Divided courts fail to see grey imports as a black-and-white issue

Russian court practice has divided sharply over the question of parallel or grey imports. However, hope is on the horizon for rights holders, as the High Arbitration Court is due to reconsider the question and resolve the confusion

by **Mark Chizhenok** and **Dmitry Makarov**, Ivanov, Makarov & Partners

The modern Russian economy cannot be called diversified by any means. Imported goods account for between 60% and 70% of the consumer goods market. In some markets, such as that for mobile phones, imported goods may account for as much as 90% and even 100% of the market. However, the wild trade of the early 1990s, when everything was selling everywhere, is long over. Foreign manufacturers interested in the Russian market have built up distribution chains along with restrictions and policies for prices, places of sale, product presentation and post-sale services. Special Russian editions of many products have been developed for import into Russia to meet the needs of Russian consumers.

However, strict contract terms and the need for considerable investment in these regulated distribution networks have effectively blocked smaller businesses from participating. This in turn has prompted traders to target consumers who care more about a product's price than its distribution history and related services. Certainly, buying original products abroad at a lower price and then offering them for sale at small booths or over the Internet gives such traders a better chance of offering competitive prices.

Of course, most foreign manufacturers importing their products to Russia through established distribution chains are less than happy about this grey market. From the point of view of intellectual property, the most convenient way to control imports is through trademark enforcement. Rights holders have always understood that Russian law prohibits unauthorised imports of branded goods into the territory of the Russian Federation, regardless of whether the goods in question are original. This understanding was supported by amendments to the Trademark Law adopted in 2002, which clearly state that a rights holder cannot interfere in the sale of original branded goods if these were introduced to the Russian market by the rights holder or with its consent. There was a general consensus that this rule stood for the so-called "exhaustion principle" of national trademark rights, meaning that the lawful sale of original products abroad does not allow third parties to import the same products to Russia without the rights holder's consent.

Taking into account the scale of the Russian territory and the technical difficulties of supervising trade in the interior, it is logical to try to prevent unauthorised imports at the borders, applying to Customs for help. In recent years Customs has helped rights holders as much as possible: a special trademark register was established by Customs and trademark-friendly rules were introduced into the Customs Code in 2003. Many counterfeit goods and grey imports have been seized at the borders as result of these efforts, leading to the confiscation of the imported goods and the grey importers being fined.

Grey importers strike back

However, grey importers have never been

"The global economic crisis, which reached Russia last year, created an unfavourable political and economic environment for such claims. Instead, the crisis had the effect of making arguments about freedom of trade, local business protectionism and fairness look more persuasive than ever"

an easy target for Customs and rights holders; they have dozens of tricks for avoiding responsibility (eg, denying knowledge of the fact that a trademark was placed on the imported goods or arguing that Customs acted prematurely where no actual import occurred). The court practice was also inconsistent. Despite this, there was never any serious doubt among IP professionals that grey imports infringe trademarks.

However, Russia is a country of surprises, even where legal matters are concerned.

The turning point occurred in a case involving a confiscated Porsche Cayenne automobile. The matter started innocuously when in early 2008 Customs seized a car after Porsche declared that it was being imported without its consent – Porsche supported Customs throughout the ensuing administrative procedure against the importer. The importer defended itself fiercely by highlighting the absurdity of the situation: one single car legally bought abroad was suddenly branded a counterfeit and confiscated without any compensation. The case was heard by three courts, all of which found in favour of Porsche. The Higher Arbitration Court of the Russian Federation was the last chance for the importer, and in February 2009 this high instance court issued a ruling which changed everything. Having thoroughly considered the wording of the Code for Administrative Offences, which was previously used to punish grey importers, the court found that the law provides for the confiscation of counterfeit goods only, whereas the car in this instance was an original product and could not be considered counterfeit. The court ordered the release of the car and the dismissal of the administrative case.

