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Parallel Trade and Exhaustion of Intellectual Property in WTO Law Revisited

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ABSTRACT

Parallel importation and reimportation amount to the most important and unresolved classical problem of intellectual property protection within the multilateral trading system of the World Trade Organization (WTO). The welfare effects of restricting trade due to national or regional exhaustion of intellectual property rights are controversially discussed, and empirical evidence is not conclusive. Facts differ in different sectors of the global economy. The law is unsettled in squaring the Trade-Related Aspects of Intellectual Property Rights (TRIPS) Agreement and in particular the General Agreement on Tariffs and Trade (GATT 1994). This chapter explores the relationship between these agreements in international law. It concludes that WTO law undermines the operation of national and regional exhaustion. These two doctrines are overbroad and cannot apply across the board. Other less intrusive trade policy instruments are available to address legitimate concerns raised in the context of parallel importation and reimportation of original products. The multilateral trading system in result is simply and essentially based upon exhaustion while allowing for sectorial control and limitations of parallel trading by other means.

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A. INTRODUCTION

Ubiquity is perhaps the most characteristic feature of intangible intellectual property (IP) rights to exclusive information. These rights to control information are inherent in all products (goods and services) protected by IP, whatever their physical or immaterial form. They follow the fate of the product and create legal uncertainty in downstream operations related to the sale and use of these products.

To what extent should a rightholder define the fate of products on the market? To what extent should the rightholder be able to control secondary markets and the parallel importation of original products on different markets, making good use of

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price differentiation? There is no doubt that the rightholder is entitled all along to protect products from piracy and counterfeiting and the use of property without consent, including products produced under compulsory licensing. The need to provide legal security in downstream markets, however, led to the limitation of proprietary rights up to the first sale of the product. Rightholders decide how and when to market a particular product. Once the product is placed on the market, rights to control the marketing of the particular products entailing IP end. This is what we call 'exhaustion of rights' (*épuisement*, *Erschöpfung*).[1] The first sale doctrine, used in the United States, deploys similar effects. An alternative approach was implied licensing, originally used in common law, which addressed legal security by presuming the absence of restrictions imposed on buyers of products protected by IP rights.

Today, the principle of exhaustion of IP rights is universally recognised within the multilateral trading system and is codified in Article 6 of the TRIPS Agreement of the WTO, which entered into force in 1995, but without legally defining the principle.[2] The precise scope of exhaustion in relation to sale and licensing agreements is a matter of domestic law.[3] In digital trade, the contours are blurred. Exhaustion raises new difficult and unresolved issues – which call into question the principle of exhaustion in the first place.[4]

[1] See generally Shuba Ghosh and Irene Calboli, *Exhausting Intellectual Property Rights: A Comparative Law and Policy Analysis* (Cambridge: Cambridge University Press 2018); Irene Calboli and Edward Lee (eds.), *Research Handbook on Intellectual Property and Parallel Imports* (Cheltenham: Edward Elgar 2016); Josef Drexl, EU Competition Law and Parallel Trade in Pharmaceuticals: Lessons to be Learned for WTO/TRIPs? in Jan Rosén (ed.), *Intellectual Property at the Crossroad of Trade* 24 (Cheltenham: Edward Elgar 2012); Guido Westkamp, Emerging Escape Clauses? Online Exhaustion, Consent and European Copyright Law in Rosén, id., 38–66; Christiane Freytag, *Parallelimporte nach EG- und WTO Recht: Patente und Marken versus Handelsfreiheit* (Berlin: Dunker & Humblot 1999); Christopher Stothers, *Parallel Trade in Europe: Intellectual Property, Competition and Regulatory Law* (Oxford: Hart 2007); Santanu Mukherjee, The Doctrine of Exhaustion in Patent Law and International Trade Regulation, PhD University of Bern 2020 (publication forthcoming through Leiden/Boston: Brill 2022); Frederick A. Abbott, Thomas Cottier, and Francis Gurry, *International Intellectual Property in an Integrated World Economy* 99–102, 250–262, 494–516, 711–733 (New York: Wolters Kluwer 4th ed. 2019). The potential implications of various most recently published contributions in Robert D. Anderson, Nuno Pires de Carvalho, and Anthony Taubman (eds.), *Competition Policy and Intellectual Property in Today's Global Economy* (Cambridge: Cambridge University Press 2021) regrettably could not be taken into account in this chapter, which was completed by March 2020.

