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THE UNITED STATES' DOCTRINE OF EXHAUSTION: PARALLEL IMPORTS OF PATENTED GOODS

by Margreth Barrett

I. INTRODUCTION

United States patent, copyright and trademark law have all traditionally been tempered by the doctrine of exhaustion, also called the doctrine of first sale.

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3. In a recent article, Professor Adelman has assigned different meanings to the labels "doctrine of exhaustion" and "doctrine of first sale" in the patent context. Martin J. Adelman, The Exhaustion Doctrine in American Patent Law (Apr. 16 & 17, 1998) (paper presented at the Fordham University School of Law Sixth Annual Conference on International Intellectual Property Law & Policy) (arguing that under the "doctrine of exhaustion," sale of a patented product exhausts the patentee's rights with respect to the product even if the parties intended otherwise, while under the "doctrine of first sale," exhaustion of rights is a default rule that applies when the parties to the sale expressed no intention to the contrary). Other commentators have recognized the same two approaches to the issue of exhaustion, but have not necessarily adopted the same terminology. See, e.g., Christopher Heath, Parallel Imports and International Trade, 28 INT. REV. INDUS. PROP. & COPYRIGHT 623, 625-27 (1997) (distinguishing between continental or "absolute" exhaustion and common-law or "implied license" exhaustion); Richard H. Stern, Some Reflections on Parallel Importation of Copyrighted Products into the United States and the Relation of the Exhaustion Doctrine to the Doctrine of Implied License, 4 EUR. INTELL. PROP. REV. 119 (1989) (distinguishing the "exhaustion doctrine" from the "implied license doctrine"); Abdulquwia A. Yusuf & Andres M. von Hase, Intellectual Property Protection and International Trade, 16 WORLD COMPETITION: L. & ECON. 115 (1992) (distinguishing the "exhaustion" doctrine of continental Europe from the "implied license" doctrine of common-law countries); see also Mark D. Janis, A Tale of the Apocryphal Axe: Repair, Reconstruction, and the Implied License in Intellectual Property Law, 58 MD. L. REV. 423, 428 (1999) (suggesting that "exhaustion of rights" and "implied license" doctrines are separate doctrines).

United States courts have not distinguished the terms, and may use the terms "exhaustion" and "doctrine of first sale" interchangeably. See, e.g., Intel Corp. v. ULSI Sys. Tech., Inc., 995 F.2d 1566, 1568 (Fed. Cir. 1993), cert. denied, 510 U.S. 1092 (1994). This article will thus treat the terms as synonymous, while recognizing that the two distinct approaches described by...
This doctrine provides that once an intellectual property owner releases or authorizes others to release goods bearing or embodying the intellectual property into the stream of commerce, it exhausts its right to control the goods; purchasers and their successors in title are free to use and resell the goods without seeking the intellectual property owner’s authorization or paying a further royalty. The doctrine of exhaustion reflects at least two important policies underlying the United States’ intellectual property laws.

First, the doctrine honors the law’s general abhorrence of restraints on alienation, and the interference such restraints impose on a free market. Second, it reflects the traditional understanding in United States law that intellectual property rights are limited rights afforded to individuals not by virtue of any natural right, but for the specific purpose of accomplishing a pragmatic goal: promotion of the general public welfare. The law contemplates that the public benefits from a robust, competitive marketplace. Granting intellectual property rights to individual creators promotes such a marketplace by providing an incentive to create, leading individuals to produce a greater selection of goods and services for public consumption. However, the rights afforded to intellectual property owners must be limited to those necessary to provide the desired incentive. By their nature, intellectual property rights restrict public access to the goods and services to which they attach. If they are not sufficiently limited, they may encumber, rather than enhance, a competitive marketplace. Thus, each of the three primary intellectual property doctrines strives to attain a balance of rights and limitations that effectively provides an incentive to create, but permits as much public and competitor access as is possible short of undermining the

Professor Adelman and others do in fact exist. This article will discuss three forms of exhaustion: 1) international exhaustion, which corresponds most closely to the concept that Professor Adelman describes as “doctrine of exhaustion” and others describe as “continental exhaustion;” 2) modified international exhaustion, which recognizes the ability of patentees to contract expressly out of what would otherwise be an international exhaustion rule; and 3) territorial exhaustion. See infra notes 13-22 and accompanying text.

4. See supra note 3. This will be discussed more fully below. Under United States patent law, the exhaustion of rights in some cases may be avoided through an express contractual agreement to the contrary.


incentive function of the rights.\textsuperscript{7}

United States case law has made it clear that free riding in the marketplace is not inherently undesirable or unlawful.\textsuperscript{8} Thus, for example, a subsequent seller of a product may take advantage of the original manufacturer/seller's reputation or expenditures to create consumer demand, as long as the subsequent seller does not injure the public in the course of doing so.\textsuperscript{9} Indeed, free riding on others' work is generally deemed beneficial to the public and is facilitated under the law, as long as it does not seriously interfere with the originator's incentive to invest in research and development of new products, services, inventions and works of authorship.\textsuperscript{10}

In line with the policies described above, the doctrine of exhaustion contemplates that an intellectual property owner will have exclusive control over the first sale of goods embodying the intellectual property, and that this should be sufficient to ensure that there is a financial incentive to invest in the creative

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\item \textsuperscript{7} See, e.g., Bonito Boats, Inc. v. Thunder Craft Boats, Inc., 489 U.S. 141, 146 (1989) ("From their inception, the federal patent laws have embodied a careful balance between the need to promote innovation and the recognition that imitation and refinement through imitation are both necessary to invention itself and the very lifeblood of a competitive economy"); Feist Publications, Inc. v. Rural Tel. Serv. Co., Inc., 499 U.S. 340 (1991).
\item \textsuperscript{8} See, e.g., Bonito Boats, 489 U.S. at 151 ("The novelty and non-obviousness requirements of patentability embody a congressional understanding, implicit in the Patent Clause itself, that free exploitation of ideas will be the rule, to which the protection of a federal patent is the exception."); Feist Publications, 499 U.S. at 349.
\item It may seem unfair that [under copyright law] much of the fruit of the compiler’s labor may be used by others without compensation. As Justice Brennan has correctly observed, however, this is not ‘some unforeseen byproduct of a statutory scheme.’ It is, rather, ‘the essence of copyright,’ and ‘a constitutional requirement.’ The primary objective of copyright is not to reward the labor of authors, but ‘to promote the Progress of Science and useful Arts.’ To this end, copyright assures authors the right to their original expression, but encourages others to build freely upon the ideas and information conveyed by a work.
\item \textsuperscript{9} See, e.g., Champion Spark Plug Co. v. Sanders, 331 U.S. 125 (1947); Prestonettes, Inc. v. Coty, 264 U.S. 359 (1924).
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process. Extending legal rights to control goods beyond their first sale is unnecessary to accomplish the incentive function, and may unduly interfere with competition and the free movement of goods in the marketplace.\footnote{See generally United States v. Masonite Corp., 316 U.S. 265, 277-80 (1942); Kendal v. Winsor, 62 U.S. (21 How.) 322, 329 (1858); Keeler v. Standard Folding-Bed Co., 157 U.S. 659, 665-67 (1895) (balancing patentee’s interest in profiting from patented invention against “inconvenience and annoyance to the public” in the course of applying the doctrine of exhaustion); The Platt & Munk Co., Inc. v. Republic Graphics, Inc., 315 F.2d 847, 854 (2d Cir. 1963); Sebastian Int'l, Inc. v. Longs Drug Stores Corp., 53 F.3d 1073, 1075 (9th Cir. 1995).}

Perhaps the most perplexing problem that arises in connection with the doctrine of exhaustion is its application to parallel imports. Parallel imports are goods that are sold, or authorized for sale, abroad by the United States intellectual property owner, but are subsequently imported into the United States without the United States intellectual property owner’s authorization.\footnote{See John S. Chard & C. J. Mello\l, Intellectual Property Rights and Parallel Imports, 12 World Econ. 69 (1989). See generally, Claude E. Barfield & Mark A. Groombridge, The Economic Case for Copyright Owner Control over Parallel Imports, 1 J. World Intell. Prop. 903 (1998) (stating parallel imports are “genuine goods or services imported by a reseller into a country without the authorization of the owner of the intellectual property right in that country”); Harvey E. Bale, The Conflicts Between Parallel Trade and Product Access and Innovation: The Case for Pharmaceuticals, 1 J. Internat. Econ. L. 637 (1998) (stating “parallel trade” is “the exportation and importation of products through distribution channels that are other than those authorized by the owner or licensee of a patented . . . product”).} Assuming that the United States intellectual property owner (or an affiliated business entity) made the first sale abroad, or authorized a licensee to do so in return for a royalty payment, it can be characterized as having received the benefit of the first sale of the good, as envisioned by the United States intellectual property laws. Should the doctrine of exhaustion apply, releasing the goods from further control by the intellectual property owner, so that subsequent purchasers can import them into the United States and resell them in competition with the United States rights owner? Two competing theories have emerged to address this quandary.

The “international exhaustion” or “universality” theory provides that the doctrine of exhaustion should apply whenever the United States intellectual property owner sells or authorizes the first sale of the good, regardless of
whether the good was manufactured or originally sold in the United States, or abroad. The reasoning, essentially, is that the United States intellectual property owner has enjoyed the opportunity to control the first sale, which occurred abroad, and can be presumed to have obtained sufficient benefit to maintain an incentive to invest in creative efforts. Regardless of whether the good is protected by intellectual property rights in the foreign country, the United States intellectual property owner's decision to sell there generally suggests that it finds the sale beneficial. Providing a "second bite of the apple," by granting the opportunity to control foreign purchasers' resale of the goods in the United States, is not necessary in order to serve the incentive function of intellectual property laws, and would interfere unnecessarily with the free international flow of goods and the competitive marketplace, depriving consumers of the benefits of competition and greater accessibility of goods. It also arguably would favor intellectual property owners selling abroad over intellectual property owners whose sales are strictly domestic, since the latter have no opportunity to control resales.\footnote{See generally Frederick M. Abbott, First Report (Final) to the Committee on International Trade Law of the International Law Association on the Subject of Parallel Importation, 1 J. INTERNAT. ECON. L. 607 (1998); Warwick A. Rothnie, Parallel Imports—Smokescreen or Brushfire Smoke? in INTERNAT. INTELL. PROP. L. & POL., 311-65 (Hugh Hansen, ed. 1996); S. K. Verma, Exhaustion of Intellectual Property Rights and Free Trade—Article 6 of the TRIPs Agreement, 29 INTERNAT. REV. INDUS. PROP. & COPYRIGHT L. 534 (1998); Yusuf & von Hase, supra note 3.}

The "territorial" or "domestic" exhaustion theory essentially limits the doctrine of exhaustion to goods manufactured and initially sold within the territory of the United States. The reasoning is that intellectual property laws only provide rights within the boundaries of individual nations, and the doctrine of exhaustion should extend no further, geographically, than the rights to be exhausted. A United States intellectual property owner selling goods abroad does not benefit from its United States intellectual property rights in the sale. Therefore, it should be able to assert those rights (for the first time) when the goods enter the United States without the owner's authorization. It is irrelevant whether the United States intellectual property owner enjoys patent, copyright or trademark rights comparable to its United States rights in the country in which the first sale took place, or otherwise reaped a benefit from the sale abroad. Each country's intellectual property laws provide a separate opportunity to benefit and control goods as they enter that country's borders. Moreover, the ability to control the movement of goods from one country to another is
necessary from a business standpoint, because it permits the United States intellectual property owner, effectively, to adapt its price and marketing methods to each country in which it does business.\textsuperscript{14}

The United States has adopted neither the international exhaustion nor the territorial exhaustion theory, to its fullest possible extent. The specific application of the doctrine of exhaustion in each of the three primary intellectual property regimes has varied, in part because of differences in the statutory language codifying each regime, and in part because of perceived differences in the purposes of each regime.

Recent case opinions construing Lanham Act § 42\textsuperscript{15} and Tariff Act § 526\textsuperscript{16} establish a partial or qualified rule of international exhaustion for United States trademark owners: as a general rule, United States trademark owners lack authority to prevent the import and resale of parallel imports, as long as the United States owner itself, or an affiliated business entity, put the goods bearing the mark on the market abroad.\textsuperscript{17} However, an important exception to this rule arises when the imported goods differ materially from those the United States trademark owner sells domestically. In such cases, courts have reasoned, consumers may be misled by the importer’s sales of the foreign goods bearing the same mark—they may rely on the mark to indicate that the foreign goods possess the same qualities that their domestic counterparts have, when they do not. Since the very purpose of trademark rights is to avoid such consumer confusion about the nature or quality of goods, courts have reasoned that trademark owners must be permitted a cause of action for trademark infringement to prevent the parallel imports under these circumstances.\textsuperscript{18}

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In a very recent decision, the Supreme Court construed the Copyright Act to apply a rule of international exhaustion when the copyrighted goods at issue were initially manufactured in the United States, and then sold to foreign purchasers.\textsuperscript{19} While the Court's reasoning in that case would seem to extend to goods that the United States copyright owner, or its licensee, manufactured abroad, the Court had no occasion to expressly address that issue. The Court of Appeals for the Third Circuit has suggested that the same rule of exhaustion should apply, at least in the case of goods manufactured abroad by the United States copyright owner itself.\textsuperscript{20} However, another line of cases has construed Copyright Act § 109(a) to establish a rule of territorial exhaustion with regard to goods manufactured outside of the United States.\textsuperscript{21}

Notwithstanding the recent judicial focus on the extent of the doctrine of exhaustion (and thus the legality of parallel imports) in the trademark and copyright context, courts have had relatively little to say about the applicability of United States patents to prohibit parallel import of goods embodying patented language of Tariff Act § 526, the Supreme Court has also differentiated sales abroad by licensees of the United States trademark owner from sales abroad by the owner itself or an affiliated entity, holding that, under § 526, United States Customs must prevent entry of parallel imports in the former case. K-Mart Corp. v. Cartier, Inc., 486 U.S. 281 (1988).

The case law has not yet indicated conclusively whether a similar distinction between goods sold abroad by an owner or its affiliates and goods sold abroad by a licensee will be made in the case of infringement claims under the Lanham Act. There is no apparent reason why that distinction should be carried over into the Lanham Act, since it relies on specific language in Tariff Act § 526 that does not exist in the Lanham Act. In the domestic context, the doctrine of exhaustion traditionally has not distinguished between goods sold by the trademark owner itself and goods sold by others who are authorized to do so by the trademark owner. See Restatement (Third) of Unfair Competition § 24, cmt. b (1995).


inventions. Yet, that topic has become the subject of important multinational trade negotiations and spirited international debate,\(^{22}\) and has been the subject of highly controversial decisions in Japanese and European courts.\(^{23}\) On the

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\(^{22}\) Parallel importation of goods protected by intellectual property rights was debated in the Uruguay Round of Negotiations on the General Agreement on Tariffs and Trade (Hereafter “GATT”), which introduced minimum standards for intellectual property protection into the GATT. See Agreement on Trade-Related Aspects of Intellectual Property Rights, Including Trade in Counterfeit Goods, 33 I.L.M. 81 (1994) (hereafter “TRIPs Agreement”). Because the parties were unable to reach agreement on the proper scope of the exhaustion doctrine, TRIPs Article 6 ultimately was added to exclude the exhaustion issue from the WTO dispute resolution process. It reads in pertinent part:

> For the purposes of dispute settlement under this Agreement . . . nothing in this Agreement shall be used to address the issue of the exhaustion of intellectual property rights. While TRIPs Article 28(1)(a) requires all World Trade Organization members to provide patentees an exclusive right of importation, a footnote to that Article clarifies: This right, like all other rights conferred under this Agreement in respect of the use, sale, importation or other distribution of goods, is subject to the provisions of Article 6.

*Id.* (internal citations and quotations omitted). For further discussion of these provisions, see discussion *infra* Part IV. It is likely that the issue of exhaustion will be taken up again in multinational trade negotiations.


\(^{23}\) See BBS Kraftfahrzeugtechnik AG v. Rashimekkusu Japan Co. Ltd. & JAP Auto Prods. Co.
domestic front, Congress recently amended the United States Patent Act to incorporate, for the first time, an express right of importation, seeming on the surface to invite litigation over parallel import of patented goods.\textsuperscript{24} United States legal literature has begun to pick up on the issue from a domestic perspective.\textsuperscript{25} However, one of the more interesting features of the legal literature is the sharp difference in commentators' interpretation of the existing United States case law on the subject. A significant number of commentators have characterized United States case law as establishing a territorial exhaustion rule for parallel-patented goods.\textsuperscript{26} Others have characterized it as establishing a modified international exhaustion rule.\textsuperscript{27}

This article undertakes a comprehensive evaluation of the status of parallel imports under the United States Patent Act. Section II provides a general overview of the doctrine of exhaustion and its underlying theoretical justifications in United States patent law. Section III provides a thorough evaluation of the existing case law regarding parallel imports of patented products, examines some unresolved issues, and concludes that the weight of United States judicial authority adopts a form of modified international exhaustion, rather than the territorial exhaustion rule that a number of commentators have asserted. Section IV examines the impact of Congress' recent amendments to provide a general importation right, concluding that it is unlikely that Congress intended to change the existing balance of rights concerning parallel import of patented goods. Finally, Section V reviews and

\textbf{24.} See infra note 133 and accompanying text.


\textbf{27.} See, e.g., 5 DONALD S. CHISUM, CHISUM ON PATENTS § 16.03[2][a][iv] (1998); Adelman, supra note 3, at 13; Donnelly, supra note 25.
evaluates arguments that have been raised in favor of the alternative territorial exhaustion doctrine, and finds that advocates of this doctrine have not made a convincing case for change.

II. THE DOCTRINE OF EXHAUSTION IN UNITED STATES PATENT LAW

The United States’ Patent Act does not codify the doctrine of exhaustion, but the doctrine is well established in the case law as a limitation on patentees’ rights. The Supreme Court embraced the doctrine in Adams v. Burke,28 noting:

[W]hen the patentee, or the person having his rights, sells a machine or instrument whose sole value is in its use, he receives the consideration for its use and he parts with the right to restrict that use. The article . . . passes without the limit of the monopoly. That is to say, the patentee or his assignee having in the act of sale received all the royalty or consideration which he claims for the use of his invention in that particular machine or instrument, it is open to the use of the purchaser without further restriction on account of the monopoly of the patentee.

* * *

[W]hen they are once lawfully made and sold, there is no restriction on [the articles’] use to be implied for the benefit of the patentee or his assignees or licensees.29

Subsequent case opinions have made it clear that the doctrine gives lawful purchasers of patented goods the unrestricted right not only to use the goods, but also to resell them,30 and applies equally to goods sold directly by the patentee

28. 84 U.S. (17 Wall.) 453 (1873).
29. Id. at 456-57. The foundation for this rule of law had been laid in earlier decisions. See Bloomer v. McQuewan, 55 U.S. (14 How.) 539 (1852); Bloomer v. Millinger, 68 U.S. (1 Wall.) 340 (1863); Mitchell v. Hawley, 83 U.S. (16 Wall.) 544 (1872).
30. See, e.g., United States v. Univis Lens Co., 316 U.S. 241, 250 (1942) ("[S]ale of [a patented article] exhausts the monopoly in that article and the patentee may not thereafter, by virtue of his patent, control the use or disposition of the article."); Intel Corp. v. U.L.S.I. Sys. Tech., Inc., 995 F.2d 1566, 1568 (Fed. Cir. 1993) ("[T]he patent owner’s rights with respect to the product end with its sale, and a purchaser of such a product may use or resell the product free of the patent."); cert. denied, 510 U.S. 1092 (1994); Unidisco, Inc. v. Schattner, 824 F.2d 965, 968 (Fed. Cir. 1987) ("Resale of the product by Unidisco could not infringe the patent if Unidisco purchased the product from an authorized seller.").
and those sold by the patentee’s licensees.31

Over the years, the case opinions applying the doctrine have explained its underlying purpose and justification. They note that the purpose of the patent law is to secure the benefit of an invention (and the investment in research and development underlying it) to the patentee, in order to provide an incentive to invent and as a means of rewarding the inventor for his act of disclosure to the public through the patent application process. However, they have stressed that this purpose is accomplished once the patentee has received the sales price or (in the case of sales by authorized licensees) royalty payment arising from the initial sale of the patented article. As the Supreme Court has explained:

The declared purpose of the patent law is to promote the progress of science and the useful arts by granting to the inventor a limited monopoly, the exercise of which will enable him to secure the financial rewards for his invention .... The patentee may surrender his monopoly in whole by the sale of his patent or in part by the sale of the article embodying the invention ....

