Article 6 Exhaustion

For the purposes of dispute settlement under this Agreement, subject to the provisions of Articles 3 and 4 nothing in this Agreement shall be used to address the issue of the exhaustion of intellectual property rights.

Paragraph 5 of the Doha Declaration on the TRIPS Agreement and Public Health

5. Accordingly and in the light of paragraph 4 above, while maintaining our commitments in the TRIPS Agreement, we recognize that these flexibilities include:

[...]

(d) The effect of the provisions in the TRIPS Agreement that are relevant to the exhaustion of intellectual property rights is to leave each Member free to establish its own regime for such exhaustion without challenge, subject to the MFN and national treatment provisions of Articles 3 and 4.

1. Introduction: terminology, definition and scope

Article 6 addresses the exhaustion of intellectual property rights. The concept of exhaustion plays an enormously important role in determining the way that intellectual property rules affect the movement of goods and services in international trade.

An intellectual property right, such as patent, trademark or copyright, is typically defined in terms of rights granted to the holder to prevent others from making use of it. For example, a patent grants to an inventor the right to prevent others from making, using, selling, offering for sale, or importing the invention without his or her consent. The trademark grants to its holder the right to prevent others from using a protected sign on identical or similar goods where such use is likely to cause consumer confusion. The copyright grants to its holder the right to prevent others from reproducing or distributing the work.

The doctrine of exhaustion addresses the point at which the IPR holder's control over the good or service ceases. This termination of control is critical to the functioning of any market economy because it permits the free transfer of goods and services. Without an exhaustion doctrine, the original IPR holder would perpetually exercise control over the sale, transfer or use of a good or service embodying an IPR, and would control economic life.

An IPR is typically exhausted by the "first sale" (U.S. doctrine) or "placing on the market" of the good or service embodying it. The basic idea is that once the right holder has been able to obtain an economic return from the first sale or placing on the market, the purchaser or transferee of the good or service is entitled to use and dispose of it without further restriction.

As illustration, consider a can of soda labelled with the famous "Coca-Cola" trademark. Because the Coca-Cola Company holds rights to that mark, it may prevent others from first-selling the can of soda without its consent. If you buy the can of soda from an authorized first-seller, the Coca-Cola Company's right in its trademark is exhausted, and it cannot prevent you from drinking the soda, or from giving or selling the can of soda to someone else. The trademark holder has lost its right to control further disposition of the product. Your purchase of the can of Coca-Cola does not authorize you to begin making your own cans of Coca-Cola, or licensing the mark to others. In other words, the first sale does not grant you rights in the trademark, but rather it extinguishes the Coca Cola Company's entitlement to control movement of that particular can of soda.

From the standpoint of the international trading system, the focus of the exhaustion question is whether it operates on a national, regional or international basis. IPRs are typically granted by national authorities. With the grant of an IPR, the patent, trademark or copyright holder obtains a "bundle of rights" that it may exercise within the territory of the granting authority. When a good or service is first sold or marketed in a country, this exhausts the IPR embodied in it.²⁰¹ Yet the same IPR holder may hold equivalent or "parallel" rights in many countries. The Coca-Cola Company, again for illustrative purposes, may hold trademark registrations for the Coca-Cola mark in every country of the world.

A country may choose to recognize that exhaustion of an IPR occurs when a good or service is first sold or marketed outside its own borders. That is, the first sale or marketing under a "parallel" patent, trademark or copyright abroad exhausts the IPR holder's rights within that country. If exhaustion occurs when a good or service is first sold or marketed outside a country, the IPR holder within the country may not oppose importation on the basis of its IPR. The importation of a good or service as to which exhaustion of an IPR has occurred abroad is commonly referred to as "parallel importation", and the goods and services subject to such trade are commonly referred to as "parallel imports". Since goods and services

²⁰¹ The manner in which IPRs are affected by exhaustion doctrine may vary depending on the characteristics of the form of protection. For example, while the first sale of a book will exhaust the copyright holder's right to control distribution of the book, the first showing of a film may not exhaust the right to control further showing of the film. For a discussion of the rental right in cinematographic works under Article 11, TRIPS, see Chapter 10.

subject to exhaustion of IPRs are exported as well as imported, the subject matter of trade in such goods is commonly referred to as "parallel trade".

If a country recognizes a doctrine of "national" exhaustion, an IPR holder's right to control movement of a good or service is only extinguished by the first sale or marketing of a good or service within the territory of that country. If a country recognizes a doctrine of "regional" exhaustion, an IPR holder's right to control movement is extinguished when a good or service is first sold or marketed in any country of the region. If a country recognizes a doctrine of "international exhaustion", an IPR holder's right to control movement is extinguished when a good or service is first sold or marketed anywhere in the world.

The flow of goods and services across borders is significantly affected by the exhaustion doctrine that WTO Members choose to adopt. Under a doctrine of international exhaustion, goods and services flow freely across borders after they have been first sold or placed on the market under certain conditions anywhere in the world. Under a doctrine of national exhaustion, the movement of goods and services may be blocked by IPR holders. Under national exhaustion, IPR holders have the power to segregate markets.

There is considerable debate concerning whether granting IPR holders the power to segregate markets is good or bad from various perspectives – economic, social, political and cultural. From the standpoint of those favouring open markets and competition, it may appear fundamentally inconsistent to permit intellectual property to serve as a mechanism to inhibit trade. Yet IPR holders argue that there are positive dimensions to market segregation, and corollary price discrimination.

During the GATT TRIPS negotiations, there was fairly extensive discussion of the exhaustion issue, but governments did not come close to agreeing upon a single set of exhaustion rules for the new WTO. They instead agreed that each WTO Member would be entitled to adopt its own exhaustion policy and rules. This agreement was embodied in Article 6, precluding anything in that agreement from being used to address the exhaustion of rights in dispute settlement, subject to the TRIPS provisions on national and MFN treatment.

2. History of the provision

2.1 Situation pre-TRIPS

Prior to negotiation of the TRIPS Agreement governments maintained different policies and rules on the subject of exhaustion of intellectual property rights in so far as those policies and rules affected international trade.²⁰² The situation in Europe and in the United States was rather complicated, as countries not only

²⁰² The first clear articulation of the concept of exhaustion of IPRs is sometimes traced to an 1873 U.S. Supreme Court decision, *Adams v. Burke* U.S. (17 Wall) 453 (1873). This case involved an attempt by the holder of a patent on a funeral casket lid to impose territorial restrictions on a purchaser's resale of caskets incorporating that lid. The Supreme Court held that the patent holder's control over the invention was exhausted on the first sale. It said:

[&]quot;in the essential nature of things, when 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, in the language of the court, 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

followed different approaches to the questions of national, regional and international exhaustion, but often differentiated their policies and rules depending upon the type of IPR affected.