[2] Agreement on Trade-Related Aspects of Intellectual Property Rights entered into force on 1 January 1995, as amended on 23 January 2017; www.wto.org/english/docs_e/legal_e/legal_e.htm (accessed 2 March 2020).

[3] See, for example, for the USA, Andrew T. Dufresne, The Exhaustion Doctrine Revived? Assessing the Scope and Possible Effects of the Supreme Court's Quanta Decision, 24 *Berkeley Technological Law Journal* 11–48 (2009) discussing the relationship of exhaustion and licensing to the sale conditions in US case law; John F. Duffy and Richard Hynes, Statutory Domain and the Commercial Law of Intellectual Property, 102 *Virginia Law Review* 1–77 (2016), discussing the roots and scope of exhaustion in US law.

[4] Reto M. Hilty, 'Exhaustion' in the Digital Age in Calboli and Lee (n 1) 64–82.

What has remained controversial ever since the term was introduced by Joseph Kohler in 1878[5] is the geographical scope of exhaustion. Does it merely apply to first sales within a particular national jurisdiction? Or do rights exhaust independently of where a product has lawfully been introduced into the market? The dichotomy of national exhaustion and international exhaustion has ever since dominated the discourse and policymaking, with both legislators and more frequently courts of law defining the concept domestically and for different forms of IP protection.

With the advent of the European Economic Community (EEC) and today's European Union, and the combination of national and international exhaustion that emerged with the doctrine of regional exhaustion or community-wide exhaustion, international exhaustion is applied among the Members of the Union, whereas national exhaustion is applied to third states and the rest of the world. The linkage of international trade law and IP was first established by means of applying the disciplines of European competition law, addressing the segregation of markets on the basis of trademark and patent law. The founding and leading case of *Grundig/Consten* in 1966 is a landmark not only for competition law but also in defining the relationship between trade law and IP law.[6] Subsequent case law placed the issue of exhaustion under the umbrella of free movement of goods.[7] Exhaustion was subsequently extended to the European Economic Area (EEA), but not to other free trade agreements or economic cooperation agreements concluded by the Union worldwide. The concept, somewhat astonishingly, has not become an essential part of the TRIPS-plus provision in preferential trade agreements in fostering freer trade and abolishing barriers to international trade.[8]

The geographical scope of exhaustion is of critical importance in dealing with parallel imports in international trade. We understand this term to refer to the trade of original products placed on the market by the rightholder in a different national

[5] Josef Kohler, *Deutsches Patentrecht: systematisch bearbeitet unter vergleichender Berücksichtigung des französischen Patentrechts*, 2 vols., (Mannheim: J. Bensheimer 1878) 100 para 56, based upon implied licensing; Joseph Kohler, *Handbuch des deutschen Patentrechts in Rechtsvergleichender Darstellung* 457 (Mannheim: J. Bensheimer 1890), rejecting the implied licensing doctrine as insufficient to englobe non-contractual relations; see Westkamp (n. 1) 38–39.

[6] Cases 56 & 58/64 *Établissements Consten S.à.R.L. and Grundig-Verkaufs-GmbH v. Commission of the European Economic Community* (Consten and Grundig) [1966] ECR 299, ECLI:EU:C:1966:41. Subsequent case law confirmed the finding that agreements restricting parallel trade violate Article 81(1) EEC. See generally Valentin Korah, The Interface between Intellectual Property and Antitrust: The European Experience, 69 *Antitrust Law Journal* 801–839 (2002); Beatriz Conde Gallego, Intellectual Property Rights and Competition Policy in Carlos Correa (ed.), *Research Handbook on the Protection of Intellectual Property under WTO Rules*, vol. I 227–265 (Cheltenham: Edward Elgar 2010).

[7] For a discussion see, e.g. Stothers *supra* (n 1); see also *infra* (n 62).