* * *

Our decisions have uniformly recognized that the purpose of the patent law is fulfilled with respect to any particular article when the patentee has received his reward for the use of his invention by the sale of the article, and that once that purpose is realized the patent law affords no basis for restraining the use and enjoyment of the thing sold.32

Sometimes the issue arises whether a transaction that purports not to be an outright “sale”, such as a licensing agreement, triggers the doctrine of first sale.

31. See, e.g., Intel Corp., 995 F.2d at 1568 (holding the doctrine of exhaustion “applies similarly to a sale of a patented product manufactured by a licensee acting within the scope of its license”); Unidisco, 824 F.2d at 968; Cyrix Corp. v. Intel Corp., 846 F. Supp. 522, 538 (E.D. Tex.), aff’d, 42 F.3d 1411 (Fed. Cir. 1994); 5 DONALD S. CHISUM, CHISUM ON PATENTS § 16.03[2][a], at 16-137 (1997) (“An authorized sale of a patented product exhausts the patent monopoly as to that product. Thus, a purchaser of such a product from the patent owner or one licensed by the patent owner may use or resell the product free of control or conditions imposed by the patent owner.”).

32. United States v. Univis Lens Co., 316 U.S. 241, 250-51 (1942); see also United States v. Masonite Corp., 316 U.S. 265, 278 (1942); B. Braun Med., Inc. v. Abbott Lab., 124 F.3d 1419, 1426 (Fed. Cir. 1997); Brandt Consol., Inc. v. Agrimar Corp., 801 F. Supp. 164, 173 (C.D. Ill. 1992) (“The purpose of the patent law is thus fulfilled with respect to any particular article once the patentee has received the reward for the use of his invention by selling the article.”).
In such cases, courts attempt to determine "whether or not there has been such a disposition of the article that it may fairly be said that the patentee has received his reward for the use of the article."\textsuperscript{33} If the patentee has received the same kind of benefit that he would have received from an outright sale, then the purpose of the patent right is fulfilled, and the patentee's rights in the article are exhausted.

One might argue that if the purpose of the Patent Act is to benefit inventors in order to incite greater creative endeavors, inventors should be able to control subsequent dispositions of the patented article, as well as the initial one. The ability to prohibit resales or demand a royalty for each resale would surely provide further benefit to the patentee. However, the courts have stressed that the purpose of the patent law is not to ensure the greatest possible financial return to the patentee. Rather, the ultimate purpose of the patent law is to benefit the public. On balance, granting patentees control over the initial sale of patented articles will benefit the public by providing a financial incentive to invent and disclose inventions to the public. However, extending the patentee's rights beyond the initial sale would exceed what is strictly necessary to provide an incentive to invent, and interfere unduly with the free market. Thus, the Supreme Court has explained that in determining the extent of the patentee's rights in articles embodying the patented invention,

[R]egard must be had for the dominant concern of the patent system .... [T]he promotion of the progress of science and the useful arts is the "main object;" reward of inventors is secondary and merely a means to that end .... Whilst the remuneration of genius and useful ingenuity is a duty incumbent upon the public, the rights and welfare of the community must be fairly dealt with and effectually guarded. Considerations of individual emolument can never be permitted to operate to the injury of these.

* * *

[S]ince patents are privileges restrictive of a free economy, the rights which Congress has attached to them must be strictly construed so as not to derogate from the general law beyond the necessary requirements of the patent statute.\textsuperscript{34}

\textsuperscript{33} United States v. Masonite Corp., 316 U.S. 265, 278 (1942); see also Cyrix Corp. v. Intel Corp., 846 F. Supp. 522, 538-40 (E.D. Tex.), aff'd, 42 F.3d 1411 (Fed. Cir. 1994).

\textsuperscript{34} Masonite Corp., 316 U.S. at 278-80 (quoting Pennock v. Dialogue, 27 U.S. (2 Pet.) 1, 19 (1829), and Kendall v. Winsor, 62 U.S. (21 How.) 322, 329 (1858)). The Kendall decision, on which the Masonite Court relied, elaborated:
Although United States courts have not generally characterized the exhaustion doctrine itself as contract-based, the Court of Appeals for the

It is undeniably true, that the limited and temporary monopoly granted to inventors was never designed for their exclusive profit or advantage; the benefit to the public or community at large was another and doubtless the primary object in granting and securing that monopoly. This was at once the equivalent given by the public for benefits bestowed by the genius and meditations and skill of individuals, and the incentive to further efforts for the same important objects. The true policy and ends of the patent laws enacted under this Government are disclosed in that article of the Constitution, the source of all these laws, viz: "to promote the progress of science and the useful arts," contemplating and necessarily implying their extension, and increasing adaptation to the uses of society.

Kendal, 62 U.S. at 328. See also Keeler v. Standard Folding-Bed Co., 157 U.S. 659, 666-67 (1895) (finding that a failure to find a patentee's rights exhausted after the first sale would constitute an "inconvenience and annoyance to the public . . . too obvious to require illustration"); Aro Mfg. Co., Inc. v. Convertible Top Replacement Co., Inc., 365 U.S. 336, 357-60 (1960) (Black, J., concurring); Lackner Co. v. Quehl Sign Co., 145 F.2d 932, 934 (6th Cir. 1944) ("The exclusive right conferred by a patent is a monopoly permitted only because of the public benefit to be derived from the invention. The maintenance of the public interest is the dominant concern of the patent law; profit to the patentee is secondary."); Cyrix Corp. v. Intel Corp., 846 F. Supp. 522, 539-40 (E.D. Tex.), aff'd, 42 F.3d 1411 (Fed. Cir. 1994).

35. The United Kingdom and other British Commonwealth nations have based their version of the exhaustion doctrine on a theory of implied consent on the patentee's part arising out of the act of sale. See ROTHNIE, supra note 22, at 106-42, 183; Stack, TRIPS, Patent Exhaustion and Parallel Imports, 1 J. WORLD INTELL. PROP. 657, 668-69 (1998); see also infra note 136. The United States Supreme Court, the Court of Appeals for the Federal Circuit, and other United States courts have, in some circumstances, found implied licenses arising from the sale of a patented article. However, they have generally done so to uphold a purchaser's subsequent use or repair of the patented article against an infringement claim, and have not tended to look to an implied license rationale as the theoretical underpinning of a purchaser's right to resell (as opposed to use) the patented article. For example, in Aro Mfg. Co., Inc. v. Convertible Top Replacement Co., 377 U.S. 476, 484 (1964), the Supreme Court reasoned that "sale of a patented article by the patentee or under his authority carries with it an 'implied license to use,'" and thus maintain and repair, the patented article. In Kendall Co. v. Progressive Med. Tech., Inc., 85 F.3d 1570, 1573 (Fed. Cir. 1996), the Court of Appeals for the Federal Circuit held that this license to use and repair the patented article is implied from the act of sale "as a matter of law." See also United States v. Univis Lens, 316 U.S. 241 (1942), in which the Court stated:
Federal Circuit has held that patentees can counteract the effect of the doctrine through express contractual provisions restricting purchasers' subsequent use or resale of the patented article. In *Mallenckrodt, Inc. v. Medipart, Inc.*, the Federal Circuit found that the patentee could restrict purchasers of its patented medical device to a single use, and hold those who reused the device in violation of the restriction liable for patent infringement. The court reasoned that the

Sale of a lens blank by the patentee or by his licensee is ... in itself both a complete transfer of ownership of the blank, which is within the protection of the patent law, and a license to practice the final stage of the patented procedure [of grinding and polishing the lens]. The entire consideration and compensation for both is the purchase price paid by the finishing licensee to the Lens Company.


The principle that a purchaser of a patented article has the right to repair it during its useful life is based upon the idea that the patentee, in selling his protected article, intends to and does part with the use thereof, and that the buyer intends to and does buy the use of the machine until it wears out or becomes substantially destroyed. For this reason, the license to repair is limited to preserving the article's fitness for use so far as it may be affected by wear or breakage; beyond this there is no license. The royalty paid by the buyer is intended by the parties as compensation to the patentee for parting with his exclusive right of use.

_Monroe_, 229 F. Supp at 353. _But see_ McCoy _v._ Mitsubishi Cutlery, Inc., 67 F.3d 917 (Fed. Cir. 1995). In _McCoy_, the patentee licensed the defendant to manufacture its patented knives. _Ibid._ The patentee ordered a number of the knives from the defendant, but later refused to pay for them. _Ibid._ When the defendant sold the knives under Texas law as a self-help remedy for the patentee's breach of contract, the patentee sued the defendant for patent infringement. _Ibid._ The Court of Appeals for the Federal Circuit held for the defendant, finding that "the law may create an implied license to enforce the contract obligations of the patent holder and recognize legal rights of aggrieved parties." _Ibid._ at 922. _C.f._ Holiday _v._ Mattheson, 24 F. 185 (S.D.N.Y. 1885) (Court seems to rely on the intent of the parties in finding exhaustion in a parallel imports case). See note 72, _infra_, and accompanying text.

The "benefit" and "implied consent" rationales for exhaustion of rights might be reconciled by finding that, as a result of the benefit the patentee received through the first sale, his consent to resell is implied as a matter of law.

36. 976 F.2d 700 (Fed. Cir. 1992).

37. _Ibid._
enforceability of restrictions on the use of patented goods derives from the patent grant itself, which is framed as “the right to exclude . . . [t]his right to exclude may be waived in whole or in part . . . . As in other areas of commerce, private parties may contract as they choose, provided that no law is violated thereby . . . . “38 In a subsequent decision, the Federal Circuit elaborated on its reasoning:

As a general matter . . . an unconditional sale of a patented device exhausts the patentee’s right to control the purchaser’s use of the device thereafter. The theory behind this rule is that in such a transaction, the patentee has bargained for, and received, an amount equal to the full value of the goods. This exhaustion doctrine, however, does not apply to an expressly conditioned sale or license. In such a transaction, it is more reasonable to infer that the parties negotiated a price that reflects only the value of the “use” rights conferred by the patentee. As a result, express conditions accompanying the sale or license of a patented product are generally upheld. Such express conditions, however, are contractual in nature and are subject to antitrust, patent, contract, and any other applicable law, as well as equitable considerations such as patent misuse. Accordingly, conditions that violate some law or equitable consideration are unenforceable. On the other hand, violation of valid conditions entitles the patentee to a remedy for either patent infringement or breach of contract.39

It is useful to note that the “contractual restriction” at issue in Mallenckrodt was not an individually negotiated agreement, but rather took the form of an inscription stating “Single Use Only” on the device itself, and reiterated in a packaging insert. While the court did not find it necessary to determine whether this was sufficient to condition the sale, it noted that “[i]n accordance with the Uniform Commercial Code a license may become a term of sale, even if not part of the original transaction, if not objected to within a reasonable time” which made it clear that purchasers must have adequate notice of restrictions before they can be deemed binding.40

38. Id. at 703.
39. B. Braun Med., Inc. v. Abbott Lab., 124 F.3d 1419, 1426 (Fed. Cir. 1997). The Mallenckrodt court acknowledged that contract law dictates whether a license restriction is binding on the purchaser, but explained that “the remedy for breach of a binding license provision is not exclusively in contract, for a license is simply a promise not to sue for what would otherwise be patent infringement.” Mallenckrodt, 976 F.2d at 708, n.7.
40. Mallenckrodt, 976 F.2d at 708. In Mallenckrodt, the defendant did not dispute actual notice of the restriction. The enforceability of similar sorts of restrictions frequently used in the sale of
In making its ruling, the *Mallencrodt* court distinguished a number of Supreme Court decisions that had found post-sale restrictions invalid, on the ground that these cases involved retail price fixing of patented goods or patent-enforced tie-ins. According to the court, these cases "established that price-fixing and tying restrictions accompanying the sale of patented goods were per se illegal. These cases did not hold, and it did not follow, that all restrictions accompanying the sale of patented goods were deemed illegal."42

The court also distinguished a line of early Supreme Court decisions,

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42. *Mallencrodt*, 976 F.2d at 704. The court relied on *General Talking Pictures Corp. v. Western Elec. Co.*, 305 U.S. 124 (1938), for the proposition that

[T]he patentee may grant a license 'upon any condition the performance of which is reasonably within the reward which the patentee by the grant of the patent is entitled to secure.' *Id.* at 704. According to the Court, "By the time of *General Talking Pictures*, price-fixing and tie-ins were generally prohibited under the antitrust law as well as the misuse law, while other conditions were generally recognized as within the patent grant. The prohibitions against price-fixing and tying did not make all other restrictions per se invalid and unenforceable.

*Id.* at 706.

The district court in *Mallencrodt* had declined to limit the earlier Supreme Court decisions in this fashion, stating that "their language suggests broader application." *Mallencrodt*, Inc. v. Medipart, Inc., No. 89-C-4524, 1990 WL 19535 (N.D. Ill. 1990). The Federal Circuit responded with the maxim that "general expressions, in every opinion, are to be taken in connection with the case in which those expressions are used. If they go beyond the case, they may be respected, but ought not to control the judgment on a subsequent suit when the very point is presented for decision." *Mallencrodt*, 976 F.2d at 708, n.8.
including Adams v. Burke. As noted supra, Adams, like several other early Supreme Court decisions, decisively stated that upon the first sale of a patented article, the article “passes without the limit of the monopoly” and is “open to the use of the purchaser without further restriction.”43 The court of appeals found that each of these decisions involved a first sale that was “without restriction,” and concluded that:

Adams v. Burke and its kindred cases do not stand for the proposition that no restriction or condition may be placed upon the sale of a patented article. . . . Unless the condition violates some other law or policy (in the patent field, notably the misuse or antitrust law), private parties retain the freedom to contract concerning conditions of sale.44

The Mallenckrodt court noted that the appropriate criterion for determining whether a restriction (other than a price-fixing or tying restriction) is unenforceable under the patent misuse doctrine or antitrust law is whether the restriction is “reasonably within the patent grant, or whether the patentee has ventured beyond the patent grant and into behavior having an anticompetitive effect not justifiable under the rule of reason.”45

III. APPLICATION OF THE EXHAUSTION DOCTRINE TO PATENTED PARALLEL IMPORTS

As noted earlier, there is disagreement in the legal literature about whether the United States follows an “international exhaustion” or “territorial exhaustion” doctrine with regard to patented goods sold abroad by, or under, the

44. Mallenckrodt, 976 F.2d at 707-708. For arguments that the Federal Circuit’s opinion misconstrued General Talking Pictures and the Adams v. Burke line of cases, see Adelman, supra note 3. See generally 5 DONALD S. CHISUM, CHISUM ON PATENTS § 16.03, at 100 (1998) (characterizing the Supreme Court’s decisions on whether a patent owner may limit exhaustion through contractual conditions as giving “apparently mixed signals”). For other criticisms of Mallenckrodt, see James B. Kobak, Contracting Around Exhaustion: Some Thoughts About the CAFC’s Mallenckrodt Decision, 75 J. PAT. & TRADEMARK OFF. SOC. 550 (1993).
45. Mallenckrodt, 976 F.2d at 708. For further elaboration of these standards, see Mallenckrodt, 976 F.2d at 706, 708-09, and infra note 82.
authority of the United States patentee, and imported into the United States by purchasers down the chain of title.46 Neither the Supreme Court nor the Court of Appeals for the Federal Circuit has directly addressed the issue.47 However, as will be demonstrated below, careful examination of the relatively sparse case authority reveals that the greater weight of authority adopts an international exhaustion doctrine, which is modified by the ability of patentees to contract out of it. Most arguments to the contrary have relied on an over-broad reading of the Supreme Court’s decision in Boesch v. Graff,48 and a single district court decision that failed to recognize, or discuss, the earlier decisions to the contrary.49 However, even those decisions that generally support a modified international exhaustion doctrine leave some important uncertainties concerning the scope of the exhaustion doctrine in the parallel imports context, which will also be explored in this Section.

The Court of Appeals for the Second Circuit initially stated the international exhaustion rule for parallel imports in Dickerson v. Matheson:50

A purchaser in a foreign country, of an article patented in that country and also in the United States, from the owner of each patent, or from a licensee under each patent, who purchases without any restrictions upon the extent of his use or power of sale, acquires an unrestricted ownership in the article, and can use or sell it in this country. The cases which have been heretofore decided by the Supreme Court in regard to the unrestricted ownership by purchasers in this country of articles patented in this country, and sold to such purchasers without limitation or condition, lead up to this principle.51

46. See supra note 22 and accompanying text.
48. 133 U.S. 697 (1890). For a discussion of the Boesch decision, see infra notes 107-110 and accompanying text.
50. 57 F. 524 (2d Cir. 1893).
51. Id. at 527 (citations omitted). Among other authority, the court cited Bloomer v. Millinger,
The Second Circuit built on the Matheson discussion in Curtiss Aeroplane & Motor Corp. v. United Aircraft Engineering Corp. In Curtiss, the plaintiff owned United States and Canadian patents for airplane-related inventions. During World War I plaintiff licensed the British government to have airplanes incorporating the patented inventions built in Canada for British use in the war. After the war, the British government sold some of the airplanes to the defendant, who imported them into the United States for resale. Plaintiff sued the defendant for infringement of its United States patents. In finding for the defendant, the Second Circuit noted:

The agreements will be searched in vain for any restriction or condition as to the right to use or vend; and in the absence of such restriction we understand the law to be that the British government obtained a full and unqualified right to use and sell the planes and engines, and that this right passed to all subsequent purchasers, and therefore to this defendant. No American or British decision asserting a contrary doctrine is known to us.

If a patentee or his assignee sells a patented article, that article is freed from the monopoly of any patents which the vendor may possess. If the thing sold contains inventions of several United States patents owned by the vendor, the article is freed from each and all of them; and if the vendor has divided his monopoly into different territorial monopolies, his sale frees the article from them all. If the vendor’s patent monopoly consists of foreign and domestic patents, the sale frees the article from the monopoly of both his foreign and his domestic patents, and where there is no restriction in the contract of sale the purchaser acquired the complete title and full right to use and sell the article in any and every country.

68 U.S. (1 Wall.) 340 (1863), and Mitchell v. Hawley, 83 U.S. (16 Wall.) 544 (1872), addressing exhaustion in the strictly domestic context and suggesting that it viewed the exhaustion doctrine to be unaffected by the site of the initial sale. For a discussion of the facts in Matheson, see infra note 63 and accompanying text.

52. 266 F. 71 (2d Cir. 1920).
53. Id.
54. Id.
55. Id.
56. Id. at 77-78. In support of its finding of no infringement, the Second Circuit relied on Holiday v. Mattheson, 24 F. 185 (S.D.N.Y. 1885). The court wrote:

That case raised the question whether the owner of a patent in the United States for an
The court distinguished earlier cases in which relief had been granted to a patentee against imported goods:

The plaintiff relies on certain cases, but an examination shows that they are plainly distinguishable, and do not support the plaintiff's contention. The cases upon which it relies belong to one or the other of two classes: (1) Those in which there has been a sale of a patented article, or a license to manufacture, but accompanied by explicit and unequivocal restrictions as to the time, or place, or manner of using the article so sold or licensed, or as to the ultimate disposal thereof. (2) Those in which there has been no participation whatever by the owner of the patent, either as a party or as a privy, in the putting out of the article which is alleged to infringe. And if a patentee retains title to the patented machine, which was not done in this case, he may restrict its manner of use, in the lease or other contract.\textsuperscript{57}

A New York district court applied this rule more recently in \textit{Kabushiki}

\underline{invention}, and who had sold the patented article in England without restrictions or conditions, could treat as an infringer one who had purchased the article in England of a vendee of the patentee, and could restrain him from using or selling the article in the United States.

