evidence of communication between or among the alleged parties thereto, but, for greater certainty, the conspiracy, combination, agreement or arrangement must be proved beyond a reasonable doubt.

Proof of intent

(2.2) For greater certainty, in establishing that a conspiracy, combination, agreement or arrangement is in contravention of subsection (1), it is necessary to prove that the parties thereto intended to and did enter into the conspiracy, combination, agreement or arrangement, but it is not necessary to prove that the parties intended that the conspiracy, combination, agreement or arrangement have an effect set out in subsection (1).

Defence

(3) Subject to subsection (4), in a prosecution under subsection (1), the court shall not convict the accused if the conspiracy, combination, agreement or arrangement relates only to one or more of the following:

(a) the exchange of statistics;
(b) the defining of product standards;
(c) the exchange of credit information;
(d) the definition of terminology used in a trade, industry or profession;
(e) cooperation in research and development;
(f) the restriction of advertising or promotion, other than a discriminatory restriction directed against a member of the mass media;
(g) the sizes or shapes of the containers in which an article is packaged;
(h) the adoption of the metric system of weights and measures; or
(i) measures to protect the environment.

Exception

(4) Subsection (3) does not apply if the conspiracy, combination, agreement or arrangement has lessened or is likely to lessen competition unduly in respect of one of the following:

(a) prices,
(b) quantity or quality of production,
(c) markets or customers, or
(d) channels or methods of distribution,

or if the conspiracy, combination, agreement or arrangement has restricted or is likely to restrict any person from entering into or expanding a business in a trade, industry or profession.

Defence

(5) Subject to subsection (6), in a prosecution under subsection (1) the court shall not convict the accused if the conspiracy, combination, agreement or arrangement relates only to the **EXPORT** of products from Canada.

Exception

(6) Subsection (5) does not apply if the conspiracy, combination, agreement or arrangement

(a) has resulted in or is likely to result in a reduction or limitation of the real value of **EXPORTs** of a product;
(b) has restricted or is likely to restrict any person from entering into or expanding the business of **EXPORTing** products from Canada; or
(c) has prevented or lessened or is likely to prevent or lessen competition unduly in the supply of services facilitating the **EXPORT** of products from Canada.
(d) [Repealed, R.S., 1985, c. 19 (2nd Supp.), s. 30]

Defences

(7) In a prosecution under subsection (1), the court shall not convict the accused if it finds that the conspiracy, combination, agreement or arrangement relates only to a service and to standards of competence and integrity that are reasonably

necessary for the protection of the public

(a) in the practice of a trade or profession relating to the service; or

(b) in the collection and dissemination of information relating to the service.

Exception

(7.1) Subsection (1) does not apply in respect of an agreement or arrangement between banks that is described in subsection 49(1).

Exception

(8) Subsection (1) does not apply in respect of a conspiracy, combination, agreement or arrangement that is entered into only by companies each of which is, in respect of every one of the others, an affiliate.

R.S., 1985, c. C-34, s. 45; R.S., 1985, c. 19 (2nd Supp.), s. 30.

SEC 86.

Order directing registration

86. (1) Where, on application by any person, and after affording the Director a reasonable opportunity to be heard, the Tribunal finds that an agreement that the person who has made the application has entered into or is about to enter into is a specialization agreement and that

(a) the implementation of the agreement is likely to bring about gains in efficiency that will be greater than, and will offset, the effects of any prevention or lessening of competition that will result or is likely to result from the agreement and the gains in efficiency would not likely be attained if the agreement were not implemented, and

(b) no attempt has been made by the persons who have entered or are about to enter into the agreement to coerce any person to become a party to the agreement,

the Tribunal may, subject to subsection (4), make an order directing that the agreement be registered for a period specified in the order.

Factors to be considered

(2) In considering whether an agreement is likely to bring about gains in efficiency described in paragraph (1)(a), the Tribunal shall consider whether those gains will result in

(a) a significant increase in the real value of **EXPORTs**; or

(b) a significant substitution of domestic articles or services for imported articles or services.

Redistribution of income does not result in gains in efficiency

(3) For the purposes of paragraph (1)(a), the Tribunal shall not find that an agreement is likely to bring about gains in efficiency by reason only of a redistribution of income between two or more persons.

Conditional orders

(4) Where, on an application under subsection (1), the Tribunal finds that an agreement meets the conditions prescribed by paragraphs (a) and (b) of that subsection but also finds

that, as a result of the implementation of the agreement, there is not likely to be substantial competition remaining in the market or markets to which the agreement relates, the Tribunal may provide, in an order made under subsection (1), that the order shall take effect only if, within a reasonable period of time specified in the order, there has occurred any of the following events, specified in the order:

(a) the divestiture of particular assets, specified in the order;

(b) a wider licensing of patents;

(c) a reduction in tariffs;

(d) the making of an order in council under section 23 of the Financial Administration Act effecting a remission or remissions specified in the order of the Tribunal of any customs duties on an article that is a subject of the agreement; or

(e) the removal of import quotas or import licensing requirements.

R.S., 1985, c. 19 (2nd Supp.), s. 45.

SEC 96.

Exception where gains in efficiency

96. (1) The Tribunal shall not make an order under section 92 if it finds that the merger or proposed merger in respect of which the application is made has brought about or is likely to bring about gains in efficiency that will be greater than, and will offset, the effects of any prevention or lessening of competition that will result or is likely to result from the merger or proposed merger and that the gains in efficiency would not likely be attained if the order were made.

Factors to be considered

(2) In considering whether a merger or proposed merger is likely to bring about gains in efficiency described in subsection (1), the Tribunal shall consider whether such gains will result in

(a) a significant increase in the real value of **EXPORTs**; or

(b) a significant substitution of domestic products for imported products.

Restriction

(3) For the purposes of this section, the Tribunal shall not find that a merger or proposed merger has brought about or is likely to bring about gains in efficiency by reason only of a redistribution of income between two or more persons.

R.S., 1985, c. 19 (2nd Supp.), s. 45.

(EMPHASIS ADDED)

APPENDIX VII

EXCERPTS FROM THE TREATY OF ROME

CHAPTER 2

ELIMINATION OF QUANTITATIVE RESTRICTIONS BETWEEN MEMBER STATES

Article 30

Quantitative restrictions on imports and all measures having equivalent effect shall, without prejudice to the following provisions, be prohibited between Member States.

Article 31

Member States shall refrain from introducing between themselves any new quantitative restrictions or measures having equivalent effect.
This obligation shall, however, relate only to the degree of liberalization attained in pursuance of the decisions of the Council of the Organization for European Economic Cooperation of 14 January 1955. Member States shall supply the Commission, not later than six months after the entry into force of this Treaty, with lists of the products liberalized by them in pursuance of these decisions. These lists shall be consolidated between Member States.

Article 32

In their trade with one another Member States shall refrain from making more restrictive the quotas and measures having equivalent effect existing at the date of the entry into force of this Treaty. These quotas shall be abolished by the end of the transitional period at the latest. During that period, they shall be progressively abolished in accordance with the following provisions.

Article 33

1. One year after the entry into force of this Treaty, each Member State shall convert any bilateral quotas open to any other Member States into global quotas open without discrimination to all other Member States. On the same date, Member States shall increase the aggregate of the global quotas so established in such a manner as to bring about an increase of not less than 20% in their total value as compared with the preceding year. The global quota for each product, however, shall be increased by not less than 10% The quotas shall be increased annually in accordance with the same rules and in the same proportions in relation to the preceding year. The fourth increase shall take place at the end of the fourth year after the entry into force of this Treaty; the fifth, one year after the beginning of the second stage.
2. Where, in the case of a product which has not been liberalized, the global quota does not amount to 3% of the national production of the State concerned, a quota equal to not less than 3% of such national production shall be introduced not later than one year after the entry into force of this Treaty.

This quota shall be raised to 4% at the end of the second year, and to 5% at the end of the third. Thereafter, the Member State concerned shall increase the quota by not less than 15% annually. Where there is no such national production, the Commission shall take a decision establishing an appropriate quota.