In the United States, for example, the Supreme Court had addressed the issue of exhaustion in the field of trademarks, and interpreted domestic law to establish a "common control" doctrine. ²⁰³ If a product protected by a U.S. trademark was first sold abroad by a company owned or under common control with a company in the United States, the U.S. trademark could not be invoked to prevent parallel imports. However, if the product was first sold abroad by an independent company, or a licensee of the U.S. trademark holder, parallel imports could be blocked.

The Supreme Court had never expressly addressed the question of parallel importation in the field of patents.²⁰⁴ Several important Court of Appeals decisions held in favour of international exhaustion of patent rights.²⁰⁵ There was some contrary opinion at the district court level.²⁰⁶ In the field of copyright, there was little in the way of judicial decision regarding national and international exhaustion prior to TRIPS, although this subject matter has been addressed with some frequency following its negotiation.

The European Court of Justice (ECJ) pioneered the exhaustion question in so far as it affected the movement of goods across borders. In 1964, shortly following the formation of the European Community, the ECJ was confronted in *Consten and Grundig* with an attempt by a manufacturer of audio equipment to prevent trade in its products among the member states by invoking parallel trademark rights.²⁰⁷ The ECJ immediately recognized that the goal of European market integration would be inhibited if trademark holders could block the free movement of goods, and at that early stage invoked competition law principles to preclude such action. Subsequently, the ECJ framed its jurisprudence on this subject, fashioning an "intra-Community exhaustion doctrine", on the basis of the prohibition in the EC Treaty against quantitative restrictions and measures with equivalent effects (Article 28, EC Treaty, 1999 numbering).²⁰⁸

or instrument, it is open to the use of the purchaser without further restriction on account of the monopoly of the patentees." (453 U.S., at 456)[footnote omitted]

²⁰³ Kmart v. Cartier, 486 U.S. 281 (1988).

²⁰⁴ A case sometimes cited to the effect that the U.S. prohibited parallel importation in patented goods is *Boesch v. Graff* 133 U.S. 697 (1890). That case, however, involved goods first sold outside the United States under a "prior user's" exception to patent rights, and without the consent of the patent holder. (According to the prior user exception, a third person using the invention in good faith prior to the filing of the patent may continue the use of the invention in spite of the granting of the patent.) The potential implications of this decision are analyzed below.

²⁰⁵ See most notably Curtiss Aeroplane & Motor Corp. v. United Aircraft Engineering Corp., 266 F. 71 (2d Cir. 1920) and further cases discussed in Margreth Barrett, The United States' Doctrine of Exhaustion: Parallel Imports of Patented Goods, 27 N. Ky. L. Rev. 911 (2000).

²⁰⁶ See, e.g., *Griffin v. Keystone Mushroom Farm, Inc.*, 453 F. Supp. 1283 (E.D. Pa. 1978).

²⁰⁷ Consten and Grundig v. Commission, Cases 56, 58/64, [1966] ECR 299.

²⁰⁸ The entire early history of ECJ jurisprudence on the subject of exhaustion is framed in terms of the tension between Article 30, EC Treaty (prohibiting quantitative restrictions and measures with equivalent effect) and Article 36, EC Treaty (allowing measures to protect IPRs). The EC Treaty was renumbered in 1999, so that former Article 30 is now Article 28, and former Article 36 is now Article 30. This makes for considerable confusion when discussing ECJ jurisprudence in this field.

Exhaustion of rights

Prior to the TRIPS Agreement negotiations all EC member states were subject to the "intra-Community" exhaustion rule in all fields of IPR protection. ²⁰⁹There was an extensive body of case law in which the ECJ had refined this rule in particular contexts. For example, the Court recognized that the showing or broadcast of films presented special circumstances that required certain limitations on the general "placing on the market" rule. ²¹⁰ In the field of trademarks, the Court allowed parallel traders flexibility in repackaging and labelling pharmaceuticals so long as this did not present a threat to consumer safety. ²¹¹ The ECJ further indicated in the context of a decision on rental rights that a certain level of approximation of IPR laws among the member states was necessary to protect the interests of rights holders. ²¹² EC member states were thus subject to a uniform rule of "intra-Community" or "regional" exhaustion across all fields of IP (or at least those with a sufficient level of approximation).

Though not free from doubt, the EC rule on patents appeared to contemplate that only goods placed on the market in a member state would be subject to the rule of exhaustion.²¹³ Thus, while the placing of a patented good on the market within the territory of the Community exhausted the patent holder's rights and allowed free movement within the Community, the placing of a patented good on the market outside the Community did not affect the patent holder's rights within the Community, and parallel importation could be blocked. EC member states maintained different approaches to international exhaustion in the field of trademarks, and until the adoption of the First Trade Marks Directive in 1988 the ECJ had not sought to impose a uniform approach. EC member states differed on the question whether the Directive mandated a uniform approach to the international exhaustion question.²¹⁴ Prior to the TRIPS Agreement negotiations, member states also maintained different approaches to the international exhaustion question in the field of copyright.²¹⁵ At the outset of the TRIPS negotiations in 1986, the EC did not approach the exhaustion question with a "single voice".

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²⁰⁹ Regarding patents, the leading case was *Centrafarm v. Sterling Drug*, Case 15/74, 1974 ECR 1147.

²¹⁰ See *Coditel SA v. Cine-Vog Films*, Case 62/79, [1980] ECR 881, [1981] CMLR 362, decision of Mar. 18, 1980 (Coditel I); see also *Coditel SA v. Cine-Vog Films*, Case 262/81, [1982] ECR 3381, [1983] 1 CMLR 49, decision of Oct. 6, 1982 (Coditel II) [regarding the potential applicability of former Article 85 EC Treaty on anti-competitive inter-firm agreements to the same facts].

²¹¹ See Pharmacia & Upjohn SA v. Paranova A/S, Case C-379/97, 12 Oct. 1999.

²¹² See Warner Brothers v. Christiansen, Case 158/86, [1988] ECR 2605, [1990] 3 CMLR 684.

 $^{^{213}}$ See, e.g., $Merck\ v.\ Stephar$, Case 187/80, [1981] ECR 2063, [1981] 3 CMLR 463 and $Polydor\ v.\ Harlequin\ Record\ Shops$, Case 270/80, [1982] ECR 329, [1982] 1 CMLR 677, Feb. 9, 1982 [broadly referring to industrial property rights]; cf. W.R. Cornish, Intellectual Property, 4^{th} ed. 1999, at 6-15/6-16 [hereinafter Cornish].

²¹⁴ First Council Directive of 21 December 1988 to approximate the laws of the Member States relating to trade marks (89/104/EEC), OJ L 040, 11/02/1989 P.0001-0007. These differences were not settled until the ECJ's decision in *Silhouette v. Hartlauer* in 1998, in which it imposed a mandatory "intra-Community exhaustion" rule in trademarks, to the exclusion of international exhaustion. See discussion below, Section 6.3.

²¹⁵ Cf. Cornish, at 1-59.