\textit{Ibid.} In deciding the question adversely, Judge Wallace said:

When the owner sells an article without any reservation respecting its use, or the title which is to pass, the purchaser acquires the whole right of the vendor in the thing sold, the right to use it, to repair it, and to sell it to others; and second purchasers acquire the rights of the seller, and may do with the article whatever the first purchaser could have lawfully done if he had not parted with it. The presumption arising from such a sale is that the vendor intends to part with all his rights in the thing sold, and that the purchaser is to acquire an unqualified property in it; and it would be inconsistent with the presumed understanding of the parties to permit the vendor to retain the power of restricting the purchaser to using the thing bought in a particular way, or in a particular place, for a limited period of time, or from selling his rights to others. It is quite immaterial whether the thing sold is a patented article or not, or whether the vendor is the owner of a patent which gives him a monopoly of its use and sale. If these circumstances happen to concur, the legal effect of the transaction is not changed, unless by the conditions of the bargain the monopoly right is impressed upon the thing purchased; and if the vendor sells without reservation or restriction, he parts with his monopoly so far as it can in any way qualify the rights of the purchaser.

\textit{Ibid.} at 78-79.

\textsuperscript{57} \textit{Ibid.} at 77.
Kaisha Hattori Seiko v. Refac Technology Development Corp.\textsuperscript{58} In that case, Refac had given Hattori a non-exclusive license to make, use and sell products coming within the scope of Refac’s United States patents.\textsuperscript{59} Hattori had subsequently sold such products abroad to purchasers who then, directly or indirectly, resold them in the United States.\textsuperscript{60} The court was required to determine whether the license authorized Hattori to sell the patented products throughout the world, or only in the United States.\textsuperscript{61} In this connection the court noted:

In general, the first sale of a product by a patentee or licensee exhausts the patent monopoly, and deprives the holder of patent rights of any further control over resale of the product. This principle applies to an authorized first sale abroad by a patentee or licensee who also has the right to sell in the United States. Following such a sale, the holder of United States patent rights is barred from preventing resale in the United States or from collecting a royalty when the foreign customer resells the article here. Refac concedes that Hattori had the right under the license to sell the products at issue in the United States. Therefore, if Hattori also was authorized to sell the products abroad, Refac’s patent rights have not been infringed by any resale in the United States by Hattori’s customers. . . . If Hattori has the right to sell abroad, it is entitled to a declaration not only of that proposition, but of the corollary proposition that Refac may not claim royalties on Hattori products purchased abroad and resold in the United States by third parties.\textsuperscript{62}

As the preceding quotations suggest, the case law appears to recognize two limitations on application of the doctrine of exhaustion in the context of parallel imports. First, as in the case of domestically sold goods, patentees may expressly prohibit importation or resale in the United States as a condition of sales abroad, and sue persons in breach of that condition for patent infringement. Second, there may be limitations that arise from the identity of the person selling the patented article abroad. The following two subsections will examine these limitations in greater depth. The final subsection will examine case authority

\textsuperscript{58} 690 F. Supp. 1339 (S.D.N.Y. 1988).
\textsuperscript{59} Id.
\textsuperscript{60} Id.
\textsuperscript{61} Id.
\textsuperscript{62} Id. at 1342 (citations omitted); see also Sanofi, S.A. v. Med-Tech Veterinarian Prods., Inc., 565 F. Supp. 931, 938 (D.N.J. 1983) (“The court will . . . not grant to Sanofi an injunction against distribution in this country of the product that it sold in France without restriction.”).
cited for the proposition that the United States employs a territorial exhaustion rule, rather than the modified international exhaustion doctrine described by the Second Circuit and New York District Court.

A. Express Prohibition of Resale in the United States

Even if a defendant purchased the patented article abroad from the United States patentee or its licensee, subsequent importation and sale may infringe if the sale was made on the express condition that the product not be imported or sold in the United States, and the defendant had adequate notice of this restriction. The Court of Appeals for the Eighth Circuit stated this proposition in Dickerson v. Tinling.63 In that case, the defendant bought the patented product abroad, but it was unclear whether the seller was the United States patentee.64 The court found that if the defendant did purchase from the United States patentee, it did so subject to a printed prohibition of importation to and sale in the United States that the patentee placed on every packet of the invention that it sold abroad.65 This prohibition would be binding on the defendant, and would render his subsequent importation and sale an infringement:

Conceding—but not deciding—that one who buys a patented article without restriction in a foreign country from the owner of the United States patent has the right to use and vend it in this country upon the general principle that a patented article purchased from the patentee passes without the limit of the monopoly, there can be no doubt that a patentee has the same right and power to sell the patented article upon conditions or with restrictions that he has to sell it at all. Bayer & Co. had the right to sell its phenacetin in Germany without restriction. It has an equal right to sell it subject to the limitation that it should not be sold or used in any way that would curtail or affect the exclusive right, which that corporation held under this patent to make, use, and vend the phenacetin in the United States. If the corporation sold the patented article subject to such a restriction, the purchasers, with notice of this limitation, whether immediate or remote, could acquire no better right than strangers to infringe upon the monopoly secured by the patent. That monopoly would still remain intact, and purchasers of the phenacetin which had been sold under the restriction must be liable for its use and sale in the United States to the same extent as those who made it or bought it of strangers within their limits. The record is that every package of this article sold by Bayer & Co. in a foreign

63. 84 F. 192 (8th Cir. 1897).
64. Id.
65. Id.
country was sold on the express condition that it should not be imported into or
sold within the United States, and that this prohibition was plainly printed upon
every package. The necessary result is that . . . [the appellee is] an infringer
upon the exclusive right to make, use, and vend the phenacetin within the
United States, which was granted to this corporation by the letters patent.66

This result appears to be consistent with the Court of Appeals for the Federal
Circuit's recent decision in the Mallenckrodt case,67 though the underlying
reasoning may vary. In Mallenckrodt, the Federal Circuit relied on a contract
theory to suggest that the purchaser of the patented article could be bound by
the restriction on the label of the product. In Tingling, the Court of Appeals for the
Eighth Circuit may have been relying on a property rationale: that one cannot
pass rights greater than one has.68 If so, this rationale may be difficult to
reconcile with the Supreme Court's decisions in Adams v. Burke, Keeler v.
Standard Folding-Bed Co. and Hobbie v. Jennison,69 which all suggest that
authorized sellers of patented articles can convey rights they do not themselves
enjoy in a patented article (particularly, the right to use or sell the article in a
different geographic territory), at least under certain circumstances.70 In those

66. Id. at 194-95 (citations omitted).
67. See supra notes 36-42 and accompanying text.
68. Several courts have invoked this property rationale in the parallel imports context. See, e.g.,
Conklin, 170 F. 70, 72 (2d Cir. 1909).
70. In each of these cases the United States patent rights had been divided into separate
geographic territories within the United States. The owner of exclusive patent rights in one
geographic territory sold patented articles to a purchaser, who transported the articles out of the
seller's exclusive territory and undertook to use or sell them in the exclusive territory of another.
In Adams and Keeler, the Supreme Court held that the purchaser's subsequent use or sale did not
infringe the rights of the non-selling rights owner in whose territory the purchaser's use or sale
occurred. In Hobbie, the Court found that the seller would not be liable, notwithstanding the
purchaser's actual use of the patented articles in the plaintiff's exclusive territory, and the seller's
knowledge that the purchaser intended to use the articles there. In effect, the Court in each of these
cases found that the seller could convey rights it did not itself enjoy, in that it could authorize its
purchaser to use or sell the patented article in parts of the country where the seller itself lacked any
rights.
cases, the Supreme Court suggested that express contractual provisions were necessary to limit the purchasers’ subsequent acts.\textsuperscript{71}

The Court of Appeals for the Second Circuit faced a similar issue in \textit{Dickerson v. Matheson},\textsuperscript{72} and relied on a contract theory, as the Federal Circuit did in \textit{Mallenckrodt}. In \textit{Matheson}, the defendant purchased the patented product in Europe from a licensee of Bayer & Co., the United States patentee.\textsuperscript{73} It was clear that the defendant and its overseas agents knew that sales of the patented good abroad were usually subject to a condition against importation to the United States.\textsuperscript{74} The defendant hoped to avoid this restriction by purchasing through a series of agents.\textsuperscript{75} However, the court found that the seller had successfully conditioned the sale.\textsuperscript{76} The invoice for the sale contained an express restriction against importation to the United States, and the goods themselves bore the label: “The importation into the United States of North America is forbidden.”\textsuperscript{77} The court found that knowledge of the contents of the invoice must be imputed to the defendant through its agents, and that by accepting the invoice, the agents (and thus the defendant) assented to the conditions to sale that it contained.\textsuperscript{78} The court noted that “the invoice was not a

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The majority did not discuss notice to the purchaser of the seller's restricted territory in any of the cases, though the dissent in \textit{Keeler} states that the purchaser/defendant in that case did in fact have notice of his seller's restricted territory. \textit{Keeler}, 157 U.S. at 667 (Brown, J., dissenting). Nor did the Court in any of the cases discuss or appear to rely on a bona fide purchaser rationale in reaching its result. Rather, in \textit{Keeler}, the Court suggested that its finding was based on the public interest: “The inconvenience and annoyance to the public that an opposite conclusion would occasion are too obvious to require illustration.” \textit{Id.} at 666. In both the \textit{Keeler} and the \textit{Hobbie} decision, the Court did, however, suggest that the defendants' rights might have been restricted through an express contractual provision. \textit{See id.} at 661, 666; \textit{Hobbie}, 149 U.S. at 363-64. It is interesting to note that the dissent in \textit{Adams} expressly raised the “property theory” suggested in \textit{Tingling}: “\textit{H}ow can they confer upon their vendees a right which they cannot exercise themselves?” \textit{Adams}, 84 U.S. at 458-59 (Bradely, J., dissenting). The majority clearly was aware of the argument and chose to ignore it.
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\textsuperscript{71} \textit{See Keeler,} 157 U.S. at 666; \textit{Hobbie,} 149 U.S. at 363.
\textsuperscript{72} \textit{57 F.} 524 (2d Cir. 1893).
\textsuperscript{73} \textit{Id.}
\textsuperscript{74} \textit{Id.}
\textsuperscript{75} \textit{Id.}
\textsuperscript{76} \textit{Id.}
\textsuperscript{77} \textit{Id.}
\textsuperscript{78} \textit{Id.}
mere notice or receipt, and was a paper which, from the nature of the business, must be expected to contain the terms of the contract of sale." See also Sanofi v. Med-Tech Veterinarian Prods., Inc., 565 F. Supp. 931, 935 (D.N.J. 1983) (finding expressly that a remote purchaser who did not receive adequate notice of a patentee’s restrictions on resale would not be bound by them). For discussion of the notice issue, see Kobak, supra note 44, at 563; J.W. SCHLICHER, PATENT LAW: LEGAL AND ECONOMIC PRINCIPLES § 8.05[1][f][iii] (1995).


82. See Dunlop Co., Ltd. v. Kelsey-Hayes Co., 484 F.2d 407, 417-18 (6th Cir. 1973). For a useful discussion of the case law relevant to this issue, see Warwick A. Rothnie, supra note 13, at 157-70; see also Adelman, supra note 3, at 14.
B. The Identity of the Person Selling the Patented Article Abroad

The doctrine of exhaustion only applies when the foreign purchaser derived the patented article through the United States patentee or the patentee’s licensees. The Supreme Court made this clear in *Boesch v. Graff*.84 In *Boesch*, the defendants purchased plaintiff’s patented lamp burners in Germany from a seller who was authorized to sell in Germany by virtue of a “prior user” law,85 but was not related to the United States patentee and derived no rights from him. Although the sale to the defendants in Germany was legal, the Supreme Court found that the defendants’ resale in the United States constituted infringement of the United States patent.86

The Court of Appeals for the Eighth Circuit applied this limitation in *Dickerson v. Tinling*.87 In *Tinling*, the composition phenacetin was patented in the United States, but not in Germany.88 The defendant purchased phenacetin in Germany, imported it to the United States and offered it for sale in competition with the United States patentee.89 Assuming that Bayer & Co. was the United States patent owner, the court noted that if the defendant bought the phenacetin from someone other than Bayer & Co. abroad:

[H]e bought with it no right to sell it in the United States, because no one but Bayer & Co. and their vendees had that right in this country .... [O]ne who purchases in a foreign country, of others than the owners of the United States patent or their vendees, pays nothing, either directly or indirectly, to the owners of the patent, and therefore he acquires no right to make, use, or vend the article which he buys within the territorial limits of their monopoly. It follows that, if the appellee bought the phenacetin he is selling of others than Bayer & Co., or its vendees, he is infringing upon the exclusive right of this patentee, and an

84. 133 U.S. 697 (1890).
85. The German law provided that a German patent would not affect “persons who, at the time of the patentee’s application, have already commenced to make use of the invention in the country, or made the preparations requisite for such use.” *Id.* at 701.
86. *Id.* at 703. See *Keeler v. Standard Folding-Bed Co.*, 157 U.S. 659, 665 (1895) (noting that in *Boesch* “neither the patentee nor any assignee had ever received any royalty or given any license to use the patented article in any part of the United States”); *Curtiss Aeroplane & Motor Corp. v. United Aircraft Eng’g Corp.*, 266 F. 71, 77 (2d Cir. 1920) (noting that in *Boesch* there had been “no participation whatever by the owner of the patent, either as a party or as a privy, in the putting out of the article which is alleged to infringe.”).
87. 84 F. 192 (8th Cir. 1897).
88. *Id.*
89. *Id.*
injunction should issue.\textsuperscript{90}

The rationale underlying this limitation is self-evident. The doctrine of exhaustion is based on the premise that a patent should secure the financial benefit of the invention to the patentee, but only once: once the patentee has enjoyed the benefit of his invention, through sale of a patented article, his rights as to that article are exhausted.\textsuperscript{91} If the patentee did not make or authorize the initial sale of the patented article, it never enjoyed the benefit of its invention as to that article, and its rights were never exhausted. Thus, it should have the opportunity to exert control over the article (for the first time) when it enters the United States.\textsuperscript{92}

However, some of the case opinions go beyond the proposition stated above and suggest that the doctrine of exhaustion should only apply when the person selling the patented article abroad has the right to sell it in the United States, as well.\textsuperscript{93} The district court in New Jersey applied this limitation in \textit{Sanofi, S.A. v.}

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\textsuperscript{90} \textit{Id.} at 194. \textit{See also} Featherstone v. Ormonde Cycle Co., 53 F. 110 (S.D.N.Y. 1892). In \textit{Featherstone}, the owner of the British patent, who had no relationship to the owner of the United States patent in the same invention, licensed the defendants to apply tires covered by its patent to a bicycle in Great Britain. \textit{Id.} The defendants then imported the bicycle into the United States and sold it. \textit{Id.} The court found infringement of the United States patent:

It is well settled that the unrestricted sale of a patented article by the owner of the patent conveys to the purchaser the right of unrestricted ownership as against the vendor. But the purchaser does not acquire any rights greater than those possessed by the owner of the patent. The owner of the British patent could not authorize either the vendee or his vendor to sell the articles in the United States, so as to conflict with the rights of the owners of the American patent. This claim of defendants seems to be disposed of by the case of \textit{Boesch v. Graff}.

\textit{Id.} at 111 (citation omitted).
\textsuperscript{91} \textit{See supra} note 11 and accompanying text.
\textsuperscript{92} \textit{Id.}
\textsuperscript{93} \textit{See, e.g.,} Dickerson v. Matheson, 57 F. 524 (2d Cir. 1893). The court found that:

A purchaser in a foreign country, of an article patented in that country and also in the United States, from the owner of each patent, or from a licensee under each patent, who purchases without any restrictions upon the extent of his use or power of sale, acquires an unrestricted ownership in the article, and can use or sell it in this country.

\textit{Id.} at 527. \textit{See also} Kabushiki Kaisha Hattori Seiko v. Refac Tech. Dev. Corp., 690 F. Supp. 1339, 1342 (S.D.N.Y. 1988) (holding the exhaustion doctrine "applies to an authorized first sale abroad by a patentee or licensee who also has the right to sell in the United States").
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Med-Tech Veterinarian Products, Inc.\textsuperscript{94} In that case, Sanofi, S.A., which owned the United States patent for acepromazine maleate (a tranquilizer used in the treatment of animals), granted American Home Products an exclusive license to sell the composition in the United States for veterinary purposes.\textsuperscript{95} The defendants, United States businesses, bought the composition from a subsidiary of Sanofi in France, through a series of intermediaries, and resold it in the United States without American Home Products' authorization.\textsuperscript{96} In the ensuing infringement suit, the court found that Sanofi, the United States patentee, had no right to an injunction, but that the exclusive United States licensee, American Home Products, did.\textsuperscript{97}

[I]t is a principle of patent law that the unrestricted sale of a patented article by the owner of the patent conveys to the purchaser the right of unrestricted ownership as against the seller. It is also a principle of patent law, however, that the purchaser does not acquire any rights greater than those possessed by the owner of the patent.

American Home holds an exclusive license to sell the drug acepromazine maleate in this country for veterinary use. Therefore, even the patent holder, Sanofi, would not have the right to sell the drug in this country.

Although defendants are correct in stating that sale of an article exhausts the patentees' monopoly in that article, they are incorrect in applying the rule to the facts of this case. The rule has only been applied where the sale is one which the seller had the authority to make in this country. Sanofi had no authority to sell acepromazine maleate for veterinary purposes in the United States. Although the sale was consummated abroad, this country's patent laws were not implicated until the product was brought into this country. Once the product entered and was sold in the United States for veterinary purposes, it was American Home's interest that was directly affected. Only American Home had the right to sell here for veterinary purposes, not Sanofi. If the court were to hold that Sanofi's sale of the product exhausted the patent, it would be crediting Sanofi with greater rights than the patentee actually had.\textsuperscript{98}

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\item \textsuperscript{94} 565 F. Supp. 931 (D.N.J. 1983).
\item \textsuperscript{95} This was the only purpose for which the drug had received the approval of the Food and Drug Administration. \textit{Id.} at 937.
\item \textsuperscript{96} Sanofi, 565 F. Supp. at 931.
\item \textsuperscript{97} \textit{Id.}
\item \textsuperscript{98} \textit{Id.} at 939-41. See also Selchow & Righter Co. v. Goldex Corp., 612 F. Supp. 19 (1985). In Selchow, the owner of a design patent in the Trivial Pursuit game board granted exclusive license
\end{itemize}
The result in Sanofi can be reconciled with the underlying purposes of the doctrine of exhaustion, but its reasoning, and the broad rule it purports to provide, may exceed those purposes, and present some questionable inconsistencies with the case law that applies the doctrine to domestic sales.

First, the Supreme Court's decisions in the Adams, Keeler and Hbbie cases all rejected the notion that a seller cannot convey greater rights than he has in the exhaustion context. In those cases, the Court found that persons owning exclusive rights in one geographical area of the United States could, in selling the patented article to a purchaser, enable that purchaser to use and sell the article throughout the United States, even in parts of the country where the seller lacked the right to do so itself. In those cases the Court apparently believed

to a manufacturer to use and sell the game in the United States to the plaintiff. Id. The defendants purchased Trivial Pursuit games manufactured in Canada by the design patent owner and imported them into the United States for sale in competition with the plaintiff. Id. The court found that this infringed the rights of the plaintiff's exclusive United States license. Id. See also PCI Parfums et Cosmetiques Int'l v. Perfumania Inc., 35 U.S.P.Q.2d 1159 (S.D.N.Y. 1995).

99. See supra note 70, and accompanying text.
[A] person who buys patented articles from a person who has a right to sell, through within a restricted territory, has a right to use and sell such articles in all and any part of the United States; [when a royalty is] paid to a party entitled to receive it, the patented article then becomes the absolute, unrestricted property of the purchaser, with the right to sell it as an essential incident of such ownership.

The conclusion reached does not deprive a patentee of his just rights, because no article can be unfettered from the claim of his monopoly without paying its tribute. The inconvenience and annoyance to the public that an opposite conclusion would occasion are too obvious to require illustration.