3. At the end of the tenth year, each quota shall be equal to not less than 20% of the national production.

4. If the Commission finds by means of a decision that during two successive years the imports of any product have been below the level of the quota opened, this global quota shall not be taken into account in calculating the total value of the global quotas. In such case, the Member State shall abolish quota restrictions on the product concerned.

5. In the case of quotas representing more than 20% of the national production of the product concerned, the Council may, acting by a qualified majority on a proposal from the Commission, reduce the minimum percentage of 10% laid down in paragraph 1. This alteration shall not, however, affect the obligation to increase the total value of global quotas by 20% annually.

6. Member States which have exceeded their obligations as regards the degree of liberalization attained in pursuance of the decisions of the Council of the Organization for European Economic Cooperation of 14 January 1955 shall be entitled, when calculating the annual total increase of 20% provided for in paragraph 1, to take into account the amount of imports liberalized by autonomous action. Such calculation shall be submitted to the Commission for its prior approval.

7. The Commission shall issue directives establishing the procedure and timetable in accordance with which Member States shall abolish, as between themselves, any measures in existence when this Treaty enters into force which have an effect equivalent to quotas.

8. If the Commission finds that the application of the provisions of this Article, and in particular of the provisions concerning percentages, makes it impossible to ensure that the abolition of quotas provided for in the second paragraph of Article 32 is carried out progressively, the Council may, on a proposal from the Commission, acting unanimously during the first stage and by a qualified majority thereafter, amend the procedure laid down in this Article and may, in particular, increase the percentages fixed.

Article 34

1. Quantitative restrictions on exports, and all measures having equivalent effect, shall be prohibited between Member States.

2. Member States shall, by the end of the first stage at the latest, abolish all quantitative restrictions on exports and any measures having equivalent effect which are in existence when this Treaty enters into force.

Article 35

The Member States declare their readiness to abolish quantitative restrictions on imports from and exports to other Member States more rapidly than is provided for in the preceding Articles, if their general economic situation and the situation of the economic sector concerned so permit.

To this end, the Commission shall make recommendations to the Member States concerned.

Article 36

The provisions of Articles 30 to 34 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 archaeological 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.

Common rules

CHAPTER 1

RULES ON COMPETITION

Section 1

Rules applying to undertakings

Article 85

1. The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market, and in particular those which:

(a) directly or indirectly fix purchase or selling prices or any other trading conditions;

(b) limit or control production, markets, technical development, or investment;

(c) share markets or sources of supply;

(d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

(e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

2. Any agreements or decisions prohibited pursuant to this Article shall be automatically void.

3. The provisions of paragraph 1 may, however, be declared inapplicable in the case of:

- any agreement or category of agreements between undertakings;
- any decision or category of decisions by associations of undertakings;
- any concerted practice or category of concerted practices;

which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not:

(a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives;

(b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

Article 86

Any abuse by one or more undertakings of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market in so far as it may affect trade between Member States.

Such abuse may, in particular, consist in:

(a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions;

(b) limiting production, markets or technical development to the prejudice of consumers;

(c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

(d) making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

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NOTES

1. In some instances, it is possible to argue that such rights have been devised by the courts as an adjunct to legislation.

2. For example, the Sony acquisition of Columbia Pictures and CBS Records, as well as the Matsushita acquisition of MCA.

3. To be semantically and legally accurate, one ought speak of the doctrine of "implied license" in North America and "exhaustion" in Europe. See Chapter I and the Glossary. However, the general phenomenon being discussed in this paper is routinely referred to as "exhaustion" and this term will be so used, unless otherwise qualified.

4. Price discrimination is a motive for market segmentation that recurs throughout the more sophisticated and/or economically oriented literature on this subject. For example, see Simon Horner, Parallel Imports, London, 1987, Collins, p. 2

5. Patent Act, R.S.C, c. P-45.

6. Trade-marks Act, R.S.C, c. T-13.

7. Copyright Act, R.S.C, c. C-42.

8. Competition Act, R.S.C., c. C-34.

9. H.J. Heinz Co. of Canada v. Edan Foods Sales Inc., (1991) 35 C.P.R. (3d) 213

10. Nestlé Enterprises v. Edan Food Sales Inc., 37 C.P.R. (3d) 480.

11. Tariff Act of 1930, 19 U.S.C., s. 1337 (the "Smoot-Hawley" Act).

12. See, for example, Christopher Morcom, Q.C., "A Long Wait for Unitary EC Trade Mark", The Times January 29, 1992

13. The notable exception is found in the Integrated Circuit Protection Act, C. I-14.6, s. 6(3). This enactment expressly provided for exhaustion because it

was generally recognized that an importation right without qualification could readily be abused to impede international trade in an item such as a television set or a computer, simply because one of the many hundreds of chips involved, which may have a value of only a few pennies or a few dollars each at the most, might be a parallel import as opposed to an authorized import.

14. Gordon F. Henderson, Intellectual Property: Litigation, Legislation and Education, CCAC, Ottawa, 1991, pp. 69-71 and 98-99.

15. Patent Act, R.S.C. 1985, c. P-4, s. 42.

16. Wellcome Foundation Ltd. v. Apotex Inc., (1990) 32 C.P.R. (3rd) 350, FCTD, per Muldoon, J., applying in turn Société des Usines Chimiques Rhône-Poulenc v. Jules R. Gilbert Ltd. , (1967) Fox Pat. C. 174, affd. 55 C.P.R. at p. 209 and [1968] S.C.R. 950.1

17. W. Hayhurst, Intellectual Property as a Non-Tariff Barrier, (1991) 31 C.P.R. 289 at 300.

18. Betts v. Wilmott, (1871) L.R. 6 Ch.App. 239

19. (1871) L.R. 6 Ch. App. 239 at 245.

20. See Taddy v. Sterious, [1904] 1 Ch 354.

21. North American Systemshops Ltd. v. King, [1989] A.J. No. 512 . "Shrink wrap" licenses are those that are contained inside a package or in some other way (such as very small print) that are unlikely to represent a meeting of the minds in a contractual sense. Typically, the printing on the package declares that by opening the package, the customer is deemed to have agreed to the conditions spelled out in the license. There s virtually no law, other than this case, directly on point in Canada and this case is considered an aberration for reasons that are not relevant here. State laws in the USA to validate shrink wrap licenses have been held to be unconstitutional, since they are "preempted" by U.S federal copyright law.

22. For example, see Fletcher v. Manitoba Public Insurance Co., [1990] 3 S.C.R. 191

23. Badische Anilin und Soda Fabrik v. Isler, (1906) 23 R.P.C. 173 at 180.(Ch. D.). as cited by Hayhurst, 31 C.P.R. (3d) 289 at 301.

24. W.L. Hayhurst, Intellectual Property: Emerging Issues, Published by ITAC & CADAPSO, Toronto, 1990, p. 15.

25. W. Hayhurst, Intellectual Property as a Non-Tariff Barrier to Trade, (1991) 31 CPR (3d) 289 at 299.

26. Hayhurst, op.cit., at 302.

27. G.F. Henderson, Intellectual Property (1991), p. 69. See also Horner, Parallel Import, p. 46-47.

28. See G.F. Henderson, Intellectual Property: Litigation, Legislation, and Education- a Study of the Canadian Intellectual Property and Litigation System, Consumer and Corporate Affairs Canada, March 5, 1991, p. 124. See also R.Stern, Parallel Importation of Copyrighted Products into the US, [1989] 4 EIPR 119, discussed below in more detail in Appendix I.

29. Hayhurst, 31 C.P.R. (3d) 289 at 302.

30. Hayhurst, 31 C.P.R. (3d) 289 at 301, note #5.

31. See Competition Act, as amended, s. 32. See D.W. Henry, Patents in Relation to the Combines Investigation Act, PTIC Bulletin, Series No. 7, V. 17, July 1966, 1 at page 9; Dominion Rubber v. Max Propas et al., (1963) 41 C.P.R. 194 (Ex. Ct); and R. Union Carbide Limited, Minutes of Settlement in the Exchequer Court of Canada, Dec. 9, 1969 and June 19, 1971 and the Annual Report of the Director of Investigation and Research for the years ending March 31, 1970 and March 31, 1972.

