Grey Market Litigation in the United States District Courts

Hugh J. Turner Jr.

Follow this and additional works at: http://scholarship.law.unc.edu/ncilj

Part of the Commercial Law Commons, and the International Law Commons

Recommended Citation
Available at: http://scholarship.law.unc.edu/ncilj/vol11/iss2/9

This Article is brought to you for free and open access by Carolina Law Scholarship Repository. It has been accepted for inclusion in North Carolina Journal of International Law and Commercial Regulation by an authorized editor of Carolina Law Scholarship Repository. For more information, please contact law_repository@unc.edu.
Grey Market Litigation in the United States District Courts

Hugh J. Turner, Jr.*

I. Introduction

A strong U.S. dollar and the recent trend of domestic manufacturers to move their manufacturing operations off-shore have made the importations of “grey market goods” a major industry in the United States.1 Sometimes referred to as “parallel imports,”2 grey market goods are authentic goods, intended for sale in foreign countries, that are diverted into, and sold in, the United States by persons other than the authorized distributor. Through arbitrage the grey market importer capitalizes on the cost difference between the authorized goods and the diverted goods. This trade practice enables U.S. consumers to purchase items at substantial discounts.3 Licensed domestic distributors complain that defective grey market goods erode the product’s goodwill because the grey goods are not covered by the distributor’s warranty.4 In response, authorized distributors have fought in the courts and legislatures to ban grey market goods.

This article analyzes the legal theories currently advanced by manufacturers and authorized distributors5 in grey market litigation,6 focusing on procedural aspects of this litigation. Because the factual circumstances and theoretical underpinnings differ widely

---

* Partner, Smathers & Thompson, Miami, Florida. B.S. 1967, Boston University; J.D. 1975, University of Miami. The author wishes to acknowledge the assistance provided by David A. Doughty, an associate with the firm of Smathers & Thompson, in preparing this article.

1 The total value of the market in grey goods may be as much as $10 billion annually. Riley, “Gray Market” Fight Isn’t Black and White, Nat’l L.J., Oct. 28, 1985, at 1, col. 3.

2 Counsel for grey market importers tend to prefer the term “parallel imports,” while counsel for authorized distributors and manufacturers prefer the term “grey market goods.” The author will use the term “grey market goods” for purposes of uniformity.


5 Unless the context requires separate treatment, the term “authorized distributor” will be used throughout this article to encompass both licensed or authorized distributors and manufacturers.

6 Litigation in the International Trade Commission (ITC), aimed at intercepting grey market goods at the customs border, is beyond the scope of this article. For a discus-
from case to case, one body of law does not singularly address the issue of grey market goods. Although the following theories have been advanced by grey market litigants, the outcome of grey market cases often depends largely upon the facts. To win a grey market case, the practitioner should be especially sensitive to the facts of the case, carefully presenting those facts that support his theory.

II. Trademark Infringement

Authorized distributors most frequently rely upon federal trademark infringement law in their battle against grey market importers. While damages are available for infringement, trademark holders usually seek injunctive relief to terminate the influx of grey market goods. Thus, the battle between the authorized distributor and the grey market importer will be won or lost through the preliminary injunction.

A. Preliminary Injunction

Unless the goods have been marketed by the grey market importer for several months with the manufacturer's knowledge and tacit agreement, the authorized distributor should immediately seek to enjoin the grey marketeer from importing the goods. To obtain a preliminary injunction, the moving party must show:

(a) irreparable harm and (b) either (1) likelihood of success on the merits or (2) sufficiently serious questions concerning the merits to ensure a fair ground for litigation and a balance of hardship tipping decidedly toward the party requesting the preliminary relief.

While not dispositive, the public interest influences a court's decision of ITC litigation, see Victor, Preventing Importation of Products in Violation of Property Rights, 53 Antitrust L.J. 783 (1984).

7 15 U.S.C. §§ 1051-1127 (1982). In addition, the plaintiff may bring an action under § 43(a) of the Lanham Act, id. § 1125(a), based on unfair competition and an action based on state and/or common law unfair competition. Ownership of a registered trademark is not required in order to maintain a suit for unfair competition. See Exxon Corp. v. Humble Exploration Co., 695 F.2d 96, 103 (5th Cir. 1983).

8 The term "grey market importers," as used throughout this article, will include distributors and dealers in the United States who obtain grey market goods from grey market importers for purpose of resale.

9 Damages available under the Lanham Act include (1) defendant's profits; (2) any damages sustained by the plaintiff; and (3) the costs of the action. The court is also authorized to enter a judgment in an amount three times the actual damages. 15 U.S.C. § 1117 (1982).

10 In an appropriate case, a trademark owner may seek to obtain an ex parte temporary restraining order from the court. Although ex parte relief is now available in appropriate counterfeiting cases (see In re Vuitton et Fils S.A., 606 F.2d 1 (2d Cir. 1979)), the extent to which such relief is available in grey market cases is unclear. Grey market goods are expressly excluded from the definition of counterfeiter marks found in the Trademark Counterfeiting Act, 15 U.S.C.A. § 1116 (d)(1)(B) (Supp. 1986).