[8] Thomas Cottier, Intellectual Property and Mega-Regionals Trade Agreements: Progress and Opportunities Missed in Stephan Griller, Walter Obwexer, and Erich Vranes (eds.), *Mega-Regional Trade Agreements: CETA, TTIP and TiSA* 151–174 (Oxford: Oxford University Press 2017).

jurisdiction and then reimported or exported to third markets in parallel to contractual distribution systems. Such trade is also called 'grey market' trade.[9] The term creates an aura of illegitimacy of such trade, allegedly facilitating counterfeiting and piracy; however, grey market trade clearly needs to be distinguished from illegal activities and the trading of competing generic products.[10]

While national and regional exhaustion, on the one hand, allow for parallel trading and arbitrage within a particular nation and union, respectively, and foster competition, they also allow for barring the importation of such products placed on the market abroad or reimported from abroad. Such exhaustion excludes competition from these products and allows full price differentiation and market segmentation. These effects are based on the theory that IP rights only exhaust in relation to particular markets independently. International exhaustion, on the other hand, limits the scope of IP rights wherever geographically an original product was placed on the market with the consent of the rightholder, irrespective of national or regional jurisdiction. In effect, parallel imports, or reimports, cannot be barred by invoking exhausted IP rights. International exhaustion, in effect, fosters free trade and competition and reduces the effectiveness of price differentiation.[11]

The introduction of national exhaustion and eventually regional exhaustion brought about such effects domestically in the process of nation building and the creation of a single European market. These doctrines, however, fostered the enclosure of national markets in Europe, substantially contributing to what is called 'Fortress Europe'. One would expect that the multilateral trading system operates on the basis of international exhaustion, fostering free trade and competition in a globalising economy. Upon the adoption of the WTO agreements, efforts were made to strengthen international exhaustion, in particular in trademark law.[12] Reality and the law are far from achieving that, as industries have consistently

[9] E.g. Peggy E. Chaudry, Confronting the Gray Market Problem, 49 *Business Economics* 263–270 (2014).

[10] Note that import restrictions imposed on generic drugs in transit do not pertain to parallel trade but concern the problem of territoriality and extraterritorial reach of patent protection prior to exhaustion; see Abbott, Cottier, and Gurry (n 1) 299–302; Drexl (n 1) 19–23. For a detailed discussion, see Henning Grosse Ruse-Khan, *The Protection of Intellectual Property in International Law* 288–299, 308–313 (Oxford: Oxford University Press 2016). The problem relating to Article V GATT on goods in transit thus is not addressed in this paper.

[11] For a comprehensive discussion and argument for international exhaustion, see Sarah R. Wasserman Rajec, Free Trade in Patented Goods: International Exhaustion for Patents, 29 *Berkeley Technology Law Journal* 317–376 (2014); Mukherjee (n 1).

[12] See Frederick A. Abbott, First Report (Final) to the Committee on International Trade Law of the International Law Association on the Subject of Parallel Importation, 1 *Journal of International Economic Law* 607–636 (1998); see the ensuing declaration of 200, ILA, Declaration Regarding the Exhaustion of Intellectual Property Rights and Parallel Trade, adopted by the 69th Conference of the International Law Association, in particular para. 8, which '[r]ecommends that WTO Members recognize a doctrine of international exhaustion with respect to trade marked goods,' ILA, Report of the Sixty-Ninth Conference, London, 22–29 July 2000, 19–21 (London: ILA 2000).

lobbied governments and courts of law to foster national exhaustion, in particular in the field of patents, in order to effectively control national distribution systems and benefit from price differentiation, with a view to increasing profits and funding research and development.[13] As a result, the world faces a panoply of different regimes among countries, frequently even varying among different forms of IP protection.[14]

The European Union consistently and comprehensively applies regional exhaustion to all forms of IP rights.[15] Efforts by the Commission to adopt international exhaustion have failed. The US case law has resulted in international exhaustion for copyright and trademarks, and in 2017 it extended the doctrine to patent protection in *Impression Products* v. *Lexmark International*,[16] while the federal government (United States Trade Representative) continues to push for national patent exhaustion in trade negotiations. Japan has relied upon the doctrine of implied licensing.[17] China's law still seems to be unsettled regarding trademark and copyright exhaustion[18] but is based on international exhaustion in patent law.[19]

Few countries adopt international exhaustion across the board but rather differentiate among different forms. For example, upon completion of the Uruguay Round, New Zealand and Australia introduced international exhaustion in copyright and trademarks, albeit in varying modalities.[20] Switzerland applies international

[13] This is most prominent in patents and in pharmaceuticals in particular; see, e.g. Harvey E. Bale, The Conflicts between Parallel Trade and Product Access and Innovation: The Case of Pharmaceuticals, 1 *Journal of International Economic Law* 637–653 (1998); Patricia M. Danzon, The Economics of Parallel Trade, 13 *Pharmacoeconomics* 293–304 (1998); but also extends to copyright, Claude E. Barfield and Mark A. Groombridge, The Economic Case for Copyright Owner Control over Parallel Imports, 1 *Journal of World Intellectual Property* 903–939 (1998).