Whether this decision denies that parallel imports infringe trademarks is less clear. Many thought so, especially supporters of parallel imports. As soon as the decision was announced, lower courts throughout Russia began to turn down customs claims concerning original products. The courts were not impressed by the issues of consumer security and obligation limitations raised by rights holders to argue against the release of grey imports onto the Russian market. The change in court practice also put an end to the confiscation of used products imported to Russia for resale: after a year of successful cooperation with Customs, one of the world's biggest tyre manufacturers failed in its attempt to have a consignment of imported renovated tyres confiscated.

Of course, the High Arbitration Court could not make this drastic change in court practice based on a literal interpretation of a single word in the law. The court decision-making procedure suggests that the panel of judges should first explain why the case in question requires reconsideration and what principles of law are affected, before going on to examine the case itself. In *Porsche Cayenne* this explanation went far beyond a literal interpretation of the law. According to the judges, the core problem was to distinguish between private interests and public interests, as represented by the Code for Administrative Offences and Customs. As regards trademark rights, the public interest extends only to protecting consumers from counterfeit products. The distribution of original products, including unauthorised imports, belongs to the field of private interests, where Customs should not intervene. In particular, the court stated that: "The whole set of civil responsibilities for violating trademark rights constitutes a separate and sufficient complex of protective measures for trademark rights. Applying public responsibilities for such violations should not be aimed exclusively at satisfying the private interests of the trademark owner, but should be designed to prevent illegal activities which abuse public order, the particular example of which is the sale of counterfeited goods."

In other words, the High Court was not about to decide whether grey imports are a type of trademark infringement. It wished only to stop original goods from being confiscated by Customs and let rights holders deal with the issue using other legal mechanisms. This position may be considered a compromise between foreign rights holders, trying to protect their authorised distributors, and the independent and in most cases small Russian businesses, which were not intending to deceive the public about the goods they sold. Reading between the lines of the decision, the court was telling rights holders that while it denied this particular administrative offence, they were free to pursue civil claims themselves.

The double-headed eagle of Russian justice

Following this hint, various rights holders embarked on a series of civil claims against grey importers. Several trademark infringement suits were launched against grey importers based on the Civil Code and information provided by Customs; these suits requested preliminary injunctions (to detain the goods at the borders), orders for the destruction of goods or compensation for damages.

However, the outcome turned to be not so positive. The global economic crisis, which reached Russia last year, created an unfavourable political and economic environment for such claims. Instead, the crisis had the effect of making arguments about freedom of trade, local business protectionism and fairness look more persuasive than ever.

Why should the state support foreign rights holders in their attempt to control the Russian market? Why should the state set barriers for consumers that wish to buy the same product at a lower price? Why should the state let foreign businesses decide what is good for the Russian market? The courts have had to face all these questions, in addition to the many legal arguments raised by grey importers to defend their right to buy and sell. A grey importer in Kayaba described the situation thus: "Parallel imports are a competitive market's natural reaction to discriminations in price, quality or supply by trademark owners. In case of such imbalances, the local market tries to meet demand for original products by importing them from countries where the trademark owner does not pursue such marketing policies. Thus, parallel imports happen only where the trademark owner, intentionally or not, supplies goods at a higher price than in other countries, of a lower quality than in other countries or stops the supply altogether. Parallel imports are a marketing tool used to protect consumers against such monopolistic discrimination."

Although the High Court's decision in *Porsche* cast no doubts over the rights holder's exclusive right to import original goods to Russia, and despite the general prohibition on any unauthorised use of the trademark (with a small list of exceptions set out in the Civil Code), grey importers kept arguing that foreign rights holders had exhausted their trademark rights in their original products by selling them first outside Russia.

Last year these arguments were heard by several Russian courts of different instances and in different locations. Some courts supported the arguments of the grey importers, while others found for the rights holders. The best examples of these two legal roads are the *Kayaba* and *Uvex* cases.