11 Bell & Howell: Mamiya Co. v. Masel Supply Co., 719 F.2d 42, 45 (2d Cir. 1983); see also Jackson Dairy, Inc. v. H.P. Hood & Sons, Inc., 596 F.2d 70, 72 (2d Cir. 1979); Osaka, 589 F. Supp. at 1165.
tion whether to issue a preliminary injunction.12

I. Irreparable Harm

Some courts have held that an inference of irreparable harm exists in the case of trademark infringement.13 Irreparable harm is more difficult to establish when a defendant can pay damages or when the plaintiff alleges damage to an intangible such as reputation.14 Courts are more likely to find, however, that damages are not an adequate remedy when the quality of the infringing products is inferior to the authorized products of the moving party.15

Other courts have held that a presumption of irreparable harm exists in trademark infringement cases. If, however, the court does not apply the presumption, the plaintiff should assert, if applicable, that an adverse impact on the authorized distribution network has occurred or that the product's goodwill or reputation has been injured. For example, in Osawa & Co. v. B & H Photo the trademark owner alleged that grey market imports caused a demoralization of the authorized distribution network, which caused a drastic decline in sales:

> Competition from grey marketers has caused demoralization, disaffection and misunderstanding among authorized dealers, 40% of whom have dropped the Mamiya line since 1980. There is evidence that some dealers have misunderstood the cause of the problem, believing that plaintiff was granting preferred price treatment to their competitors.16

The court further noted that the plaintiff had laid off a large number of its personnel, including a significant segment of the repair force, and had suffered consequent delays in time needed for warranty repairs.17

Similarly, in Selchow & Righter Co. v. Goldex Corp.18 the plaintiff claimed that grey market "Trivial Pursuit" games imported from Canada generated dissatisfaction among licensed distributors who were in consistently short supply but who could not import the game from Canada. Selchow sought two forms of relief. The first was a permanent injunction to keep the defendant from infringing its

12 See, e.g., Bill Blass, Ltd. v. SAZ Corp., 751 F.2d 152, 156 (3d Cir. 1984); Le Beau v. Spirito, 703 F.2d 639, 642 (1st Cir. 1983); William Inglis & Sons Baking Co. v. ITT Continental Baking Co., 526 F.2d 86, 87 (9th Cir. 1975).
16 Osawa, 589 F. Supp. at 1168.
17 Id.
trademarks, copyrights, and patents. The second was money damages. The court granted the injunction, but ordered a trial on the issue of damages. Therefore, in any case alleging an adverse impact on a distribution network, the U.S. trademark owner should offer evidence to prove the expense incurred in establishing the distribution network.

Another type of irreparable harm caused by grey market goods is a loss of mark promotion. Goods intended to be distributed in the United States may contain advertisements of the domestic trademark owner. Foreign copies diverted into the domestic market normally lack such advertisements, which reduces the domestic trademark owner's advertising. Moreover, significant grey market competition causes independent dealer dissatisfaction. This dissatisfaction could significantly affect an advertising campaign which depends in part on a cooperative advertising allowance to independent distributors.

2. Success on the Merits

Grey market importers affirmatively plead that no likelihood of confusion between its products and those of the authorized domestic distributor exists because the products share a common manufacturing origin. To meet this contention, the authorized distributor must emphasize that the modern view of trademark protection recognizes that the reasons for the mark's protection extend beyond mere source identification. The International Trade Commission recently confirmed this view in *In re Certain Alkaline Batteries*:

We are, however, aware of the number of divergent cases holding that imports of foreign trademarked goods do not infringe U.S. trademarks where there is no confusion. These decisions are based on the theory that the only function of trademark law is to prevent consumer confusion.

We do not believe that this is the only purpose of trademark law. A trademark has several functions including: (1) to enable buyers to identify one seller's goods and distinguish them from goods sold by others; (2) to signify that all goods bearing the trademark come from a single, albeit, anonymous source; (3) to signify that all goods bearing the trademark are of an equal level of quality; and (4) to assist the seller in the advertising and selling of his goods. A trademark is also the objective symbol of the goodwill built up by the trademark owner. A function of the trademark law is to protect a trademark owner's investment in goodwill because it is considered unfair to allow one to appropriate goodwill and profits which a competitor has built up by quality and advertising in a trade symbol. When a trademark symbolizes a trade or business, the trademark owner has the

---

19 See *Osawa*, 589 F. Supp. at 1168.
20 See *Nintendo of Am., Inc. v. Uniglobe Int'l, Inc.*, No. 84-1767 (S.D.N.Y. filed Dec. 6, 1985).
exclusive right to use the mark on the goods of the same description of his manufacture or sponsorship. . . . [A United States trademark] does not just protect consumers from likelihood of confusion, but it also protects the trademark owner's goodwill and the benefits that are derived from that goodwill, including profits.\textsuperscript{22}

To establish a probability of success on the merits, a plaintiff need only show that a likelihood of customer confusion, rather than actual confusion, exists.\textsuperscript{23} Toward this end, an authorized distributor should show as many differences as possible between his goods and services and the grey goods and services, or the absence of services, sold on the grey market.

The discrepancy between the authorized distributor's goods and the grey goods is seen best in warranty service provided by the authorized distributor. Usually, authorized distributors go to great length to provide warranty service for their products. In contrast, grey market importers rarely provide any warranty service. Focusing on this difference, the court in \textit{Bell & Howell: Mamiya Co. v. Masel Supply Co.}\textsuperscript{24} granted a preliminary injunction:

It is plaintiff that defines the warranty and provides the repair services for the cameras it sells. The cameras defendant sells lack that warranty. . . . [P]laintiff's warranty and assurances of quality are signified by the MAMIYA marks in this country. Defendant's use of those marks carries with it none of these assurances.\textsuperscript{25}

The Second Circuit, however, vacated the injunction, ruling that the grey goods' lack of warranty did not amount to irreparable injury. The court reasoned that the distributor could alert the consumer of whether the camera carried warranties by labels, advertisements, or other things.\textsuperscript{26} Without reaching the merits, the Second Circuit concluded that less drastic means than an injunction were available to avoid the likelihood of confusion.