Other countries and regions had also considered the question of national or international exhaustion. Japan²¹⁶ and Switzerland²¹⁷ each had substantial jurisprudence on the subject. The countries of Latin America appeared largely to favour international exhaustion. Decision 85 on Industrial Property of the Andean Commission excluded the right to prevent importation from patent holders, effective to the countries of the Andean Commission excluded the right to prevent importation from patent holders, effective to the countries of the countries

tively providing for international exhaustion.²¹⁸ Decision 85 established an express rule of regional exhaustion in respect of trademarks.²¹⁹ South Africa maintained a rule of international exhaustion in the fields of patent²²⁰ and trademark.²²¹

Prior to the TRIPS negotiations there had been little in the way of systematic investigation of the potential impact of various exhaustion regimes on international trade and/or economic development. The European Court of Justice had identified that enforcement of national IPRs rules might play an important role in European efforts to integrate markets.

2.2 Negotiating history

2.2.1 Initial proposals

The subject of exhaustion of rights and parallel importation was discussed in the TRIPS Negotiating Group (TNG) on a substantial number of occasions during the Uruguay Round. It is evident from those discussions that delegations perceived the subject matter of importance, and had different views regarding the appropriate outcome. It is important to note that contemporaneous discussions on this subject matter were taking place at WIPO in the context of patent law harmonization negotiations throughout much of the TRIPS negotiations. In neither forum

²¹⁶ Report of Mitsuo Matsushita to Committee on International Trade Law of the International Law Association, noted in Abbott, First Report, 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. Int'l Econ. L. 607 (1998).

²¹⁷ See Thomas Cottier and Marc Stucki, *Parallelimporte im Patent-, Urheber- und Muster-und Modellrecht aus europarechtlicher und völkerrechtlicher Sicht*, in B. Dutoit (edit.), Conflits entre importations parallèles et propriété intellectuelle?, Librairie Droz, Geneva 1996, p. 29 et seq.

²¹⁸ Article 28, Decision 85, provided:

[&]quot;Article 28. With the limitations stipulated in the present Regulation, the patent shall confer on its owner the right to exploit the invention itself in an exclusive manner, to grant one or more licenses for its exploitation, and to receive royalties or compensation deriving from its exploitation by third persons.

The patent shall not confer an exclusive right to import the patented product or one manufactured under his patented process." [13 Int'l Legal Matl's 1478, 1492 (1974)]

See Frederick M. Abbott, Bargaining Power and Strategy in the Foreign Investment Process; A Current Andean Code Analysis, 3 Syr, J, INT'L L & COMM. 320, 346–51 (1975).

²¹⁹ Article 75, Decision 85, provided:

[&]quot;Article 75. The owner of a trademark may not object to the importation or entry of merchandise or products originating in another Member Nation, which carry the same trademark. The competent national authorities shall require that the imported goods be clearly and adequately distinguished with an indication of the Member Nation where they were produced." [13 Int'l L. Matl's 1478, (1974)].

[[]It is not clear whether this rule was intended to exclude international exhaustion in the field of trademarks.]

²²⁰ See Stauffer Chemical Company v. Agricura Limited 1979 BP 168.

²²¹ See Trade Marks Act 1993, Article 34(2)(d).

did governments come close to agreeing on uniform treatment of the exhaustion question.

The initial 1987 U.S. proposal for a TRIPS Agreement did not reference the subject of exhaustion.²²²

A compilation of written and oral submissions regarding trade in counterfeit goods circulated by the GATT Secretariat in April 1988 noted concerns regarding parallel imports. It said:

"27. The question has been raised as to what would be the substantive intellectual property norms by reference to which counterfeit goods should be defined. In this regard the following points have been made:

. . .

– parallel imports are not counterfeit goods and a multilateral framework should not oblige parties to provide means of action against such goods."²²³

This compilation noted similar observations concerning the need to preserve rights of parallel importation in connection with border measures and safeguards to protect legitimate trade.²²⁴

The first EC proposal on substantive standards of July 1988 acknowledged the subject matter of exhaustion in regard to trademarks, though not specifically in the import context.²²⁵

Through the course of negotiations in 1989, a number of comments were directed at assuring that any rules developed in regard to border enforcement measures not be applied to parallel import goods, both in respect to copyright and trademark.²²⁶ The Indian delegation specifically objected to a U.S. proposal to provide for national exhaustion in respect of trademarks:

"The representative of India said that he disagreed with the United States proposal in relation to the exhaustion of rights. Referring to paragraph 38 of the Indian paper, he said that the principle of international exhaustion of rights should apply to trademarks." ²²⁷

²²² United States Proposal for Negotiations on Trade-Related Aspects of Intellectual Property Rights, Nov. 3, 1987, at Patents (text reprinted in *U.S. Framework Proposal to GATT Concerning Intellectual Property Rights*, 4 BNA INTL TR REPTR 1371 (Nov. 4, 1987)).

²²³ Trade in Counterfeit Goods: Compilation of Written Submissions and Oral Statements, Prepared by the Secretariat, MTN.GNG/NG11/W/23, 26 April 1988.

²²⁴ *Id.*, para. 38(iii).

²²⁵ The EC proposal stated:

[&]quot;Limited exceptions to the exclusive rights conferred by a trademark, which take account of the legitimate interests of the proprietor of the trademark and of third parties, may be made, such as fair use of descriptive terms and exhaustion of rights." Guidelines and Objectives Proposed by the European Community for the Negotiations on Trade Related Aspects of Substantive Standards of Intellectual Property Rights, Negotiating Group on Trade-Related Aspects of Intellectual Property Rights, including Trade in Counterfeit Goods, MTN.GNG/NG11/W/26, July 1988, at III.D.3.b(i).

²²⁶ Note by the Secretariat, Meeting of Negotiating Group of 3–4 July 1989, MTN.GNG/NG11/13, 16 August 1989, e.g., at para. D7; Note by the Secretariat, Meeting of Negotiating Group of 12–14 July 1989, MTN.GNG/NG11/14, 12 September 1989, at para. 26.

²²⁷ *Id.*, Meeting of 3–4 July 1989, at para. 45.

In 1989, Canada made a proposal to specifically provide for international exhaustion of rights in respect to the protection of layout-designs of integrated circuits.228

In March 1990, the EC tabled a draft text for a TRIPS Agreement²²⁹ that provoked substantial comment from other delegations on the subject of exhaustion. As stated in a note by the GATT Secretariat:

"Article 4: Customs Unions and Free Trade Areas....The representative of the Community said that the underlying purpose of the Article was to enable the Community to continue to apply the principle of Community exhaustion in respect of trade among the member States.

Trademarks. A participant expressed concern that provisions on the very important concepts of parallel imports and exhaustion of rights were absent in the proposed draft agreement. Another participant asked if, under the Community proposal, trademark rights could or could not be used to prevent parallel imports. A further participant was of the view that the proposed Articles on trademarks would enable parallel imports of genuine goods to be prohibited; this conflicted with the Paris Convention and might lead to a division of markets, thus resulting in impediments and distortions of trade.