32. Competition Act, R.S.C. 1985, (3rd Supp) s. 32. See D.W.Henry, Patents in Relation to the Combines Investigation Act, PTIC Bulletin, Series 7, v.17, July, 1966, p.2.

33. Pindoff v. CBS Record Sales Inc., (1989) 27 C.P.R. (3d), 380 (Ont. H.C.J.)

34. H. G. Fox, The Canadian Law and Practice Relating to Letter Patents of Inventions, Carswell, 1969, p. 541.

35. The only economic examination involving actual data --- and the data is limited -- that examines patents and the exhaustion issue in Canada is that of S. Globerman, Canada's Interest in Two Way Exhaustion in Trade with the USA, CCAC, Mimeo, 1987. Globerman's conclusions are somewhat ambiguous. He feels that exhaustion would improve allocative efficiency in Canada "on the margin" with respect to patent law (p. 55), but that,apart form the chemical industry, there is little conclusive evidence of price discrimination arising as a result of patent law. He does not deal with the local manufacturing legal requirements.

36. See Trade-marks Act, s. 52 included in Appendix IV.

37. See ss. 44 and 45 of the Copyright Act, R..S., c. C-30.

38. For a detailed analysis of the earlier cases up to and including Seiko, the reader is advised to consult analyses such as R. Barrigar, Grey Marketing in Canada: The Seiko Case, (1985) 1 I.P.J 109 and W. Hayhurst, Importation of Grey Goods Into Canada", (1986) 2 I.P.J. 23..

39. Remington Rand Limited v. Transworld Metal Company Limited [1960] Ex. C. R. 463

40. [1960] Ex. C.R. 463 at 464. R. Barrigar seems to imply that the Remington case might be decided differently today, given the apparently identical labelling on identical products sold by two different entities. He made this point in a comment on Seiko which also noted (prescient of the Heinz decision) that a plaintiff's case would be "considerably better if the goods sold in Canada are non-equivalent in some way to comparable goods sold under the same trade-mark in other countries". See R. Barrigar, Grey Marketing in Canada: the Seiko Case, (1985) 1 I.P.J. 109 at 133 ff.

41. 1960 Ex. C.R. 463 at 465.

42. Wilkinson Sword (Canada) Ltd. v. Juda, [1967] Fox Pat. C., 77

43. Ulay (Canada) v. Calstock Traders Ltd., (1969) 59 C.P.R. 223.

44. ibid. p. 225.

45. ibid. p.234

46. ibid. p. 235.

47. ibid. p. 238.

48. ibid. p. 139.

49. It is cited in other contexts. See Rowell Laboratories, Inc. et al. v. ICN Canada Ltd., (1986), 10 C.P.R. (3d) 78 and Dominion Dairies Ltd. et al. v. The Borden Co., Ltd., (1978) 41 C.P.R. (2d) 185.

50. Breck's Sporting Goods v. Magder, [1976] 1 S.C.R. 527.

51. [1976] S.C.R. 527 at 539.

52. See, for example, S.C. Johnson v. Marketing International, 1980 1 S.C.R. 99, Philip Morris Inc. v. Imperial Tobacco Ltd. (No. 2), (1987) 17 C.P.R. (3d) 237 (C.A.), Philip Morris Inc. v. Imperial Tobacco Ltd. (No. 1), (1987) 17 C.P.R. (3d) 289 , Orkin Exterminating Co. Inc. v. Pestco Co. of Canada Ltd. (1985) 50 O.R. (2d) 726, and the recent decision of White Consolidate v. Beam of Canada, FCTD Action # T-343-90, [1991] F.C.J. No. 1076.

53. See Hayhurst, Intellectual Property as a Non-Tariff Barrier, (1990) 31 C.P.R. (3d) 289.

54. Coke Would Like the World to See the Same Ads, Globe and Mail, Report on Business, Nov. 21, 1991, p. B4.

55. Given the myriad of Canadian labelling, environmental, and other laws, not to mention freight costs and the highly structured and localized nature of the bottling industry, it is unlikely that American made Coke would find its way into Canada in commercial quantities via the grey market. Similar conditions would likely obtain in most countries, with the exception that language requirements for labelling might not be so restrictive elsewhere. In any case, even in Canada, language requirements for labels can generally be complied with by adding a sticker with the correct wording.

56. Consumers Distributing v. Seiko Time Canada, (1984) 10 D.L.R. (4th) 161. For detailed commentary, see H. Knopf, Seiko v. Consumers Distributing: More Shades of Grey Marketing Law, 1 I.P.J. (Intellectual Property Journal) 337, June, 1985

57. Erven Warnink BV et al. v. J. Townend & Sons (Hull) Ltd. [1979] 2 All E.R. 927, (House of Lords). The well-known five-fold test for passing-off is stated by Lord Diplock:
(1) a misrepresentation (2) made by a trader in the course of trade, (3) to prospective customers of his or ultimate consumers of goods or services supplied by him, (4) which is calculated to injure the business or goodwill of another trader (in the sense that this is a reasonably foreseeable consequence) and (5) which causes actual damage to a business or goodwill of the trader by whom the action is brought or (in a quia timet action) will probably do so. (pp. 929-33)

58. (1984) 10 D.L.R. (4th) 161 at 181.

59. (1984) 10 D.L.R. (4th) 161 at 181.

60. See Seiko v. Consumers, (1984) 10 D.L.R. (4th) 161.

61. Trade Marks Act, R.S.C. 1970, c.T-10. Judgment, p. 184. There is also a broad hint at a trade marks action at (1984) 10 D.L.R. (4th) 161 at 179.

62. cf. S.C. Johnson & Son ltd. v. Marketing International Ltd., 105 D.L.R. (3rd) 423.

63. Trade Marks Act, R.S.C. 1970, c.T-10 , s. 49(4). This particular point may be hinted at in the reference by Estey, J. to Fox, Canadian Law of Copyright, p. 440-441 at p. 184 of the judgment. Otherwise, the reference to copyright jurisprudence in this context is extremely difficult to understand.

64. (1980) 29 O.R. 2nd 211 at 240.

65. Judgment, p. 175. See also Breck's Sporting Goods v. Magder, [1976] 1 S.C.R. 527 at 534. See also, Horner, Parallel Imports, p. 23.

66. These cases are all cited and discussed below. As well, there was a potentially important action launched by Kraft, discussed below, which was settled at an early stage.

67. Sharp Electronics of Canada Ltd. v,Continental Electronic Info. Inc., (1988) 23 C.P.R. 3rd 330.

68. 23 C.P.R. 3rd at 336.

69. American Cyanamid v. Ethicon, [1975] A.C. 396 (H. of L.); Turbo Resources v. Petro-Canada, [1989] 2 FCR 451, 24 C.P.R. 3rd 1, and Yule Inc. v. Atlantic Pizza Delight (1968) Ltd., (1977) 35 C.P.R. (2nd) 273. Turbo Resources Ltd. v. Petro-Canada Ltd., [1989] 2 F.C.R. 451, 24 C.P.R. (3d) 1; and Syntex v. Novopharm, (1991) 36 C.P.R. (3d) 129 at 136.

70. 23 C.P.R. (3d) 337.

71. See C.S.A. product classifications #3861-01 and #3861-02.

72. See Business on Sunday News Page 006, US minds its own business , Larry Black, The Independent, February 16, 1992 and January 2, 1991 p. 23, International Boat Show, Tim Jeffrey, Daily Telegraph.

73. It would seem that in Europe, under the doctrine of "Measures of Equivalent Effect" and Article 30 et seg. of the Treaty of Rome, such electrical safety standards would be subject to review as to their legitimacy on the evidence as to whether they were truly justifiable. See P. Oliver, Free Movement of Goods in the E.E.C., London, European Law Centre Limited, 1988, p. 62 ff. , 197 ff. 208 ff.