Other courts, however, have found that substantial differences in warranty and post-sale service may contribute to the likelihood of confusion. For example, in \textit{Osawa}\textsuperscript{27} and in \textit{Weil Ceramics & Glass, Inc. v. Dash}\textsuperscript{28} the courts rejected the grey market importers' claims that they would provide warranty service. \textit{Osawa} stated that the grey market importers' warranties would not be effective, which would aggravate the likelihood of confusion:

\textquote{[T]he warranty is of value to the goodwill of the mark only if offered by one who has the incentive to uphold the reputation of the

\begin{thebibliography}{9}
\bibitem{24} 548 F. Supp. 1063 (E.D.N.Y. 1982), vacated and remanded, 719 F.2d 42 (2d Cir. 1983).
\bibitem{25} Id. at 1079.
\bibitem{26} Bell, 719 F.2d at 46.
\bibitem{27} 589 F. Supp. 1163.
\bibitem{28} 618 F. Supp. 700 (D.N.J. 1985).
\end{thebibliography}
mark.... [The trademark owner] would have no assurances that the [grey market importers'] warranty repairs would be properly performed or that the obligation would be graciously accepted. [The trademark owner] would be constantly subject to the risk that [the grey market importers] would disavow the obligation or perform inadequate repairs. Disparities between plaintiff's and defendants' performance of warranty work would further confuse the marketplace as to the standing and meaning of the Mamiya mark.29

Furthermore, the plaintiff in Osawa successfully showed that it maintained a vast inventory of accessory equipment to satisfy promptly the needs of its professional clientele.30 Plaintiff contended, and the court agreed, that the inventory was a cost incurred exclusively by the authorized distributor, which further distinguished the authorized distributor's goods from the grey market importer's goods.

In Weil Ceramics the grey market importers argued that plaintiff's warranty to replace defective goods was similar to their obligations to purchasers of goods under the Uniform Commercial Code.31 The court rejected this claim noting that consumers rely on authorized distributors—not grey market importers—to maintain the quality of the product.32 The court adopted Osawa's reasoning and concluded that the disparity between warranty service would compound the confusion.

The dubious quality of the goods sold by grey market importers may damage the goodwill established by a trademark owner. In Johnson & Johnson Products, Inc. v. DAL International Trading Co.,33 Johnson & Johnson contended that there would be customer dissatisfaction if their toothbrushes, intended for sale abroad without the American Dental Association seal of acceptance, were diverted to the United States. In Selchow the exclusive licensee, distributor, and domestic manufacturer of "Trivial Pursuit" brought suit to enjoin defendant from importing Canadian versions of the game. The defendant also imported "Sexual Trivia" games. Selchow, a manufacturer of family games, alleged that the importer's importation and sale of "Sexual Trivia" games injured Selchow's reputation. Noting that domestic consumers associated Selchow's reputation with "Trivial Pursuit," the court concluded that Selchow demonstrated that a substantial likelihood of confusion existed, which proved Selchow's case for stat-

29 589 F. Supp. at 1169.
30 Id. at 1167.
31 618 F. Supp. at 714.
32 Id. New York now requires stores selling grey market goods to post disclosures if they are selling brand-name merchandise not covered by the manufacturer's standard U.S. warranty. See N.Y. Assembly Bill No. 5971, effective October 22, 1985; see also Taylor, N.Y.: To Start Gray Market Warnings, Wash. Post, Oct. 22, 1985, at E3, col. 1.
Packaging differences also may cause confusion, which damages a product's goodwill. In *Nintendo of America, Inc. v. Uniglobe International Inc.* packaging of products destined for the domestic market was designed to appeal specifically to the tastes of the U.S. consumer. Foreign packaging, which utilized different color schemes and included instructional material in foreign languages, caused confusion when sold in the United States.

An authorized distributor's quality control further distinguishes those products imported through the domestic mark holder from those imported on the grey market. In *Weil Ceramics* the authorized distributor inspected all porcelain pieces and most of the other larger pieces that it received. The authorized distributor submitted the remaining smaller pieces to a shake test to determine breakage. While the authorized distributor visually inspected only four to five percent of the porcelain pieces, the court found this inspection to be sufficient evidence of the licensed distributor's separate goodwill.

Similarly, in *Model Rectifier Corp. v. Takachiho International, Inc.* the court stated that the licensed distributor maintained quality control by keeping an inventory of parts for the model automobile kits that it distributed. The court affirmed the preliminary injunction, noting that the licensed distributor's employees opened and inspected each kit and replaced broken or missing parts before distribution.

3. Balance of Hardships

If the grey market importer's only hardship will be lost profits and plaintiff's losses are substantial, the court will usually grant a preliminary injunction. For example, in *Osawa* the defendants dealt in various types of photographic equipment, and realized significant profits from the sale of grey goods. The court found that an injunction would not seriously affect the grey marketeers' overall business. On the other hand, the plaintiff already had sustained large losses that threatened to undermine its entire business. Accordingly, the court granted plaintiff preliminary relief.