Id. This result can be justified under the circumstances of the Adams, Keeler and Hbbie cases, for to find infringement would permit patentees, through their private business arrangements, to interfere quite considerably with the free flow of commerce within the country, and with the public convenience. As the Keeler court asked:

If, as is often the case, the patentee has divided the territory of the United States into 20 or more "specified parts," must a person who has bought and paid for the patented article in one part, from the vender having an exclusive right to make and vend therein, on removing from one part of the country to another, pay to the local assignee for the privilege of using and selling his property, or else be subjected to an action for damages
that policy considerations, rather than the mechanical "can't convey rights greater than you have" formulation, should govern the contours of the exhaustion doctrine.\footnote{101}

Three separate scenarios are useful to explain why the result in \textit{Sanofi} may be consistent with the purposes of the exhaustion doctrine, while a rule limiting the doctrine to foreign sales made by persons owning rights in the United States is too broad. The first entails facts similar to those in \textit{Sanofi}: the United States patentee has sold exclusive rights in the invention to X Co. (a company that is unrelated to the patentee) in the United States, but continues to sell the patented invention itself in other countries. Y purchases a patented article from the patentee abroad, and imports it into the United States. While X Co. is technically a licensee, it has purchased exclusive United States rights, and has a legitimate expectation of an exclusive United States market. Moreover, it has not benefited financially from its licensor's sale abroad. Under these circumstances it may be consistent with the purposes of the exhaustive doctrine to protect the exclusive licensee's market, finding that the patentee's foreign sale does not exhaust X Co.'s rights in connection with the article the patentee sold. That is the result the court reached in \textit{Sanofi}.

The second situation entails the opposite situation: the United States patentee grants a license to X Co. to sell the patented article in a foreign country, but grants X Co. no rights in the United States. The patentee continues to sell the patented article in the United States. Y purchases the patented article from X Co. abroad, and imports it into the United States for resale. Under the rule broadly expressed in \textit{Sanofi}, the exhaustion doctrine would not apply here, either, because the seller, X Co., had no rights in the United States. However, the United States right holder received the benefit of X Co.'s sale, either in the form of a royalty payment or in the purchase price of the license. From a

\begin{quote}
\textbf{as a wrongdoer? And is there any solid distinction to be made, in such a case, between the right to use and the right to sell?}
\end{quote}

\textit{Id.} at 662. At the least, the patentee should be required to obtain contractual consent to the territorial restrictions by the purchasers to be bound by them. Moreover, in the \textit{Adams} line of cases, at least one person owning United States patent rights had received compensation for the sale. Whether the balance of policy considerations differs when the exclusive territories are separate countries, rather than regions within the United States will be explored in the following Section. However, the \textit{Adams/Keeler/Hobbie} decisions do suggest that policy considerations are the appropriate basis for a different rule, rather than the mechanical formulation that "one cannot grant greater rights than he has."

\footnote{101. See supra note 70.}
theoretical standpoint, there is no reason why the exhaustion doctrine should not apply. Courts have routinely held that the exhaustion doctrine applies equally to sales by the patentee and authorized sales by its licensees. There is no apparent reason to deviate from that rule simply because the licensees are not authorized to sell in the United States.

In the third situation, the patentee has granted an exclusive license to X Co. in the United States and an exclusive license to Y Co. in France. The patentee, X Co. and Y Co. are all unrelated entities. Z purchases the patented article from Y Co. in France, and imports it for resale in the United States. In this case, the patentee has benefited from Y Co.’s sale, but X Co., the exclusive United States right holder, has not. Again, as in situation number one, it is not inconsistent with the underlying purposes of the exhaustion doctrine, as described by the courts, to find that the exclusive United States rights holder’s rights are not exhausted by Y Co.’s sale.

The ultimate question, then, should not be whether the foreign seller enjoys rights in the United States, but whether the plaintiff enjoys exclusive rights in the United States and benefited, directly or indirectly, from the foreign sale. One might characterize the statement that “the seller must have rights in the United States” as dicta, since it goes well beyond what was needed to resolve the issues before the courts that made it. In any event, in the absence of a case decision specifically applying that rule to the facts set forth in the second hypothetical situation, the proposition that the doctrine of exhaustion would not apply to the facts in that situation is open to question.

One unresolved, but important question remains: how does the doctrine of exhaustion apply when the United States patent right holder and the foreign seller are separate but, related corporate entities? Can sale by the latter exhaust the rights of the former? For example, assume that a multinational business entity owning patents in a number of different countries assigns exclusive rights in each country to a different corporate subsidiary. Should sale of a patented article by one subsidiary, for example, in Germany, be deemed to exhaust the rights of a separate corporate subsidiary that is the exclusive licensee of the multinational entity’s United States patent rights?

There is significant precedent for considering such related corporate entities (such as entities in a brother-sister or parent-subsidiary relationship) as a single entity for purposes of applying the doctrine of exhaustion. For example, that has become the general rule in applying the doctrine of exhaustion in trademark

102. See supra note 31 and accompanying text.
infringement claims involving parallel imports. There is also some precedent for this approach in the United States patent cases. For example, in Sanofi, the Court treated a sale abroad by the French subsidiary of a subsidiary of the United States patent owner as a sale by the United States patentee itself, and found that the sale gave rise to exhaustion of the patentee’s United States patent rights.

103. See, e.g., K-Mart Corp. v. Cartier, Inc., 486 U.S. 281 (1988) (determining that the United States Customs Service acted reasonably in construing Tariff Act § 526, 19 U.S.C. § 1526, to prohibit parallel imports when the foreign manufacturer placing a mark on imported goods and the United States trademark registrant are unrelated corporate entities, but not to prohibit the imports when “the foreign and domestic trademark . . . owners are parent and subsidiary companies or are otherwise subject to common ownership or control.”); Weil Ceramics and Glass, Inc. v. Dash, 878 F.2d 659 (3d Cir.), cert. denied, 493 U.S. 853 (1989) (holding Lanham Act §§ 32 and 42 do not prohibit import or domestic sale of imported goods bearing a United States registered trademark when the imported goods are the same as those sold domestically by the United States mark registrant and the foreign corporation that placed the mark on the imported goods is related to the United States corporate mark registrant). In Weil, the defendant, Jalyn, had purchased “Lladro” porcelain manufactured by Lladro, S.A. in Spain, and imported it into the United States for resale in competition with Weil, the United States registrant of the Lladro mark. Id. Weil was the wholly owned subsidiary of Lladro Exportadora, S.A., a Spanish corporation which was a sister corporation of the foreign manufacturer. Id. In finding that Jalyn’s acts did not constitute trademark infringement, the court reasoned:

[Even if Weil loses some share of its United States market to Jalyn, it nonetheless benefits from the profits it received as part of the corporate entity from which Jalyn purchased the goods abroad. Moreover, if that corporate entity decides that the profit margin from the sale of the goods to Jalyn abroad is not as significant as would be the profit margin from a United States market in which Jalyn did not compete, it has an obvious self-help mechanism; it can cease the sale to Jalyn abroad and thereby eliminate effectively its United States competition with Weil. We do not read the Lanham Act, however, to protect a foreign manufacturer—that either owns or is owned by a domestic trademark holder—from competition in the sale of its product in the United States by a domestic importer that it has supplied.

Id. at 668.

104. But cf. Sanofi, S.A. v. Med-Tech Veterinarian Prods., Inc., 222 U.S.P.Q. 143 (D. Kan. 1983). In a case related to the New Jersey decision discussed in text, the Kansas District Court notes:

The defendants would have us hold that acquiring the patented product from the subsidiary of the patent holder in the normal course of business is sufficient to grant an implied license. We cannot accept such an argument. First, we have not been presented
Finally, at least one court has treated related corporate entities as a unit for purposes of the exhaustion doctrine in the copyright context, as well.\textsuperscript{105}

One might also argue that even if the separate legal status of related corporate entities is recognized for purposes of the exhaustion doctrine, the entities may be viewed as consenting to one another’s sales of the patented article. Ultimately, the question of whether to treat such multi-entity international business structures as single entities for purposes of the doctrine of exhaustion, or to imply their consent to sales, must turn on one’s assessment of whether application of the doctrine of exhaustion in such cases is consistent with the underlying purposes of the doctrine of exhaustion, and the policy issues to be discussed in Section V, infra. One could certainly argue that it is consistent with the underlying purposes, since sales proceeds going to one subsidiary benefit the entire international business entity. Moreover, companies under common ownership and control should be able to engage in the kinds of self-help discussed in the following sections to protect themselves from injuries that might otherwise be inflicted by parallel imports.\textsuperscript{106}

\textbf{C. Authority for the Proposition that the United States Employs a Territorial Exhaustion Rule}

Advocates of the theory that the United States employs a territorial exhaustion rule, so that no foreign sales exhaust the United States patentee’s

with sufficient evidence to disregard the corporate separateness of Semppra-Chimie and Sanofi. Second, were we to hold as defendants suggest, we would throw the current licensing system into a state of chaos. Anytime someone acquired a patented product from a seller in privity with the patentee, they would have an implied license.

\textit{Id.} at 148-49.


\textsuperscript{105} \textit{See} Red Baron-Franklin Park, Inc. v. Taito Corp., 883 F.2d 275 (4th Cir. 1989).

\textsuperscript{106} \textit{See} \textit{Weil Ceramics}, 878 F.2d 659.
rights, generally cite two cases: Boesch v. Graff and Griffin v. Keystone Mushroom Farm, Inc. As will be discussed below, the Supreme Court’s decision in the Boesch case simply does not support the proposition. The support the Griffin decision provides is weak because of internal flaws in the court’s opinion.

In Boesch, the defendants purchased lamp burners, covered by the plaintiff’s United States patent in Germany, from a seller who was authorized to sell in Germany free from liability under the corresponding German patent by virtue of a “prior user” law.\textsuperscript{107} The seller was not related to the United States patentee and derived no rights from him or from any related entity. Although the sale to the defendants was lawful in Germany, the Supreme Court found that it did not exhaust the United States patentee’s rights. The Court stated:

The right which [the German seller] had to make and sell the burners in Germany was allowed him under the laws of that country, and purchasers from him could not be thereby authorized to sell the articles in the United States in defiance of the rights of patentees under a United States patent . . . . The sale of articles in the United States under a United States patent cannot be controlled by foreign laws.\textsuperscript{108}

Some commentators have cited this language as authority for the proposition that foreign sales do not affect the rights of a United States patentee,\textsuperscript{109} but that is an over broad reading of the opinion. The Court was merely saying that a German law, excepting certain third-party sales of patented goods from liability under a German patent, does not itself remove the goods from the reach of the United States patent if they are later resold in the United States without the United States patentee’s authorization. German law cannot itself authorize sales in the United States, or bind United States courts applying a United States patent, to a finding that sales made in Germany by a third party are attributable to the United States patentee. It is United States law that determines whether a sale abroad exhausts a United States patentee’s rights, not the law of another country.

That is not the same as saying that United States law ignores all foreign sales by United States patentees or their licensees. Boesch construes United States

\textsuperscript{107.} See Boesch v. Graff, 133 U.S. 697 (1890).
\textsuperscript{108.} Id. at 703.
\textsuperscript{109.} See, e.g., Wegner, supra note 14, at 4; Tessenshon & Yamamoto, supra note 22, at 741; Yusuf & von Hase, supra note 3, at 124; Laurenson & Kolegraff, supra note 26, at 25; Barfield & Groombridge, supra note 22, at 197-98.
law to provide that sales by parties who are unrelated to the United States patentee and derive no rights from the United States patentee do not exhaust the United States patentee's rights, even if the sales were authorized under foreign law. That is because the United States patentee received no benefit from such sales. The opinion does not address the effect of foreign sales by the United States patentee or its licensees. In the Keeler case the Supreme Court itself explained its earlier decision in the Boesch case, emphasizing that very point:

[T]he [Boesch] court held that the sale of articles in the United States under a United States patent cannot be controlled by foreign laws. In this case neither the patentee nor any assignee had ever received any royalty or given any license to use the patented article in any part of the United States.110

In Griffin v. Keystone Mushroom Farm, Inc., the plaintiff owned United States and Italian patents in a composting device.111 It had granted an exclusive license to sell the device to a different (apparently unrelated) entity in each country.112 The defendant bought three of the devices from the Italian exclusive licensee, imported them to the United States without the authorization of the

110. Keeler v. Standard Folding-Bed Co., 157 U.S. 659, 665 (1895). See also Curtiss Aeroplane & Motor Corp. v. United Aircraft Eng'g Corp., 266 F. 71, 77 (2d Cir. 1920) (distinguishing Boesch on the ground that there had been "no participation whatever by the owner of the patent, either as a party or as a priy, in the putting out of the article which is alleged to infringe"); Sanofi, S.A. v. Med-Tech Veterinarian Prods., Inc., 565 F. Supp. 931, 937-38 (D.N.J. 1983). In Sanofi the court stated:

Boesch is distinguishable from this case. In Boesch, it was not the patentee who made the sale abroad. In fact, it was not even a licensee of the patentee who made the sale. Rather, the seller was one who had a right to sell by operation of the patent laws of Germany, which provided that patents do not affect persons who, at the time of the patent application, were already making use of the invention. Under the circumstances of Boesch, the patentee neither received compensation for the use of his invention, nor consented to its importation into this country.

Id. at 937-38.

111. 453 F. Supp. 1283 (E.D. Pa. 1978). This case is also frequently cited as authority for the proposition that the United States adopts a territorial exhaustion doctrine. See, e.g. Wegner, supra note 14, at 10; Tessenshon & Yamamoto, supra note 22, at 741; Laurenon & Kolegraff, supra note 26, at 26.

United States exclusive licensee, used one, and sold the other two. The patentee sued for infringement of its United States patent and the district court held that it could prevail. The court construed the Supreme Court's decision in *Boesch* to hold that the doctrine of exhaustion never applies to sale of a patented article abroad, regardless of who made the sale or the circumstances surrounding the sale. It deemed it irrelevant that the plaintiff/patentee had received a royalty arising from the sale in Italy, reasoning that a patentee should be entitled to separate compensation in each country a patented article enters after its original sale. To hold otherwise, the court reasoned, would be to give extraterritorial effect to foreign patent law.

The *Griffin* decision is open to criticism on several grounds. First, the court fails to explain why a finding for the defendant would give extraterritorial effect to the Italian patent law. A decision that the defendant's parallel import did not infringe the United States patent would rest on application of United States patent law--specifically the case decisions establishing and construing the scope of the United States exhaustion doctrine. While the United States law may attach significance to an event occurring in a foreign country--a sale of an article incorporating the patented invention--that is no reason to say that the patent law of the foreign country is dictating the United States patentee's rights. It is the United States law that determines whether, or how, the foreign act affects the United States patentee's United States patent rights.

113. *Id.*
114. *Id.*
115. *Id.*
116. *Id.*
117. *Id.*
118. A number of issues in patent law turn on events that occur in foreign countries, yet it is not seriously suggested that these instances entail giving foreign patent or other laws extraterritorial effect in the United States. For example, Patent Act § 102(a) provides that a United States patent may be denied if the same invention was patented or the subject of a printed publication in a foreign country prior to the United States applicant's invention date. 35 U.S.C. § 102(a) (1994). Section 102(b) provides that a United States patent may be denied if the same invention was patented or the subject of a printed publication in a foreign country more than a year before the United States patent application filing date. 35 U.S.C. § 102(b). Section 102(d) denies a United States patent if the United States applicant filed for a patent abroad more than a year prior to filing in the United States, and the foreign patent was granted prior to the United States filing date. 35 U.S.C. § 102(d). At one point, the *Griffin* court seems to recognize the weakness of its argument:

It may be that the limited nature of the effect that would be given Italian patent law, *i.e.*,
involving the parallel import of copyrighted goods, the Supreme Court rejected such an argument out of hand.119

Second, the court construed the Boesch decision far too broadly, in a manner that reaches well beyond the facts before the Supreme Court, and is contrary to other courts’ construction of the opinion.120 It might also be noted that the only other opinion, involving parallel imports, the Griffin court cited for authority is the Second Circuit’s decision in Daimler Mfg. Co. v. Conklin.121 In that case, the Second Circuit held that the domestic use of an imported car would infringe the United States patent in the car, but made a point of noting that the car had not been sold abroad by the United States patentee.122 The Daimler Court set forth the proposition that a “purchaser abroad cannot get any greater right than the patentee has from whom he buys,” and noted that the foreign patentee had no right to use the patented article in the United States.123 Thus, the Daimler decision does not stand for the proposition that the doctrine of exhaustion never applies to sales made abroad. The Griffin court did not attempt to distinguish, and indeed did not even acknowledge, two other Second Circuit decisions—the Curtiss and Dickerson decisions—which expressly state that the doctrine of exhaustion may apply against a United States patentee who made an unrestricted

as a legitimate source of rights and compensation rendering plaintiff’s infringement case an attempt at a double recovery, brings it outside the rationale for the broadly stated rule of ’no extraterritorial effect.’ The defendant has not so argued, however; and its claim that it is not attempting to attribute extraterritorial effect to the plaintiff’s Italian patents,

Reply Brief at 4, is erroneous.

120. See infra note 133. As noted earlier, the Boesch defendant had purchased abroad from a German seller who was unrelated to the United States patentee and derived no rights from him. The sale did not constitute an infringement of the corresponding German patent, due to an exception to liability recognized under German patent law, but not under United States patent law. The Supreme Court found the German exception irrelevant to the question of whether resale of the patented articles in the United States would infringe the plaintiff’s United States patent. Since the United States patentee had received no benefit from the German sale, the Court held that the United States doctrine of exhaustion was inapplicable.
121. 170 F. 70 (2d Cir. 1909).
122. Id.
123. Id. at 72. The court cited Featherstone v. Ormonde Cycle Co., 53 F. 110 (S.D.N.Y. 1892), for the proposition. Featherstone is discussed supra note 90.
sale, or authorized another to make an unrestricted sale, of a patented article abroad. One wonders whether the Griffin court was even made aware of this contrary precedent.

Finally, the Griffin court pointed to "certain practical problems" in finding that a foreign sale by a United States patentee, or its licensee, exhausted rights under the United States patent. First, the court would have to determine whether "the plaintiff's rights and the scope of the patented art are the same under the Italian [and United States] patent laws." The court suggested that it would need to find "that the United States and foreign patent monopolies were 'virtually identical or, at least, very similar' prior to finding exhaustion." The court considered it "unwise to involve ourselves in the niceties of Italian patent law." In a footnote, the court added that it would also need to compare the terms under which the composting machines were licensed in the two countries, in order to ensure that the plaintiff got as much benefit from the Italian license as it did from the United States license.

Other courts have not found it necessary to construe foreign patents in determining whether a United States patentee's sales under the foreign patents exhaust its rights in the United States. Indeed, United States patent law does not seem to require that the United States patentee have a patent in the foreign country in which it made the first sale of the article. Nor have courts found it necessary, in either a parallel import, or strictly domestic application of the exhaustion doctrine, to examine whether the United States patentee got as good a price under the first sale of the article at issue as it might have gotten under other circumstances. The key is that the United States patentee voluntarily made, or authorized, the first sale of the article embodying the patented invention abroad. Presumably patentees, like all other business people, can be counted on to make or authorize only those sales that they deem to be beneficial. The United States patent law does not undertake to second-guess the patentee's judgment concerning the benefit to be gained from the sale. Nor does it guarantee that the patentee will always get the same price or royalty for the patented good, so that

125. Id.
126. Id.
127. Id. at 1287 n.2.
128. See, e.g., Sanofi, S.A. v. Med-Tech Veterinarian Prods., Inc., 565 F. Supp. 931, 938 (D.N.J. 1983) (dealing with sales in a country where the invention was not patented); see also Dickerson v. Tingling, 84 F. 192 (8th Cir. 1897) (focusing on the enforceability of a contractual restriction, but not finding the absence of patent protection in the country of sale to be of importance).
if it must accept a lower level of benefit in one sale than in others, that sale “doesn’t count” for purposes of the exhaustion doctrine. 129 Such a rule would be unworkable in the business world, for it would leave purchasers of patented articles without any meaningful guidance regarding their rights in the articles they purchased. A blanket rule that applies the doctrine of exhaustion to all sales made or authorized by the patentee is essential to provide the certainty needed to facilitate business transactions in patented goods. Patentees who wish to restrict further resales of patented goods have the option of negotiating contractual restraints.