74. Mattel Canada Inc. v. GTS Acquisitions and Nintendo of America Inc., (1989) 27 C.P.R. 3rd 358.

75. 27 C.P.R. (3d) 362.

76. 27 C.P.R. (3d) 365.

77. 27 C.P.R. (3rd) 359 ff.

78. [1976] 1 S.C.R. 527 at 534.

79. There is an excellent and timely comment on the Mattel case by Dan Bereskin in an article generally dealing with trade-marks as a potential barrier to free trade. See D. Bereskin, THE CANADA - UNITED STATES FREE TRADE AGREEMENT: ARE TRADEMARKS A BARRIER TO FREE TRADE?, 80 TMR 272. Bereskin feels that Mattel was wrongly decided. He adopts the traditional classification of two streams of grey goods cases.

80. Colgate Palmolive Company v. Markwell Finance Ltd., 17 RPC 497 (1987).

81. Castrol v. Automotive Oil supplies Ltd.., [1983] P.R.C. 315 (Ch.D).

82. See Hayhurst, Intellectual Property as a Non Tariff Barrier in Canada, (1990) 31 C.P.R. (3d) 289 at 309.

83. Champagne Heidsieck et Cie Monopole S.A. v. Buxton, 47 RPC 28 (1930).

84. Bereskin, op.cit. p. 281.

85. Ibid. at 283.

86. H.J. Heinz Co. of Canada v. Edan Foods Sales Inc., (1991) 35 C.P.R. (3d) 213

87. Remington Rand Limited v. Transworld Metal Company Limited [1960] Ex. C.R. 463.

88. See Philip Morris Inc. v. Imperial Tobacco Ltd. (No. 1), (1987) 17 C.P.R. (3d) 289 (FCA).

89. See "Ketchup Maker Sees Red", Globe and Mail, report on Business, March 11, 1991.

90. See Manhattan Industries v. Princeton Manufacturing, (1971) 4 C.P.R. 2nd 6 re the "use" of a mark where the are sold f.o.b. the U.S.A. for the Canadian market. Note the editorial note to this report wherein the editor indicates that "The question is not who is using the mark but whose mark is being used."

91. See Appendix IV.

92. Charles Heintzman v. 751056 Ontario Limited et al, (1990) 34 C.P.R. (3d) 1 (FCTD).

93. ibid.

94. There is some sign that the Federal Court is normalizing the criteria for injunctions in intellectual property cases. See Syntex v. Novapharm, cited below.

95. The most recent Federal Court important pronouncement on injunctions can be found in Apotex Inc.. v. Syntex Inc. (F.C.A.) Federal Court Judgments: [1991] F.C.J. No. 423, Action No. A-517-89

96. Heinz (Canada) holds about 70% of the Canadian market share for ketchup. Heinz (US), its parent, has about 50% of the U.S. ketchup market. See Respondent's

memorandum of Fact and Law, para. # 20.

Heinz (Canada) has annual sales of $550 million and 1,500 employees. Heinz (US) has annual sales of $6.5 billion and about 39,000 employees. See Respondent's memorandum of Fact and Law, para. #9.

The Canadian ketchup market appears to be worth $70,000,000 per annum, divided 70% for retail and 30% for food service sales. See Respondents memorandum of Fact and Law, para. # 21.

97. Nestlé Enterprises v. Edan Food Sales Inc., (1991) 37 C.P.R. (3d) 480.

98. Trade Marks Act, R.S.C. 1970, c.T-10 , s. 49(4).

99. See Kraft General Foods Canada Inc. v. Edan Food Sales Inc., FCTD T- 1935-91. The Statement of Claim was filed on July 24, 1991 and the action was discontinued on October 30, 1991.

100. Gordon F. Henderson, Intellectual Property: Litigation, Legislation and Education, CCAC 1991, p. 22 ff.

101. (1986) 17 C.P.R. (3rd) 73, per Savoie, J., Quebec Superior Court.

102. (1991) 39 C.P.R. (3rd) 1, per LeBel, J., Quebec Superior Court. See also Sony du Canada v. Multitronic Stereo Inc., Quebec Court of Appeal, October 22, 1991, no. 500 -09-000728-915.

103. Insurance Corporation of British Columbia v. Registrar of Trade Marks, (1979) 44 C.P.R. (2d) 1 (FCTD).

104. See Gordon F. Henderson, op.cit., pp. 53, 98.

105. H. Knopf, "New Forms and Fora of Intellectual Property Law", paper presented the 1988 PTIC Annual Meeting at Gray Rocks, St. Jovite, Québec, October 28, 1988, 5 CIPR 247 (1989)

106. Customs Tariff, R.S. c. C-54.01, [R.S. , 1985, c. C-41 (3rd Supp.)]

107. Copyright Act, R.S. 1985, s. 27(4) See D. Card, Parallel Importation of Copyright Property: A Proposal to Amend the Canadian Copyright Act,(1990) 6 I.P.J. 97.

108. So named after a former Deputy Minister of National Revenue.

109. A recent case involving books is that of Les Dictionnaires Robert v. Librairie du Nomade, (1987) 16 C.P.R. (3rd) 319.

110. Canada (Director of Investigation and Research, Competition Act) v. Laidlaw Waste Systems Ltd., Decision: January 20, 1992, unreported p. 49 of typed reasons.

111. Feist Publications Inc., Petitioner v. Rural Telephone Service Co. Inc., 1991 WL 39298 (U.S.), U.S. Supreme Court. Decided March 27, 1991

112. See Exxon Corporation v. Exxon Insurance Consultants International Limited, [1981] 5 All E.R. 241 at 247 (C.A.)

113. Sebastian International, Inc. v. Consumer Contacts (Pty) Ltd., (1988) 847 F.2d 1093

114. Dennison Manufacturing v. MNR, (1987) 15 C.P.R. 3rd, 67

115. Mattel v. GTS Acquisitions and Nintendo of America, (1989) 27 C.P.R. (3d) 358

116. Beamscope Canada Inc. v. 2439-0692 Quebec Inc., Federal Court Judgments: [1991] F.C.J. No. 441

117. Clarke Irwin v. C. Cole & Co. Ltd., [1960] O.R. 117, Godfrey, MacSkimmings & Bacque v. Coles Book Stores Ltd., (1973) 1. O.R. (2nd) 362, McLelland and Stewart v. Coles Books Ltd., (1974) 7 O.R. 2nd 426 (which shows some of the difficulties with ss. 44 and 45 of the Copyright Act)

118. See Communications Canada Press release dated January 28, 1992.

119. Minister Beatty, speaking notes for news conference of January 28, 1992, p. 5

120. Interestingly, the Australian Government has just gone completely in the other direction, and has enacted copyright measures that permit parallel importation of books unless they are published in Australia within a

certain periods of time. This was in response to prolonged controversy about unnecessarily high book prices in Australia. The Australian development is dealt with in Chapter II below.

121. Holiday v. Matheson, 24 Fed. 185 (S.D.N.Y. 1885).

122. Kabushiki Kaisha Hattori Seiko v. Refac Technology Dev. Corp., 690 F. Supp. 1339, 1343, 9 U.S.P.Q. 2nd 1046, as cited by Peter D. Rosenberg, Patent Law Fundamentals, Clark Boardman, New York, N.Y., 1991, Section 18.09, p. 18-32.

123. Rosenberg, loc.cit.

124. See General Talking Pictures v. Western Electric, 304 U.S. 175 (1938) as cited by Carvill, et. al., Patents and Antitrust Overview, PLI Patent Antitrust 1989, p. 120.