Kayaba Industry Co, Ltd, a Japanese manufacturer of automobile spare parts, has long suffered as a result of unauthorised imports of its products to Russia. Kayaba's longstanding collaboration with Customs was ruined by the *Porsche Cayenne* case; it lost several administrative cases one after the other due to the fact that the imported parts were genuine. Based on the facts discovered by Customs and investigated in the administrative cases, Kayaba tried its luck in a civil suit. This was heard by the Arbitration Court of Moscow, commonly considered to be the most experienced IP court in Russia. Surprisingly, the court was persuaded by the grey importer's arguments and denied Kayaba's suit. According to the court, Russian law does not recognise the import of a branded good as trademark use. Instead, it held that the cross-border use of a trademark must comprise at least two actions: marking up goods and then importing them. Consequently, the grey importer's import of the original goods could not be considered as trademark infringement.

Kayaba appealed to the Ninth Arbitration Appellation Court, which upheld the decision. Kayaba made a second attempt before the Moscow court, filing a similar suit against a different grey importer. However, the result was the same and the court ruled against Kayaba for a second time.

While this was ongoing, another victim of parallel imports in a different region of Russia managed to succeed in having its exclusive rights to its trademark recognised. Uvex Arbeitsschutz Gmbh, a German manufacturer of protective wear under the UVEX mark, won its trademark infringement case before the St Petersburg Arbitration Court against the grey importer of its original goods. Despite the grey importer's best efforts and the Moscow court's opposite practice, this decision was confirmed by the Thirteenth Arbitration Appellation Court and, more importantly, by the Federal Arbitration Court of the Northwest Region (which supervises lower courts' application of the law).

The St Petersburg courts demonstrated their immunity to the legal juggling attempted by the grey importer. Their rulings were based on a straightforward reading of the law, which provides the rights holder with an exclusive right to use its trademark in any way not prohibited by the law; whereas the exception about the exhaustion of trademark rights comes into play only where the goods were introduced onto the Russian market with the rights holder's consent.

The latest decision (the Federal Arbitration Court of the Northwest Region announced its verdict on 9th February 2010) appears extremely important for Russian court practice in respect of the issue of grey imports. It will be appealed to the High Arbitration Court, which will then have to address the issue of parallel imports once again, but this time from the perspective of the rights holder's private interests.

End of story?

The reader may now wonder how he or she should do business in Russia before the High Arbitration Court addresses the question of grey imports to take into account the practices of different Russian courts. The advice is simple: if the law of your country provides that it is illegal for local distributors to sell your products without your consent, then you should affix a label to the product stating that it is not intended for sale outside your country or region. You can also differentiate products destined for the Russian market from those intended for other regions, even improving aspects mostly likely to appeal to Russian consumers. In addition, a disclaimer should be included in all your Russian advertisements stating that the ad relates only to goods imported with the rights holder's consent. These steps should help your lawyers to protect your trademark rights in Russia against grey imports; although in the current environment of divided and contradictory case law, there are no guarantees. iam

Mark Chizhenok is an attorney at law and a patent and trademark attorney. He is an experienced IP practitioner and litigator, as well as a speaker and legal researcher. He has been involved in IP practice for over 10 years, often dealing with important and groundbreaking cases. In 1999 Mr Chizhenok joined a major Russian IP law firm, where he specialised in internet-related disputes. From 2005 until 2007 he was an associate at a foreign boutique law firm, where he was responsible for building the IP practice.

Mark Chizhenok
Partner
mark.chizhenok@impartners.ru
+7 926 2357679

Ivanov, Makarov & Partners
Russia
www.impartners.ru

Dmitry Makarov is a lawyer and trademark attorney. He began his career as a lawyer in a major Russian IP firm and qualified as a trademark attorney in 2006. He advises on the protection and exploitation of intellectual property, in particular trademarks, copyright, patents, design rights, confidential information and trade secrets. Mr Makarov has extensive experience in IP transactions and due diligence. He is a member of the Licensing Executives Society, Russia.

Dmitry Makarov
Partner
dmitry.makarov@impartners.ru
+7 916 1142703

Ivanov, Makarov & Partners
Russia
www.impartners.ru