

Enforcing outside the trademark box

IN SUMMARY

- The rules on grey imports in emerging markets are highly varied
- Creative enforcement strategies can help address the challenge and improve brand protection

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Effective options for grey imports in emerging markets

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Today's global economy offers brand owners increasing access to so-called "emerging" markets. This new openness also means that national borders rarely impede the unauthorised movement of goods – including grey goods – in emerging markets. As a result, brand owners may find themselves with brand protection issues in far-flung markets, including those in which they have not yet contemplated commercial operations.

Emerging markets may be culturally and legally diverse, but they are almost universally disposed to fostering grey business practices – practices that erode a rights owner's control over their brand and damage the brand's integrity. Enforcement options for grey imports and product diversion vary significantly from market to market, but the consistent themes are that the civil court systems move slowly, IP cases are not prioritised, and the threat of civil (or even criminal) enforcement may not carry the same weight as in developed markets. The varied nature of the legal regimes

governing grey imports in emerging markets, coupled with the lack of expeditious and effective judicial processes, necessitates a customised approach to the problem. This article first explores the challenges of grey market trademark enforcement in four developing regions – emerging EU markets, non-EU CEE markets, Russia and China – and then outlines possible approaches to address these challenges.

Emerging markets in the European Union

European courts at the highest level have confirmed that brand owners may rely on trademark rights to prevent the sale of grey imports from outside the European Economic Area (EEA) (comprising the 27 EU Member States along with non-EU markets Iceland, Norway and Lichtenstein). Once a good has been put on the market in the EEA with the brand owner's consent, however, the right is "exhausted" and the good can travel freely across national borders.

This rule flows from the 1989 Trade

Marks Harmonization Directive (“the Directive”). With limited exceptions, in order to promote the free movement of goods and services within the common European market, Article 7(1) of the Directive prohibits brand owners from invoking trademarks to prevent the distribution of goods that have already been put on the market in the European Community with their consent. Until last year, however, it was an open question as to whether this regional exhaustion of rights applied only to the 27 EU Markets, or whether EEA markets were bound by a regional exhaustion rule as well; as a result, Norway served as a legal route for parallel imports to enter the EEA.

The European Court of Justice (ECJ) and the EFTA court, which together with the EFTA Surveillance Authority is responsible for ensuring that Norway, Iceland and Lichtenstein respect their obligations under the EEA Agreement, have now aligned their diverging views on the interpretation of Article 7(1). In the 1997 *Mag Instruments* case, the EFTA court ruled that Article 7(1) permits the EEA markets to introduce or maintain the principle of international exhaustion – thereby sanctioning Norway’s principle of international exhaustion and providing an entry point into the Community for grey imports. Just over six months later, the ECJ, in the *Silhouette* case, ruled the contrary, concluding that national laws providing for the international exhaustion of rights are contrary to Article 7(1). This was subsequently confirmed by the ECJ in the 1999 *Sebago* case, which established that Member States’ national laws cannot provide for the international exhaustion of trademark rights. Nearly a decade later, in the 2008 *L’Oréal* case, the EFTA Court finally aligned its view with that of the ECJ and confirmed that there is no justification to interpret Article 7(1) differently in EEA law and EC law. As a result, Norway can no longer be considered to be a legal gateway for grey imports to enter into the EU.

This string of cases also makes it doubly clear that regional exhaustion and trademark rights should be the guiding principle throughout the entire EEA and that its Contracting Parties (which include the now 27 EU Member States) are precluded from following the principle of international exhaustion. In practice, however, this is not the case in some of the newer Member States. Illustrating the chasm between theory and practice, Romanian trademark law

imposes a blanket restriction to enforcing trademark rights on brand owners who have put their product on the market anywhere in the world, effectively permitting grey imports entry into the EEA via Romania.

Even in the new EU Member States whose national law adheres to the EU principle of regional exhaustion, national authorities may not consider grey goods as harmful and hence may be reluctant prevent their importation. In Estonia, for example, on paper the legal regime conforms to EU principles; in practice, however, law enforcement agencies are generally unwilling to take action. Some Member States consider grey goods to be a consumer friendly price control regulator, as is the case in Bulgaria.