[14] Ghosh and Calboli (n 1) 56–136.

[15] Thomas Cottier and Matthias Oesch, *International Trade Regulation: Law and Policy in the WTO, the European Union and Switzerland* 945–952 (Cameron May / Staempfli (2005); for a more recent analysis of the case law, see Samuel Dobrin and Archil Chocia, The Concepts of Trademark Exhaustion and Parallel Imports: A Comparative Analysis between the EU and the USA, 6(2) *Baltic Journal of European Studies* 28–57 (2016).

[16] 137 US S. Ct 1532 (2017) reprinted in Abbott, Cottier, and Gurry (n 1) 253–256; prior rulings in the USA were based upon national exhaustion in patent law, *Fuji Photo Film v. Jazz Photo*, 249. F. Supp. 2d 434 (D.N. J. 2003).

[17] *BBS Kraftfahrzeug Technik AG and BBS Japan Inc. v. Rasimex Japan Inc.* Supreme Court Heisei 7(0) No. 1988 (1 July 1997), Judgment of Supreme Court No. 1198, (15 July 1997) 8–10, reprinted in Abbott, Cottier, and Gurry (n 1) 251–253.

[18] Daniel Chow, Exhaustion of Trademarks and Parallel Imports in China, 51 *Santa Clara Law Review* 1283 (2011). Fabio Ciapello, Parallel Imports: The Battle between the Safe and Cheap Imports, HFG Law and Intellectual Property (2019); www.lexology.com/library/detail.aspx?g=6c9c110c-863c-447d-a71b-a2ef2b893521 (accessed 29 February 2020).

[19] Wei Zhuang, Evolution of the Patent System in China in Frederick M. Abbott, Carlos M. Correa, and Peter Drahos (eds.), *Emerging Markets and the World Patent Order* 155 (Cheltenham: Edward Elgar 2013) reprinted in Abbott, Cottier, and Gurry (n 1) at 327, 334.

[20] For a comprehensive analysis of divergent approaches and experience of Australia and New Zealand in removing national exhaustion in copyright and trademarks, see Louise Longdin,

exhaustion in trademark and copyright but applies regional exhaustion in patent law, with the exception of national exhaustion of products subject to regulatory approval, especially pharmaceutical and agrochemical products.[21]

These examples show that doctrines of exhaustion are applied in line with economic structures and vested interests. Even developing countries, which are interested in attracting competing products, refrain from using international exhaustion across the board due to fears of undersupply and the growing interest of domestic producers that depend on IP protection. There is hardly a field in IP law which is more defined by market power and political representation of industries and traders than by rational choice in light of weakly organised consumers.

The Paris Convention for the Protection of Industrial Property and the Berne Convention for the Protection of Literary and Artist Works[22] do not address the problem of exhaustion of rights, and efforts to argue in favour of national exhaustion on the basis of territoriality of IP protection are not conclusive one way or the other. Territoriality of rights does not exclude considering facts produced abroad and assessing them legally for the purpose of domestic effect (as we prominently know from competition law). Arguments that the function of patent law and limited duration of rights, unlike trademark law, inherently call for national exhaustion have been refuted in the literature.[23] Articles 4bis(1) and 6(3) Paris Convention use the same concept of independence, and a different interpretation is not justified. Territoriality is limited to defining the existence and the scope of rights and their legal effects in a particular jurisdiction. It inherently includes the possibility of different regulations of exhaustion and thus the role of parallel importation.

