The parallel importation myth

Brand owners have long felt the law to be on the side of parallel importers. However, recent case law offers another perspective

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Parallel importation has increasingly become a flashpoint for commercial entities that own intellectual property. In the trademark context, it refers to the act of importing into and selling in the host market products that were purchased legally in another market, but not from the trademark holder's authorised distribution channels.

Legislation

Until October 2012, a definitive Indian trademark law position on the legality of parallel importation was conspicuous by its absence. This was brought into sharp relief by the fact that other branches of intellectual property (eg, patent and copyright) clearly and statutorily support the legality of parallel importation.

Central to determining the legality of parallel importation is the principle of the exhaustion of rights – that is, the question of whether a rights holder can prevent the importation of the product into a market where it holds exclusive rights. For legal and policy reasons, most countries take one of two broad stances:

- international exhaustion – a rights holder's rights (eg, preventing the importation and re-sale of its product) are exhausted once the product is sold anywhere in the world); and
- national exhaustion – a rights holder's rights are exhausted only by sale in the market in which it holds rights.

The decision on whether to permit parallel importation of IP-protected products is a fine balancing act, and usually involves an extremely subjective determination by each country regarding the pros and cons of parallel importation relative to that country. On the whole, a national exhaustion regime which outlaws parallel importation is seen as fortifying rights holders' freedom to sell products in the host market on their own terms and giving them strong control over virtually every stage of the marketing process, including pricing, product differentiation and after-sales customer services. An international exhaustion regime, on the other hand, is more *laissez-faire*, and permits parallel importers to offer stiff pricing competition to rights holders, in addition to promoting local peripheral businesses – although possibly, in cases where the law is blurred as to the extent of legality, at the cost of exposing consumers to confusion and quality-related risk, since they are now confronted with seemingly genuine products sold outside the rights holder's traditional model of authorised sellers or franchisees. It is no secret that even though India is swarming with importers of authentic and legally imported products from abroad, this parallel import channel is prone to abuse, raising concerns about product dumping and product safety in the long run. Given these complications, therefore, it is no surprise that the World Trade Organisation, through Article 6 of the Agreement on Trade-Related Aspects of IP Rights (TRIPs), leaves the decision of what kind of exhaustion of rights regime to follow up to individual countries.

The Indian trademark law dealing with parallel imports is captured in Section 30 of the TRIPs-compliant Trademarks Act

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1999, which sets down limitations on the exploitation of trademark rights by rights holders. Early instances of trademark litigation before the Indian courts regarding parallel imports were largely uncontested injunction orders, in which the courts appeared happy to issue orders stopping parallel imports by small-time traders on the grounds that these imports involved the unauthorised use of various rights holders' trademarks.

Nevertheless, these early cases were notable more for the fact that small-time traders attempted to pass off the parallel imported products as products imported or authorised by the rights holders, rather than the courts making any specific ruling on the substance of the legal provisions on trademark infringement.

Provisions relating to imported products were expressly included in the Intellectual Property (Imported Goods) Enforcement Rules 2007 and further notifications issued under the rules, which for the first time permitted rights holders to record their registered trademarks, copyrights and patents with the commissioner of customs, and thereafter request the suspension of imported products suspected of infringing their IP rights. These rules, contrary to popular perception, do not outlaw all types of product bearing infringing trademarks; rather, they specifically apply only to products bearing a false trademark or a false trade description. Thus, Customs has consistently taken the position that as long as goods are genuine and all relevant taxes and duties have been paid, it will not seize such goods at the borders (an understandable position, given that Customs is a division of the Ministry of Finance, which obtains revenue from imports). However, a violation of the law pertaining to packaging and labelling, weights and measures or food adulteration would render parallel imported goods separately actionable with Customs, albeit not under the 2007 rules.

Judicial interpretation

The most prominent judgment on the legality of parallel imports under trademark law was issued in October 2012 by the Division Bench of the Delhi High Court in *Kapil Wadhwa v Samsung Electronics* – a case that was tailormade for testing the exceptions to trademark infringement provided under Section 30 of the Trademarks Act. The appellant purchased Samsung printers after their first sale in another country and then imported them into and sold them in India. Samsung claimed trademark infringement on account of the presence of the SAMSUNG trademark on products imported and sold by the appellant without its authorisation. The Division Bench's ruling is interesting as it noted that even the products sold by Samsung in India were imported; therefore, Samsung's objection could be distilled down to "a difference in the features of the compatible products".

The key holding of the Division Bench was its interpretation of Section 30 as supporting the principle of international exhaustion. This was based on two grounds:

- a purely interpretive legal ground, to the effect that the section used the expression 'the market' in a manner consistent with

the generic placing of products in the commercial stream, and not in reference to a specific, geographically limited market; and
- reliance on the legislative history of the section to support the view that the market at issue was indeed the global market.

Another notable aspect of the Division Bench ruling was a disavowal of the policy behind the decision to pick one type of exhaustion regime over another, although in addressing Samsung's arguments on the benefits of national exhaustion, the Division Bench noted that national exhaustion may not necessarily encourage industry – as in the present case, a manufacturer abroad may simply get its trademark registered in a country and import goods manufactured by it in a foreign country. Consequently, dual pricing may cause injury to the consumer, as was exhibited in this case by the fact that the functional equivalents of the products imported and sold by the appellant were cheaper than Samsung's pricing in India.