Hopefully, as European regulators forge ahead with efforts for closer cooperation, it should only be a matter of time before the practices in emerging Europe fall in step with the practices in older Member States. Furthermore, pending changes in EU legislation may provide brand owners with additional tools to fight grey market activities. EU Regulation 1383/2003 (the “Regulation”) enables right-holders, with the help of national customs authorities, to prevent counterfeit goods from crossing the EU’s external border; the Regulation does not, however, provide brand owners with a cause of action in relation to genuine products, or grey goods. In a move to further harmonise the customs actions that can be taken by brand owners, the European Commission is currently considering extending the scope of the Regulation to cover grey imports from outside the Community, which ideally would further align divergent practices among Member States.

Emerging European markets outside the EU

A number of the EU’s bordering countries in Central and Eastern Europe (“CEE”) are already candidates (Croatia, the former Yugoslav Republic of Macedonia and Turkey) or potential candidates (Albania, Bosnia and Herzegovina, Kosovo, Montenegro and Serbia) for future accession to the EU. The ongoing negotiations over the intellectual property chapter of the accession agreements should ultimately result in candidates’ national laws conforming to EU principles of exhaustion. However, for the time being brand owners seeking to protect their brand have to go to great lengths to fathom their options from a patchwork of extremely divergent regimes in these markets. With national exhaustion of trademark rights being the legal

state of play in Croatia and international exhaustion in Serbia, for example, it is inadvisable to rely on a one-size-fits-all strategy. What is consistently crucial to take into account is how the relevant local authority views grey imports and their willingness to take enforcement measures.

Russia

Grey market imports seemingly flourish in Russia, and even careful vetting of partners and robust distribution agreements may leave a brand owner facing product diversion problems. Recent changes to the trademark enforcement regime have only served to further complicate enforcement options for brand owners.

In practice, historically, Russian customs authorities and courts have treated grey imports as an administrative offence. More recently, however, courts have moved away from this view. The Code on Administrative Offences requires that goods must be “unlawfully” marked with a trademark to give rise to an infringement; because grey goods are original (rather than fraudulent), courts have concluded that the marks are not unlawfully affixed to the goods per se, and thus there is no administrative cause of action. Unhelpfully, the long-awaited Resolution of the Russian Supreme Court and Arbitration Court reinforces this view, despite earlier drafts of the Resolution having indicated that grey imports are administrative offences.

Prior to these decisions and the Resolution, the Russian customs authority was empowered and generally willing to seize grey goods if a brand owner had registered its marks in Russia and filed seizure requests with the Federal Customs Register. The new view embodied in the Resolution, that grey goods de facto cannot be counterfeit, throws this practice into limbo and it remains to be seen whether the customs authority will be rendered impotent with respect to the seizure of grey goods.

Brand owners may take solace in the fact that the same reasoning is unlikely to be applied to civil trademark enforcement. Based on the general interpretation of the Civil Code, which states that placing a mark on goods for the purpose of import into Russia is the exclusive right of the owner of the marks, the import of original (grey) goods without the consent of the brand owner should remain actionable as civil trademark infringement – with all its attendant pros and cons.

China

In China, the legal situation in relation to grey market goods remains unclear. A literal reading of Chinese Trademark Law suggests that parallel imports are prohibited. If accurate, a brand owner has recourse to a broad range of remedies including seizure, administrative fines, civil compensation and criminal prosecution. However, there is a commonly held view amongst the legal profession that the function of a trademark is to avoid confusion as to the source of a good to which the trademark is applied and that, consequently, there should be no cause of action under the Chinese Trademark Law for the importation of grey market goods.

Chinese case law does support a brand owner's ability to rely on trademark law to stop parallel imports. In 1999, for example, the Guangzhou Intermediate People's Court held that trademark rights were infringed when "Lux" soap was imported from Thailand into China without the brand owner's consent. As China is not a common law jurisdiction, however, this decision does not afford brand owners much security as this otherwise-valuable case law will not bind other courts.

