# CHALLENGES OF THE IMPLEMENTATION OF THE PRINCIPLE OF EXHAUSTION OF THE EXCLUSIVE RIGHT TO A TRADEMARK IN THE CONDITIONS OF PARALLEL IMPORT

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***Abstract*** *– The article discusses the implementation of the principle of exhaustion of the exclusive right to a trade mark in the conditions of parallel importation. The article analyses the approaches to the understanding of parallel import. Conclusions are drawn about the advantages and disadvantages of the phenomenon of parallel import. The author analyses two models of implementation of the principle of exhaustion of the exclusive right to trademark - international and national on the example of Russia, the USA and Canada. The author made conclusions about the most relevant model of exhaustion of exclusive right to a trademark for importers, right holders and consumers.*
***Keywords:*** *exclusive right, trademark, parallel importation, national exhaustion regime, international exhaustion regime.*

## INTRODUCTION

The division of commodity markets leads to a different range of goods on national markets and, consequently, to unequal access to goods for buyers from different countries. In order to obtain goods that are not sold on the national market, it is necessary to purchase them on a foreign market and import them into the national market, which is often contrary to the interests of the right holder of the trademark, who di-vided the commodity markets by countries and the corresponding assortment. Since the actions of importing goods without the authorisation of the right holder occur in contradiction with the main import channel, this import was called parallel import.

Due to the lack of a unified approach to the regulation of parallel imports, in cer-tain markets the right holders were allowed to implement their economic policy and prohibit the import of products labelled with their trademark, and in some markets they were restricted in this right. There are also restrictions under which the right holder is more likely to prohibit parallel imports - for example, the import of goods with substantial differences from the goods normally sold on the national market by the right holder or his licensees, including repackaged goods and goods with material differences [1]. The possibility of prohibiting parallel imports depends on the principle of "exhaus-tion" of trade mark rights adopted in the country of importation of goods.

According to this principle, the exclusive right to a trademark is subject to exhaustion (termination) if the goods on which it is placed are introduced into civil turnover by the right holder himself or by another person with his consent [2]. In the frame-work of the implementation of this principle, the sale of the original product under the manufacturer's trademark by the first buyer is neither a violation of the exclusive right to a trademark, nor unfair competition. This kind of restriction of exclusive rights to trademarks is based in the interests of free trade and free movement of goods [3]. From the legal point of view, approaches to the choice of the regime of exhaustion of the right to a trademark are differentiated in different legal orders. Both in practice and in the legal doctrine they are reduced to two main regimes - international (by the example of the USA) and national (by the example of the Russian Federation). Each of these regimes to a greater or lesser extent violates the balance of interests of right holders, importers and consumers, as well as allows or prohibits parallel imports.

The purpose of this study is to identify approaches to understanding parallel im-ports, to study the existing regimes of exhaustion of the exclusive right to a trade-mark and to determine the most

optimal option of applying the regime of exhaustion of the exclusive right, taking into account the balance of interests of importers, right holders and consumers.

In the present study we studied the results of Cohen Jehoram, H. (1999) [2], Bonadio E. (2011) [4], Skoko H., Krivokapic-Skoko B. (2005) [5], who in their studies subjectively studied parallel imports as an economic phenomenon in its rela-tionship with intellectual property rights. Also, within the framework of the study were used the results of the works of Clugston, C. [6], Coke, E. [7], Ghosh Sh. [8], Khusainov R. I. [9], Grigoriadis, L.G. [10], Calboli, I. [11] in the field of research of national and international regimes of exhaustion of the exclusive right to a trade mark, including in Russia, the USA and Canada. As part of the research of the inter-national regime of exhaustion of exclusive right to a trademark, the results of court cases Original Appalachian Artworks Inc. v. Granada Electronics [12], Lever Brothers Co., Appellant, v. United States of America [13], Skullcandy v. Filter USA [14]. Moreover, in view of the special role of Internet trade in the conditions of parallel import, the works of Frolova E.E. were studied. [15-17], Rusakova E.P. [16-17], and Kupchina E.V. Frolova E.E. [15], Rusakova E.P. [16-17], and Kupchina E.V. [15], which are devoted to the resolution of digital disputes including those involving intellectual property.

The present study is based on general scientific (system method, analysis, compari-son, historical analysis) and special (comparative-legal method, method of legal inter-pretation, formal-legal method) methods of cognition. The research focuses on the study of judicial practice and legislation in the field of exhaustion of the exclusive right to a trademark, including in the conditions of parallel importation. The main methods used in this study were the analysis of available empirical data in scientific literature, judicial practice and normative legal acts.

**1. Approaches to Understanding Parallel Imports**

Parallel importation is understood as the importation of original goods protected by a trademark without the permission of the right holder of this mark into the territory of third countries [4]. Parallel import is not always an offence, because these goods can be purchased legally, but these goods inevitably form a "grey market". One of the main incentives for grey market importers is the prospect of selling products quickly and profitably at a reduced price compared to goods sold by official distributors [18]. Since the goods imported under the parallel import scheme do not differ from the original goods, and in fact they are them, and also by virtue of the fact that they were legally produced and purchased, and are patented and copyrighted, they create direct competition in the market [18].