125. See U.S. v Imperial Chemical Industries, 100 F. Supp. 504 (SDNY) 1959), Timken Roller Bearings v. U.S., 341 US 593 (1950) U.S. v. Sealy, 388 U.S. 350 (1967). See also Adams v. Burke, 17 Wall. 453 (19883), Hobbie v. Jennison, 149 U.S. 355 (1893), Kelly v. Standard Folding Bed, 157 U.S. 659 (1895) for early cases on "first sale" as cited by T.A. Dieterich, Interrelationships Between Federal Antitrust laws and Industrial Property, Patent Antitrust 1989, Practising Law Institute, N.Y., p.35.

126. 433 U.S., 36 (1977). See also L.J. Lafaro, Innovation and Antitrust, PLI Patent Antitrust 1989, p. 354.

127. David Bender, Gray Market Goods and the Antitrust Laws, Bender et al., in Gray Market Goods and Importation, Practising Law Institute, N.Y., N.Y., 1986, 303 at 311.

128. Bender. op.cit., at 331.

129. 19 U.S.C., s. 1337.

130. Rosenberg, op.cit., p. 18-33.

131. Bender, op.cit., 321.

132. Bender and Gerber, Gray Markets and Parallel Importation: Protectionism v. Free Trade, Practising Law Institute, NYC, 1986.

133. 108 S. Ct. 1811.

134. 27 F. 18 (S.D.N.Y. 1886).

135. _ibid._ p. 21.

136. S. Lippner, _The Legal and Economic Aspects of Gray Market Goods_, 1990, Quorum Books, Westport, CT., U.S.A., p. 14.

137. See Appendix I of this work, and, generally, Bereskin, _op.cit._

138. _A. Bourjois & Co., Inc. v Katzel_, 260 U.S. 689 (1923).

139. 260 U.S. at 692.

140. Lippner, _op.cit._, p.18.

141. _U.S. v. Guerlain_, 155 F. Supp., 77 (S.D.N.Y) 1957). vacated and remanded, 358 U.S. 915 (1958), action dismissed, 172 F. Supp. 107 (S.D.N.Y 1959).

142. Vacated and remanded, 358 U.S. 915 (1958), action dismissed, 172 F. Supp. 107 (S.D.N.Y 1959). See _Lippner_, _op.cit_, p. 21 ff. and chapters 4 and 5.

143. U.S. _Trademark Act_ of 1946.

144. 19 CFR 133.21

145. 15 U.S.C. 1124

146. 19 U.S.C. 1526

147. _K Mart Corp. v. Cartier_; _47th Street Photo Inc. v. Copiat_; _U.S. v. Copiat_, 108 S.Ct., 1811.

148. 790 F.2d 903

149. 598 F.Supp. 844

150. 598 F.Supp. 844 at 852.

151. 486 U.S. 281 at 286

152. 486 U.S. 281 at 293

153. As might be expected, three are dozens of excellent articles. One of the best is by V. Palladino. See V. Palladino, _Gray Market Goods: The United States Trademark Owners' View_ , 79 TMR 158. Lippner's book, cited elsewhere in this chapter, is also very useful.

154. Senator Hatch, 134 Cong. Rec. S17042, Oct. 20, 1988.

155. For example, see V. Palladino, Gray Market Goods: The United States Trademark Owners' View, 79 TMR 158 at 208.

156. See PTCJ April 12, 1990.

157. 877 F. 2d 101 (1989)

158. 877 F.2d 101 at 111.

159. Lever Brothers Company v. United States of America April 15, 1992, 1992 WL 130830 (D.D.C.), 796 F. Supp.1, 21 USPQ (2d) 1297.

160. Customs Service: Customs Suspends Affiliate Exception for Physically Different Gray Goods, (Issue No. 1088), BNA's Patent, Trademark & Copyright Journal, News & Comment, July 02, 1992

161. 878 F.2d 659

162. 878 F.2d 659 at 668 Fn. 11

163. 877 F.2d 101 at 109.

164. 1992 WL 72005 (D.C.Cir.), decided April 14, 1992.

165. 1992 WL 72005 at p. 7

166. 1992 WL 72005 at p. 13.

167. Yamaha Corp. of America v. ABC International Traders Inc. (91-1066), which appeals an unpublished Ninth Circuit opinion affirming the dismissal of claims under 19 USC 526 on the ground that a wholly owned subsidiary of a foreign manufacturer is not entitled to protection against unauthorized imports of genuine goods. See the district court's opinion at 703 F.Supp. 1398.

168. 17 U.S.C. 101 et seq.

169. Title 17, U.S. Code:

s 106. Exclusive rights in copyrighted works

Subject to sections 107 through 120, the owner of copyright under this title has the exclusive rights to do and to authorize *any of the following:*

(1) to reproduce the copyrighted work in copies or phonorecords;

(2) to prepare derivative works based upon the copyrighted work;

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

(4) in the case of literary, musical, dramatic, and choreographic works, pantomimes, and motion pictures and other audiovisual works, to perform the copyrighted work publicly; and

(5) in the case of literary, musical, dramatic, and choreographic works, pantomimes, and pictorial, graphic, or sculptural works, including the individual images of a motion picture or other audiovisual work, to display the copyrighted work publicly.

(Pub.L. 94-553, Title I, s 101, Oct. 19, 1976, 90 Stat. 2546.)

(As amended Pub.L. 101-318, s 3(d), July 3, 1990, 104 Stat. 288; Pub.L. 101- 650, Title VII, s 704(b)(2), Dec. 1, 1990, 104 Stat. 5134.)

s 602. Infringing importation of copies or phonorecords

(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. This subsection does not apply to--

(1) importation of copies or phonorecords under the authority or for the use of the Government of the United States or of any State or political subdivision of a State, but not including copies or phonorecords for use in schools, or copies of any audiovisual work imported for purposes other than archival use;

(2) importation, for the private use of the importer and not for distribution, by any person with respect to no more than one copy or phonorecord of any one work at any one time, or by any person arriving from outside the United States with respect to copies or phonorecords forming part of such person's personal baggage; or

(3) importation by or for an organization operated for scholarly, educational, or religious purposes and not for private gain, with respect to no more than one copy of an audiovisual work solely for its archival purposes, and no more than five copies or phonorecords of any other work for its library lending or archival purposes, unless the importation of such copies or phonorecords is part of an activity consisting of systematic reproduction or distribution, engaged in by such organization in violation of the provisions of section 108(g)(2).

(b) In a case where the making of the copies or phonorecords would have constituted an infringement of copyright if this title had been applicable, their importation is prohibited. In a case where the copies or phonorecords were lawfully made, the United States Customs Service has no authority to prevent their importation unless the provisions of section 601 are applicable. In either case, the Secretary of the Treasury is authorized to prescribe, by regulation, a procedure under which any person

claiming an interest in the copyright in a particular work may, upon payment of a specified fee, be entitled to notification by the Customs Service of the importation of articles that appear to be copies or phonorecords of the work.

(Pub.L. 94-553, Title I, s 101, Oct. 19, 1976, 90 Stat. 2589.)

170. *s. 109. Limitations on exclusive rights: Effect of transfer of particular copy or phonorecord (a) Notwithstanding the provisions of section 106(3), the owner of a particular copy or phonorecord lawfully made under this title, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy or phonorecord.*

171. Hearst Corp. v. Stark, 639 F. Sup. 970

172. CBS Inc. v. Scorpio Music Distributors, 738 F.2d 424. See also T.B. Harms v. Gem Records, 655 F. Supp. 1575 (D.N.J. 1987)

173. (1988) 847 F.2d 1093 (U.S. Court of Appeals for the Third Circuit).

174. 847 F.2d 1093 at 1094.

175. 569 F. Supp. 47 (E.D. Pa. 1983). Also followed in BMG v. Perez, 9th Circuit, CA (No. 8953618, 12/24/91).

176. 847 F.2d 1093 at 1099.

177. 847 F.2d 1093 at 1099 (emphasis added). Lippner states, somewhat enigmatically, that "Judge Weiss's invitation to Congress to address the issue is sound advice but might be written off as wishful thinking." See Lippner, op.cit, p. 160.

178. (1989) 9 U.S.P.Q.2d 1901, reversed in 11 U.S.P.Q.2d 1548 on other grounds.