[Patents] Article 24: Rights Conferred. A participant expressed the view that the proposed provisions on rights conferred were not in line with the principles of intellectual property protection, for example because they tried to invalidate parallel imports and the doctrine of exhaustion of rights....²³⁰

A proposal from the United States²³¹ shortly following the EC proposal likewise elicited a significant number of concerns regarding the exhaustion question. According to the GATT Secretariat:

Article 2. [Copyright] ... In answer to a question, he [i.e. the U.S. delegate] said paragraph (2)(b) could be clarified at a later stage, but the intent was that exhaustion of rights in one territory would not exhaust rights elsewhere. In that light, if goods put on the market in one country were exported to another country where exhaustion had not taken place, it would not undermine the rights established by paragraph (2)(a). Some participants said that they were concerned about the introduction of a right of importation, both here and in Article 9(b), since it could affect the right to effect parallel importations; such a right was not called for by the Berne Convention and could in itself give rise to trade distortions, especially in small countries. Another participant felt the relationship between the right of importation and the right of first distribution was not clear, the latter seeming to

²²⁸ Note by the Secretariat, Meeting of Negotiating Group of 30 October-2 November 1989, MTN.GNG/NG11/16, 4 December 1989, at discussion of paragraph 13 of proposal.

²²⁹ European Communities, Draft Agreement on Trade-Related Aspects of Intellectual Property Rights, MTN.GNG/NG11/W/68, 29 March 1990.

²³⁰ Note by the Secretariat, Meeting of Negotiating Group of 2, 4 and 5 April 1990, MTN.GNG/NG11/20, 24 April 1990.

²³¹ Communication from the United States (NG11/W/70).

Exhaustion of rights

cover the former. In response to a question, the representative of the United States indicated that paragraph (2)(a) would not prevent imports of legitimate goods.

19. In relation to the proposed provisions on trademarks, a participant expressed concern about the absence of provisions... on parallel imports and exhaustion of rights. The following specific points were made in relation to the United States proposal on trademarks:

. . .

Article 12: Rights Conferred. Answering a query, the representative of the United States said that the last sentence of the first paragraph did not refer to parallel imports. The reason for this formulation was that his delegation had a difficulty with the comparable statement in the Community text which suggested that confusion should not be required where an identical sign was used on an identical good, because it had some difficulty in providing rights in the trademark area where confusion did not exist. The proposal that confusion would be presumed to exist in such cases was aimed at bridging this difference. A participant wondered if "use" of a mark included advertising and distribution and whether it could be presumed that exhaustion of rights would be left to national legislation. Some participants felt that the balance in the second paragraph leant perhaps too strongly towards the interests of international companies and could create uncertainty for domestic industry..." 232

2.2.2 The Anell Draft

The text prepared and distributed by Chairman Anell in July 1990 contained limited reference to the subject of exhaustion.²³³ It provided:

"4. Exceptions

- 4A Limited exceptions to the exclusive rights conferred by a trademark, such as fair use of descriptive terms, may be made, provided that they take account of the legitimate interests of the proprietor of the trademark and of third parties.
- 4B Rights shall be subject to exhaustion if the trademarked goods or services are marketed by or with the consent of the owner in the territories of the PARTIES.

. . .

SECTION 4: SPECIAL REQUIREMENTS RELATED TO BORDER MEASURES 1

- 15. Suspension of Release by Customs Authorities
- 15A Without prejudice to point 21 of this Part, PARTIES shall, in conformity with the provisions set out below, establish procedures according to which a right holder, who has valid grounds for suspecting that the importation of [goods which infringe his intellectual property right] [counterfeit trademark or pirated copyright goods] may take place, may lodge an application in writing with the competent authorities, administrative or judicial, for the suspension by the customs authorities of the release into free circulation of such goods. [This provision does not create an obligation to apply such procedures to parallel imports]."

²³² Note by the Secretariat, Meeting of Negotiating Group of 14-16 May 1990 MTN.GNG/NG11/21, 22 June 1990.

 $^{^{233}}$ Status of Work in the Negotiating Group, Chairman's Report to the GNG, MTN.GNG/NG11/W/76, 23 July 1990 [hereinafter Anell Draft].

2. History of the provision

[...]

[Note 1]: It will be made clear at an appropriate place in any agreement that, for the European Communities and for the purposes of this Section, the term "border" is understood to mean the external border of the European Communities with third countries.

2.2.3 The revised Anell Draft

However, subsequent to formal distribution of the July 1990 text, Chairman Anell distributed in October 1990 an informal text that incorporated a revised provision on exhaustion. Although that informal text has not yet been made publicly available, it was commented upon in a TNG meeting of 1 November 1990.

- "3. Speaking on behalf of a number of developing countries, a participant welcomed the structure of the paper which, he said, was in line with the mandate provided in the Mid-term Review. By separating the text into two distinct agreements respectively dealing with trade-related aspects of intellectual property rights and trade in counterfeit and pirated goods, the paper conformed to the intent of the Punta del Este negotiating mandate..... Regarding its substantive contents, he wished to put on record the view that the paper did not adequately take into account the special needs and problems of developing countries. Flexibility in favour of developing countries was required in any TRIPS agreement, in view of their special developmental and technological needs....
- 4. Continuing, he then highlighted some provisions of the text which differed from other provisions because the problems involved were of a more fundamental character, while emphasising that this should not be interpreted as an acceptance of provisions he would not mention..... He welcomed the inclusion in the text of a general provision on exhaustion, which was a basic principle relating to intellectual property rights and as such should not be subject to any exceptions or conditions which might weaken or invalidate its application. In this connection, he said that it should be clarified throughout the text that any references to exclusive rights of importation implied a right to exclude only infringing goods. Alternatively, the grant of this right should be left to the discretion of Parties."²³⁴

2.2.4 The Brussels Draft

The Brussels Draft began to approximate the final text of Article 6, but the differences are important and instructive.

"Article 6: Exhaustion³

Subject to the provisions of Articles 3 and 4 above, nothing in this Agreement imposes any obligation on, or limits the freedom of, PARTIES with respect to the determination of their respective regimes regarding the exhaustion of any intellectual property rights conferred in respect of the use, sale, importation or other distribution of goods once those goods have been put on the market by or with the consent of the right holder.

[Footnote 3]: For the purposes of exhaustion, the European Communities shall be considered a single Party."

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²³⁴ Meeting of the Negotiating Group of 1 Nov. 1990, MTN.GNG/NG11/27,14 Nov. 1990.

It may first be noted that the Brussels text was framed in terms of substantive obligations under TRIPS and not as a limitation on dispute settlement on the subject of exhaustion. The later move toward preclusion of dispute settlement is emblematic of the inability of the parties to reach any substantive agreement on the exhaustion issue.