Since the plaintiff patentee in Griffin had received the benefit (presumably, through royalty payments) of the first sale of the composting machines in Italy, it would have been more consistent with prior case precedent, as well as with the underlying justifications of the United States exhaustion doctrine, to deny the patentee a cause of action. 130 Even if one accepts the Sanofi court’s broad limitation of the doctrine to sales made by persons having rights to sell in the United States, as well, the Griffin court found for the wrong plaintiff. The exclusive United States licensee, rather than the patentee, should have had the cause of action under the Sanofi rationale. 131

Regardless of one’s evaluation of the reasoning in Griffin, its construction of Boesch is at odds with both the Second Circuit’s and the Supreme Court’s subsequent construction of the same language in that opinion. Moreover, its decision that the doctrine of exhaustion applies only to domestic sales is inconsistent with virtually all other prior decisions on that issue, which it fails to distinguish or even acknowledge. 132 Under these circumstances, the district court’s decision in Griffin cannot be afforded much weight.

IV. THE IMPACT OF THE URUGUAY ROUND AGREEMENTS ACT

In 1994, Congress amended the United States’ Patent Act to provide patentees an express right of importation, which became effective January 1,
1996.133 Congress added the importation right in order to bring the United States into compliance with Article 28 of the GATT Uruguay Round Agreement on Trade-Related Aspects of Intellectual Property Rights, Including Trade in Counterfeit Goods (hereafter, "TRIPs").134 The question arises whether this new express statutory importation right will be tempered by the doctrine of exhaustion, long established in the case law with regard to the patentee's rights of sale and use, or whether Congress intended the new importation right to give patentees an absolute right to prohibit all unauthorized importation of goods embodying the patented invention.135 The Uruguay Round Agreement


Every patent shall contain a short title of the invention and grant to the patentee, his heirs or assigns, the right to exclude others from making, using, offering for sale, or selling the invention throughout the United States or importing the invention into the United States, and, if the invention is a process, of the right to exclude others from using, offering for sale or selling throughout the United States, or importing into the United States, products made by that process, referring to the specification for the particulars thereof.

35 U.S.C. § 154(a)(1) (1994). Section 271(a), as amended, provides: [e]xcept as otherwise provided in this title, whoever without authority makes, uses, offers to sell, or sells any patented invention, within the United States or imports into the United States any patented invention during the term of the patent therefore, infringes the patent. 35 U.S.C. § 271(a).

134. See TRIPs, supra note 22. Under TRIPs Article 28, a product patent must provide the exclusive rights "to prevent third parties not having the owner's consent from the acts of: making, using, offering for sale, selling, or importing . . . that product . . . ." Id.

135. Patentees have long enjoyed the opportunity to prohibit the importation of infringing articles through resort to the International Trade Commission. 19 U.S.C. § 1337 (1994). See also supra notes and accompanying text. This § 1337 right against importation, however, has been tempered by the doctrine of exhaustion. See discussion supra Section III. The International Trade Commission has only excluded imported articles that will infringe a patent under the existing case law. If a patentee's rights in imported articles are exhausted under the existing case law, the article's subsequent use or sale in the United States will not infringe. See Duvall, Unfair Competition and the ITC A-481, n.1 (1996); Terry L. Clark, The Future of Patent-Based Investigations Under Section 337 After the Omnibus Trade and Competitiveness Act of 1988, 38 AM. U. L. REV. 1149, 1157, 1159 (1989).

At least one set of authors has assumed, without further analysis, that the importation amendment provides "full statutory backing for United States patent holders to block parallel imports." Barfield & Groombridge, supra note 22, at 198.
amendments themselves make no reference to the doctrine of exhaustion, or to any other limitation on the scope of the new importation right. Thus, in determining the applicability of the doctrine of exhaustion to the new statutory importation right, resort must be had to the legislative history of the amendments, and to rules of statutory construction.

The TRIPs Agreement itself expressly disclaims any position on the effect of the doctrine of exhaustion on patentees’ importation rights. 136 Thus, TRIPs

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136. A footnote to TRIPs Article 28 elaborates that the right of importation “is subject to the provisions of Article 6.” Article 6, in turn, provides that for the purposes of dispute settlement under the TRIPs Agreement, “nothing in this Agreement shall be used to address the issue of the exhaustion of intellectual property rights.” Thus, while the TRIPs Agreement requires adhering nations to provide a right of importation, it deliberately avoids directly addressing the applicability of the doctrine of exhaustion to temper that right.

This is because the nations negotiating the TRIPs Agreement were unable to reach agreement about the applicability of the doctrine of exhaustion to goods sold internationally. While the United States’ Clinton Administration and some other developed nations took the position that intellectual property owners should be able to assert their intellectual property rights to prevent parallel imports in some or all instances, many developing countries advocated a rule of international exhaustion. See Herman C. Jehoram, Prohibition of Parallel Imports Through Intellectual Property Rights, 30 INTERNAT. REV. INDUS. PROP. & COPYRIGHT 495, 506-07 (1999); Ana M. Pacon, What Will TRIPs Do For Developing Countries?, in FROM GATT TO TRIPs--THE AGREEMENT ON TRADE-RELATED ASPECTS OF INTELLECTUAL PROPERTY RIGHTS 329, 337 (Friedrich-Karl Beier & Gerhard Schricker, eds. 1996); Rothnie, supra note 13, at 314; Watal, TRIPs and the 1999 WTO Millennium Round, 3 J. WORLD INTELL. PROP. 3, 17-18 (2000).

Notwithstanding the language of Article 6, some commentators have argued that other provisions of TRIPs or other Agreements within the General Agreement on Tariffs and Trade, indirectly prohibit a policy of international exhaustion. See, e.g., Thomas Cottier, The Prospects for Intellectual Property in GATT, 28 COMMON MARKET L. REV. 383, 399-400 (1991) (argument based on GATT Art. XXIII(1)(b)); Straus, Implications of the TRIPs Agreement in the Field of Patent Law, in FROM GATT TO TRIPs--THE AGREEMENT ON TRADE-RELATED ASPECTS OF INTELLECTUAL PROPERTY RIGHTS 160, 192-93 (Friedrich-Karl Beier & Gerhard Schricker, eds. 1996) (relying on TRIPs Art. 27(1) and 28(1)); Harvey E. Bale, The Conflicts Between Parallel Trade and Product Access and Innovation: The Case of Pharmaceuticals, 1998 J. INTERNAT. ECON. L. 637, 644, n. 7 (relying on TRIPs Art. 28); see also Watal, TRIPs and the 1999 WTO Millennium Round, 3 J. WORLD INTELL. PROP. 3, 17-18 (2000) (describing similar arguments).

Others have argued that a policy of territorial exhaustion is prohibited under the GATT and TRIPs. See Abbott, supra note 13, at 632 (discussing a number of approaches to this issue,
would not appear to require Congress to enact an absolute right against importation in order to bring the United States into compliance.\textsuperscript{137} While the reports that Congress drafted itself do not refer to the doctrine of exhaustion,\textsuperscript{138} the President’s Statement of Administrative Action,\textsuperscript{139} which accompanied the TRIPs implementing legislation under the House and Senate’s special “fast track” procedural rules,\textsuperscript{140} does. The Statement of Administrative Action notes that the TRIPs Agreement “requires few changes in United States law and regulations and does not affect United States law or practice relating to parallel importation of products protected by intellectual property rights.”\textsuperscript{141} Further into its report, the Statement lists the changes to existing law deemed “required or appropriate” to implement TRIPs, and notes, “[o]ther areas of United States Intellectual property law are unaffected by the Agreement on TRIPs. For including arguments based on Article XI:1 of GATT 1994, GATT Art. III, GATT Art. XI and XX(d)). Professor Abbott argues that, all things being equal, GATT and TRIPs favor international exhaustion standing alone. \textit{Id.} However, he also subscribes to the proposition that TRIPs Art. 6 was intended as an “agreement to disagree” that puts off action on this subject until further considered by the TRIPs Council. \textit{Id. See also} S. K. Verma, \textit{Exhaustion of Intellectual Property Rights and Free Trade—Article 6 of the TRIPs Agreement}, 29 INTERNAT. REV. INDUS. PROP. & COPYRIGHT 534, 553-558 (1998) (relying on GATT Art. III(4) and GATT Art. XI(1), and responding to arguments to the contrary).

\textsuperscript{137} \textit{But see} sources cited \textit{supra} note 22.


\textsuperscript{140} The Omnibus Trade and Competitiveness Act of 1988 authorized the President to negotiate and enter into the Uruguay Round agreements, and provided for Congressional approval of implementing legislation under special “fast track” procedural rules of the House and Senate. See 19 U.S.C. §§ 2902-03, 2191 (1994). As a part of the fast track approval of the implementing legislation, the President was required to submit a statement to Congress providing information about how the implementing legislation would change or affect existing law and explaining why the proposed amendments were required or appropriate to implement the trade agreement. 19 U.S.C. § 2903(a)(2) (1994). The fast track approval rules limit the opportunity for debate in the House and Senate and prohibit amendments to the implementing legislation. 19 U.S.C. § 2191 (1994).

\textsuperscript{141} \textit{MESSAGE FROM THE PRESIDENT, supra} note 139, at 981, 1994 U.S.C.C.A.N.S. at 4280.
example, the Agreement does not require any change in current United States law or practice with respect to parallel importation of goods that are the subject of intellectual property rights."

The quoted language does not specifically address the new importation right for patentees, and does not expressly say that the Uruguay Round Agreements Act (as opposed to TRIPs) has no effect on the existing law regarding parallel imports. Moreover, one could note that the existing United States law regarding parallel imports of patented goods addresses the legality of defendants’ use and sale of imported patented goods. Prior to the Act, importation, by itself, did not infringe a patent, so there was no occasion for the case law to address the applicability of the doctrine to the act of importation itself. A statement that existing law (regarding use and sale) will be unaffected does not necessarily mean that the existing rule regarding exhaustion of rights will be extended to an express new right of importation.

Such arguments seem too technical to be taken seriously, however. The purpose of the Uruguay Round Agreements Act was to make those amendments necessary to implement the TRIPs Agreement. Because of the restrictions on debate and amendments entailed in the procedural rules for fast track legislation, it is unlikely that Congress intended to do anything more than was strictly necessary to accomplish that purpose. Since TRIPs did not require that the importation right be applied free of the doctrine of exhaustion, it seems unlikely that Congress would undertake to make it so, since this would shift the existing balance of rights among the parties in parallel import situations, and the legislative history suggests a strong intent to leave the parallel import situation at the status quo. Moreover, it would be incongruous to assume that Congress intended to make the act of importing parallel imports an infringement, when using or selling the goods once they reached the United States would not be. The clear implication of the quoted language from the Statement of Administrative Action is that the doctrine of exhaustion, as defined in the case

143. Patentees did (and still do) have a right to prohibit importation of infringing goods through the auspices of the International Trade Commission and Tariff Act § 337. See notes 135 and 148.
144. See supra note 15.
145. A court’s task is to “interpret the words of [a statute] in light of the purposes Congress sought to serve.” Chapman v. Houston Welfare Rights Org., 441 U.S. 600, 608 (1979). Here, Congress’ purpose in enacting the Uruguay Round Agreements Act was merely to amend existing United States law sufficiently to bring it into compliance with TRIPs.
law, will extend to the new importation right, as well as to the pre-existing use and sale rights. Because of the particular nature of the fast track implementation procedure, the Statement of Administrative Action should carry significant weight in interpreting the Uruguay Round Agreements Act amendments.146

While the quoted language from the Statement of Administrative Action seems to support a finding that the new statutory importation right will be tempered by the modified doctrine of international exhaustion, as tailored to date by the courts, there is other language in the Statement that could be used to construct an argument to the contrary. The Statement asserts that the amendment “adds to the [patentee’s] current rights . . . the right to preclude others from . . . importing a product covered by a United States patent.”147 One could argue that if the new importation right is interpreted to be subject to the doctrine of exhaustion, it adds rather little to the rights that United States patentees already enjoyed.

Tariff Act § 337 has long enabled United States patent owners to prevent importation of infringing goods through resort to the International Trade Commission.148 While the International Trade Commission is not authorized to award damages, patentees have been able to sue importers for damages through a cause of action for inducing the infringement of those who use or sell the imported articles in the United States.149 Both the International Trade

146. Congress approved the Administrative Statement when it implemented the Uruguay Round Agreements Act. Uruguay Round Agreements Act, Pub. L. No. 103-465 § 101(a), 108 Stat. 4809, 4814 (1994). Section 102(d) of the Act provides that “[t]he statement of administrative action approved by the Congress under section 101(a) shall be regarded as an authoritative expression by the United States concerning the interpretation and application of the Uruguay Round Agreements and this Act in any judicial proceeding in which a question arises concerning such interpretation or application.” Pub. L. No. 103-465, § 102(d), 108 Stat. at 4819.
148. 19 U.S.C. § 1337 (1994). Section 337 authorizes the International Trade Commission to prohibit the importation of articles that “infringe a valid and enforceable United States patent” or “are made, produced, processed or mined under, or by means of, a process covered by the claims of a valid and enforceable United States patent” by excluding their entry into the country or by means of a cease and desist order.
149. 35 U.S.C. § 271(b) (1994). A cause of action for inducement entails a showing that the defendant actively, intentionally assisted another to infringe, with knowledge that infringement was likely to occur. 4 DONALD S. CHISUM, PATENTS: A TREATISE ON THE LAW OF PATENTABILITY, VALIDITY AND INFRINGEMENT § 17.04 (1991). Thus, any importer who was aware that the goods it imported infringed would be likely to be liable for inducing the subsequent infringement of
Commission cause of action and the cause of action for inducement have been tempered by the doctrine of exhaustion.\textsuperscript{150} If the new importation right added by the Uruguay Round Agreements Act is likewise tempered by the doctrine of exhaustion, then one might argue that patentees' rights have not been augmented much by addition of an express statutory importation right. As a practical matter, the only substantive right patentees will have gained is a cause of action for damages (as opposed to an exclusionary or cease and desist order) against importers who do not qualify for protection from the doctrine of exhaustion, who do not themselves use or sell the goods in the United States (for purposes of a direct infringement claim), and who lack the requisite knowledge and intent for purposes of an inducement claim. That group of potential new defendants is likely to be a small one. If, on the other hand, the new importation right is not subject to the doctrine of exhaustion, the new importation right will have added quite significantly to the existing rights of patentees.

In support of this argument, one might invoke the rule of statutory construction that "[w]hen Congress acts to amend a statute, we presume that it intends its amendment to have real and substantial effect,"\textsuperscript{151} and argue that construing the new importation right to be subject to the doctrine of exhaustion would greatly undercut the significance of Congress' actions. If Congress had intended essentially to maintain the status quo, it could have determined that persons who took possession of the imported goods and used or sold them in the United States.

It should also be noted that Congress had already provided process patent owners a cause of action for infringement against persons who import products made abroad by their patented process. 35 U.S.C. § 271(g) (1994). This right was added by the Omnibus Trade and Competitiveness Act of 1988, Pub. L. No. 100-418 §§ 9001-9007, 102 Stat. 1107, 1563-67 (1988).

150. The International Trade Commission applies domestic patent law, as developed in the courts, in determining whether imported goods are infringing, and thus must be excluded from the country. See supra note 147. Thus, section 337 does not prohibit importation of goods initially sold abroad without condition by or under the authorization of the United States patentee. Since sale or use of the goods in the United States would not infringe the United States patentee's rights, the goods should not be deemed "infringing" for purposes of exclusion under section 337. See supra note 148.

One may only be liable for inducement under Patent Act § 271(b) if his actions assist another to infringe. DeepSouth Packing Co., Inc. v. Laitram Corp., 406 U.S. 518, 526 (1972). Thus, if use or sale of imported goods does not infringe because of the doctrine of exhaustion, the importer should not be deemed liable for acts inducing or assisting the use or sale.

United States law already complied with the TRIPs requirement that patentees enjoy a right against importation.\textsuperscript{152} In light of the Statement of Administrative Action’s assertion that the amendment “adds to the [patentee’s] current rights . . . the right to preclude others from . . . importing a product covered by a United States patent,” the amendment should be construed not as essentially stating the existing rule, but as creating a significant new substantive right.

Given that the new importation right does provide some new rights to patentees, however narrow, this argument would be unlikely to carry the day.\textsuperscript{153} Nonetheless, in the case of ambiguities in statutory language, it is appropriate to consider the consequences of alternative interpretations, and determine which results would be more reasonable or desirable in light of the overall purposes of the Patent Act.\textsuperscript{154} Thus, the following Section will discuss some of the key

\textsuperscript{152} There is certainly precedent for such an approach in Congress’ adoption of legislation to implement international intellectual property treaties. For example, when Congress ratified the Berne Convention, it initially determined that it would not be necessary to add express moral rights of integrity and attribution to the Copyright Act, notwithstanding Article 6 of the Berne Convention mandating their provision, because a collection of existing federal and state tort and unfair competition doctrines were sufficient to protect the interests at stake. Berne Convention Implementation Act of 1988, H.R. Rep. No. 609, 100th Cong., 2d Sess. 33-34 (1988).

\textsuperscript{153} Indeed, the Supreme Court rejected a very similar argument recently in \textit{Quality King Distsibs., Inc. v. Lanza Research Int’l, Inc.}, 523 U.S. 135 (1998), concerning the applicability of the doctrine of exhaustion to the express right of importation in Copyright Act § 602(a). \textit{Id.} There the plaintiffs argued that if Copyright Act § 602(a) were construed to be subject to the doctrine of exhaustion (which is codified in Copyright Act § 109(a)), then “both the section 602(a) right itself and its exceptions would be superfluous.” \textit{Id.} at 145. Prior to the enactment of section 602(a), the Copyright Act already prohibited the importation of “piratical” or unauthorized copies of copyrighted works, and that provision was retained in section 602(b). Thus, unless the Court construed section 602(a) to cover non-piratical (“lawfully made”) copies sold by the copyright owner, it would add nothing to copyright owners’ existing rights. \textit{Id.} at 146. The Court rejected the argument, finding that even if subject to the doctrine of exhaustion, section 602(a) provided copyright owners with some new, albeit rather narrow rights: a private cause of action against importers of goods that were not subject to the doctrine (before, enforcement of copyright owners’ importation rights had been vested in the Customs Service); rights against non-owner importers, such as bailees, licensees or consignees whose possession was lawful; and rights against copies that were “lawfully made” under the law of another country, but not with the United States copyright owner’s authorization. \textit{Id.} at 147.

\textsuperscript{154} \textit{See, e.g.}, Pennock & Sellers v. Dialogue, 27 U.S. (2 Peter) 1 (1829); Knowlton v. Moore, 178 U.S. 41, 77 (1899).
policy considerations arising from the parallel import of patented articles, to
determine whether they support an interpretation of the new importation right
free of the doctrine of exhaustion.