The Chinese Trademark Office is expected to introduce a new trademark law before the end of 2010, updating the current (2001) law. It remains to be seen whether the new law will resolve the question of whether and how trademark law can be relied upon to tackle grey market activities.

Trademark enforcement

When local legislation offers criminal or administrative trademark enforcement mechanisms, the brand owner may leverage the less costly and often more expeditious nature of such enforcement (in contrast to civil trademark enforcement). Nonetheless, even if trademark enforcement mechanisms exist, be they criminal or civil, a brand owner should consider the practical implications of trademark enforcement action; often what is written in the law does not work quite as well in practice.

For example, customs authorities may have the power to seize grey goods in some markets, but a brand owner should only request the seizure of grey goods if it has the resources to follow up. A brand owner would be better off not to request the seizures than to do so and not follow up, as the latter may be perceived as implicit authorisation of grey imports and will certainly undermine future

enforcement efforts involving customs authorities. Ironically, even the perverse and unexpected can thwart trademark remedies when a brand owner seeks to protect its marks – the positive benefits of pursuing an action in emerging markets can be completely undone if the seized goods are subsequently sold by the government.

Alternative enforcement

In light of the legal and enforcement challenges outlined above, brand owners seeking to develop a broad, effective strategy for combating grey goods in emerging markets are well advised to look beyond traditional trademark enforcement strategies. Part of this strategy should include measures designed to prevent product diversion in the first instance; where such diversion has already occurred, legal remedies outside of trademark may provide opportunities for enforcement.

Effective preventative measures take several forms:

- First, a brand owner must vet its manufacturers and distribution channel with care. Unscrupulous business practices may be commonplace in emerging markets, and brand owners can unwittingly become involved with unsavory or disreputable companies. Thus, it is especially important to place a great deal of emphasis on building a reliable network of local partners. Brand owners should also enter into localised manufacturing and distribution agreements containing familiar and locally enforceable remedies;
- Second, to ensure that enforcement actions are pursued most efficiently, the brand holder should craft a strategy for training for local police, prosecutors, and customs officials. It is unlikely that efforts to stop grey imports will garner support from local law enforcement absent significant education. Many law enforcement officials find the legal issues confusing; and some consider grey imports to be counterintuitive (the product is genuine, so how can it be illegal?) and believe the harm to the brand owner is dubious. Furthermore, irrespective of the letter of the law, some prosecutors may be reluctant to act in cases where there is no obvious health and safety risk to the consumer or they do not perceive there to be any social harm;
- Third, even the best planned and orchestrated training programmes will not succeed in effecting the desired policy change unless there is the political will to

do so. Training programmes and awareness campaigns thus also need to focus on policy makers. Arguments in support of reducing the grey market are likely to carry more weight in front of government officials when focused on political motivations such as increased consumer protection or increased tax revenues as opposed to the protection of rights holders; and

- Finally, public reports of successful enforcement efforts undertaken by the brand holder may be a good deterrent for those who may be tempted to divert brand owners products away from their intended distribution channels. Brand owners should not be reluctant to widely publicise their enforcement activities at a national and regional level.

When prevention fails to stop problems, alternative enforcement avenues can complement trademark enforcement remedies, or provide a viable option when IP legislation does not address grey market imports. Among these avenues, audits of distributors and brokers can be a relatively inexpensive and expeditious enforcement tool. The national laws in some emerging markets may even facilitate a brand owner's request to audit goods carrying its mark. Consumer protection legislation may also present an enforcement option when the grey goods involved implicate health and safety, or where consumer regulations dictate localised handbooks, instructions, safety information or technical conformity certificates – the absence or deficiency of which may offer the brand owner a back door to stop grey goods. And tax regulations may present an enforcement vehicle that engenders a sympathetic response from law enforcement officials, shifting the enforcement focus to lost tax revenue due to below market sales prices of grey goods.

Conclusion

The trademark enforcement landscape in emerging markets is varied in its options and effectiveness to address grey market imports. Therefore, irrespective of the extent to which trademark law offers brand owners recourse to prevent their brand being eroded by grey market activities, creative enforcement strategies are a must in emerging markets. Alternative enforcement activities are a valuable complement to more traditional methods and produce measurable improvements in brand protection. 