179. Duracell Inc. v. U.S. International Trade Commission, 778 F.2nd 1578 (Fed.Cir. 1985).

180. In the Matter of Certain Alkaline Batteries U.S. International Trade Commission No. 337-TA-165 Decided Nov. 5, 1984,

The appropriate question in a section 337 case is not whether the parent company is injured but

whether an industry in the United States is injured by respondents' unfair acts. Section 337 states that unfair methods of competition are unlawful under section 337 when their "effect or tendency * * * is to destroy or substantially injure an industry, efficiently and economically operated, in the United States * * * ." Thus it is irrelevant that the lost sales are to Duracell Belgium and that Duracell is benefited by those sales. The health of Duracell U.S.A. is intertwined with the goodwill of the U.S. mark. To the extent that Duracell has been deprived of the benefits of its goodwill, which it is legally entitled to, e.g., profits, it has been injured. See p. 13 of Westlaw reasons.

181. 50 Fed.Reg. 1,655 (Jan. 11, 1985).

182. Duracell, Inc. v. U.S. International Trade Commission Court of Appeals, Federal Circuit No. 85-2072 Decided December 9, 1985, 778 F.2d 1578, 54 U.S.L.W. 2332, 7 ITRD 1529, 4 Fed. Cir. (T) 29

183. 778 F.2d 1578 at 1581

184. See EMI Records Limited CBS United Kingdom Limited, 18 Comm. Mkt. L.R. 235 (1976)

185. R. Swift, Panel on Grey Market Goods, EEC Position, USTA Meeting in Toronto, Canada, May, 1992, p. 5. He states that , in the case of the UK at present, goods put on the market anywhere in the world by or with the consent of the intellectual property right owner, as long as they are legitimate, can be imported into the UK **"unless the circumstances of the first marketing made it clear that no consent was given for the use of the UK rights** Colgate v. Markwell [1989] RPC 497. This case is also discussed in Chapter I of this work.

186. Pharmon BV v. Hoechst AG, [1985] E.C.R. 2281

187. See the discussion of the Haq I and Haq II cases below.

188. First Council Directive of 21 December 1988 to approximate the laws of the member states relating to trade marks (89/104/EEC) *Article 7 Exhaustion of the rights conferred by a trade mark 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.*

189. H. Smit, The Relation of Intellectual Property Rights to Cross-Border Trade in the EEC, Canada- United States Law Journal, V. II, 1986, 69.

190. Two very good articles are these. F-K Beier, **Industrial Property and the Free Movement of Goods in the Internal European Market**, IIC v. 21, p 1131 (1990) and H. Smit, The Relation of Intellectual Property Right to Cross-Border Trade in he EEC, (1986) v. II, Canada-US Law Journal, 69.

191. See Beier, op.cit.,, p. 155.

192. See Pharmon v. Hoechst, 1974 ECR 1183.

193. SA CNL-Sucal NV v. Hag GF AG, [1990] 3 CMLR 571.

194. [1974] ECR 731, 2 CMLR 127.

195. See R. Joliet, Trade Mark Law and the Free Movement of Goods: The overruling of the Judgment in Hag I, IIC c. 22, p. 303. See also W.A. Rothnie, Putting the Common Origin Doctrine to Sleep, [1991] 1 EIPR 25, and C. Morcom, Trademarks in the European Community after Cafe Hag II, 81 TMR 534.

196. EEC Competition Policy in the Single Market, Office for Official Publications of the European Communities, Luxembourg, 1989, p.39.

197. W.R. Cornish, Intellectual Property: Patents, copyright, Trade Marks and Allied Rights, second edition, London, Sweet and Maxwell, 1989, p.20.

198. For example, see After Uruguay, the Economist, February 8, 1992, p. 16

199. Smit, op.cit., p. 79

200. See generally C. Howard, Australian Federal Constitutional Law, second edition, 1972

201. See Bulletin 73 of the Australian Copyright Council, 1991, p. 3 ff.

202. See the Copyright Amendment Act 1991; An Act to Amend the Copyright Act of 1068, No. 174 of 1991, given Royal Assent of November 26, 1991 and effective December 23, 1991. (Australia)

203. As reported in 8 ITR 1818.

204. <u>Publishers Weekly</u>, November 29, 1991.

205. 9 ITR 1818.

206. See Australian Copyright Council Bulletin #73, 1991, p.7.

207. <u>CBS (UK) Ltd. v. Charmdale</u>, [1980] 2 All ER 807.

208. For example, some enterprises are said to knowingly supply the grey market even when such practices are against their corporate policy. See <u>1-Stops: Majors Sidestep Own Export Rules</u>, Billboard Magazine, June 22, 1991.

209. W.L. Hayhurst, <u>Intellectual Property as a Non-Tariff Barrier in Canada</u>, (1990) 31 C.P.R. (3d) 289 at 292 - 293.

210. F. Cespedes, E.R. Corey, and V. Kasturi Ranga, <u>Grey Markets: Causes and Cures,</u> Harvard Business Review, July/August 1988 p. 75

211. See Preamble and Article 102 of the <u>Canada - US Free Trade Agreement</u>.

212. See Gordon F. Henderson, <u>Intellectual Property: Litigation, Legislation and Education</u>, Ottawa, Consumer and Corporate Affairs, 1991, p. 67 ff.

213. i.e. through an exclusive territorial distributorship, franchise, assignment or other commercial arrangement.

214. <u>Distillers v. Commission</u> [1980] ECR 2229.

215. Horner, <u>op.cit</u>., p.3 ff., also p.87.

216. Lippner, <u>op.cit.</u>, p. 75 ff.

217. Lippner, <u>op.cit.,</u> p. 75.

218. For example, see Robert Nozick, <u>Anarchy, State and Utopia</u>, Basic Books, inc., New York, N.Y., 1974, at p. p. 181.

219. See affidavit material in <u>Heinz v. Edan</u>, Court No. T-3228-90, affidavit of E. Gryschuk, dated January 11, 1991, para. 4.

220. See Article 27(1) of the Dunkel text of December 20, 1991.

221. For a pro-Chicago approach, see Anderson, Hughes, Khosla, and Ronayne, Working Paper on intellectual property rights and International Market Segmentation Implications of the exhaustion Principle, CCAC mimeo, Oct. 1990 available from the Economic and International Affairs Branch of the Bureau of Competition Policy, Consumer and Corporate Affairs Canada. Note that this paper does not deal in any specificity with trade-marks issues. For a contrary Canadian economic view, see S. Globerman, Canada's Interest in Two Way Exhaustion of Intellectual Property Rights in Trade with the USA., CCAC mimeo, May 1987. The author of the present study, speaking in his personal capacity, generally takes issue with the "Chicago" approach of his colleagues in the Bureau of Competition Policy on the issues relating to grey marketing. However, this author salutes the scholarship and principled research of his colleagues, even if we are not in agreement on all issues.

222. See Lippner, op. cit., , p. 75, and p. 82 ff.

223. See P. Leslie, The European Community: A Political Model for Canada?, Minister of Supply and Services, Ottawa, 1991, p. 34.

224. 433 U.S. 36

225. See Director of Investigation and Research v. The NutraSweet Company, (1991) 32 C.P.R. (3d) 1. It should be noted that an appeal was sought from this decision by NutraSweet. However, this appeal has now been formally abandoned.

226. See N. Gallini, An Economic Analysis of Grey Market Imports in Canada, November, 1992, prepared for the Bureau of Competition Policy ("BCP"), Economic Policy Division of the BCP Policy Directorate, to be published in the BCP Directorate Discussion Paper series, p. 34 of November, 1992, final draft.

227. See S. Fairley and J. Contini, Lunge, Parry and Riposte: Coping with United States Laws in the Intellectual Property Transactions of Canadians, (1991) 9 C.I.P.R. 126.

228. See also the statement of Sir Leon Brittan in Appendix II. See also s. 45(5) of Canada's Competition Act for an example of an export exemption with respect to conspiracy.