That inability to reach any substantive conclusion may at least in part be explained by the phrase "once those goods have been put on the market by or with the consent of the right holder". There was considerable debate concerning the scope of the exhaustion doctrine throughout the Uruguay Round. A number of developing countries did not wish to limit application of the doctrine to circumstances in which the IPR holder had consented to placing goods on the market, because there are other circumstances that were considered potentially to exhaust rights, such as sales under compulsory license.

In addition, reference to exhaustion of "rights conferred in respect of the use, sale, importation or other distribution of goods" differed substantially from the formula on exhaustion of rights contemporaneously under negotiation at WIPO in the patent law harmonization context, which is discussed in the next paragraphs.

It is also important to observe that at this stage the EC's intra-Community exhaustion doctrine would have been expressly addressed in a footnote to Article 6, and this was subsequently dropped.

The negotiating parties ultimately rejected a formula that would have essentially defined the scope of exhaustion doctrine.

Commencing in 1985,²³⁵ a Committee of Experts on the Harmonization of Certain Provisions in Law for the Protection of Inventions was established under the authority of the International (Paris) Union for the Protection of Intellectual Property. As the name of this Committee implies, it was charged with seeking to establish common rules in the field of patents. The scope of this project was initially broad, as governments sought to agree upon harmonized substantive provisions of patent law. In late 1992, the scope of this project was limited by the removal of a number of basic articles from the negotiations.²³⁶

Article 19 of the Committee of Experts Draft Treaty on the Harmonization of Patent Laws (Eighth Session, June 11 to 22, 1990) concerns Rights Conferred by the Patent. The first two paragraphs of the proposal are directed at establishing basic rights in respect to product and process patents. The third paragraph concerns permissible exceptions to patent rights, and the fourth deals with the subject of contributory infringement (not relevant here). The text provides:

"Article 19 (formerly Article 302 [of prior draft text]) Rights Conferred by the Patent Alternative A

²³⁵ See WIPO Experts Make Progress On Patent Harmonization Draft, BNA's Patent, Trademark & Copyright Journal, Analysis, January 10, 1991, 41 PTCJ 231 (Issue No. 1013), Lexis/Nexis Database, at Introduction.

²³⁶ See Paris Union Assembly, Nineteenth Session, WIPO doc. P/A/XIX/3, July 31, 1992.

[Products] Where the subject matter of the patent concerns a product, the owner of the patent shall have the right to prevent third parties from performing, without his authorization, at least the following acts:

the making of the product,

the offering or the putting on the market of the product, the using of the product, or the importing or stocking of the product for such offering or putting on the market or for such use.

[Processes]...

[Exceptions to Paragraphs (1) and (2)] (a) Notwithstanding paragraphs (1) and (2), any Contracting Party shall be free to provide that the owner of a patent has no right to prevent third parties from performing, without his authorization, the acts referred to in paragraphs (1) and (2) in the following circumstances:

where the act concerns a product which has been put on the market by the owner of the patent, or with his express consent, insofar as such an act is performed after that product has been put on the market in the territory of that Contracting Party, or, in the case of a regional market, in the territory of one of the members States of such group."

The WIPO draft text would have permitted a state to adopt national or regional exhaustion, but not international exhaustion. This was in fact an issue that remained controversial within the WIPO negotiations until the time the negotiations were suspended. The important aspect for present purposes is that the WIPO text uses a formula for substantively defining the exhaustion principle that is different than that under discussion at the GATT. The WIPO text refers to permitting "acts" in relation to patented products, with reference back to rights otherwise ascribed to the patent holder.

2.2.5 The Dunkel Draft

The Dunkel Draft text of Article 6 distributed in late 1991 is identical to Article 6, TRIPS Agreement.

At a 1998 meeting on the subject of exhaustion of rights and parallel importation, Mr. Adrian Otten, Director of the WTO Intellectual Property Division, who served as Secretary to the Trade Negotiating Group during the Uruguay Round negotiations, presented an oral description of the negotiations. That presentation was summarized in a report on the 1998 meeting:

"Adrian Otten (WTO) – Mr. Otten pointed out that the treatment of exhaustion of rights in the TRIPS Agreement was the subject of difficult and intensive negotiations during the Uruguay Round. The formula in Article 6, TRIPS Agreement, reflects a compromise between governments favoring an explicit recognition of national discretion in regard to exhaustion practices, including the choice of national or international exhaustion, and governments not wanting to provide such recognition although not seeking to regulate such practices specifically. The penultimately proposed formula would have indicated that the TRIPS Agreement did not address the issue of exhaustion of rights, while the final formula indicates that for purposes of dispute settlement under the TRIPS Agreement, nothing in that Agreement (subject to articles 3 and 4) will be used to address the issue of

exhaustion. Both sides to the negotiations preferred the final formula. Mr. Otten observed that earlier proposals, on the one hand, for a provision restricting the scope for parallel imports in situations where prices had been influenced by government measures such as price controls and for a specific rule providing rights against parallel imports in the copyright area and, on the other hand, a provision requiring international exhaustion, at least in the trademark area, were rejected during these negotiations. In a subsequent comment from the floor, Mr. Otten indicated that he remains to be convinced that provisions of WTO agreements outside the TRIPS Agreement may not be used to address national laws on the exhaustion of IPRs, where the treatment accorded depends on the geographical origin of the goods rather than the nationality of the persons involved."²³⁷

3. Possible interpretations

Interpretation of Article 6 is among those aspects of TRIPS that have been most intensively discussed and written about. There are two main areas of controversy, although one of these has been definitively resolved by the Doha Declaration on the TRIPS Agreement and Public Health (see discussion below).

"For the purposes of dispute settlement under this Agreement..."

The first clause refers specifically to "dispute settlement under this Agreement." Rights in intellectual property may have effects in other areas of WTO regulation. For example, technology protected by IPRs may be part of a technical standard that is regulated by the Agreement on Technical Barriers to Trade (TBT Agreement). The conformity of a technical standard with the TBT Agreement may be challenged in dispute settlement. The plain language of Article 6 suggests that rules of TRIPS might be used to address an exhaustion of IPRs issue in dispute settlement under the TBT. Moreover, the question of exhaustion is intricately connected with the free movement of goods, as recognized early on by the European Court of Justice. An IPR may have the same effects as a quota. There is a possibility for a Member to assert that a rule of national exhaustion that permitted IPRs holders to block importation of goods is inconsistent with Article XI, GATT 1994, that provides:

"1. No prohibitions or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licences or other measures, shall be instituted or maintained [...]"

