UNITED STATES UPDATE

Increased U.S. Barriers for Grey Market Goods: Customs Hears the Supreme Court

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1. INTRODUCTION

A recent revision in a U.S. Customs Service ("Customs") regulation has expanded protection against parallel imports, also known as grey market goods, by closing U.S. doors to merchandise produced abroad by authorized foreign users and licensees. The U.S. Supreme Court ruled in 1988 that a Customs regulation provision, which had permitted importation of merchandise manufactured abroad and with the trade-mark applied under authorization of the U.S. trade-mark holder, was invalid under one of the two primary statutes that govern grey market importation. In response to that ruling, Customs has now completely eliminated the statute-offending provision. The result is that Customs will now seize goods that have been manufactured abroad by authorized licensees and users but that are imported into the United States without the authorization of the U.S. trade-mark holder. However, imports of goods where the foreign and domestic manufacturer are one and the same, i.e., subject to the same ownership and control, will not be prevented from entering the United States, as such goods continue to be considered genuine goods manufactured abroad.

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2. GREY MARKET GOODS DEFINED

A grey market good is a good manufactured abroad for which a valid U.S. trade-mark has been issued, but is imported into the United States without the consent of the holder of the U.S. trade-mark. As outlined in *K Mart Corp. v. Cartier, Inc.*,[1] there are three basic contexts in which the grey market arises. In a scenario that the Supreme Court called Case One, a U.S. corporation purchases from an independent foreign firm the rights to register and use that foreign firm's trade-mark in the United States and to sell that foreign firm's goods in the United States. However, the foreign firm independently, exports the trade-marked goods to the United States, or sells the goods abroad to a third party who then exports them to the United States. In a so-called Case Two scenario, foreign manufactured goods are registered in the United States by an affiliated domestic firm. However, goods from abroad bearing identical, but foreign, trade-marks are imported into the United States by the foreign affiliate or third party. In a Case Three scenario, goods imported to the United States are manufactured abroad by an independent foreign firm who has received authorization from the domestic holder of a U.S. trademark to use the trade-mark, somewhere other than in the United States.[2]

3. STATUTORY AND REGULATORY BACKGROUND

The importation of grey market goods is principally governed by two statutory provisions: section 526 of the *Tariff Act* of 1930[3] and section 42 of the *Lanham Act* of 1946.[4]

Under section 526(a) of the *Tariff Act*, it is "unlawful to import into the United States any merchandise of foreign manufacture if such merchandise . . . bears a trade-mark owned by a citizen of, or by a corporation or association created or organized

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[1] 486 U.S. 281 (1988).

[2] *See generally* id. at 286-87.

[3] 19 U.S.C. § 1526 (1982).

[4] 15 U.S.C. § 1124 (1982).

In 1988, however, in *K Mart Corp.*, the Supreme Court invalidated 19 C.F.R. § 133.21(c)(3), the portion of the regulation that permitted importation of goods trademarked under authorization of the U.S. trade-mark owner (a Case Three situation).[13] The Court found that the provision conflicted with the plain language of section 526 of the *Tariff Act* because "[u]nder no reasonable construction of the statutory language can goods made in a foreign country by an independent foreign manufacturer be removed from the purview of the statute."[14] The Court did not consider whether the regulation conflicted with section 42 of the *Lanham Act*.

As for Case Two, the Court upheld the portions of the regulations that permit grey market imports from related companies.[15] Allowing entry of goods made in a foreign country by the "same person" who holds a U.S. trade-mark,[16] or by someone "subject to common . . . control"[17] with the U.S. holder was said to be "consistent" with section 526 of the *Tariff Act*.[18] The Court found that the regulation, as an interpretation of the *Tariff Act*, was reasonable in light of the possibly differing interpretations of the phrases "owned by" and "merchandise of foreign manufacture" in section 526. In the Court's view, difficulties in establishing whether a subsidiary or a parent "owns" a trademark, and whether "foreign manufacture" means manufactured by a foreign company or manufactured in a foreign country, indicate great ambiguity.[19] The Court held that since the language of the statute was imprecise, the provision of the agency's regulation excepting related company parallel importation from the

[13] The invalidated provision had stated that the restriction on grey market goods does not apply when "articles of foreign manufacture bear a recorded trademark or trade name applied under authorization of the U.S. owner." 19 C.F.R. § 133.21(c)(3) (1990).

[14] 486 U.S. at 294.

[15] Id. at 294.

[16] 19 C.F.R. § 133.21(c)(1).

[17] 19 C.F.R. § 133.21(c)(2).

[18] 486 U.S. at 294.

[19] Id. at 292.

within, the United States," provided that the trade-mark is properly registered, "unless written consent of the owner of such trade-mark is produced at the time of making entry."[5] Such unlawfully imported merchandise is subject to seizure and forfeiture.[6] A person dealing in such illegally imported goods can be enjoined from doing so and may be required to export or destroy the goods or remove the trade-mark from them.[7] Such a dealer can be liable for the "same damages and profits provided for wrongful use of a trade-mark."[8] Section 42 of the *Lanham Act* forbids, *inter alia*, the importation of any article of merchandise that "cop[ies] or simulate[s] a trade-mark registered [in the United States]" or that is "calculated to induce the public to believe that the article is manufactured in the United States . . ."[9] Customs generally considers the two statutes to be complementary and its regulations implement section 526 of the *Tariff Act* and section 42 of the *Lanham Act* in tandem.