With the advent of WTO law in 1995, conventional wisdom suggests that Article 6 of the TRIPS Agreement comprehensively deals with the issue of exhaustion of IP rights, leaving Member States of the WTO ample policy space to adopt suitable variants of the exhaustion doctrine commensurate with their needs, industrial structure and welfare policies, subject to the principles of national treatment and most-favoured nation (MFN) treatment.[24]

Parallel Importing Post TRIPS: Convergence and Divergence in Australia and New Zealand, 50 *International and Comparative Law Quarterly* 54–89 (2001).

[21] Cottier and Oesch (n 15) 952–964; IGE/IPI Parallel Imports and Exhaustion, www.ige.ch/en/law-and-policy/national-ip-law/patent-law/parallel-imports-and-exhaustion.html (accessed 29 February 2020).

[22] www.wipo.int/treaties/en/ (accessed 2 March 2020).

[23] For a discussion see Freytag (n 1) at 233.

[24] Graeme B. Dinwoodie and Rochelle C. Dreyfuss, *A Neofederalist Vision of TRIPS: The Resilience of the International Intellectual Property Regime* 138 (Oxford New York: Oxford University Press 2012). Note that recent major works on parallel importation do not address the impact of GATT 1994 and GATS, or the TBT Agreement of the WTO in specific chapters: Ghosh and Calboli; Calboli and Lee (n 1). The TRIPS Agreement is still considered by the epistemic community of IP scholars rather in isolation; see also Reto M. Hilty, Matthias Lamping, and Josef Drexl (eds.), *TRIPS plus 20: From Trade Rules to Market Principles* (Heidelberg, New York, Dordrecht, London: Springer 2016).

This paper argues that Article 6 TRIPS does not exhaust the issue of exhaustion and that other provisions and agreements within the multilateral trading system need to be taken into account in assessing the problem of parallel trading of products protected by IP rights. We set out with a brief analysis of pertinent TRIPS provisions, including the Paris Convention for the Protection of Industrial Property and the Berne Convention for the Protection of Literary and Artistic Works. The main focus is on the impact of GATT 1994 and the General Agreement on Trade in Services (GATS). Finally, we look at preferential trade and cooperation agreements beyond the realm of the European Union.

In doing so, we keep in mind that important sectors are subject to strict governmental regulation, in particular pharmaceutical and chemicals. We also keep in mind that the control of and enforcement related to parallel trade are increasingly difficult in the age of electronic commerce and digital trade,[25] while security interests in trade are increasing. The doctrines of national and regional exhaustion imply that parallel importation can be effectively controlled and stopped at borders and within jurisdictions, which is increasingly difficult. Monitoring cross-border flows of goods in retail is thus increasingly difficult, and it is almost impossible for non-physical products and digitally traded services. Preventing and limiting parallel trading by taking recourse to contractual and non-contractual policies of companies to segment markets and to achieve price differentiation become more important.

The field has increasingly shifted to disciplines of competition policy, which still lack global standards and operate under the influence of major jurisdictions, in particular the United States and the European Union. IP protection in turn needs to focus on combating counterfeiting and piracy. However, these are distinct from parallel trade, albeit often termed 'grey' and allegedly difficult to separate.

This paper concludes that WTO law undermines the operation of national and regional exhaustion. These doctrines are overbroad and cannot apply across the board. Other less intrusive trade policy instruments are available to address legitimate concerns raised in the context of parallel importation and reimportation of original products. The multilateral trading system is, in result, simply and essentially based upon exhaustion while allowing for sectorial control and limitations of parallel trading by other means. The WTO law revisited offers a more solid ground than national and regional exhaustion in the age of cyberspace and the digital economy. Whether or not the issue discussed in the paper will eventually be litigated in the WTO is of secondary importance. The analysis of WTO allows for formulating new approaches to an age-old problem in the process of policy formulation and law-making.

The paper thus makes a contribution to the interface and interaction of different international agreements. In doing so, it is hoped that the paper may also contribute to countering the tradition of there being divergent epistemic academic

[25] Ghosh and Calboli (n 1) at 163 et passim.

communities in law – IP, commercial law, competition law, and trade and public international law – in discussing exhaustion and parallel trade. The problem requires a holistic approach.

B. THE IMPACT OF WTO LAW

With the advent of the TRIPS Agreement, IP standards were introduced in the multilateral trading system of the WTO. While IP so far had been limited to restricting trade under the exceptions, it now became a constituting pillar of the multilateral trading system.