V. THE CASE AGAINST THE PRESENT RULE

Can a compelling case be made to move to a rule of territorial exhaustion,
which would enhance United States patentees' ability to prohibit parallel import
of their products? There is a notable lack of empirical data through which to
gauge the actual impact of parallel imports on industrial development,
international trade and technology transfer. However, there has been some
lively debate in the literature over the policy implications of parallel imports
(most notably in the field of trademarks, though addressing copyrights and
patents to some extent) and their likely effect on industry and trade. Some
commentators have argued that parallel imports undermine both domestic and
international industrial development, and that the underlying purposes of
intellectual property rights would be more effectively served through application
of a territorial exhaustion rule. Indeed, the Clinton Administration has
advocated prohibitions of parallel imports in a number of international trade and
intellectual property treaty negotiations, in seeming disregard of the present state
of United States law.155

This final Section will first review explanations of why parallel imports

155. See Herman C. Jehoram, Prohibition of Parallel Imports Through Intellectual Property
Rights, 30 INT. REV. INDUS. PROP. & COPYRIGHT L. 495 (1999) (describing stated United States
position on parallel imports in various contexts); Wegner, supra note 14, at 43. Ironically, when
the Japanese Supreme Court recently adopted a modified international exhaustion rule in
connection with the parallel import of patented goods, which was surprisingly similar to the rule
already existing in the United States, the Clinton Administration suggested that it would consider
trade sanctions in retaliation. See Abbott, supra note 13, at 634; Jehoram, supra, at 510. See also
a case involving parallel import of goods with copyrighted labels, the Supreme Court notes that
"the Executive Branch of Government has entered into at least five international trade agreements
that are apparently intended to protect domestic copyright owners from the unauthorized
importation of copies of their works sold in those five countries," notwithstanding the existence of
a Third Circuit decision holding that parallel import of goods sold abroad by the United States
copyright owner does not infringe the United States copyright).
occur,\textsuperscript{156} and then review and evaluate the primary arguments that have been, or might be, made in favor of a territorial exhaustion rule for patents.\textsuperscript{157} These arguments can be divided into three topic areas: (1) promotion of the underlying purposes of patent law; (2) effect of parallel imports on domestic competition and public welfare; and (3) global considerations. The article will conclude that on the present record, there is no compelling case for a move to a territorial exhaustion rule, and that adoption of such a rule would be an impediment to general world movement in the direction of free trade.

\textit{A. Why Parallel Imports Occur}

A number of explanations have been offered for why parallel imports occur, and they are by no means mutually exclusive. It appears that parallel imports arise, in part, in response to intellectual property owners’ practice of international price discrimination, charging whatever the market will bear in a particular country.\textsuperscript{158} Since the United States is a relatively affluent market, patentees may be able to charge higher prices here than they can in less affluent countries. This creates opportunities for third parties to purchase quantities of the patented article abroad, ship the articles to the United States and resell them in competition with the United States patentee. Even after paying the costs of transport, the parallel importer may be able to charge a lower price to United States consumers than the United States patentee does and make a significant

\textsuperscript{156} There have been few studies of the cause of parallel importing, and the literature that addresses the issue tends to focus on parallel importing of trademarked goods (sometimes called “gray market” goods), rather than patented goods. However, much (albeit not all) of the reasoning regarding the cause of trademark parallel imports seems logically to apply to explain parallel imports of patented goods. Thus, this article will draw to some extent on discussions that address parallel imports of trademarked and copyrighted goods, as well as on the relatively few discussions that specifically address parallel imports of patented goods.

\textsuperscript{157} As noted above, a large portion of the literature addresses the use of trademark and copyright law to block parallel imports. The underlying purposes of trademark law, in particular, differ from those of patent law, and this may render some of the arguments made in the trademark context inapplicable to the patent context. However, some of the considerations arising in the trademark context, as well as the copyright context, have some bearing on the patent exhaustion debate, and thus may be addressed in the discussion that follows.

\textsuperscript{158} See Rothnie, supra note 22, at 567-579; Stack, supra note 22, at 682; see also John Hilke, \textit{Free Trading or Free-Riding: An Examination of the Theories and Available Empirical Evidence on Gray Market Imports}, 32 \textit{WORLD COMPETITION} 75, 78 (1988).
It is probable that most decisions to engage in international price discrimination are made independently by the business/intellectual property owner involved, which is generally a business having some degree of United States market power. However, in some cases, the decision may result from collusion by competing United States business entities within a particular industry that are seeking to raise their margins across the board. They may accomplish higher margins by agreeing to raise prices and simultaneously undertaking to limit intrabrand competition by restricting parallel imports.

However, the price differentials, that attract parallel importers, are not all attributable to price discrimination. In some cases they may reflect higher costs that an intellectual property owner incurs in putting the protected product on the market. For example, a patentee may incur higher costs of labor or expensive regulatory requirements in the United States that it does not incur abroad, or it may pursue a more expensive marketing strategy in the United States than it does abroad. Parallel importers who purchase the patented good abroad for resale in the United States may free ride on some of the patentee’s greater United States expenditures—particularly its advertising and marketing expenditures, which facilitate consumer demand for the patented article.

Price differentials may also be attributable to changes in international monetary exchange rates. Finally, it has been suggested that intellectual

159. See Hilke, supra note 158, at 80-81.
160. As Hilke explains:
Manufacturers’ output constraints, strategic output and pricing considerations, barriers to entry, and long-run marketing considerations may make foreign suppliers reluctant to change their United States prices in lock step with changes in exchange rates. To the extent that foreign suppliers base their decisions on these longer-run considerations, their pricing decisions may differ from those of independent middlemen. The available evidence on trade reactions to changes in exchange rates suggests that lags are extremely common....

Where suppliers either individually or collectively do not respond to exchange rate changes with prompt price adjustments, sufficient price differences may emerge to encourage [parallel imports]. Hilke, supra note 158, at 81-82. See also Barfield & Groombridge, supra note 12, at 923 ("[P]rices might vary due to fluctuations in foreign currency exchange markets. An extensive literature documents that parallel imports surge when a country’s exchange rate appreciates because import prices do not decrease in the same proportion as the appreciation of the other country’s currency."); SETH E. LIPNER, THE LEGAL AND ECONOMIC ASPECTS OF GRAY MARKET
property owners themselves may sometimes orchestrate or encourage parallel import shipments to perpetuate their own ends. For example, the United States intellectual property owner may facilitate parallel imports as a means of improving the bottom line of the foreign subsidiary that sells to the parallel importers. Or it might quietly orchestrate parallel imports as a means of disciplining distributors, who are increasing their margins by refusing to pass reductions in their cost along to consumers, or who are engaged in industry-wide collusion.

While there is little empirical data to demonstrate which of these spurs to parallel importing is the most prevalent, it seems likely that all of them play a role at one time or another.

GOODS, 3 (1990) (“the meteoric rise in the value of the United States dollar in 1981 and 1982 caused gray market importation to become a lucrative business. During this time, it was not unusual to see prices for gray market goods one third lower than the price of their authorized counterparts. As the United States dollar declined in value in 1987 and 1988, the profitability of international gray market sales was undoubtedly reduced.”); ROTHNIE, supra note 22 at 567-79.
161. See LIPNER, supra note 160, at 4-5.
162. Hilke, supra note 158, at 79-80. As Hilke explains, manufacturers may find parallel imports to be a useful, non-public way to discipline their retailers, “particularly where contractual obligations or legal restrictions prevent the manufacturer from explicitly establishing additional distributors, imposing maximum price limitations, or establishing volume requirements.” Id. at 80.
163. As Hilke explains, excessive retail or wholesale margins resulting from collusion will reduce overall demand for the product, leading the manufacturer to attempt to undermine the retailer or wholesaler collusion through means of parallel imports. Hilke, supra note 158, at 80-81.
164. For a discussion of the few studies that have been done, see ROTHNIE, supra note 22, at 567-78; Abbott, Second Report (Preliminary) to the Committee on International Trade Law of the International Associate on the Subject of the Exhaustion of Intellectual Property Rights and Parallel Importation, 7-10 (Aug. 10, 1999) (unpublished paper) (a copy is on file with this author).
165. See ROTHNIE, supra note 22, at 571 (noting that “a large role for currency exchange rate movements is clear, as also for attempts to practice some form of price discrimination. Certainly, there are strong grounds for the conclusion that parallel imports may arise for any, or a combination, of several reasons.”); Hilke, supra note 158, at 80-91. The author concludes, in context of parallel imports of trademarked goods, that the available evidence points away from free riding on United States trademark owners’ investments as a primary cause of parallel importing. Id. Rather, the hypothesis that parallel imports result from exchange rate adjustments is generally more consistent with the evidence in most industries. Id. The author also notes the likelihood that trademark owners also orchestrate parallel imports as a means of disciplining distributors. Id.
B. Arguments for a Rule of Territorial Exhaustion

1. Promotion of the Underlying Purposes of Patent Law

a. The Purpose of the Patent Law

One of the arguments that has been made for a territorial rule of patent exhaustion is that the purpose of patent law is to give the patentee the benefit of monopoly rights in selling the patented article. Thus, the doctrine of exhaustion permits a patentee to exercise patent rights once with regard to each patented article that is sold. Once this has occurred, the doctrine applies to prevent a second exercise of patent rights in the same article.

Accordingly, when a United States patentee sells a patented article in the United States, that sale constitutes an exercise of the patent right, and triggers exhaustion. However, if the patentee sells the article outside of the United States, the sale does not constitute an exercise of the United States patent right because the United States patent does not convey rights outside of the territory of the United States. Thus, even though the United States patentee got the benefit of the foreign sale, it did not exercise its United States patent in making the sale, and its rights under the patent are not exhausted. If subsequent purchasers later bring the article to the United States, the patentee can prevent them from doing so, or extract a royalty in return for permission, because, in doing so it is exercising its rights under the United States patent for the first time. Under this line of reasoning, the doctrine of exhaustion focuses on the “exercise” of patent rights, rather than on the exchange of title in the article being sold in return for compensation.

It follows that if the patentee owns parallel patents in the same invention in a number of countries, each nation’s patent represents a separate bundle of rights that must be exercised once before the doctrine of exhaustion can apply. The patentee may sell a patented article in one country and then assert its patents in other countries to exact a separate tribute in each country through which subsequent purchasers move the article, or to completely prohibit any international movement of the article.166 The patentee’s monopoly rights, in a given article, are multiplied by the number of countries where it has obtained a patent.

166. This general argument is noted in Coggio & Antler, supra note 14, at 483, 488-89; Rothnie, supra note 13, at 326; ROTHNIE, supra note 22, at 563.
If one takes this argument on its face, it follows that a territorial exhaustion doctrine is more compatible with the underlying purpose of the patent law. However, there are at least two criticisms that might be raised with regard to the argument. First, on a more technical level, the “exercise of rights under the patent” concept is flawed because it appears to assume that the patent gives the patentee an affirmative right to sell the invention in the United States, which can be exercised once and then exhausted. However, the United States patent law does not grant patentees an affirmative right to sell their patented inventions, but only a right to prevent others from doing so.¹⁶⁷ Thus, characterizing a patentee’s sale in the United States (as contrasted with a sale outside of the United States) as an “exercise” of the patent right is questionable at the outset, and provides a shaky foundation for the rest of the theory.

A second criticism can be directed to the argument’s characterization of the patent law’s purpose. The district court in Griffin v. Keystone Mushroom Farm appears to have adopted the assumption that the purpose of patent law is to ensure that patentees enjoy monopoly rights in connection with all sales, but there is little in the earlier case precedent to suggest such a precise purpose.¹⁶⁸

¹⁶⁷. Patent Act § 154(a) provides:

Every patent shall contain a short title of the invention and a grant to the patentee, his heirs or assigns, of the right to exclude others from making, using, offering for sale, or selling the invention throughout the United States or importing the invention into the United States, and, if the invention is a process, of the right to exclude others from using, offering for sale or selling throughout the United States, or importing into the United States, products made by that process, referring to the specification for the particulars thereof.


¹⁶⁸. 453 F. Supp. 1283 (E.D. Pa. 1978). The decision is discussed in some detail at supra note 111 and accompanying text. There is a great deal of judicial language suggesting that a sale (as opposed to an exercise of patent rights) exhausts the patentee’s rights, and that the rights that are exhausted are in the article itself. See, e.g., United States v. Univis Lens Co., 316 U.S. 241, 250-52 (1942). The Court stated:

The patentee may surrender his monopoly in whole by the sale of his patent or in part by the sale of an article embodying the invention. His monopoly remains so long as he retains ownership of the patented article. But sale of it exhausts the monopoly in that article and the patentee may not thereafter, by virtue of his patent, control the use or disposition of the article... The first vending of any article manufactured under a patent puts the article beyond the reach of the monopoly which that patent confers.

Id. See also Bloomer v. McQuewan, 55 U.S. (14 How.) 539, 549 (1852) (“When the machine
Rather, the Supreme Court decisions that have developed and justified the doctrine of exhaustion suggest that the patent laws serve a more general, flexible purpose: to provide an incentive to invent by giving inventors the means of profiting from their inventions, while ensuring that inventors’ rights do not exceed what is necessary to fulfill that purpose and, thus, interfere unnecessarily with free competition.\(^{169}\) The patent law does not undertake to ensure that patentees extract the greatest possible benefit from their inventions—only a generally sufficient benefit.\(^{170}\) It is true that the law adopts a form of United States monopoly right as the means to that end, but it does not necessarily follow that the law insists upon receipt of a price enhanced by the United States patent monopoly in connection with every sale the patentee makes, regardless of where that sale occurred. The extent of the patentee’s ability to insist upon such a price logically turns on the extent to which it is necessary in order to provide an incentive to invent. Entitling the patentee to rely on the United States monopoly right in the case of goods it sells abroad (through adoption of a territorial exhaustion rule) carries its own countervailing cost—among other things, the cost of interfering with the alienability of goods already in the stream of commerce. Thus, this opportunity to interfere should not be extended unless it is necessary to provide the desired incentive.

The appropriate approach to determining whether the United States’ existing modified international exhaustion doctrine is consistent with the purposes of the patent law, therefore, is to ask whether patentees need to control subsequent importation and sale of patented articles they sell, or authorize to be sold abroad, in order to have an incentive to invent. If parallel imports interfere too greatly with their ability to benefit from their inventions, then a change in the rule may be warranted.

\(b. \textit{The Effect of Parallel Imports on Accomplishment of the Purpose of Patent Law}\)

It seems self-evident that patentees do benefit from their foreign sales, or presumably they would not make them. They generally have the right to choose whether or not to sell, and may decline to sell if they deem the available terms to

\(^{169}\) \textit{See supra} note 28-32 and accompanying text.

\(^{170}\) \textit{See supra} note 33 and accompanying text.
be disadvantageous, either in isolation or in the context of their overall international sales strategy. However, advocates of territorial exhaustion have advanced two reasons why the benefit is insufficient: first, the benefit from foreign sales may be of a lesser magnitude than the benefit from United States sales; and second, importation of patented goods sold abroad may undermine the benefit of patentee’s domestic sales. These arguments will be examined in turn below.

    i.  The Relative Degree of Benefit from Foreign and Domestic Sales

    Some advocates of territorial exhaustion have suggested that the differing conditions under which foreign sales may be made justify a finding that those sales do not count, across the board, for purposes of the United States exhaustion doctrine. They note that the country of first sale may not provide patent protection for the particular kind of invention at issue, or if it provides patents, it may provide a lower level of protection or, as a practical matter, make enforcement difficult or impossible. Or, the country of first sale may impose price controls on the invention, or subject patented inventions to compulsory licensing. 171 All of these circumstances may make it harder for the United States patentee to obtain as high a price in the foreign sale as it does in United States sales, meaning that it may not benefit as much from foreign sales as it does from domestic sales.

    This line of argument suggests that the possibility of lower benefit abroad, in itself, justifies recognizing a second right to benefit from the article, if subsequent owners attempt to bring it within the reach of United States patent law: because the patentee cannot be certain of reaping as high a price in foreign sales as in United States sales, the purpose of the patent law to benefit the patentee is not satisfied in foreign sales.

    In response to this argument, one might initially note that some foreign sales may provide an equal or greater overall benefit to the United States patentee than its United States sales do, particularly if costs of placing products in the market abroad tend to be lower, as is sometimes asserted. In such cases there would be little justification in finding the doctrine of exhaustion inapplicable. However, a rule that made exhaustion turn on a case-by-case evaluation of the relative level of benefit gained in the first sale of patented articles would be impractical,

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171. See, e.g., Wegner, supra note 14, at 24, 30; Bale, supra note 12 at 643; Rothnie, supra note 13, at 331.
imposing an unmanageable level of uncertainty in the market place.\textsuperscript{172} 

In any event, an argument that the potential for lower benefit abroad justifies elimination of foreign sales from the exhaustion doctrine finds little support in case precedent or in logic. United States patent law has never undertaken to guarantee any particular level of return on patented articles. It primarily seeks to make it more feasible for the patentee to exploit the invention by enabling it to prevent others from free riding on its research and development investment. There may be no market at all for the patented invention. The Patent Act does not intervene to provide one. The price the patentee is able to charge for the patented article may vary from one geographic location to another within the United States, and from one year to another, as other products become available that the public might prefer. The doctrine of exhaustion does not restrict itself to the sales that bring the highest price. Nor does the law enable the patentee to come back to purchasers and demand further compensation if they have found uses for the patented article (such as using it for a different purpose, or reselling it in a different market) that provide them with a greater value than the patentee anticipated when he set the purchase price.\textsuperscript{173} 

The key is that the patentee chose to make the initial sale. If a sale is not sufficiently beneficial, or undercuts his financial position in other sales, the patentee may refrain from making it. The law is not intended to ensure that the patentee is able to squeeze every possible penny out of the invention.\textsuperscript{174} There are numerous limitations on his right that are meant to protect the interests of the public.\textsuperscript{175} Thus, as a general matter, the fact that the patentee may not obtain as great a price abroad\textsuperscript{176} as in the United States should not in itself lead to a

\textsuperscript{172} See supra note and accompanying text.

\textsuperscript{173} See Wilbur-Ellis Co. v. Kuther, 377 U.S. 422 (1964). In that case, the Supreme Court found that a purchaser of a patented machine did not infringe the patent by altering the machine to serve a more valuable use than was anticipated by the patentee. \textit{Id.} For further discussion of this issue see Stern, \textit{supra} note 3, at 122.

\textsuperscript{174} See supra note 170 and accompanying text.

\textsuperscript{175} See supra note 6 and accompanying text. Apart from the exhaustion doctrine, which seeks to ensure that goods move freely in the marketplace, the Patent Act limits the duration of patent protection. Antitrust law and the patent misuse doctrine limit lucrative uses the patentee might make of the patent. Moreover, the patent itself may be refused or invalidated if the patentee failed to make adequate disclosure of the invention, 35 U.S.C. \textsection 112, or fails to satisfy other statutory criteria. See, e.g., 35 U.S.C. \textsection\textsection 102, 103 (1994).

\textsuperscript{176} As noted earlier, a failure to obtain as high a price as in the United States is not necessarily a
finding that the doctrine of exhaustion is inapplicable to those sales, as long as the patentee decided to go forward with the sale.177

Foreign courts have rejected the suggestion that a finding of exhaustion should depend upon the availability and quality of patent protection in the country of first sale.178 Moreover, even if one considers the lack or inadequacy

failure to obtain as great benefit from the sale, since costs of manufacture and sale abroad may be lower than in the United States, as well.

177. As Professor Abbott points out, the market environments of the various World Trade Organization members differ considerably. However, the differences provide no basis under the GATT for imposing quotas or other protectionist measures to prohibit import of goods produced and sold in lower cost regions. See Abbott, supra note 13, at 622-23.

178. In the European Union, which follows a rule of international exhaustion within the territory of the Union, the European Court of Justice ruled that the doctrine of exhaustion applied to pharmaceutical products sold with the patentee’s consent in member nations that did not afford patent protection for such goods. Case 187/80, Merck & Co. Inc. v. Stephar, 1981 E.C.R. 2063. In Merck, the plaintiff held patents for its drug in all the E.U. members except Luxembourg and Italy, where the drug was excluded from patent protection. Id. It marketed the product in Italy, the defendant purchased it there and shipped it to the Netherlands for resale. Id. Merck argued that the doctrine of exhaustion should not shield the defendant from an infringement claim because, due to the unavailability of a patent in Italy, it had been unable to collect the full reward for its creative effort in the first sale. Id. The court rejected the argument, stating:

That right of first placing a product on the market enables the inventor, by allowing him a monopoly in exploiting his product, to obtain the reward for his creative effort without, however, guaranteeing that he will obtain such a reward in all circumstances.

It is for the proprietor of the patent to decide, in the light of all the circumstances, under what conditions he will market his product, including the possibility of marketing it in a Member State where the law does not provide patent protection for the product in question. If he decides to do so he must then accept the consequences of his choice as regards the free movement of the product within the Common Market, which is a fundamental principle forming part of the legal and economic circumstances which must be taken into account by the proprietor of the patent in determining the manner in which his exclusive right will be exercised.