In *Johnson & Johnson* the court stated that no countervailing equities existed for the grey market distributor because the defendant "operates in a commercial environment in which it is a trade practice

---

34 612 F. Supp. at 24.
35 *Nintendo*, No. 84-1767.
36 *St. Bell*, 548 F. Supp. at 1069.
37 618 F. Supp. at 711.
39 Id. at 509.
40 589 F. Supp. at 1170.
41 Id.
42 Id. at 1179.
to close one's eyes to defects in title or other factors which would subject a transaction to nullification. Those who operate in such a manner must accept the consequences of self-imposed blindness." 43 In contrast, the court in El Greco Leather Products Co. v. Shoe World, Inc. 44 held that the balance of hardships would not lie in favor of the trademark owner if, by exercising sufficient control over its foreign manufacturers, the mark owner could prevent any future unauthorized disposition of its trademarked goods. The court stated that the plaintiff may have had an adequate legal remedy for any contract damage it could prove, which obviated the need for a preliminary injunction. 45

B. Affirmative Defenses

1. Antitrust Claims

If a plaintiff has violated antitrust laws, he may be estopped from enforcing his trademark rights. A grey market importer may allege a relationship in restraint of trade as an affirmative defense and counterclaim in a trademark infringement action. 46 The gravamen of an antitrust claim is that the licensed distributor would have an unjustified monopoly on the domestic sale of the goods. The Osawa court dismissed the grey market importers' antitrust claim, holding that the enforcement of the licensed distributor's rights in the United States would not bar defendant from selling the same equipment in Japan. 47 The court noted that the defendant may compete in the United States if the infringing trademark were removed, as specified in the Genuine Goods Exclusion Act. 48

In Selchow 49 the court upheld the grant of an exclusive license under a patent to the United States. Selchow noted that 35 U.S.C. § 261 expressly authorizes the assignment of an exclusive right under a patent to the whole or any part of the United States. After referring to cases interpreting the statute, Selchow held that such an assignment is not an illegal territorial restriction.

2. Acquiescence Claims

A licensed trademark holder may be estopped from seeking injunctive relief if his protest to the importation of grey market goods

43 No. 85-3966 at 27 (order granting preliminary injunction).
45 Id. at 1401.
46 Litigation regarding the antitrust issues raised in a grey market case is beyond the scope of this article. For a discussion of the antitrust law in this area, see supra note 6.
47 589 F. Supp. at 1178.
49 612 F. Supp. at 27.
is untimely. In *Parfums Stern, Inc. v. United States Customs Service* the court found that the grey market importers relied upon the trademark holder’s apparent acquiescence to the grey market importation of fragrance products. The court noted that an injunction would cause the grey market importers to default on delivery orders necessary to place goods on the shelves during one of the most significant selling seasons of the year. Accordingly, the court held that possible injury to the grey market importers would be far greater than to the trademark holder.

3. **Exhaustion Doctrine**

The exhaustion doctrine prohibits a trademark holder from controlling branded goods after releasing them into the stream of commerce. The trademark holder’s control is deemed exhausted after the first sale of the goods. After the mark holder exhausts his control, secondary dealers may advertise and sell the merchandise in competition with the mark holder as long as they do not represent themselves as authorized agents.

The exhaustion defense may not apply, however, if the authorized domestic distributor has developed goodwill separate from that of the mark originator. In *Osawa* the authorized U.S. distributor developed separate goodwill through significant warranty service, promotional rebates, educational activities, and product advertisement. The court found that the authorized distributor had not exhausted its rights to the goods in the domestic market. Thus, to prevail against the exhaustion defense the authorized distributor must distinguish itself from the foreign mark holder and prove that an independent goodwill exists.

C. **Investigation and Discovery**

1. **The United States Distributor**

Typically, the domestic distributor and the foreign mark owner have devoted substantial time, energy, and money to create a U.S. market. Often, the authorized distributor feels that the grey market importer gets a free ride on the goodwill developed by the distributor. The grey marketeer profits unfairly, if not illegally, from the authorized distributor’s investment.

Grey goods have wreaked havoc among the authorized distributors’ marketing and quality control infrastructure. Increased competition from grey market goods demoralizes dealers, which erodes the authorized distributor’s network of distribution. Likewise, as the

---

51 Id. at 420.
52 589 F. Supp. at 1174.
53 Id.
grey market importer gains a buyer share of the market, the domestic distributor's sales decrease. Once sales decline, jobs are lost.

To advance a legal theory which affords relief from grey market imports, the authorized distributor must marshal those facts that permit a suit to be maintained successfully. A plaintiff should examine the authorized distributor's contribution in developing the product which has been introduced on the grey market. A complete internal investigation should be conducted to establish those facts that distinguish the authorized distributor from the foreign mark owner. All elements that demonstrate independent goodwill from the foreign mark owner should be established. The following inquiries should be made:

1. Do customers associate the product with the authorized distributor or the foreign mark owner?
2. How much money has the authorized distributor spent to advertise and promote the product and to establish the product distribution network?
3. Does the authorized distributor furnish a warranty, service, accessories or rebates?
4. Does the authorized distributor attend trade shows and market the product in the United States?
5. Does the authorized distributor provide quality control before the product reaches the consumer or does it simply act as a middleman between the foreign manufacturer and the U.S. consumer?
6. How long have the grey market goods been entering the country? How long has the authorized distributor and foreign mark owner known about the importation?
7. Has the foreign mark owner made any attempt to terminate distribution of the goods to the grey market by the mark owner's foreign manufacturer(s)?