The plain language of Article 6 appears to allow a GATT panel to evaluate an IPR as a measure with the equivalent effect of a quota. This possibility is acknowledged

²³⁷ Remarks of Adrian Otten in Frederick M. Abbott, *Second Report (Final) to the Committee on International Trade Law of the International Law Association on the Subject of the Exhaustion of Intellectual Property Rights and Parallel Importation*, presented in London, July 2000, at the 69th Conference of the International Law Association, rev. 1.1 [hereinafter "Second Report"] (posted at http://www.ballchair.org).

by several leading TRIPS experts who were closely involved in the Uruguay Round negotiations.²³⁸

Other TRIPS experts have argued that the Agreement constitutes a "lex specialis" or self-contained set of rules applicable to IPRs and trade regulation, and that the exhaustion question could not be examined by a GATT panel.²³⁹ There is no WTO DSB jurisprudence on this issue, and for the time being the subject matter is open. However, the Appellate Body has placed great reliance on the plain language and meaning of the WTO Agreements, and the plain meaning certainly appears to support the view that the issue of exhaustion and relevant TRIPS rules could be examined in a dispute under an agreement other than TRIPS.

Another aspect of the first clause is that it is directed to WTO dispute settlement, and so does not directly preclude actions before national courts on exhaustion issues. This limitation was argued by certain Members and their industry groups to be synonymous with saying that Members are not permitted to adopt their own policies and rules on the subject of exhaustion, but rather that rules on this subject are established by TRIPS. Most prominently, pharmaceutical industry associations argued that Article 28, TRIPS Agreement, establishing the rights of patent holders, including to prevent importation, precluded adoption of an international exhaustion policy in the field of patents.

The argument that TRIPS precludes Members from adopting their own policies and rules on the subject of exhaustion is inconsistent with the terms of the Agreement, the practice of WTO Members, and the negotiating history of the Agreement.

Article 6 says that the rules of the Agreement may not be used to address the subject of exhaustion for purposes of WTO dispute settlement. This suggests that the rules of the Agreement may be used to address the subject in national court proceedings. It does not, however, say that Members are restricted in their choice of exhaustion policies, and these are very different matters.

Article 28, for example, grants patent holders the right to prevent third parties from importing patent protected goods without their consent. It does not, however, prescribe a rule as to how their consent will be determined. In Members that have adopted a rule of national exhaustion, consent only exhausts rights as to goods placed on the market within the territory of that Member. In Members that have adopted a rule of regional exhaustion, consent affects goods placed on the market in any Member within the regional group. In Members that have adopted a rule of international exhaustion, consent affects goods placed on the market anywhere in the world. TRIPS does not prescribe a rule regarding the geographic basis on which consent is determined, and clearly allows for international exhaustion.

²³⁸ See Thomas Cottier, *The WTO System and the Exhaustion of Rights*, draft of November 6, 1998, for Conference on Exhaustion of Intellectual Property Rights and Parallel Importation in World Trade, Geneva, Nov. 6-7, 1998, Committee on International Trade Law, and Remarks of Thomas Cottier, in Second Report, and Remarks of Adrian Otten in Second Report, taking the position that Article 6 does not preclude application of the GATT 1994 or GATS to issues involving parallel importation.

²³⁹ See Marco C.E.J. Bronckers, *The Exhaustion of Patent Rights under World Trade Organization Law*, 32 J. World Tr. L. 32 (1998) and Remarks of Marco Bronckers and Remarks of William Cornish, Second Report.

Footnote 6 to Article 28, TRIPS Agreement, provides: "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." This indicates that the right of importation granted to patent holders under Article 28 may not be used to address the subject matter of exhaustion in dispute settlement under TRIPS. In other words, no Member may be challenged in the WTO for adopting an international exhaustion rule based on the word "import" in Article 28.

At the time TRIPS was negotiated, GATT Contracting Parties applied different rules of exhaustion, often varying with the field of IPR protection.²⁴⁰ There is no suggestion in the negotiating history of the TRIPS Agreement that Members reached agreement on uniform exhaustion rules at the time of its conclusion. Moreover, as noted later, since TRIPS entered into force, Members have continued to adopt and apply different exhaustion policies.²⁴¹

If there was any doubt whether Article 6 prevents Members from adopting their own policies and rules on the subject of exhaustion of IPRs, this doubt was firmly eliminated by paragraph 5(d) of the Doha Declaration on the TRIPS Agreement and Public Health, which provides:

"(d) The effect of the provisions in the TRIPS Agreement that are relevant to the exhaustion of intellectual property rights is to leave each Member free to establish its own regime for such exhaustion without challenge, subject to the MFN and national treatment provisions of Articles 3 and 4."²⁴²

The express recognition that Members may establish their own exhaustion regime does not, however, resolve all interpretative issues under Article 6. The main question remaining "on the table" involves whether Members must limit their recognition of the basis for exhaustion to IPR protected goods or services placed on the market with the "consent" of the right holder.

IPRs generally confer on right holders the right to prevent others from taking acts in relation to the IPR, such as selling an IPR protected product. The rationale behind basing exhaustion on the consent of the right holder is that the right holder has voluntarily surrendered its right to prevent the undertaking of the relevant act. Once the right holder "consents", it may no longer "prevent". The concept of exhaustion of IPRs is that the right holder is not granted a perpetual or indefinite right of consent, but rather a limited right.

IPR holders may suggest that limiting or interfering with their right to consent is a violation of fundamental rights in property. Since exhaustion signals an end to control over the good or service protected by the IPR, to exhaust without consent is an impermissible taking of rights in property.

Governments do not, however, confer absolute rights in IPRs. All IPRs are subject to exceptions in the public interest. Some exceptions are potentially more intrusive than others.

One circumstance that is often suggested as a basis for exhaustion without the consent of the IPRs holder is compulsory licensing. TRIPS acknowledges that

²⁴⁰ See discussion above, Section 2.1.

²⁴¹ See, e.g., discussion of the domestic legislation of various WTO Members, below, Section 6.1.

²⁴² See WT/MIN(01)/DEC/W/2 of 14 November 2001.

3. Possible interpretations

Member.²⁴³

governments may grant compulsory licenses, and establishes controls on terms and processes involved in granting them. Some TRIPS experts take the view that the first sale or marketing of an IPR protected good exhausts the IPR in the same manner as consent to the first sale or marketing, and that WTO Members may adopt international exhaustion rules that recognize compulsory licensing as the basis for exhaustion. Other TRIPS experts take the view that consent of the IPR holder is the only acceptable basis for an international exhaustion policy. The latter view is largely rooted in the concept of territoriality. The suggestion is that IPR holders outside the Member that grants a compulsory license should not have their right to prevent a first sale (that is, their "property right") affected by that Member's decision. To allow one Member to make exhaustion decisions that affects other Members would place too much power in the hands of the first

Although allowing international exhaustion based on compulsory licensing does place power in the hands of the granting Member, since TRIPS permits each Member to determine its own policy and rules on the exhaustion issue, it is not clear why there is a threat to importing Members. They are not required to recognize compulsory licensing as the basis for exhaustion, but they may do so.