Id. at 2081-2082. See Yusuf & von Hase, supra note 3, at 120-22; Rothnie, supra note 13, at 316-19. The Court of Justice recently reaffirmed this reasoning. Joined Cases C-267/95 and C-268/95, Merck & Co., Inc. v. Primecrown Ltd. & Beecham Group plc v. Eurpharm of Worthing Ltd., 1996 E.C.R. 16285. Of course, the European Union’s circumstances may be distinguishable to some extent, since the economic development of its member nations is more uniform than that of the
of foreign patent protection to be relevant in determining whether a foreign sale exhausts the United States patentee's rights, inconsistencies in the world's patent laws are quickly diminishing. The TRIPs Agreement\(^1\) made tremendous strides in harmonizing the world's patent laws, thus reducing the concern that patents may be unavailable, weaker, or unenforceable for United States inventions in other countries.\(^2\) While it is true that some countries may defer

world as a whole. See generally Abbott, supra note 13, at 619-21.

The Japanese Supreme Court recently adopted a modified international exhaustion approach for parallel imports of patented articles that is similar in many respects to the United States' approach, and in the course of doing so, stated that it should not matter whether a parallel patent existed in the country in which the parallel import was initially sold. BBS Kraftfahrzeugtechnik AG v. Rashimekkusu Japan Co., Ltd. and JAP Auto Prods. Co., Ltd., supra note 23. In that particular case, the plaintiff did in fact have a parallel patent in Germany, where the product was first sold.

179. See supra note 22.

180. See Yusuf & von Hase, supra note 3, at 128; Abbott, supra note 13, at 619.

TRIPs mandates broad subject matter protection, bringing classes of inventions, such as agricultural chemicals and pharmaceuticals, that had been excluded from patent protection in a number of developing countries, within worldwide patent protection. TRIPs Article 27 provides:

1. Subject to the provisions of paragraphs 2 and 3, patents shall be available for any inventions, whether products or processes, in all fields of technology, provided that they are new, involve an inventive step and are capable of industrial application....

2. Members may exclude from patentability inventions, the prevention within their territory of the commercial exploitation of which is necessary to protect ordre public or morality, including to protect human, animal or plant life or health or to avoid serious prejudice to the environment, provided that such exclusion is not made merely because the exploitation is prohibited by their law.

3. Members may also exclude from patentability:

(a) diagnostic, therapeutic and surgical methods for the treatment of humans or animals;

(b) plants and animals other than micro-organisms, and essentially biological processes for the production of plants or animals other than non-biological and microbiological processes. However, Members shall provide for the protection of plant varieties either by patents or by an effective sui generis system or by any combination thereof. \*

TRIPs also mandates the provision of a broad, uniform range of rights. TRIPs Article 28 provides:

1. A patent shall confer on its owner the following exclusive rights:
full compliance with the TRIPs provisions until 2006, or even longer in special circumstances, it is clear that within the next decade, the world’s patent laws and enforcement mechanisms will be considerably harmonized. Even if that goal is not fully accomplished at this point in time, it hardly makes sense to change United States law to address a problem that is rapidly dissipating.

As noted earlier, advocates of a territorial exhaustion rule have sometimes cited the prospects of compulsory licensing abroad as a justification for excluding parallel imports. Articles sold abroad pursuant to compulsory licenses could logically be excluded from the exhaustion doctrine because their sale was compelled by law, and whatever royalty the patentee received was set by a foreign governmental authority, rather than by the patentee in voluntary negotiations. It has been suggested that patented articles sold through compulsory licenses are already exempt from exhaustion, but there is no specific United States case or statutory authority to that effect.

(a) where the subject matter of a patent is a product, to prevent third parties not having the owner’s consent from the acts of: making, using, offering for sale, selling or importing for these purposes that product;

(b) where the subject matter of a patent is a process to prevent third parties not having the owner’s consent from the act of using the process, and from the acts of: using, offering for sale, selling, or importing for these purposes at least the product obtained directly by that process.

2. Patent owners shall also have the right to assign, or transfer by succession, the patent and to conclude licensing contracts.

Agreement on Trade-Related Aspects of Intellectual Property Rights, Including Trade in Counterfeit Goods, 33 I.L.M. 81 (1994). Finally, TRIPs mandates provision of the means meaningfully to enforce those rights, and spells out in unprecedented detail what those means are. See TRIPs, supra note 22, Art. 41-64.


182. See supra note 164 and accompanying text.

183. See, e.g., Straus, supra note 136, at 195; Verma, supra note 13, at 562. Presumably, this is because the patentee is not able freely to negotiate the royalty paid by the compulsory licensee. The royalty is generally set by the government authority that grants the compulsory license. See generally TRIPs, supra note 22, Art. 31. The European Court of Justice has found that a patentee’s rights in goods sold pursuant to a compulsory license are not exhausted. See Case 19/84, Pharmon v. Hoechst, 1985 E.C.R. 2281; Joined Cases C-267/95 & C-268/95, Merck & Co., Inc. v. Primecreek Ltd. & Beecham Group plc v. Europharma of Worthing Ltd., 1996 E.C.R. I-6285, I-6387.

184. Copyrighted articles sold pursuant to United States compulsory licenses are subject to
The actual effect of foreign compulsory licensing provisions is far from clear. First, there is little evidence to establish how frequently compulsory licenses are granted. Moreover, to the extent that they are granted, the TRIPs Agreement, Article 31, now regulates their granting in a manner that may reduce their potential severity. However, even if advocates of a territorial rule were to provide evidence that compulsory licenses are sufficiently prevalent and detrimental to justify action (which they have not done to date), the justified action would be to exclude articles sold pursuant to compulsory licenses from the doctrine of exhaustion, not to exclude all articles sold abroad from the doctrine.

With regard to the suggestion that foreign price controls compel a territorial exhaustion rule, one might respond that sales in countries imposing price controls are voluntary sales, and so are not strictly comparable to sales pursuant to compulsory licenses. Moreover, the issue of price controls generally arises only in connection with one category in the broad range of United States patented inventions--pharmaceutical products--and only in a limited number of countries. Thus, even if special considerations would lead the United States to


185. It has been suggested that few compulsory licenses have ever been granted in developing countries, and that a significant increase in granting compulsory licenses is unlikely. See Watal, supra note 136, at 20-21.

186. Article 31 provides that compulsory licenses "shall be authorized predominantly for the supply of the domestic market" of the granting nation. TRIPs, supra note 22, Art. 31(f). It also requires that the patentee be paid "adequate remuneration" in light of the economic value of the authorization, Id., Art. 31(h), and provides procedural safeguards. See id., Art. 31(b) (notice); 31(i) & (j) (judicial review). For a discussion of ongoing concerns regarding compulsory licenses, see Watal, supra note 136, at 20-21.

187. It may be that while compulsory licenses are not frequently granted, the threat of compulsory licenses leads patentees to charge lower prices in some countries in order to avoid being subjected to them. However, again, such an argument is speculation in the absence of some reliable evidence that this is actually the case.

188. The European Court of Justice has held that the doctrine of exhaustion will apply to goods sold with a patentee's consent within the European Union, subject to government price controls. Joined Cases C-267/95 & C-268/95, Merck & Co., Inc. v. Primecrown Ltd. & Beecham Group plc v. Europharm of Worthing Ltd., 1996 E.C.R. I-6285, I-6388-89.
take account of price controls in fashioning its doctrine of exhaustion,\textsuperscript{189} it would not be necessary to change the general rule of exhaustion that applies to the wide-ranging majority of patented goods that are not subject to price controls.\textsuperscript{190}

\textit{ii. The Effect of Parallel Imports on the Domestic Market}

In addition to suggesting that the possibility of lower prices, in itself, should disqualify foreign sales from the doctrine of exhaustion, advocates of a territorial rule have noted that if foreign-sold goods are permitted to be resold in the United States, the patentee may be forced by the competition to reduce its domestic sales price, leading to less benefit from domestic sales.\textsuperscript{191} Thus, a rule of territorial exhaustion is necessary to avoid having parallel imports subject patentees to domestic price competition, undercutting the benefit of the United States patent in domestic sales.

One’s response to this argument may depend in part on one’s evaluation of the cause of parallel imports. As noted above,\textsuperscript{192} several causes have been cited, but there is little evidence to indicate what portion of parallel imports is

\textsuperscript{189} It has been suggested that the United States should avoid adopting an international exhaustion rule, because that would deter United States pharmaceutical companies from selling their drugs in countries that engage in price controls, depriving individuals of therapeutic treatments that they might need. See generally Wegner, supra note 14, at 30-31; Bale, supra note 12; Barfield & Groombridge, supra note 22. However, there may be less drastic ways to deal with this concern. For example, there are means of self-help that United States pharmaceutical patentees might pursue to avoid parallel import of their drugs from price-controlling nations. In his recently published First Report (Final) to the Committee on International Trade Law of the International Law Association on the Subject of Parallel Importation, Professor Abbott suggests that United States patentees produce or sell only enough of their patented drug in the price control nation to satisfy the local market. If a shortage of the drug arises there due to wholesalers diverting the supply to exporters, and the shortage is contrary to public health policy, then the government of the price control nation may have to “reconsider the structure of its health care market,” perhaps to restrict exports or eliminate wholesale buyers from the system. Abbott, supra note 13, at 623, 635-36.

\textsuperscript{190} See Abbott, supra, note 13, at 623, 635-36 (suggesting incorporation of an international exhaustion rule into the TRIPs Agreement, along with a possible exception or limitation for articles subject to government price controls, which can be viewed as a form of export subsidy).

\textsuperscript{191} See, e.g., Wegner, supra, note 14 at 2, 30-31.

\textsuperscript{192} See supra note 12 and accompanying text.
attributable to each of the suggested causes. To the extent that the higher United States prices that attract parallel imports result from price discrimination against United States consumers, or price collusion in the industry, one may be less inclined to credit the argument than if they result from higher United States costs. In the former case, parallel imports are beneficial to the United States public in neutralizing the discrimination and anticompetitive behavior.\textsuperscript{193} If the price disparities result from higher United States costs, one might wish to examine the nature of the costs. For example, if the higher costs are primarily attributable to more intensive advertising or promotion strategies in the United States than are employed abroad, or other voluntary business practices, then an alternative might be to encourage United States patentees to rethink their business strategies, at least if parallel imports otherwise benefit the public.\textsuperscript{194}

Thus, one answer to the argument that parallel imports undercut the domestic value of United States patents is simply that there is presently little reliable evidence to indicate what prompts parallel imports or how they affect domestic sales. There is evidence of increased investment in research and development, and of a significant increase in the number of patent applications filed by United States businesses in recent years.\textsuperscript{195} Thus, the United States' present modified international exhaustion rule does not appear to have had a negative impact. To the extent that patentees advocate a change of the existing exhaustion doctrine, they should bear the burden of demonstrating a genuine need, which outweighs the potential loss of public benefit from parallel imports. Another answer is that patentees are not without means under the United States' modified international exhaustion doctrine to protect themselves against potentially detrimental effects of parallel imports.

The United States' modified international exhaustion doctrine appears to permit patentees to prohibit importation of goods sold abroad through means of contractual provisions and label notice on the patented articles. Violation of the prohibition can be enforced as patent infringement against defendants who had notice of it.\textsuperscript{196} It has been suggested that this measure may not be effective in all cases. For example, a defendant may have had inadequate notice because the

\textsuperscript{193} Moreover, if a significant portion of parallel imports results from the efforts of United States patentees to serve their own ends, then that may also suggest that no change in the doctrine of exhaustion is needed, at least to protect the patentees.

\textsuperscript{194} The potential benefit of parallel imports to the public will be discussed in the next section.

\textsuperscript{195} See Barfield & Groombridge, supra note 22, at 207-208.

\textsuperscript{196} See supra notes 71-79 and accompanying text.
restrictive label was removed or packaged over, or the laws of the country of original sale may prohibit contractual limitations on exportation. However, in many cases, contractual restrictions may provide the means to prevent parallel imports, if the patentee finds them sufficiently detrimental to justify the effort.

And there are additional means of self-help available to patentees seeking to avoid parallel imports. For example, the patentee may decide not to sell in foreign markets where the risk of parallel imports is great, or to limit its sales there. Or the patentee may vertically integrate in order to better control its chain of distribution, making it harder for parallel importers to buy large quantities of the patented article abroad at wholesale prices. Or the patentee might reduce price disparities in the various nations in which it sells, thus reducing the margin that can be earned by parallel traders, and the incentive to engage in parallel trading. United States courts have emphasized the availability of self-help measures in judging the effect of parallel imports on intellectual property owners’ rights.

Given the lack of reliable evidence that parallel imports really do undercut the effectiveness of United States patents to serve as an incentive to create, and the existing measures that patentees may take to control or prevent parallel imports, the case for abandoning the United States’ modified international exhaustion doctrine as inconsistent with the underlying purposes of patent law is a weak one.

197. See Tessensohn & Yamamoto, supra note 22, at 735-36.
198. See Chard & Mellor, supra note 12, at 72. There may also be some issues regarding the enforceability of label notice restrictions. See supra note 35.
199. See Chard & Mellor, supra note 12, at 81; Yusuf & von Hase, supra note 3, at 122. Or the patentee may limit sales to the minimum required to satisfy the local market. See Abbott, supra note 13, at 623.
200. See Chard & Mellor, supra note 12, at 72, 81.
201. Id.
203. It should also be borne in mind that moving to a territorial rule may give multinational corporations an unnecessary competitive advantage over strictly domestic companies. This is because the company engaged in multinational sales may obtain two opportunities to control and benefit from patented articles it sold abroad, while a company who sells domestically has only one such opportunity. As Yusuf and von Hase explain: “Such discrimination between domestic and imported products is inconsistent with Article II(4) of the General Agreement [on Tariffs and
2. The Effect of Parallel Imports on Competition and General Public Welfare

Some advocates of the territorial rule of exhaustion point out that dividing the international marketplace into exclusive geographic territories is an efficient business practice which encourages authorized distributor/licensees to invest in promoting the patented product and to provide services related to the product, such as pre-sale quality control, warranties, and after-sale repair, within their exclusive market area. Distributor/licensees may be unwilling to make such investments if their investments are subject to free riding by parallel importers, and they are forced to cut prices in order to engage in intrabrandon competition. Thus, to promote distributor/licensee investment, the rule both in the United States and worldwide should be one of territorial, rather than international, exhaustion.

It has also been suggested that a territorial rule better serves the interests of the United States public. If parallel importing is permitted in the United States, domestic prices may go down—at least temporarily—but the overall public welfare will be decreased in the long term because there will be fewer product-related services, a less stable supply of goods, and generally less marketplace competition. Advocates of a territorial rule add that restricting intrabrandon trade, which obliges contracting parties to grant imported products a treatment no less favorable than that accorded to like products of national origin in respect of all laws and regulations affecting their internal sale, purchase, distribution or use.” Yusuf & von Hase, supra note 3, at 128 (emphasis in original).

204. See, e.g., Chard & Mellor, supra note 12, at 73-79; Barfield & Groombridge, supra note 12, at 921-22; Bradley, supra note 14.

205. See, e.g., Chard & Mellor, supra note 12, at 73-75; Tessensohn & Yamamoto, supra note 22, at 731-34.

206. See, e.g., ROTHNIE, supra note 22, at 564-65; Chard & Mellor, supra note 12, at 73-74.

207. See Chard & Mellor, supra note 12, at 77-79 (“Parallel imports may reduce efficiency to the detriment of the consumer by denying them things they are willing to pay for (namely, consistent quality and pre-sales and after-sales services), by raising the costs of supplying consumers (disruption of investment planning) and by reducing the level of innovation”); Barfield & Groombridge, supra note 12, at 925-26 (“there is strong reason to believe that consumers would have fewer choices of goods or services in the long run in a world where parallel imports were allowed.”); Bradley, supra note 14, at 3. Bradley writes:

The eventual effects of permitting parallel importation and making exclusive market
competition may have the effect of enhancing interbrand competition, leading to a net increase in marketplace competition, to the public’s benefit.208

Several responses might be made to these arguments in support of a territorial exhaustion rule. First, one might question whether they are appropriate for consideration in the context of patent protection, as opposed to trademark and unfair competition protection. The patent laws are generally understood to protect an inventor’s investment in research and development against free riders. Trademark and unfair competition laws are designed to protect and promote investment in the marketing process. Thus, considerations of free riding on marketing investments would seem best addressed in determining the scope of the doctrine of exhaustion in trademark law, rather than

rights unenforceable must be to concentrate supplies of IP products on single world suppliers who may or may not be willing to undertake the investment required to secure effective supply arrangements worldwide. And without exclusive rights, the incentive to invest in stockholding in a territory will become minimal.

Id. See also ROTHNIE, supra note 22, at 562 (advocates of prohibiting parallel imports claim that “short-term advantages of cheaper prices are a mirage which, in the longer term, seriously prejudice incentives to make desirable investments locally in innovation”).

208. See Chard & Mellor, supra note 12, at 75-76 (“attempts to restrict parallel imports might result from a trademark owner’s desire to compete more effectively with rival brands by protecting the functions of his trademark and thereby better satisfying consumers. This is pro-competitive, efficiency-enhancing behavior.”); Barfield & Groombridge, supra note 12, at 925. Barfield and Groombridge write:

Producers can use vertical restraints to induce retailers or distributors to promote products unfamiliar to consumers, such as a new artist, author, or software program. These vertical restraints are useful for exactly the types of products that intellectual property rights are designed to protect, namely, new and innovative products. It was with this in mind that United States Supreme Court Justice Powell observed that:

‘Vertical restrictions promote inter-brand competition by allowing the manufacturer to achieve certain efficiencies in the distribution process.

Id. (citations omitted). See also Robert J. Staaf, The International Gray Market: The Nexus of Vertical Restraints, Price Discrimination and Foreign Law, 19 INTER-AMERICAN L. REV. 37, 58 (1987) (“The purpose of vertical restraints is to restrict intrabrand competition in order to maintain price margins, thereby creating incentives for retailers to invest in quality assurance or the provision of services.”).

For a contrary, “post-Chicago school” view, see Barfield & Groombridge, supra note 22, at 228-29 (providing a succinct description of the post-Chicago school view that vertical restraints may be anticompetitive, citing various authorities, and then arguing that this view is incorrect).
patent law.\textsuperscript{209}

Second, a number of Supreme Court decisions make it clear that free riding is not inherently undesirable, and may be highly beneficial to the public, as long as it does not undermine the incentive to offer the product or service that is the subject of the free riding.\textsuperscript{210} Thus, the existence of some free riding by parallel importers is not, in itself, a reason to prohibit parallel importing. For purposes of the doctrine of exhaustion in \textit{patent} law, the question is whether the effect of the free riding is so severe as to undermine the ability of the patent laws to provide an effective incentive to invent. But, once again, there is little empirical data to establish the extent or impact of parallel importer free riding on authorized distributor/licensees' marketing investments. It might be noted that there have been very few litigated patent infringement claims against parallel importers in the United States, which may suggest that United States patentees do not find parallel importing to be particularly problematic. Given the general disagreement about the legal permissibility of parallel importing under the patent laws,\textsuperscript{211} and the lack of a definitive ruling from either the Supreme Court or the Court of Appeals for the Federal Circuit, one might expect to have seen more litigation if it were.\textsuperscript{212}

\textsuperscript{209} Many of the commentators who have addressed this issue have done so in the context of “gray market” goods under trademark law. See, e.g., Staaf, \textit{supra} note 184; Hilke, \textit{supra} note 133. However, the United States has not adopted a territorial rule in the trademark context, see \textit{supra} note and accompanying text. This may have contributed to the tendency to raise the issue in debate concerning the doctrine of exhaustion in the copyright and patent arenas. See, e.g., Barfield & Groombridge, \textit{supra} note 22 (copyright); Bradley, \textit{supra} note 14 (patents); Chard & Mellor, \textit{supra} note 12 (discussing intellectual property rights generally); ROTHNIE, \textit{supra} note 22 (discussing trademark, copyright and patent law).

\textsuperscript{210} \textit{See supra} note 8.

\textsuperscript{211} \textit{See supra} notes and accompanying text.