229. See Lippner, op.cit., pp. 23-24, and 84 ff.

230. See 43 PTCJ 3. ff., Nov. 7, 1991.

231. 57 FR 8359-02 (March 9, 1992)

232. See _Director of Investigation and Research v. The NutraSweet Company_, (1991) 32 C.P. R. (3d) 1.

233. _The Director of Investigation and Research, and Laidlaw Waste Systems Ltd._, Tribunal no. CT-91/2, January 20, 1992

234. _U.S. v. Guerlain_, 155 F. Supp., 77 (S.D.N.Y) 1957). vacated and remanded, 358 U.S. 915 (1958), action dismissed, 172 F. Supp. 107 (S.D.N.Y 1959).

235. The constitutionality of this section has recently been upheld. See _R. v. Nova Scotia Pharmaceutical Society_ [1991] N.S.J. No. 169 Action No. S.C.C. 02368

236. As to theoretical economic analysis of these issues, see N. Gallini, _op.cit._, p. 22 ff. The Gallini study is a very important contribution t the economic theory of grey market goods in Canada. However, it is not based upon empirical data analysis.

237. Suppose that a manufacturer of widgets has been selling 100 items at $10 each per month, for total revenues of $1,000 and a profits of $500 per month, assuming that the marginal cost of each widget is $5. Suppose he determines that he can double the price to $20, keep the same marginal cost of $5, and lose only 25% of the transactions. Thus, his sales revenues will be 75 x $20 = $1500. His costs will be 75 x $5 = $375. Thus, his profit will be $1,125. This is an example of demand inelasticity.

238. See _Director of Investigation and Research v. The NutraSweet Company_, (1991) 32 C.P.R. (3d) 1.

239. _Eastman Kodak Company v. Polaroid Corporation_, U.S. Dist. Ct. 641 F. Supp. 828; U.S.C.A. (Federal Circuit) 833 F. 2d 930; 789 F. 2d 1556; 867 F. 2d 1415, 479 US 850; 109 S. Ct. 1956.

240. See S. Globerman, _Canada's Interest in Two Way Exhaustion of Intellectual Property Rights in Trade with the United States_, mimeo of a study prepared for CCAC, May 1987, p. 15 ff. Available from the

Intellectual Property Review Branch, Consumer and Corporate Affairs Canada.

241. Globerman, op.cit., p. 42.

242. See Director of Investigation and Research v. The NutraSweet Company, (1991) 32 C.P.R. (3d) 1.

243. For example, see the recent decision in Reckitt and Coleman Products Ltd. (Trading as Coleman's of Norwich) (Original Respondents and Cross-Appellants) v. Borden Inc. and Others (Original Appellants and Cross-Respondents), House of Lords Judgments: [1990] H.L.J. No. 18, February 8, 1990

244. See Horner, op.cit., p. 4 and 104. See also R. Swift, op.cit., pp. 11-13.

245. See Canada (Director of Investigation and Research, Competition Act) v. Laidlaw Waste Systems Ltd., Decision: January 20, 1992, unreported.

246. Competition Act, s. 79 (5): *For the purpose of this section, an act engaged in pursuant only to the exercise of any right or enjoyment of any interest derived under the Copyright Act, Industrial Design Act, Patent Act, Trade-marks Act or any other Act of Parliament pertaining to intellectual or industrial property is not an anti-competitive act.*

247. Competition Act, s. 79(4): *In determining, for the purposes of subsection (1), whether a practice has had, is having or is likely to have the effect of preventing or lessening competition substantially in a market, the Tribunal shall consider whether the practice is a result of superior competitive performance.*

248. The bassoon is the lowest pitched instrument in the woodwind section of a symphony orchestra. This example is hypothetical.

249. See Director of Investigation and Research v. The NutraSweet Company, (1991) 32 C.P.R. (3d) 1.

250. H.J. Heinz Co. of Canada v. Edan Foods Sales Inc., 35 C.P.R. (3d) 213.

251. E. Mansfield, Microeconomics, New York, N.Y., W.W. Norton, fourth edition, 1982, at p. 330 ff.

252. supra.

253. Price maintenance as a factor was noted by the Court. See above.

254. Tokyo (AFP), Nov. 13, 1990.

255. Canada (Director of Investigation and Research, Competition Act) v. Chrysler Canada Ltd. IN THE MATTER OF an application by the Director of Investigation and Research under section 75 of the Competition Act, R.S.C., 1985, c. C-34, as amended; AND IN THE MATTER OF a refusal to supply automotive parts for export by Chrysler Canada Ltd. to Richard Brunet. Canada Competition Tribunals Decisions: [1989] C.C.T.D. No. 49 Tribunal no. CT-88/4; Document no. 185(a)

256. Canada (Director of Investigation and Research, Competition Act) v. Xerox Canada Inc., Canadian Competition Tribunal Decisions: [1990] C.C.T.D. No. 2 Tribunal no. CT-89/4; Document no. 11

257. Competition Act

C-34

SEC 75.

PART VIII

MATTERS REVIEWABLE BY TRIBUNAL

Restrictive Trade Practices

Refusal to Deal

Jurisdiction of Tribunal where refusal to deal

75. (1) Where, on application by the Director, the Tribunal finds that (a) a person is substantially affected in his business or is precluded from carrying on business due to his inability to obtain adequate supplies of a product anywhere in a market on usual trade terms, (b) the person referred to in paragraph (a) is unable to obtain adequate supplies of the product because of insufficient competition among suppliers of the product in the market, (c) the person referred to in paragraph (a) is willing and able to meet the usual trade terms of the supplier or suppliers of the product, and (d) the product is in ample supply,

the Tribunal may order that one or more suppliers of the product in the market accept the person as a customer within a specified time on usual trade terms unless, within the specified time, in the case of an article, any customs duties on the article are removed, reduced or remitted and the effect of the removal, reduction or remission is to place the person on an equal footing with other persons who are able to obtain adequate supplies of the article in Canada.

When article is a separate product

(2) For the purposes of this section, an article is not a separate product in a market only because it is differentiated from other articles in its class by a trade-mark, proprietary name or the like, unless the article so differentiated occupies such a dominant position in that market as to substantially affect the ability of a person to carry on business in that class of articles unless that person has access to the article so differentiated.

Definition of "trade terms" "trade terms"

(3) For the purposes of this section, the expression "trade terms" means terms in respect of payment, units of purchase and reasonable technical and servicing requirements. R.S., 1985, c. C-34, s. 75; R.S., 1985, c. 19 (2nd Supp.), s. 45.

258. Competition Act, s. 61(10)
Where, in a prosecution under paragraph (1)(b), it is proved that the person charged refused or counselled the refusal to supply a product to any other person, no inference unfavourable to the person charged shall be drawn from that evidence if he satisfies the court that he and any one on whose report he depended believed on reasonable grounds

(a) that the other person was making a practice of using products supplied by the person charged as loss-leaders, that is to say, not for the purpose of making a profit thereon but for purposes of advertising;

(b) that the other person was making a practice of using products supplied by the person charged not for the purpose of selling the products at a profit but for the purpose of attracting customers to his store in the hope of selling them other products;

(c) that the other person was making a practice of engaging in misleading advertising in respect of products supplied by the person charged; or

(d) that the other person made a practice of not providing the level of servicing that purchasers of the products might reasonably expect from the other person.

R.S., 1985, c. C-34, s. 61; R.S., 1985, c. 19 (2nd Supp.), s.

259. See, for example, Horner, op.cit., p. 118 ff.

260. See generally Clyde Prestowitz, Trading Places, N.Y., N.Y., Basic Books, 1988.

261. John H. Jackson, World Trade and the Law of the GATT, New York, The Bobbs-Merrill Company, Inc., 1969, pp. 504, 511-512.

262. For example, see 1 - Stops: Majors Sidestep Own Rules, Billboard Magazine, June 22, 1991, p. 1.

263. Mexico, La Ley de Fomento y Proteccion de la Proprieda Industrial, Diario Offical, June 27, 1991 and La Ley Federal Derochos de Autor, Diario Official, July 27, 1991, amending copyright statute found in Diario Offical, December 21, 1963.