In addition, the authorized distributor should determine if consumer confusion exists by making the following inquiries:

1. Has the authorized distributor received warranty claims on grey market goods?
2. Based upon the authorized distributor's own pre-suit investigation, what differences exist between the authorized distributor's goods and those of the grey market importer?

A consumer survey can be invaluable in documenting consumers' confusion.

Courts will usually expedite discovery so that it can be taken within the truncated period available before the preliminary injunction hearing. The authorized distributor should consider discovery and investigation (perhaps with the assistance of a private investigator) concerning the following areas:

1. The manner in which the grey market goods are shipped to the United States.
2. The identities of all suppliers who have furnished the grey market importer with the grey goods.
(3) The identities of all customers who have purchased or obtained the grey goods.
(4) Any correspondence, including complaints, received by the grey market importer concerning the grey goods.
(5) How the grey market importer first learned of the grey goods.
(6) Advertising or promotion of the grey goods, if any, by the grey market importer.
(7) Any warranties provided by the grey market importer in connection with the grey goods.
(8) All information about the handling of the grey goods (including repackaging and storage) following receipt by the grey market importer.
(9) The extent to which the grey marketeer services the grey goods.
(10) The identity of all importers, freight forwarders, and customs brokers who handle the grey goods.
(11) Any disclosures that are made by the grey market importer to customers that the grey goods are not warranted by the authorized distributor.
(12) The depth of the grey market importer’s line of inventory in the grey goods.
(13) Any customer profiles done by the grey market importer to ascertain who is purchasing the grey goods.
(14) A complete analysis of the grey market importer’s business (present and past), including the percentage of present business that grey goods represent.

2. The Grey Market Importer

The grey market importers stress the competitive advantages and cost savings that the market of “parallel imports” affords consumers. These importers often characterize the product’s distribution network as noncompetitive, if not monopolistic. Frequently, grey market importers attempt to persuade the court to apply a narrow definition of trademark protection, which focuses upon the origin of the grey market goods.

The grey market importer should show that the authorized distributor has no separate identity from the foreign mark owner and no independent goodwill in connection with the product. Investigation and discovery by the grey market importer should explore the following areas:

(1) The validity of the trademark.
(2) A detailed examination of the global marketing and distribution network of the authorized goods, including the relationship between the domestic authorized distributor and the foreign mark owner.
(3) Does the authorized distributor provide a warranty with its goods? If so, how often are claims presented? How many service claims has the authorized distributor received for the goods? How much money, if any, has the authorized distributor spent to provide repair services for the grey market goods?
(4) A detailed examination of every contact the authorized distrib-
utor has with the goods (e.g., inspection, servicing), including a review of the authorized distributor's books and records. The grey market importer should determine each additional cost increase attributable to value added by the distributor.

(5) A detailed examination of all possible bases that the authorized distributor claims create confusion and that allegedly establish the authorized distributors' independent goodwill.

(6) A detailed examination of all claims of irreparable harm resulting from competition from the grey goods.

(7) Ascertainment of specific customer complaints lodged with the authorized distributor through the use of interrogatories.

(8) A detailed examination of the domestic distribution network and the quality control and other features which the authorized distributor claims are compromised by importation and sale of the grey goods.

(9) An investigation of the degree of control the foreign mark owner exercises over its foreign manufacturer(s) to eliminate sale at the source of the grey market goods.

D. Summary Judgment

The authorized distributor should consider a motion for summary judgment if it appears that no genuine issue of material fact exists. The motion's outcome depends on the grey market importer's ability to establish whether there is any genuine issue of fact about the existence of separate and independent goodwill. In Weil Ceramics the court held, as a matter of law, that the authorized domestic distributor had developed independent goodwill. The court relied on the distributor's careful inspection of the products, warranty on the merchandise, and promotion of the products. The court stated that the licensed distributor had established independent goodwill in the United States for the trademark and that the grey market importer's use of the mark was likely to cause confusion. Therefore, the court found that no genuine issue of material fact existed and granted the authorized distributor's motion for summary judgment.

Similarly, the Selchow court granted summary judgment in favor of the plaintiff-manufacturer. The court in Selchow held that the defendants failed to establish that the authorized distributor was merely a fragment of a single international enterprise. On this basis, Selchow distinguished Parfums Stern, and held that the authorized distributor's domestic goodwill deserved protection.

III. Copyright Infringement

Because some courts have been unwilling to grant injunctive re-
Lief for trademark infringement, an authorized distributor should also assert a claim for copyright infringement. A copyright is generally defined as an intangible property right given to creators of certain kinds of artistic or intellectual property. Generally, a copyright claim may be asserted if the copyright holder has the exclusive right to sell the goods in the United States. The holder’s rights last fifty years after the creator’s death or, in some cases, seventy-five years from publication or one hundred years from creation. While the copyright need not be registered to own the rights to that copyright, registration is a condition precedent to initiating suit.

A. Preliminary Injunction

As in trademark infringement actions, the most effective device to halt the flow of grey goods is a preliminary injunction. An injunction is even more effective if the alleged infringer has paid the supplier and cannot recover its money. The criteria for issuing a preliminary injunction in a copyright case are the same as those used in a trademark infringement action.