\textsuperscript{212} In the trademark context, Hilke undertook to determine whether the available empirical data generally supported the claim that gray market imports were primarily the result of gray marketers' free riding on the promotional and service efforts of authorized distributors. He concluded that even though a theoretical case could be made that the opportunity to free ride on authorized distributors' marketing investments motivates gray marketing, the available evidence was “inconsistent with the strong form of [a] hypothesis that links all gray market activity to free-riding.” Thus, while there might be specific instances of free riding by gray marketers, a general

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Third, parallel imports may provide benefits that counteract the possible detriment caused by free riding on marketing investments. It appears that at least some parallel importing is spurred by price discrimination against United States consumers.\textsuperscript{213} Parallel imports can play an important role in neutralizing that discrimination,\textsuperscript{214} and undercuts any retailer or wholesaler collusion that may have precipitated it.\textsuperscript{215} Moreover, even in the absence of price discrimination, as such, parallel imports may provide beneficial price competition that may lead to lower prices for consumers and prompt patentees and their licensees to find ways to manufacture and distribute patented goods more efficiently. And, to the extent that parallel importers sell patented articles stripped of pre or after-sales services, they may provide consumers with valuable options.

Lacking information about the extent to which parallel imports result from price discrimination and collusion, the extent to which they result from free ban on gray market imports, particularly one imposed by the government, was “probably unjustified.” Hilke, \textit{supra} note 158, at 91.

Hilke published his findings in 1988. He noted that his primary source of data was a memorandum entitled “Economic Effects of Parallel Imports; A Preliminary Analysis,” compiled by the United States Patent and Trademark Office in 1985. This source summarized the results of a Customs Service survey conducted in 1984. \textit{See} Hilke, \textit{supra} note 158, at 76 n. 5. Hilke cautioned that the data was “fragmented and anecdotal” and made definitive conclusions impossible. \textit{Id.} at 83, 91. He also noted that “gray market distributors do not necessarily provide services inferior to those of authorized dealers.” “Several major retailing chains that participate in the gray market, such as K-Mart and Wards, provide their own substitute warranties and other services. Wholesalers and small retail establishments may have taken this step as well.” \textit{Id.} at 89. In his book on parallel imports, Dr. Rothnie questions some of Hilke’s conclusions. \textit{See} ROTHNIE, \textit{supra} note 22, at 568-71. \textit{See also} David Malueg & Marius Schwartz, 37 J. INTERNAT. ECON. 37, 167, 174 (1994).

\textsuperscript{213} \textit{See} Hilke, \textit{supra} note 158, at 90; ROTHNIE, \textit{supra} note 22, at 571; Malueg & Schwartz, \textit{supra} note 211, at 172-74.

\textsuperscript{214} \textit{See} Abbott, \textit{supra} note 13, at 622 (“Parallel imports will serve to assure that an adequate level of price competition is maintained in international markets. Price competition is essential to the effective operation of comparative advantage, and to achieving efficiency gains throughout the international trading system.”); Robert J. Staaf, \textit{The Law and Economics of the International Gray Market: Quality Assurance, Free-Riding, and Passing Off}, 4 INTELL. PROP. J. 191, 234 (1989) (“Parallel competition decreases United States prices. Any restriction on parallel imports will result in increased prices and thus a decrease in United States consumer welfare.”).

\textsuperscript{215} \textit{See generally} Hilke, \textit{supra} note 158, at 80-81; Chard & Mellor, \textit{supra} note 12, at 76, 78-79.
riding, and the effect of the free riding, it is difficult to determine which side of the argument is stronger.\textsuperscript{216} To the extent that there is simultaneously collusion and price discrimination and free riding sufficient to undermine incentive, then parallel imports are simultaneously detrimental and beneficial. Abuses are possible, both on the part of patentees, and on the part of parallel importers.

While the more thoughtful commentators have tended to acknowledge this, they have disagreed over how the burden of preventing abuses should be apportioned. Professors Chard and Mellor, conclude that “the overall balance of the effects of parallel trading is probably adverse,”\textsuperscript{217} and advocate territorial exhaustion, with the proviso that antitrust law should be used to deal:

[W]ith those relatively infrequent situations where the use of intellectual property rights to prevent parallel importation has detrimental economic effects. It can defer such abuses of intellectual property rights while allowing those rights to be used to prevent parallel importation in the majority of situations where this is likely to be economically beneficial to the country.\textsuperscript{218}

Dr. Rothnie concludes that “parallel imports may be desirable in some situations while not in others.”\textsuperscript{219} His resolution is to adopt a territorial principle, but to make “careful use of presumptions or rebuttable rules” under the antitrust law, to permit parallel importers in a given case to show that an intellectual property right owner is acting anti-competitively by using

\textsuperscript{216} Other possible causes of parallel imports--fluctuating currency exchange rates and patentee-condoned imports to discipline distributors--have not figured as prominently in the debate about the merits of parallel importing. Obviously, patentee-condoned imports to discipline distributor abuses may benefit consumers. Hilke views passing the benefit of fluctuating exchange rates to consumers as a positive effect of parallel imports, too, presumably because they force greater flexibility of response to consumer interests and promote greater distributional efficiency. See Hilke, \textit{supra} note 158, at 81-82, 86; \textit{ROTHNIE, supra} note 22, at 587 n.31. However, Rothnie voices reservations on this issue. He notes that “sound and effective business operation will not result in immediate pass through of currency exchange movements. Effective marketing may require strategic planning and commitment to orders many months in advance. Sound business practice will often warrant hedging against currency movements. In either case, price changes caused by currency movements will not be passed on to the consumer in the short term.” \textit{id.} at 587.

\textsuperscript{217} Chard & Mellor, \textit{supra} note 12, at 79.

\textsuperscript{218} \textit{id.} at 80.

\textsuperscript{219} \textit{ROTHNIE, supra} note 22, at 590.
infringement proceedings to block the parallel imports.\textsuperscript{220} Rothnie does not specify what the presumptions or rebuttable rules should be, suggesting that they should depend upon the “perceived characteristics of the national market,” for example, whether the market is generally perceived to be open and highly competitive or not. If the infringement plaintiff has significant market power in the relevant market, Rothnie suggests that the rebuttable presumption should be against allowing parallel imports to be blocked.\textsuperscript{221} Otherwise, presumably, the burden of proof that blocking the parallel imports is anticompetitive in a given case would be on the parallel importer.\textsuperscript{222}

The difficulties of identifying the relevant market, identifying how much market power exists and how much should be deemed excessive in any given case make antitrust litigation highly complex and expensive. Imposing the risk and cost of such litigation as the purchase price of liability-free parallel importation, even with the benefit of Dr. Rothnie’s presumptions, is likely to deter most prospective parallel importers; notwithstanding the possible merits of their position. Given the long existence of the present modified doctrine of international exhaustion in the United States, the lack of empirical evidence or

\textsuperscript{220} Id. at 594.
\textsuperscript{221} Id. at 596.
\textsuperscript{222} In Continental T.V. v. GTE Sylvania, Inc., 433 U.S. 36 (1977), the United States Supreme Court ruled that antitrust challenges to non-price vertical restraints, specifically geographic restrictions on sales, should be judged by a rule of reason analysis, requiring the challenger to demonstrate that the restraint in fact has the effect of reducing competition. \textit{Id.} The Court distinguished intrabrand competition (competition between competing sellers of the same manufacturer’s product) and interbrand competition (competition between competing sellers of different manufacturers’ products), and held that a court should balance reductions in one against improvements in the other in order to evaluate the net effect of the patentee’s restriction. \textit{Id.} While a geographic restriction on sales will reduce intrabrand competition, it may have the effect of strengthening interbrand competition, by encouraging distributors, wholesalers or retailers to invest in point-of-sale advertising and pre and post-sale services. Of course, if the patentee is demonstrated to have excessive market power, the negative effect of restricting intrabrand competition may outweigh any positive effect on interbrand competition. However, in the absence of excessive market power, the enhancement of interbrand competition may win the day. Presumably, in evaluating the net effect of a restraint, courts should take into account whether the product at issue is one that requires significant advertising and servicing, as this may vary significantly from one patented product to another. For a useful discussion of these issues and the existing case law in the field of trademark gray marketing, see Seth E. Lipner, \textit{The Legal and Economic Aspects of Gray Market Goods} 76-97 (1990).
litigation to suggest that this rule poses a significant threat to the effectiveness of patents, and the potential benefits arising from parallel imports, the current way in which the burdens are divided would seem to be more appropriate and efficient: apply a modified international exhaustion theory, placing the burden on patentees to protect their exclusive geographic territories and avoid potentially harmful parallel importer free riding by engaging in reasonable self-help measures,223 such as contractual restraints and label restrictions on the products themselves.224

3. Global Considerations

A final argument that has been raised in favor of adopting a territorial exhaustion rule focuses on the United State’s and other developed countries’ international obligations and overall world welfare. The argument is that a worldwide rule of territorial exhaustion is in the best interests of developing countries, because it will encourage technology transfer and the making available of innovative products at affordable prices within those countries.225

223. See supra note and accompanying text. It might be noted that to the extent that parallel importers free ride on marketing investments, much of that free riding can be avoided by use of different trademarks in different countries. See Hilke, supra note 158, at 78 for further discussion of self-help measures.

224. Dr. Rothnie may opt against this approach in part because of his apparent perception that contractual measures are not enforceable against third parties to the contract of first sale, as parallel importers frequently are. See Rothnie, supra note 13, at 331. However, this concern fails to take into account the United States case law suggesting that any third party who has notice of a patentee’s restriction on import or resale will be bound by it. See supra notes and accompanying text.

In his First Report (Final) to the Committee on International Trade Law of the International Law Association on the Subject of Parallel Importation, Professor Abbott acknowledges that vertical territorial allocation of markets may be beneficial, but finds that this benefit can be achieved by contract, without the necessity of laws generally prohibiting parallel imports. He notes that the availability of parallel imports plays an important role in ensuring that an adequate level of price competition is maintained in international markets. Abbott, supra note 13, at 622. See also Hilke, supra note 158, at 91 (finding insufficient evidence to support a prohibition of gray market goods).

225. An additional “international obligation” argument that has been raised asserts that Article 4 of the Paris Convention mandates a rule of territorial exhaustion. Article 4 provides, in relevant
In an article published in 1994, Malueg and Schwartz engaged in mathematical modeling to reach the conclusion that a rule of law that prohibits parallel importation will lead to greater global economic welfare than a rule that leaves parallel imports unrestricted. They reasoned that parallel imports undercut the ability of intellectual property owners to engage in price discrimination. If faced with the prospect of parallel importation, intellectual property owners will take steps to protect their higher prices in developed part:

1. Patents applied for in the various countries of the union by nationals of countries of the Union shall be independent of patents obtained for the same invention in other countries, whether members of the Union or not.

2. The foregoing provision is to be understood in an unrestricted sense, in particular, in the sense that patents applied for during the period of priority are independent, both as regards the grounds for nullity and forfeiture, and as regards their normal duration.


The general effect of [Article 4bis] is that the protection granted by a patent in one contracting country is not affected in any way whatsoever by the exercise of a parallel protection existing abroad. The consent given by the patentee to a licensee abroad to make and sell the subject matter of the foreign patent cannot legally be assumed or presumed to be also a consent with respect to his protection rights in another country.

Stephen P. Ladas, *Exclusive Territorial Licenses Under Parallel Patents*, 3 *Internat. Rev. Indus. Prop. & Copyright* L. 335, 346 (1972). See also Strauss, *supra* note 136, at 194. This argument has been generally discredited, most recently by the Japanese Supreme Court. See BBS Kraftfahrzeugtechnik AG v. Rashimekkusu Japan Co., Ltd. & JAP Auto Prod. Co. Ltd., *supra* note 23, at 332-33. Article 4 is meant to prevent Paris Convention members from making the grant, validity or duration of a patent dependent upon the grant, validity or duration of a patent for the same invention in another country, such as the applicant's home country. It does not generally prohibit member nations from finding, as a matter of domestic law, that acts occurring abroad influence domestic patent rights. For example, it is common for nations to find that publication or grant of a patent abroad undermines the novelty or non-obviousness (inventive step) of an invention that is the subject of a domestic patent or patent application. See, e.g., 2 J.W. Baxter, *World Patent Law & Practice*, Cl. 4 (1999). Likewise, member nations are free to determine that a patentee's sale abroad exhausts its right in a particular patented article. See Christopher Heath, *Parallel Imports and International Trade*, 28 *Internat. Rev. Indus. Prop. & Copyright* L. 623, 627-28 (1997).

countries--by either raising prices in developing countries to make parallel importing unprofitable, or ceasing to supply developing countries altogether. Thus, they concluded, while a rule that allows patentees to enforce a system of price discrimination may be detrimental to consumers in developed countries, where prices are higher, it is ultimately beneficial to developing countries, leading to a net overall increase in world welfare.

Others have stressed, in a similar vein, that a rule permitting parallel imports will lead not only to a reduction in exports of patented goods to developing countries, but also to a general reduction in technology transfer to developing countries, as patentees decline to engage in manufacturing operations, or to license manufacturing operations in those countries for fear that the manufactured goods will find their way back to developed countries as parallel imports.

In his First Report (Final) to the Committee on International Trade Law of the International Law Association On the Subject of Parallel Importation, Professor Abbott notes the limited nature of the Malueg and Schwartz inquiry, and argues that its findings are inadequate to support a rule to restrict parallel imports. First, “Malueg and Schwartz do not consider the impact of an international price discrimination system on developing country producers and consumers acting outside the field of the monopolist’s product.” More importantly, “they do not consider the broader effects of an international price discrimination system on the international allocation of resources.” Professor Abbott reasons that the absence of price competition from parallel imports will lead to inefficient allocation of resources in developed countries. In developing countries, the lower prices imposed on licensed manufacturers will limit profitability and thus future capital investment in industrial development, resulting in developing countries continuing to rely on exports from developed countries.

227. See Malueg & Schwartz, supra note 22, at 190-93.
231. Id. at 620.
232. Id.
233. Id. at 621.
developing country markets were to prove true in a world of parallel imports, developing countries might justifiably resort to compulsory licensing to supply their citizens with needed patented products.234

With regard to the argument that parallel imports will lead to a refusal to transfer technology to developing country manufacturers, it is useful to consider that a patentee’s licensing and plant building decisions are likely to turn on more than just the potential for parallel imports. For example, lower production costs, availability of raw materials, proximity to intended markets, and other economic and political factors may carry considerable weight in a multinational patentee’s decision to license production in a developing country or set up a manufacturing subsidiary there.235 Moreover, in many cases, contractual restrictions may suffice to alleviate the concerns of patentees, leading them to move forward with exportation and technology transfer, even in the absence of a worldwide rule of territorial exhaustion.

It is interesting to note that the governments of many developing countries have taken a strong stand in favor of international exhaustion, suggesting that they themselves do not subscribe to the Malueg & Schwartz reasoning.236 Their view is that their own local markets may benefit from the lower prices of parallel imports.237 Moreover, they have expressed concern that a rule of territorial exhaustion will be used as a non-tariff barrier to exclude lower-priced, patented goods lawfully produced in developing countries from developed country markets, impeding the ability of their developing world industries to compete in

234. Abbott, supra note 13, at 621. It bears noting that we do not presently see much evidence of the results that the Malueg & Schwartz study predict, even though the world lacks a uniform territorial exhaustion rule to prevent parallel imports. As noted earlier, the United States has not adhered to a rule of territorial exhaustion, and Japan has recently adopted a rule of modified international exhaustion that is very similar to that of the United States. See supra note 178. A number of developing countries have adopted an international exhaustion rule. See infra note 236.


236. See Abbott, supra note 13, at 620; Verma, supra note 13, at 562; Chard & Mellor, supra note 12, at 69; Ans M. Pacon, What Will TRIPs Do for Developing Countries?, in FROM GATT TO TRIPs—THE AGREEMENT ON TRADE-RELATED ASPECTS OF INTELLECTUAL PROPERTY RIGHTS, 329, 337 (Friedrich-Karl Beier & Gerhard Schricker, eds., 1996); Watal, supra note 136, at 18.

237. See Marco C.E.I. Bronckers, The Impact of TRIPs: Intellectual Property Protection in Developing Countries, 31 COMMON MKT. L. REV. 1245, 1266 (1994); Pacon, supra note 236, at 337. Both of these authors express doubt that parallel imports will provide the desired lower prices.
the world marketplace.238

Thus, again, the case for a move to a territorial exhaustion rule lacks convincing force. An additional, and very important, consideration weighing against adoption of a territorial exhaustion rule is that such a rule would erect significant barriers to the free movement of goods across international borders, contrary to the spirit of the General Agreement on Tariffs and Trade and the World Trade Organization.239 The trend would seem very much in the direction of reducing, rather than increasing, such barriers.240

238. See Abbott, supra note 13, at 620; Chard & Mellor, supra note 12, at 69. See also Yusuf & von Hase, supra note 3, at 130.
239. See Abbott, supra note 13, at 611-12:

The rules of the World Trade Organization (WTO) proceed from one very basic idea: that the elimination of barriers to the movement of goods and services across and within national boundaries is beneficial to global economic welfare because this encourages specialization and efficiency in production and distribution, and results in an increased output of goods and services. . . . Flowing from this basic idea is an extraordinarily complex set of formal and informal rules designed to reduce and eliminate tariff and nontariff barriers to trade in goods and services.

Id.

In his First Report (Final) to the Committee on International Trade Law of the International Law Association on the Subject of Parallel Importation, Professor Abbott provides a useful discussion of how a rule of territorial exhaustion could conflict with the specific provisions of the WTO and TRIPs Agreement, and addresses arguments that have been made to the contrary. See id. at 632-35. See also Abbott, Second Report (Preliminary), supra note 22, at 12-18. For arguments to the contrary, see Barfield & Groombridge, supra note 22, at 91-93.

See also Verma, supra note 13, at 552-58 (describing the purposes of GATT and TRIPs and explaining how a rule of territorial exhaustion would conflict with various provisions of these Agreements); Yusuf & von Hase, supra note 3, at 116 (article argues "that a territorial regime of exhaustion is no longer justifiable in view of the increasing globalization of the world economy, the efforts for greater liberalization of international trade, and the drive towards the establishment of internationally uniform standards of intellectual property protection and their incorporation into a GATT-based international trading system"); Bronckers, supra note 237, at 1268 (arguing that the GATT "does not lend itself to a limitation of the "worldwide exhaustion" principle."). For arguments to the contrary, see Stack, supra note 22, at 685.
240. See, e.g., Herman C. Jehoram, Prohibition of Parallel Imports Through Intellectual Property Rights, 30 INTERNAT. REV. INDUS. PROP. & COPYRIGHT 495, 508-11 (1999) (reviewing a number of recent developments which, taken together, suggest general world movement toward a rule of
VI. CONCLUSION

Notwithstanding assumptions and arguments to the contrary in some of the literature, a close examination of United States case precedent demonstrates that this country has tended to apply the doctrine of exhaustion to patentees’ sales both inside and outside of the country, though in both cases it permits patentees to contract to avoid the effects of the doctrine. Absent a ruling to the contrary, from either the Supreme Court or the Court of Appeals for the Federal Circuit, this rule, which authorizes parallel importing in the absence of enforceable contractual restrictions, should be deemed the prevailing rule in the United States. The legislative history of the Uruguay Round Agreements Act suggests that Congress intended to maintain the status quo with regard to parallel imports, so that the Act’s provision of an express importation right for patentees did not alter the general legality of parallel importing.

The policy arguments that have been made in support of a contrary rule are theoretically unsound in some instances. Moreover, claims that parallel imports interfere with the effectiveness of patents to provide an incentive to invent, and undercut competition tends to be highly speculative, unsupported by empirical evidence. They do not convincingly overcome countervailing arguments suggesting that parallel imports may have beneficial effects for the public. While it is impossible at this point to measure the overall impact of parallel imports on public welfare, the case to change the existing rule to prohibit parallel imports has not been made. Given that patentees have a number of self-help measures available to them to avoid or mitigate any detrimental effects that might arise from parallel imports, and given the general world trend in the direction of free movement of goods in international trade, there seems little justification to change the United States’ doctrine of exhaustion to prohibit parallel imports of patented goods.

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international exhaustion and predicting that, “in the long run international exhaustion will prevail for all intellectual property rights”).