264. "The National" (January 5, 1992) by Mr. Ian Gordon of Ernst and Young (who studies cross border shopping). See below with respect to the Ernst and Young Study.

265. (1984) 10 D.L.R. 4th 161 at 181.

266. The validity of manufacturers' warranties and how they can be enforced in the absence of privity of contract is a study unto itself. See E.P. Belobaba, Consumer Product Warranty Reform, v.II, Consumer and Corporate Affairs Canada, 1983. In the Seiko case, the court seems to find that the manufacturer is bound by the packaged warranty but there may be no party in Canada against which it can be legally enforced. See (1984) 10 D.L.R. (4th) 161 at 183 ff.

267. Quaere how a traveller abroad would be expected to carry receipts for all his or her warrantied products that may require warranty service. If serial numbers or bar codes can be used to trace authenticity of distribution, quaere whether such techniques cannot be used to prevent the complained of grey-marketing in the first place.

268. For a contrasting America case involving Seiko where consumers were misled, see Seiko Time Corp. v. Alexander's Inc., 218 U.S.P.Q. 560 (S.D.N.Y. 1982).

269. N.Y. Gen. Bus. L., s. 218-aa, (McKinney 1988) cited by Lippner, op.cit., p. 168.

270. See Lippner, op.cit., p. 168 ff. and p. 203.

271. See Lippner, op.cit., p. 169 ff. and p. 204 ff.

272. (1984) 10 D.L.R. (4th) 161.

273. Address by VP of Toshiba at CBA meeting in Toronto, March 27, 1991.

274. DATE: Ottawa, February 12, 1992

SOURCE: Canada Department of Finance Information, 92-012

HEADLINE: GOVERNMENT ANNOUNCES MEASURES ON CROSS-BORDER SHOPPING AND TOBACCO SMUGGLING

Removal of Tariffs on Consumer Goods Not Made in Canada
Mr. Mazankowski tabled a Notice of Ways and Means Motion in Parliament today removing Customs duties on about 25 consumer products which are not made in Canada and which represent approximately $1 billion worth of annual imports. This initiative was requested by Canadian retailers who indicated higher tariffs in Canada than in the U.S. were a contributing factor to higher prices on some consumer goods sold in Canada.

Mr. Mazankowski noted that the list of products on which tariffs were being removed had been arrived at in consultation with the National Task Force on Cross-Border Shopping and Canadian industry. The list includes such products as VCRs, sewing machines, cameras and some sports equipment. The Minister said that retailers selling these products would now be able to do so on a more competitive basis with retailers in the U.S.

275. Ernst and Young, A Preliminary Study of the Competitiveness of Distribution Channels, Study done for Department of Industry, Science and Technology Canada, 1991, pp. 14, 16, 35-38.

276. See Anderson, Ronayne, et al. Working Paper on Intellectual Property Rights and International Market Segmentation: Implications of the Exhaustion Principle, CCAC, October, 1990.

277. Unfortunately, the current "guru" of competitiveness, Prof. Michael Porter, has found little or no time to in his recent writings, including those pertaining to Canada, to examine the role of intellectual property in his *schema*. Such an investigation certainly warrants considered research.

278. See Globerman, op.cit., p. 23.

279. Globerman, <u>op.cit</u>, and Anderson, et al. <u>op.cit.</u>. These two authorities have concluded that we should not do so, at least in the case of patents.

280. Ernst and Young, <u>op.cit</u>., p.38.

281. Globerman, <u>op.cit</u>, 23.

282. See appendix III.

283. Hayhurst, 31 C.P.R. (3d) 289 at 303.

284. See draft GATT TRIPs text of December 20, 1991, article 27 (1).

285. For example, in the year 1989-1990, 14,274 out of 15,348 patents granted in Canada were granted to foreigners. This proportion (i.e. 93%) is typical, See Consumer and Corporate Affairs Canada, Annual Report for year Ending March 31, 1990, p. 22.

286. C. Prestowitz, generally, <u>op.cit.</u>

287. Note that Sir Leon Brittan asserts that interbrand competition may not be very vigorous, and that the Japanese may cartelize their exports. See Appendix II.

288. However, see <u>Director of Investigation and Research v. The NutraSweet Company</u>, (1991) 32 C.P.R. (3d) 1.

289. Such is arguably the case under the current provisions of Canada's <u>Copyright Act.</u>

290. The whole context of the section is provided in Appendix III.

291. See above, Chapter I and Appendix I.

292. Note European Patent Treaty and the European Patent Office, which do not amount to one European Patent, but are an important step on the way. Also, note the move towards a single European trade-mark. See The Times January 29, 1992, <u>A long wait for unitary EC trade mark</u>, Christopher Morcom, QC

293. See <u>Lotus Development v. Paperback Software</u>, (1990) 740 F. Supp. 37. However, a very recent appellate case in the second circuit may signal a change in direction. See <u>Computer Associates International, Inc., v. Altai, Inc.</u>, Nos. 762, 91-7893, 91-7935. United States Court of Appeals, Second Circuit, June 22, 1992 (unreported as yet).

294. See _Competition Act,_ as amended, s. 32. See D.W. Henry, _Patents in Relation to the Combines Investigation Act,_ PTIC Bulletin, Series No. 7, V. 17, July 1966, 1 at page 9; _Dominion Rubber v. Max Propas et al._, (1963) 41 C.P.R. 194 (Ex. Ct); and _R. Union Carbide Limited_, Minutes of Settlement in the Exchequer Court of Canada, Dec. 9, 1969 and June 19, 1971 and the _Annual Report_ of the Director of Investigation and Research for the years ending March 31, 1970 and March 31, 1972.

295. For example, see Laurence J. Cohen, _Warding off the Foe: How Trade Marks can Still offer Some protection against Parallel Imports_, [1990] 10 EIPR 369.

296. The author does not suggest that this is the particular motivation in the _Heinz_ case.

297. See generally N. Gallini, _op. cit._, p. 60 ff.

298. cf. _Seiko v. Consumers Distributing_, (1984) 10 D.L.R. (4th) 161 (SCC).

299. Article 27 (1) of the December 20, 1991 draft text.

300. Stern, _op.cit._, p. 127.

301. N. Gallini, _op.cit._, p. 143 ff.

302. Prof. Gallini's study is expected to be published in due course by the Bureau of Competition Policy of Consumer and Corporate Affairs, Canada. It is the most thorough economic analysis to date of these issues in the Canadian context of which the author is aware.

303. See Beier, _op.cit._, p. 141 ff.

304. Beier, _op.cit.,_. p. 160.

305. See H. P. Knopf, "_The Proposed Rental Right for Video and Sound Recordings_": Consumer and Corporate Affairs Canada, Ottawa, mimeo, June, 1985

306. E.A. Mansfield, _Microeconomics Theory and Applications_, Mew York, N.Y., Norton, 1982, p. 294.

307. Mansfield, _op.cit._, p.300

308. Questions relating to "market power" and "dominance" are discussed in NutraSweet (1991) 32 C.P.R. (3rd) 1, and the recent and very important case of The Director of Investigation and Research, Applicant, and Laidlaw Waste Systems Ltd., Respondent, Canada Competition Tribunal Decision: January 20, 1992

309. Betts v. Wilmott, (1871) L.R. 6 Ch. 239.

310. See G.F. Henderson, Intellectual Property: Litigation,Legislation, and Education- a Study of the Canadian Intellectual Property and Litigation System, Consumer and Corporate Affairs Canada, March 5, 1991, p. 124.

311. R. Stern, Parallel Importation of Copyrighted Products into the U.S., [1989] 4 EIPR 119.

312. British Leyland Motor Corp. Ltd. v. Armstrong Patents Co. Ltd., [1986] 1 All ER 850.

313. Stern, op.cit., p. 126.

314. Stern, op.cit., p. 125.