The emergence of parallel imports is determined by its profitability for the unoffi-cial distributor. Obtaining this profit depends largely on the official suppliers them-selves. Thus, in particular, it is a matter of differentiated pricing policy: the manufac-turer sets different prices for different markets, which makes it possible for other trad-ers to take advantage of this by reselling goods purchased at a lower price in one country to the markets of third countries, where the same goods are much more expensive [18]. W.A. Rothnie in his study on parallel imports defined it as follows: "Taking advantage of lower prices, some enterprising middlemen buy goods in a cheaper foreign country and import them back to their own country at higher prices. Consequently, this type of import can be described as imported 'in parallel' to the official distribution network" [5].

The special role of Internet trade should be noted: the modern development of technology makes it possible to make purchases in almost any online shop around the world without any obstacles. For this reason, parallel imports can be used to increase sales and market share in foreign countries [19]. Hence, there are two main disadvantages of parallel imports: financial losses of trademark right holders, which cannot compete with the prices of the "grey" market, and a decrease in consumer confidence in the quality of goods [20]. Obviously, con-sumers will seek to buy a high quality product protected by a trademark at a lower price. However, an unofficial distributor cannot provide a guarantee of the quality of the purchased goods.

From the consumer's point of view, trademarks are important in the purchase deci-sion because they serve as a guarantee of the quality of the product to which consum-ers are accustomed [21]. "Parallel" importer cannot provide various ancillary services such as licence warranty and service.

In addition to the above, the main disadvantages of parallel imports should also include: a change in consumer attitudes towards the trademark and a decrease in brand loyalty as a consequence of this; reduced investment on the part of the official seller in the promotion of goods in a particular market [5]; loss of a unified product posi-tioning strategy, which leads to consumer confusion about the origin and quality of goods [21].

Ultimately, the main benefits of parallel imports are received by end consumers, who have the opportunity to buy original goods at lower prices.

On the other hand, parallel imports also have a number of advantages that can con-tribute to economic recovery. The main ones are: increased competition in the market and increased entrepreneurial activity; increased choice and the ability to buy from a much wider distribution network [22].

Ultimately, the main benefits of parallel imports accrue to end consumers, who have the opportunity to buy original goods at lower prices, which negatively affects the interests of right holders.

**2. National Regime of the Exhaustions of the Exclusive Right to a Trademark under Conditions of Parallel Import (on the Example of Russia)**

Under the national regime of exhaustion of exclusive rights, the exclusive rights to a trademark are considered exhausted at the moment when the goods protected by this mark have been introduced into civil circulation with the consent of the right holder or by him in this country [6].

The national regime, which has been applied in Russia for twenty years, is on the side of the right holder.

The approach of the legislator to the issue of choosing the regime of exhaustion of the right to a trade mark in modern Russia has been transformed three times. In the 1990s, the international regime of exhaustion was applied [23], which in the early 2000s was replaced by the national regime, later transferred to Part Four of the Civil Code of the Russian Federation. However, in 2010, first the EurAsEC Agreement and then the EAEU Treaty established a regional regime, which currently coexists with the national regime, recorded in Article 1487 of the Civil Code of the Russian Federation.

The symbiosis of the two regimes, national and regional, was confirmed by the Constitutional Court of the Russian Federation in Resolution No. 8-P of 13 February 2018. Moreover, the Constitutional Court of the Russian Federation differentiated sanctions for the import of counterfeit goods and products of so-called "grey", or parallel imports, and thus demonstrated, although not the most significant, the nar-rowing of the monopoly of trademark right holders.

In this context, it should be mentioned that the Federal Antimonopoly Service has been consistently advocating the legalisation of parallel imports for more than a dec-ade. The FAS of the Russian Federation twice in 2014 and 2019 prepared a draft law "On Amendments to Part Four of the Civil Code of the Russian Federation" in terms of legalisation of parallel imports6, but to date this position, firstly, does not meet the interests of all EAEU member states, and secondly, faces resistance from various interest groups.

The above circumstances confirm the absence of a firm position of the legislator regarding the choice of the territorial regime of exhaustion of the right to a trade mark in Russia and adequate legal regulation of this issue.

**3. International Regime of Exhaustion of the Exclusive Right to a Trademark under Conditions of Parallel Importation**

International exhaustion of rights is characterised as follows - the right holder loses exclusive rights to the trademark after the first sale of the goods protected by it on the market of any of the countries where this trademark is registered, with the consent of the right holder or by him [24]. Thus, the right holder will have no legal defence against the importation without his consent of trademark-protected goods after the first sale. This principle most fully promotes the free and unimpeded movement of goods, and, accordingly, contributes to the liberalisation of trade. In particular, it is applied in the United States, where this principle in relation to copyright and trade-marks has been called the first sale doctrine.

Its origin is associated with the name of the English lawyer Lord E. Coke, who pointed out back in the early XVII century that the law should not limit the freedom of trade and transactions by giving the owner of copyright the opportunity to dispose of the object already once sold [7].