Loss of control over the copyrighted work and loss of “advertising clout” may cause customer dissatisfaction and irreparable injury. Conversely, a copyright owner’s receipt of profits from the sale of the goods abroad militates against a finding of irreparable injury.

The balance of hardships are usually in the copyright owner’s favor, with at least one court stating that the defendant’s lost profit “merits little equitable consideration.” Some courts have held that the grey market benefits the public because the grey market importer can offer consumers the same goods as the authorized distributor, but at a lower price. In contrast, other courts have held that the Copyright Act promotes the public interest in creativity by providing an economic reward for creative expression. If the injunction is denied, then the intent of the Act would be frustrated.

B. Impoundment of Goods and Documents

A plaintiff may request the impoundment of defendant’s goods. Under the Copyright Act, the court has discretion whether to im-

---

59 See supra notes 10-43 and accompanying text.
60 See supra note 19 and accompanying text.
61 See Selchow, 612 F. Supp. at 23.
64 See Helene Curtis, 560 F.2d at 1333.
pound the goods. The standard of proof required for impoundment varies, but at least one court has applied the criteria for issuing a preliminary injunction.

To meet this standard, the plaintiff must present complete information regarding the location, identity, and number of targeted products. Prior to the impoundment hearing, the plaintiff should obtain authorization from a surety company for a bond and should contact the U.S. Marshal's office to arrange for moving trucks and personnel. Because grey market goods generally appear identical to authorized goods, the plaintiff should petition the court for a field expert to accompany the Marshal during the impoundment to identify the goods subject to seizure.

In addition, the plaintiff may move to impound relevant documents in the defendant's possession. Document impoundment is authorized under the All Writs Act, which provides that the courts may issue "all writs necessary or appropriate in aid of their respective jurisdictions and agreeable to the usages and principles of law." Document impoundment can prove invaluable to the plaintiff. Through impoundment, a variety of documents often come to light—ones that might not otherwise surface in a request for production. A seal order should be obtained from the court to prevent the defendants from gaining advance knowledge of the documents sought.

C. Affirmative Defenses

In grey market copyright litigation, a defendant may assert a limited number of meritorious defenses.

1. First Sale Doctrine

Under the first sale doctrine, the buyer of legally-made copyrighted goods does not need the copyright owner's consent to sell to a secondary purchaser. In Columbia Broadcasting System v. Scorpio Music Distributors, Inc., the grey market importer argued that it was not a proper defendant because it did not directly import the goods from abroad. Rather, it transacted its business within the United States with an intermediary corporation. The court rejected this defense finding that the defendant had ordered the records from the intermediary with full knowledge of the importation problem. The
court noted that the plaintiff need not proceed against the intermediary corporation because a copyright holder may proceed against any member in the distribution chain.\textsuperscript{76}

2. Innocence of the Infringer

While not an actual defense to copyright infringement, innocence may reduce the amount of statutory damages, if damages are sought. Under the Copyright Act, the court has discretion to award damages for each work infringed within the statutory range of \$250 to \$10,000.\textsuperscript{77} Regardless of the number of infringements, the court makes only one statutory damage award for each work infringed. The \$10,000 ceiling may be lowered to \$100 in cases of innocent infringement.\textsuperscript{78}

IV. Fraud

In New York and New Jersey,\textsuperscript{79} grey market importers have been sued for fraud. The authorized distributors sought to rescind sales by grey market wholesalers abroad and sought to award the seller-manufacturer possession of the goods. The plaintiff, Johnson & Johnson Products, Inc., alleged that a buyer, who acquired grey market goods by fraud, took only voidable title to the goods. Thus, the defrauded seller-manufacturer had superior title and a right to recover possession of the goods from anyone participating in the fraud. Johnson & Johnson maintained that it was entitled to recover possession of the goods from a subsequent purchaser who obtained the goods with knowledge of the fraud, or under circumstances that should have placed the purchaser on notice that its supplier might not have good title to the goods.

A. Preliminary Injunction

The critical determination in a grey market action based on fraud is the propriety of granting a preliminary injunction.\textsuperscript{80} In \textit{Johnson & Johnson Products, Inc. v. DAL International Trading Co.}\textsuperscript{81} the plaintiff claimed that DAL International Trading Company, a Polish state-

\textsuperscript{76} Id.
\textsuperscript{77} 17 U.S.C. § 504(c)(1) (1982).
\textsuperscript{78} Id. § 504(c)(2).
\textsuperscript{79} The New York case, Johnson & Johnson, Ltd. v. Allou Distributors, Inc., No. 85-3233 (E.D.N.Y. filed Nov. 7, 1985), is presently in the discovery stage. Johnson & Johnson has alleged that the grey market distributor is a third-party tortious converter of the goods that were obtained by fraud. No injunction was sought since the goods had already been distributed to retailers and were no longer in the distributor's possession. Johnson & Johnson, however, was successful in obtaining an injunction in \textit{DAL Int'l}, No. 85-3966, which is currently on appeal.
\textsuperscript{80} The criteria for a preliminary injunction is the same as in an action brought under trademark or copyright infringement law.
\textsuperscript{81} No. 85-3966, slip op. at 2 (D.N.J. Aug. 22, 1985).
owned trading agency, ordered large quantities of Johnson & Johnson "Reach" toothbrushes and baby products. An export manager, who negotiated the transaction, testified that Johnson & Johnson intended the goods be used only in Poland—not resold for distribution in the United States.  