The TRIPS Agreement substantially enlarged the rules on IP, but did not remove the potential relevance of other agreements within the system – and of public international law in general.[26] Intellectual property rights are partly addressed in Article IX and Article XX(d) of GATT, and the TRIPS Agreement did not remove the existence of these provisions.[27] There was no intention in the negotiations on IP to reduce existing GATT obligations. The preamble of the TRIPS Agreement explicitly recognises in para. (a) 'the applicability of the basic principles of GATT 1994'. TRIPS is not part of Annex I, which prevails over GATT. Similarly, new agreements – such as GATS or the Agreement on Technical Barriers to Trade (TBT) and the Agreement on the Application of Sanitary and Phytosanitary Measures – may have a bearing on parallel trade issues.[28] They are not consumed by the provisions of the TRIPS Agreement on exhaustion of rights.[29]

It was argued that the TRIPS Agreement, in particular Article 6 on exhaustion, amounts to *lex specialis* which consumes, and exhausts, so to speak, related provisions of other agreements under the Vienna Convention of the Law of

[26] Thomas Cottier, Embedding Intellectual Property in International Law, in P. Roffe and X. Seuba (eds.), *Current Alliances in International Intellectual Property Law-Making*, 15–44 (Geneva: ICTSD/CEIPI 2017).

[27] Section IV, on Article IX GATT see Japan – Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages (10 November 1987) GATT BISD 34/83 (1983).

[28] Thomas Cottier and Alexandra Leber, *Parallelimporte und technische Handelshemmnisse im Welthandelsrecht und im bilateralen Verhältnis der Schweiz zur EU: Das Beispiel der Pharmazeutika*, in Astrid Epiney, Andrea Egebunda-Joss, and Markus Wyssling (eds.), *Schweizerisches Jahrbuch für Europarecht /Annuaire Suisse de droit européen 2005/2006*, 327–345) (Zürich/Bern: Schulthess and Staempfli 2006).

[29] Thomas Cottier, The Exhaustion of Intellectual Property Rights – A Fresh Look [Editorial], 39 *International Review of Intellectual Property and Competition Law* 755–757 (2008); See also Thomas Cottier, Rachel Liechti, Die internationale Erschöpfung im Patentrecht, in Peter V. Kunz, Dorothea Herren, Thomas Cottier, René Matteotti (eds.), *Wirtschaftsrecht in Theorie und Praxis, Festschrift für Roland von Büren* 325–342 (Basel: Helbling und Lichtenhahn 2009). Chang-Fa Lo, Potential Conflict between TRIPS and GATT concerning Parallel Importation of Drugs and Possible Solution to Prevent Undesirable Market Segmentation, 66 *Food & Drug Law Journal* 73 (2011); Freytag (n 1) 236–251; Abbott (n 12).

Treaties (VCLT).[30] The doctrine applies to the treatment of the same subject matter, and the more specific and detailed rules apply.[31] However, the subject matter of defining IP rights and exhaustion on the one hand, and of parallel importation products placed on markets of different countries on the other, do not share the same object and angle. While the former defines the scope of rights, the latter deals with import or export restrictions. The former is based upon the nationality of the rightholder while the latter conceptually relies upon the geographical origin of goods traded, independently of the nationality of the rightholder. Of course, the two areas are closely interrelated, but conceptually they remain separate.

Issues of parallel trade thus exist legally independent of the doctrine of exhaustion. The problem of banning parallel importation in international economic law is therefore not one of conflicting norms but rather competing norms in different agreements, which need to be reconciled within the overall WTO system to the utmost extent possible.[32]

It is well established in WTO law and jurisprudence that several agreements may apply to a particular issue. For example, the assessment of plain packaging of cigarettes entailed the TBT, GATT, and the TRIPS Agreement. The examination of protection of trademarks and geographical indications in the European Union concerned both TRIPS and GATT provisions, in particular Article XX(d). One agreement does not consume the other, and neither occurs earlier or later in time.[33] The principle of *lex posterior* of Article 60 VCLT does not apply among WTO agreements. They all, including the substantive provisions of the Paris and Berne Conventions, entered into force on 1 January 1995 for the purpose of WTO law.