In the past, Customs has narrowly construed section 526 of the *Tariff Act* and section 42 of the *Lanham Act* and has not prohibited the importation of all types of grey market goods. The pertinent Customs regulation authorized seizure and forfeiture only of foreign-made articles bearing a trade-mark identical to one owned and recorded by a U.S. company.[10] Seizure and forfeiture were not authorized where the foreign and the U.S. trade-mark companies were related (the common control, or related company, exception)[11] and, until recently, where the trade-mark had been applied by the foreign company by permission of the U.S. trade-mark owner.[12] The upshot was that, under Customs regulations, grey market goods were for many years excluded from the U.S. market only in a Case One context.

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[5] 19 U.S.C. § 1526(a).

[6] 19 U.S.C. § 1526(b).

[7] 19 U.S.C. § 1526(c).

[8] Id.

[9] 15 U.S.C. § 1124.

[10] 19 C.F.R. § 133.21(b) (1990).

[11] 19 C.F.R. § 133.21(c)(1) & (2).

[12] 19 C.F.R. § 133.21(c)(3).

Act's purview was a permissible construction, designed to resolve ambiguity.[20] Again, no mention was made of the *Lanham Act*.

The Court in *K Mart Corp.* also declared Customs' prevention of Case One imports proper under the *Tariff Act*. The Court noted that "[a]ll Members of the Court are in agreement that [Customs] may interpret the statute to bar importation of grey market goods in what we have denoted case 1."[21] Challenges to the Customs regulation provision that excludes goods imported by an independent foreign firm, or third party, where a U.S. firm has purchased the trade-mark and exclusive rights of distributorship from the foreign firm are practically non-existent. In a Case One scenario, the interests of the American trade-mark holder are most clearly threatened, and it is unlikely that Customs could be prevented from barring such imports.

4. CUSTOMS REGULATION REVISION

Responding to the *K Mart Corp.* ruling on goods manufactured by a foreign firm with trade-mark authorization by the U.S. trade-mark owner, Customs, which since the decision apparently had continued to allow the importation of such goods, has now revised its regulations by eliminating 19 C.F.R. § 133.21(c)(3), the offending provision. The result is that goods in Case Three situations are now prohibited from entering the United States. According to Customs, completely eliminating subsection (c)(3), in light of silence by the Supreme Court on whether subsection (c)(3) was valid under the *Lanham Act*, should "resolve any ambiguity" resulting from the Supreme Court's invalidation of the procedure under only the *Tariff Act* and "maintain [Customs'] long-standing practice of interpreting both statutory provisions in tandem."[22]

Customs, of course, continues to bar Case One imports and permit Case Two grey market goods under the related company

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[20] Id. at 292-93.

[21] Id. at 292.

[22] 8 I.T.R. 9, Jan. 2, 1991.

exception. However, the Court's holding permitting a related company exception to the ban of parallel import without reference to the *Lanham Act* leaves the legal picture somewhat unclear. For example, the District of Columbia Court of Appeals recently held, but only tentatively, that the related company exception conflicts with section 42 of the *Lanham Act* when the product manufactured abroad, although under genuine trademark, has different physical characteristics than the U.S. product.[23] The D.C. court emphasized that trade-mark law is meant to, *inter alia*, prevent consumer confusion.[24] The case was remanded to the lower court for a full briefing by the parties of whether the related company exception does indeed violate section 42.[25]

5. CONCLUSION

The imperfect and confusing prohibitions on parallel imports may eventually be clarified, perhaps even in a drastic manner. In 1989, the Senate and the House of Representatives introduced two nearly identical bills[26] that would have amended the *Lanham Act* by adding a new section to prohibit importation of grey market goods in all three of the Cases described in *K Mart Corp*. The proposed prohibition would have applied to all goods manufactured outside the United States that bear the same trademark as one held by a U.S. trade-mark holder. However, during that Congress, no action was taken on those bills. Although a similar bill was introduced in the Senate this year,[27] its prospects for passage seem slim.

With its recent regulation revision, Customs has expanded the list of grey market merchandise that may not be imported into the United States. However, until Congress legislates further, or

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[23] *Lever Bros. Co. v. United States*, 877 F.2d 101 (D.C. Cir. 1989).

[24] Id. at 111.

[25] Id.

[26] S. 626, 101st Cong., 1st Sess. (1989); H.R. 3484, 101st Cong., 1st Sess. (1989).

[27] S. 894, 102d Cong., 1st Sess. (1991).

the courts strike more Customs regulation provisions that permit grey market imports, a few types of grey market goods will still be able to gain entry into the increasingly protected U.S. markets.