In relation to trademarks, the doctrine of first sale has been integrated into the US jurisprudence since the 1920s. In 1924, in the case of Prestonettes v. Coty, the court sided with the defendant, the New York corporation Prestonettes, which had pur-chased compact powder and toilet water for resale from the French company Coty [25].

Subsequently, a judicial precedent has developed in the United States that general-ly permits parallel imports and thus follows the international regime of exhaustion, but with a rather wide range of exceptions. The current flexible approach to the ex-haustion of the right to a trademark is produced in the legal rules enshrined in § 1526 of the Tariff Act and § 1124-1125 (Articles 42-43) of the Lanham Act (Trademark Act), which, as a rule, are interpreted by the courts in a systemic relationship. And if § 1526, included in the Tariff Act in 1922, prohibits "grey importation" of goods without the consent of the right holder [26], the provisions of the Lanham Act of 1946 establish a number of exceptions to this rule - first of all, they are directed against consumer disorientation and unfair competition of producers when using iden-tical or confusingly similar trademarks [27].

As Sh. Ghosh writes, "the application of Articles 42 and 43 (Lanham Act) extends the protection of the parallel import market provided by Article 526 (§ 1526 of the Tariff Act) beyond the relations "licensee-licensor"" [8].

In turn, this allows R.I. Khusainov to argue that in reality the U.S. approach to the concept of exhaustion of rights is more complicated, and there are exceptions to the general rule, which allow right holders to prevent unauthorised sales [9]. One of the main such exceptions is a change in the internal or external properties of the goods (including repackaging), which took place already in 1924 and, in the absence of an appropriate indication, can mislead the consumer. For example, in the case of "Origi-nal Appalachian Artworks" against "Granada Electronics" the court sided with the American right holder and imposed an indefinite ban on parallel import of dolls im-ported from Spain with adoption documents in Spanish [12]. Thus, despite the origi-nality of the products, these documents qualified as capable of misleading US con-sumers.

A landmark case for approval in US jurisprudence was the Lever Brothers Compa-ny case, in which soap produced by an affiliated US English company was imported into the US from the UK - the product differed slightly in composition from the US product [28]. As a result, the Lever Rule, which prohibits the importation of goods with significant differences from the original, was included in § 133.23 of the Tariff (Customs) Regulations as an exception.

An insurmountable obstacle to the application of the Lever rule is the presence of labelling indicating a product modification. As I. Calboli writes, as long as products are properly labelled in accordance with the U.S. Customs Regulations, trademark owners cannot rely on the Lever Brothers rule (on substantial differences in goods) to prevent the importation of genuine products into the U.S. market [11].

Another exception to overcome the exhaustion of a trademark right is the failure of parallel importers to comply with the quality control measures required by the right holder. In the case of the American corporation "Skullcandy" v. B. Friedlander, head-phones and speakers under the plaintiff's trademark were sold by the defendant online on the Amazon site with the failure to comply with warranty standards, contrary to the contractual rule, according to which "Skullcandy" prohibits authorised dealers to sell goods through third-party Internet resources [14]. In such cases, it is not so much the quality of the product that matters, but rather the ability of the right holder to control it and maintain a certain level of reputation in the eyes of consumers.

In another case, Mars Canada v. Bemco Cash & Carry, the court favoured the in-terests of the trademark owner twice in 2016 and 2018, basing its position on a set-tlement agreement concluded between the parties in 2006, under which Bemco Cash, together with its affiliates, undertook not to import products under the Mars trade-mark into Canada without the consent of the right holder or the court. In addition, the defendant failed to comply with the requirements for product labelling in accordance with technical standards (no weight and product information in French and English); in

contrast, the imported products contained nuts and did not have a similar logo, unlike the original products with the "nut-free" logo [29].

These exceptions to the principle of exhaustion of the right to a trade mark prohibit parallel imports and allow L.G. Grigoriad is to claim that Canada has a national exhaustion regime [10]. In our opinion, this is not quite true - we should agree with I. Calboli, who argues that, as a rule, Canadian courts "with relative understanding perceive unauthorised parallel imports and rarely prohibit the importation of "grey market" goods into Canada" [11]. Exceptions to the strong doctrine confirm Canada's flexible approach to the exhaustion of trade mark rights despite the broad discretion of the courts, in most cases international treatment is applied and parallel imports are authorised.

## CONCLUSION

Based on the above, it can be concluded that the international principle of trademark exhaustion has its positive and negative sides, the impact of which depends on many factors and conditions of a particular state or international association. In those coun-tries where the international principle is applied, specific mechanisms are provided by law or in practice, aimed at balancing the interests of the right holder, parallel import-ers, consumers and the state.

In the case of the application of national treatment, it is the right holders who have the most advantageous position. This approach is less flexible than the international one

Based on the studied literature and judicial practice, it seems that at the moment the most flexible approach, which takes into account the interests of importers, right holders and consumers, is fixed in the USA. Due to a large number of exceptions to the regime of international exhaustion of the exclusive right to a trade mark, the USA managed to achieve a balance of interests of all subjects involved in this process.

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