A liberal approach to international exhaustion would recognize the "lawful" or "legitimate" placing of IPR protected goods or services on the market anywhere in the world as exhausting the right of importation. As noted earlier, there are exceptions to IPR protection other than provided by compulsory licensing, such as those recognized under Article 30, TRIPS Agreement. Consider a product placed on the market in the European Community under a so-called prior user's exception to patent rights. ²⁴⁴ The prior user of the invention acts without the consent of the patent holder, but the goods placed on the market are treated for internal market purposes just as if the patent holder had authorized the marketing. Should WTO Members outside the EC be required to differentiate in their exhaustion policies as between goods first marketed by the patent holder and goods first marketed by the prior user?

The text of Article 6 does not provide a definitive answer to the scope that Members may give to their doctrine of exhaustion, and this may argue in favour of allowing recognition of compulsory licensing, for example, as a basis.

Although Article 6 provides that nothing in TRIPS should be used to address exhaustion of IPRs, it does not define "exhaustion". If a Member adopts an exhaustion policy or rules that another Member considers to extend the concept beyond reasonable limits, there would not appear to be a bar to challenging that interpretation in dispute settlement.

... subject to the provisions of Articles 3 and 4....

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 $^{^{243}}$ As with other aspects of IPRs and exhaustion policy, the rules respecting compulsory licensing might differ depending on the form of protection.

²⁴⁴ According to the prior user exception, a third person using the invention in good faith prior to the filing of the patent may continue the use of the invention in spite of the granting of the patent.

Article 6 is not without express limitations. The exhaustion policy and rules of Members is subject to Articles 3 and 4, TRIPS Agreement.²⁴⁵

Application of the TRIPS national treatment provision to exhaustion doctrine suggests that Members must treat foreign nationals on at least an equivalent basis as local nationals regarding protection of IPRs by exhaustion rules. From a right holder's perspective, this would suggest that a Member may not apply a doctrine of international exhaustion that allows importation as regards foreign IPRs holders, and apply a doctrine of national exhaustion that prevents importation as regards local IPRs holders. This would assure that foreign nationals do not face greater competition from lower priced products than local nationals.

Application of the TRIPS MFN principle to exhaustion doctrine suggests that Members must not apply different exhaustion rules to nationals of different Members. Thus, for example, if the United States applies a doctrine of international exhaustion to IPRs held by Chinese nationals, it must apply the same rule to IPRs held by nationals of the EC. On the assumption that the nationals of Members are most likely to hold the IPRs relating to goods produced in their countries of origin, as a practical matter this means that imports from China and imports from the EU should be subject to the same U.S. rules on exhaustion.

Regional exhaustion doctrines could be considered not consistent with the basic MFN principle in TRIPS because they accord a different status in practical effect to goods imported from countries within the region than to countries from outside the region. In this case, right holders within Members that are part of the region may suffer *vis-à-vis* right holders in Members outside the region. A right holder whose good is first placed on the market outside the region may be able to block import into a Member of the region (and control the distribution of its product), while a right holder within the region could not prevent an importation from another Member within the region. This raises the interesting question whether a national of an EC member state or another regional arrangement could succeed on a claim that it was subject to less protection of IPRs than a national residing outside the EC. The EC claims that Article 4(d) allows it to discriminate against IPR holders residing within the region by precluding them from preventing the intra-Community free movement of goods and services.

4. WTO jurisprudence

None of the WTO Dispute Settlement Body, Appellate Body nor any panel has been asked to interpret Article 6. There are no dispute settlement decisions that discuss it.

However, as noted above, Ministers meeting in Doha adopted the Declaration on the TRIPS Agreement and Public Health that expressly addresses "the provisions in the TRIPS Agreement that are relevant to the exhaustion of intellectual property." Paragraph 5(d) of the Doha Declaration does not limit its reference to Article 6 precisely to account for arguments from some Members and industry groups that other Articles (such as Article 28) override it by implication.

²⁴⁵ For a consideration of the purpose and effect of these Articles addressing national and MFN treatment, respectively, see Chapter 4.

Although there is some debate among legal experts as to precisely the character that should be ascribed to the Doha Declaration, there is no doubt that it will be taken into account by decision-making bodies in the context of dispute settlement. The Ministers clearly acted in Doha with a purpose, and there would be no reason to "recognize" an interpretation of the TRIPS Agreement if they did not intend this recognition to influence interpretation of the Agreement. The legal character of the Doha Declaration is discussed further in Chapters 6 and 33.²⁴⁶

5. Relationship with other international instruments

5.1 WTO Agreements

As discussed earlier, Article 6 specifically refers to settlement of disputes under the TRIPS Agreement. This leaves open the possibility that provisions of TRIPS relevant to the issue of exhaustion of rights will be applied in dispute settlement under other WTO Agreements.

As also mentioned, a claim might arise under the GATT 1994 that enforcement of IPRs to prevent importation of goods involves application of measures equivalent to quotas. If a Member permitted the adoption of a technical standard that incorporates IPR-protected subject matter, questions might arise regarding the extent to which the IPR-holder could control use or modification of the standard, implicating TRIPS rules relevant to exhaustion under the TBT Agreement. Since audio-visual services, as example, frequently incorporate IPR protected elements, it is certainly possible that a GATS dispute could implicate provisions of TRIPS relevant to exhaustion.

The relationship between TRIPS provisions relevant to exhaustion, including Article 6, and other WTO Agreements, remains to be determined in dispute settlement. There are different views among legal experts regarding whether Article 6 precludes exhaustion issues from being considered under other WTO Agreements. The "plain text" of Article 6 does not appear to preclude TRIPS rules relevant to exhaustion from being applied in dispute settlement under other agreements, but this does not exclude the possibility that TRIPS will be found to "occupy the field" of exhaustion subject matter as a special agreement governing trade and IPRs subject matter, or *lex specialis*.

5.2 Other international instruments

In December 1996 two new treaties with respect to intellectual property rights were adopted at WIPO: the Copyright Treaty (WCT) and the Performances and Phonograms Treaty (WPPT).²⁴⁷ These two treaties include provisions with respect

²⁴⁶ See Section 6.2 (International instruments) of both Chapters; see also F. Abbott, *The Doha Declaration on the TRIPS Agreement and Public Health: Lighting A Dark Corner at the WTO*, in: Journal of International Economic Law (2002), 469–505.

²⁴⁷ World Intellectual Property Organization: Copyright Treaty [adopted in Geneva, Dec. 20, 1996], 36 I.L.M. 65 (1997) and World Intellectual Property Organization: Performances and Phonograms Treaty [adopted in Geneva, Dec. 20, 1996], 36 I.L.M. 76 (1997).

government of Australia announced, following the recommendation of its Intellectual Property and Competition Review Committee, that it would further liberalize its rule of international exhaustion in the field of copyright by eliminating a requirement that importers await the Australian copyright holder's release of the work on the local market.²⁵²

6.1.2 Japan

In 1997 in the *BBS* case,²⁵³ the Japanese Supreme Court held that the right under the Japanese Patent Act of a patent holder in Japan to block importation of a patented product was exhausted when the product was first sold abroad, subject to the possible imposition of contractual restrictions to the contrary.