Johnson & Johnson contended that the goods destined for the Polish market were not identical to those destined for domestic distribution. For example, the plaintiff's baby products designated for domestic distribution were packaged with tamper-resistant "Quality Seals." These "Quality Seals" were part of Johnson & Johnson's efforts to restore the confidence of U.S. consumers after tampered Tylenol surfaced in the U.S. market in 1982. Johnson & Johnson claimed that similar precautions were not required for goods to be distributed abroad.

In addition, Johnson & Johnson alleged that its baby products were formulated to appeal to consumer tastes in foreign markets, which differed from the domestic market. Plaintiff further claimed that marketing and sales costs were much lower in Poland, which permitted plaintiff to sell its products in the Polish market at less than the wholesale price. The price reduction was justified, however, only if the products would not be resold in markets where Johnson & Johnson had substantial marketing and sales costs.

Next, plaintiff set forth the steps that the defendants allegedly went through to perpetrate the fraud. The Polish buyer sought the approval and registration of the goods with regulatory authorities in Poland, which was required if the goods were to be used in that country, to foster the impression that the buyer intended the goods for Polish consumption. The goods were loaded onto the Polish buyer's trucks in West Germany and shipped through East Germany to the Polish border. At the border, the trucks turned around and proceeded to Belgium, where the goods were loaded onto vessels bound for New Jersey. Then the goods were shipped to the grey market wholesaler's warehouse in New York, where the manufacturer's production code numbers were stripped off the cartons.

Finding that Johnson & Johnson would likely prevail on the issue of fraud, the court granted plaintiff's motion for a preliminary injunction. The court held that the grey market distributor could not claim to be a good faith purchaser; therefore, because the grey market importer had closed its eyes to circumstances surrounding

---

83 Id.
84 Id. at 6.
85 Id. at 7.
86 DAL Int'l, No. 85-3966.
the transaction that "cried out for inquiry," the grey market importer only acquired voidable title. These circumstances included: (1) the low price of the goods, (2) the stripped production codes, and (3) the grey market distributor's unfamiliarity with the grey market wholesaler.

The court also found that the grey market goods would harm Johnson & Johnson's sales and distributor relations. This damage would be impossible to evaluate with "any degree of accuracy." Moreover, plaintiff would also lose its statutory right to rescission.

In the court's view, the public interest in discouraging fraudulent conduct outweighed any consumer interest in purchasing Johnson & Johnson products at low prices.

B. Affirmative Defenses

Because Johnson & Johnson represents the first attempt by a manufacturer to stop the influx of grey market goods through an action based on fraud, the availability of affirmative defenses in this area is undetermined. However, certain defenses, if proven, may apply to such a claim. These defenses are claims of a good faith purchaser for value and an overriding public interest.

1. Good Faith Purchaser Status

To qualify as a good faith purchaser for value under section 2-403(1) of the Uniform Commercial Code, a merchant must show honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade.

The Johnson & Johnson court found that the circumstances of the transaction "cried out for inquiry" as to the origin of the goods. The court stated that the defendant failed to make such an inquiry and had deliberately insulated itself from the truth. This behavior, the court noted, does not confer the status of bona fide purchaser.

2. Public Interest Considerations

The court further found that public interest considerations would not preclude injunctive relief. The court observed that "an injunction will prevent the public from buying genuine, quality products at lower prices, but on the other hand, in the long run the public will surely benefit from implementation of a rule of law which dis-

---

87 Id. at 24.
88 Id.
89 Id. at 26.
90 Id. at 27.
92 DAL Int'l, No. 85-3966 at 24.
courages fraudulent conduct."\(^{93}\)

V. Racketeering

Although no grey market case has been decided on racketeering grounds, some courts have indicated that the Racketeer Influenced and Corrupt Organizations Act (RICO)\(^ {94}\) may provide a basis for obtaining injunctive relief and civil damages. RICO\(^ {95}\) makes it unlawful for any person associated with an enterprise affecting interstate commerce to conduct the enterprise's affairs through a pattern of racketeering activity.\(^ {96}\)

An instructive case in this area is Fieldcrest Mills, Inc. v. Congo Agencies, Inc.,\(^ {97}\) in which the court held that Fieldcrest Mills stated a cause of action under RICO.\(^ {98}\) Fieldcrest, the manufacturer of "Royal Velvet" towels, alleged that Congo Agencies induced Fieldcrest to sell over $650,000 worth of Royal Velvet towels to Congo at a discounted price. Congo's executive officer represented that the towels would be sold in Central and West Africa. According to its complaint, Fieldcrest desired to expand its foreign market; thus it was willing to sell the towels at prices substantially below those offered to direct domestic retail customers. Instead, the towels were allegedly sold at a substantial discount at defendant's domestic retail outlets in the United States. According to Fieldcrest, Congo never intended to export the Royal Velvet towels. Defendants allegedly devised a scheme in which Congo could purchase the towels at the reduced rate for foreign markets, then sell them in the United States. Fieldcrest sought permanent injunctive relief as well as monetary damages.\(^ {99}\)

The district court broadly interpreted RICO and denied defendant's motion to dismiss the RICO counts. The court stated that the statute did not require a distinct "racketeering injury" as a prerequisite to recovery.\(^ {100}\)