The judgment was widely misunderstood in the IP community as encouraging the flooding of the Indian market with grey-market goods. However, the decision should be seen as clarifying the unsettled legal position by distinguishing between parallel imports which are actionable and those which are not.

Tackling parallel importation – lessons for brand owners

When viewing the issue from a rights holder's perspective, it must be remembered that Indian trademark law provides for a range of exceptions to the principle under which a rights holder can oppose parallel importation – a fact recognised by the Division Bench. Such exceptions are set out in Sections 30(3) and (4) of the Trademarks Act, as follows.

Goods must have been lawfully acquired

The foremost prerequisite that parallel imported goods must fulfil in order to avoid being deemed infringing is that the importer have acquired the goods legally under the laws of the jurisdiction where the acquisition was made. Therefore, the acquisition of the goods must have been legal and the importer should have legal title over the goods. Thus, this does not apply to goods which were stolen or smuggled by the importer into the country from where it is importing them into India. Such goods will be infringing goods from the outset, since lawful acquisition is an essential qualification for the further handling of the goods.

Legitimate reasons to oppose parallel importation

Section 30(4) protects the rights holder's right to oppose further dealings in the goods bearing its trademark. India recognises a rather broad 'legitimate reasons' exception to international exhaustion, while specifically setting down a 'change or impairment' exception. This is in addition to the explicit exception that applies in instances where the importer changes or impairs the condition of the (parallel imported) goods after the rights holder placed them on the market. The Division Bench's decision embraced this position and highlighted what could be specific instances of legitimate reasons to oppose parallel imports. The court observed:

> *it would be relevant to note that further dealing in the goods placed in the market under a trade mark can be opposed where legitimate reasons exist to oppose further dealing and in particular where the condition of the goods has been changed or impaired. With respect to physical condition being changed or impaired, even in the absence of a statutory provision, the registered proprietor of a trade mark would have the right to oppose further dealing in those goods inasmuch as they would be the same goods improperly so called, or to put it differently, if a physical condition of goods is changed, it would no longer be the same goods. But, sub-section 4 of Section 30 is not restricted to only when the conditions of the goods has been changed or impaired after they have been put on the market. The section embraces all legitimate reasons to oppose further dealings in the goods. Thus, changing condition or impairment is only a specie of the genus legitimate reasons, which genus embraces other species as well.*

Referring to certain US court decisions with respect to cases of legitimate differences, the court listed these as:
- a difference in services and warranties;

- a difference in advertising and promotional efforts;
- a difference in packaging;
- differences in quality control, pricing and presentation; and
- a difference in the language of the literature provided with the product

Consequently, if the rights holder has a manufacturing base in India and makes goods specially tailored for India, whereas the parallel importer offers different goods in the same market, the rights holder could invoke the legitimate reasons outlined in Section 30(4) of the Trademarks Act and have the goods declared infringing. Likewise, even if the rights holder has India-specific packaging for its goods, or has different characteristics, ingredients or quality standards for different markets, those factors could also qualify as legitimate reasons to have differing parallel imported goods declared infringing.

The court has interpreted 'legitimate reasons' fairly widely and in a non-exhaustive manner, thus including circumstances which may not yet have been contemplated. Whether an action by a rights holder constitutes a legitimate reason will depend on the specific facts of each case. Ultimately, a legitimate reason enquiry must also be tested on the anvil of consumer confusion and deception.

Disclaimer requirement

The most common difference between a parallel imported product and an authorised product is that the former rarely provides an official warranty and after-sales support. Since in *Samsung* the importer provided his own warranty and after-sales care equivalent to that provided by the brand owner, the court observed that any likelihood of confusion on this basis can be obviated if the importer prominently displays a disclaimer at the point of sale that the goods are warranted not by the brand owner, but solely by the importer itself. Other parallel importers may also follow and resort to this safeguard to shield themselves from potential actions. However, the mere display of a disclaimer is insufficient; not only must the disclaimer be prominently displayed so that it is easily visible to customers, but the parallel importer must also provide a credible and adequate warranty and after-sales service. The absence thereof could well qualify as a legitimate reason to seek an injunction against a parallel importer.

Thus, in laying down the framework for international exhaustion in Indian trademark law, the Division Bench has established key safeguards for brand owners along similar lines to the US position. The United States uses a material differences test, where differences between the branded and parallel imported products are sufficient for the latter to be deemed infringing; while India follows a material alterations test, which requires a change to be made to the products at the importer's behest. Thus, in India, parallel imported goods could be deemed to be infringing in the following cases:

- They are not legally acquired under the laws of the country of origin and the country of import.
- Their condition has been physically altered, changed or impaired after they were put on the market.
- The brand owner has a legitimate reason to oppose circulation of the goods in India.

Therefore, the existing Indian trademark law strikes a healthy balance between a brand owner's genuine concerns about preserving the goodwill associated with its brands and an attempt to create artificial price segmentation in the Indian market to the detriment of consumers, for the sole purpose of maximising profit.

The authors represented Kapil Wadhwa before the Delhi High Court. At the time of writing, Samsung had filed a special ;eave petition before the Supreme Court of India challenging the decision, and the authors were contesting the same on Wadhwa's behalf. The views expressed here are those of the authors and are based on materials available in the public domain.

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