6.1.3 South Africa

The South Africa Medicines and Related Substances Control Amendment Act of 1997 included a provision permitting the Minister of Health to establish the conditions under which parallel importation of patented medicines would be authorized. Since South Africa recognized international exhaustion as to patents as a matter of its common law, and since there was no indication that the parliament intended to change this rule when it amended the Patent Act to implement TRIPS, it is unlikely that Section 15C of the Medicines Amendment Act made new law in South Africa, except to provide regulatory authority to the Health Minister. Nonetheless, this legislation regarding parallel importation provoked intense diplomatic protest from the United States and European Community, and a lawsuit by 39 pharmaceutical companies (which also addressed other provisions of the Medicines Amendments Act). The challenges to the Medicines Amendment Act were withdrawn in 2001.

6.1.4 Other developing countries

A recent WIPO report identifies developing countries with regard to whether their legislation (a) allows for compulsory licensing and (b) adopts national or international exhaustion in respect to IPRs.²⁵⁴

Importing in New Zealand: Historical Origins, Recent Developments, and Future Directions, [1999] EIPR 63.

²⁵² See Fourteenth Copyright Newsletter of the Intellectual Property Branch of the Attorney-General's Department, http://law.gov.au/copyright_enews, June 29, 2000:

"The Government announced on 27 June 2000 that it will amend the Copyright Act 1968 to allow for parallel importation of legitimately produced books, periodicals, printed music, and software products including computer-based games. When implemented, this decision will remove the legal impediment imposed by the Copyright Act on Australian importers obtaining these products and making them available to consumers as soon as they are released anywhere in the world. They will not be obliged to wait for the Australian copyright owners to release them in Australia."

- ²⁵³ BBS Kraftfahrzeugtechnik AG and BBS Japan, Inc. v. Rasimex Japan, Inc., Supreme Court Heisei 7 (o) No. 1988 (July 1, 1997), J. of S. Ct., No. 1198 (July 15, 1997).
- ²⁵⁴ See Legislative Assistance provided by the World Intellectual Property Organization (WIPO) in relation to the Implementation of the Agreement on Trade-Related Aspects of Intellectual Property Rights (the TRIPS Agreement) and the Doha Declaration, at http://www.wipo.int/cfdiplaw/en/trips/index.htm, visited 8 April 2004.

to adopt higher standards. TRIPS does not preclude Members from agreeing to relinquish rights to permit parallel importation. Yet, it seems inconsistent with the spirit of the Doha Declaration that Members that have agreed on the multilateral level to national autonomy in the determination of exhaustion policy would have been asked to relinquish that autonomy as part of a package of bilateral trade concessions.

6.4 Proposals for review

The adoption of the Doha Declaration on the TRIPS Agreement and Public Health resolved the question whether WTO Members are permitted to adopt their own regimes regarding exhaustion of rights (see above, Section 3). There are no present proposals to reopen this issue.

However, the relationship between rules on exhaustion of patent rights and proposals to facilitate price discrimination in favour of developing countries to address public health needs has resulted in renewed discussion concerning the extent to which restrictions on parallel trade may be desirable in certain contexts. These issues are being considered in the context of continuing negotiations regarding implementation of paragraph 6 of the Doha Declaration.

7. Comments, including economic and social implications

There is considerable debate regarding the economic and social implications of different exhaustion of rights regimes.²⁶⁸ It is important to acknowledge at the outset that the same conclusions may not apply to all forms of IPRs, or for that matter to different goods and services protected by these different forms. There may or may not be a single optimum exhaustion rule. With that said, there are a few general observations that can be made.

First, rules of exhaustion are designed to foster competition among producers, and to benefit consumers. Exhaustion of IPRs limits the legal capacity of producers to control the movement of goods and services after the first sale or lawful placing on the market, and reduces the potential for trade-restrictive (including anti-competitive) behaviours. As a "first principle", it is to the consumer's advantage that exhaustion of rights is accepted.

In the international setting, there are two main arguments made by proponents of limiting exhaustion and parallel importation. The first is that by allowing IPR holders to segregate markets and charge different prices, producers can achieve higher rates of return on their investments in intellectual property. This will permit producers to reinvest greater amounts in the creation of new and better goods and services, which is to the benefit of consumers.

²⁶⁸ See, e.g., 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. Int'l Econ. L. 607 (1998); Keith Maskus, Parallel Imports in Pharmaceuticals: Implications for Competition and Prices in Developing Countries, Final Report to the World Intellectual Property Organization, draft of April 2001; Commission on Macroeconomics and Health, CMH Working Paper Series, Paper No. WG4:1 – Scherer, F.M. and Watal, Jayashree, Post-TRIPS Options for Access to Patented Medicines in Developing Countries, June 2001.

Similar arguments are often made to promote higher levels of IPR protection generally, and there is good reason to be sceptical about the need for higher levels of protection and increasing returns to IPR-holders at a cost to the public of higher prices.

A second argument is that parallel imports hurt developing country interests because, if goods placed on the market in developing countries can freely flow to developed countries, producers will refrain from charging lower prices in developing countries.

It is curious that some developed countries that are the most aggressive promoters of liberal trade – which is about maintaining free movement of goods and services, competitive markets and operation of comparative advantage – favour market segregation and differential pricing when it comes to IPRs and parallel trade. It is difficult to reconcile the view that open markets benefit developing countries by allowing them access to developed markets for their low-production cost products, and the view that low-priced goods must remain in developing countries. If it is correct that price discrimination as a general proposition favours developing countries, this might imply that liberal trade rules are not the most beneficial for them.

As a general proposition, international exhaustion of IPRs may be the principle most consistent with fostering competition, specialization and global economic welfare (assuming that economists would not advocate a rethinking of the foundations of the WTO system). Yet does this mean that price discrimination will never benefit developing countries? Probably not. There are circumstances in which it may be desirable to limit inter-country price competition to promote the interests of consumers in developing countries, such as when the prospects for developing countries to establish their own globally competitive sources of supply are limited. There may not be many such cases, and even those cases may result from IPR protection granted to developed country technologies. The point is, however, that there may be exceptional cases in which the advantages of an international exhaustion regime would be outweighed by competing developing country consumer interests. In such cases it may be possible to grant an exception to the otherwise applicable rules, rather than opting for a closed exhaustion regime that on the whole disadvantages developing countries.

The argument by some developed countries that rules allowing parallel trade harm developing country interests because such rules inhibit the sale of lower priced goods in many cases proceeds from a false factual premise. Perhaps paradoxically, goods and services are often sold in developing countries at prices higher than in developed countries, and developing country consumers will benefit from importing from the developed countries.

²⁶⁹ For example, the Commission on Intellectual Property Rights established by the British government recommended that supply of patented pharmaceuticals to developing countries at lower differential prices might be facilitated if developed countries prevented parallel importation of those medicines. The Commission, however, recommended that developing countries continue to allow parallel importation of patented medicines to assure the lowest cost source of supply. IPR Commission, at Chpt. 2.