The court also rejected the defendants' claim that a RICO civil action required a prior criminal conviction for the underlying predicate act.\(^ {101}\) The court held that Fieldcrest adequately alleged the existence of an "enterprise" as required in section 1962(c) by claiming that the U.S. distributor was an active participant and direct beneficiary of the scheme to defraud Fieldcrest.\(^ {102}\)

---

\(^{93}\) Id. at 27.
\(^{95}\) Similar state RICO statutes have been enacted in over 24 states.
\(^{97}\) No. 85-305 (D.N.J. filed April 8, 1985) (order denying motion to dismiss).
\(^{98}\) The Fieldcrest case is currently in the discovery stage of litigation.
\(^{99}\) Fieldcrest, No. 85-305 at 3.
\(^{100}\) Id. at 7.
\(^{101}\) Id. at 10.
\(^{102}\) Id. at 11.
found that Fieldcrest adequately alleged that the defendants con-
spired to assist in the enterprise’s corrupt activities.\textsuperscript{108}

Because no case has been decided on RICO grounds, the effect-
iveness of a civil RICO claim cannot be determined.\textsuperscript{104} Plaintiffs
have alleged racketeering violations in other grey market cases, but
the cases were usually decided on trademark infringement
grounds.\textsuperscript{105} If applicable to the facts of the case, affirmative defenses
and counterclaims based on antitrust law may constitute valid de-
fenses in a RICO action.\textsuperscript{106}

VI. Dilution

Anti-dilution statutes protect not only commercial goodwill, but
also the selling power a distinctive mark engenders in the consuming
public’s mind.\textsuperscript{107} Over twenty states provide a statutory remedy for
trademark dilution.\textsuperscript{108} The elements of the parties’ competition and
confusion about the product’s origin, are not needed for recovery.\textsuperscript{109}
Anti-dilution statutes provide a cause of action distinct from other
state law actions for trademark infringement and unfair competition.
The parties’ competition and consumer confusion are not elements
of the claim; thus a plaintiff need not prove them to recover.\textsuperscript{110}
Under pendent jurisdiction, plaintiffs may assert various state claims
in grey market cases that are litigated in federal courts.

In \textit{Sally Gee, Inc. v. Myra Hogan, Inc.}\textsuperscript{111} the court considered a
cause of action based on an anti-dilution statute. The court affirmed
the lower court’s refusal to grant injunctive relief because the plain-
tiff failed to “set forth some proof that its marks conjure up images
of its clothing in the minds of the consuming public in order to es-
tablish associational qualities entitling it to protection from dilu-
tion.”\textsuperscript{112} The record did not contain any evidence that the use of
defendants’ “Sally Lee” name on expensive women’s clothing would

\begin{footnotes}
\footnotetext{103} Id. at 16.
\footnotetext{104} A criminal RICO claim was alleged in United States v. Weinstein, 762 F.2d 1522
(11th Cir. 1985), in which the court found sufficient fraudulent acts committed by a grey
market pharmaceutical enterprise to support conviction of the participants under the fed-
eral RICO Act.
\footnotetext{105} For example, the plaintiff in \textit{Osawa}, 589 F. Supp. at 1163, alleged a RICO claim,
but the court held for the plaintiff on trademark infringement grounds.
\footnotetext{106} For a discussion of antitrust defenses, see supra notes 44-47 and accompanying
text.
\footnotetext{107} Pattishall, \textit{Dawning Acceptance of the Dilution Rationale for Trademark—Trade Identity
\footnotetext{108} See Dallas Cowboys Cheerleaders, Inc. v. Pussycat Cinema, Ltd., 604 F.2d 200, 205
n.8 (2d Cir. 1979).
\footnotetext{109} Allied Maintenance Corp. v. Allied Mechanical Trades, Inc., 42 N.Y.2d 538, 544,
\footnotetext{110} See Note, Trademark—368-d Dilution Relief in New York—Abandoning the Confu-
\footnotetext{111} 699 F.2d 621 (2d Cir. 1983).
\footnotetext{112} Id. at 626.
\end{footnotes}
likely blur plaintiff’s “Sally Gee” product identification in low-cost, ready-to-wear items. The court declined to determine whether the “Sally Gee” mark was sufficiently distinct to warrant protection under the anti-dilution statute because Sally Gee could not prove any damage to its reputation by Sally Lee’s handmade, higher-priced, and higher quality clothing.\(^\text{113}\)

In *El Greco Leather Products Co. v. Shoe World, Inc.*\(^\text{114}\) New York’s anti-dilution statute was specifically held inapplicable. *El Greco* cited *Sally Gee*\(^\text{115}\) stating that the concept of dilution is nebulous and usually characterized as a “whittling down” of the identity or reputation of a trade name. While the plaintiff’s trademark was distinctive, the court noted the plaintiff offered no proof of dilution caused by the defendant’s acts.\(^\text{116}\) To prevail on a dilution theory, a plaintiff must show that he has suffered a distinct “dilution” injury which tarnishes its reputation.

**VII. Conclusion**

Because no single body of law governs all grey market cases, grey market litigation draws upon related doctrines for analytical theories to be applied. Litigants should allege as many alternative theories as possible, consistent with the facts of each case. They should keep in mind, however, that a grey market case will generally be decided on the basis of its facts, with success usually being achieved by the party best able to present facts in support of its theory of the case.

\(^{113}\) Id. at 625-26.
\(^{114}\) 599 F. Supp. 1380.
\(^{115}\) 699 F.2d 621.
\(^{116}\) *El Greco*, 599 F. Supp. at 1395.