[30] Marco Bronckers, The Exhaustion of Patent Rights under World Trade Organization Law, 32 *Journal of World Trade* 1 (1998); Sue Frankel, Daniel Gervais, International Intellectual Property Rules and Parallel Imports, in Calboli and Lee (n 1) at 91 short of a detailed analysis; Luis Mariano Genovesi, The TRIPS Agreement and intellectual property rights exhaustion, in Carlos Correa (ed.)., *Research Handbook on the Protection of Intellectual Property under WTO Rules*, vol I 216–225, at 221/222 (Cheltenham: Edward Elgar 2010), arguing that this results from good faith interpretation under Article 31 VCLT and that the application of GATT would render Article 6 obsolete. The argument does not take into account the pertinent case law of panels and the Appellate Body. Drexl (n 1) concludes that that international exhaustion is not suitable for pharmaceuticals, yet without discussing the implications of GATT 1994.

[31] Henning Grosse Ruse-Khan, *The Protection of Intellectual Property in International Law* 42–44 (Oxford: Oxford University Press 2016). He offers a comprehensive review of the law and literature of norm conflicts in international law, id. 31–68. See also Joost Pauwelyn, *Conflict of Norms in Public International Law* (Cambridge: Cambridge University Press 2003); Graham Cook, *A Digest of WTO Jurisprudence on Public International Concepts and Principles* 61–65 (Cambridge: Cambridge University Press 2015) documenting a narrow understanding of norm conflict in WTO jurisprudence.

[32] Matthew Kennedy, *WTO Dispute Settlement and the TRIPS Agreement: Applying Intellectual Property Standards in a Trade Law Framework* 226–238 (Cambridge: Cambridge University Press); Chang-Fa Lo, (n 29).

[33] Australia – Certain Measures Concerning Trademarks, Geographical Indications and other Plain Packing Requirements Applicable to Tobacco Products and Packaging, WT/DS435/R, WT/DS441/R, WT/DS458/R, WT/DS467/R (28 June 2018) (under appeal).

Even looking at exhaustion and parallel trade in tandem does not exclude the potential application of WTO agreements beyond TRIPS. A particular regulation or measure may be consistent with one but not another of the agreements. In such cases, if a failure to comply with WTO law is found in one agreement and not the other, Members nevertheless are called upon to remedy domestic law and practices.[34] The more stringent rules apply.[35]

Each of the WTO agreements has its own internal balance, and provisions specifically relating to one agreement – such as Article 6 TRIPS or Article XX GATT and its interpretation – cannot simply be transferred and read into another agreement.[36] The provisions of these agreements mutually inform each other in the process of interpretation of particular rules.[37] They are context in the meaning of Article 31(3)(c) VCLT and need to be taken into account in construing particular provisions in one of the agreements. Thus, even if the reach of Article 6 is extended beyond the TRIPS Agreement to all WTO law, including GATT and GATS, the carve-out and exemption do not render other pertinent provisions of the multilateral trading system inoperable in assessing restrictions of parallel imports and reimportation. Henning Grosse Ruse-Khan convincingly argues that measures permissible under the TRIPS Agreement do not exclude that they are inconsistent with GATT obligations.[38] It will be seen that Article 6 TRIPS allows Members to choose different variants of exhaustion; it does not oblige them to do so, whereas they incur mandatory obligations under GATT.

[34] Canada – Certain Measures Concerning Periodicals, WT/DS31/AB/R (30 June 1997); EC – Regime for the Importation, Sale and Distribution of Bananas, WT/DS27AB/R (9 September 1997) both GATT and GATS applying; see generally Cottier and Oesch (n 15) 90–97.

[35] But see Grosse Ruse-Khan (n 30) 317, arguing that compliance with one agreement cannot amount to a breach of another WTO agreement.

[36] European Communities – Protection of Trademarks and Geographical Indications for Agricultural Products and Foodstuffs, WT/DS174/R (15 March 2005) para. 7.211 (Article XX GATT has no impact on the interpretation of Article 3.1. TRIPS); China – Measures relating to the Exportation of Rare Earth, Tungsten, and Molybem, WT/DS431/AB/R, DS432/AB/R, DS 433/AB/R (7 August 2014), para. 5.1–5.73 (Article XX GATT not applicable to Protocol of Accession); European Communities – Measures Prohibiting the Importation and Marketing of Seal Products, WT/DS400/Ab/R, WT/DS401/AB/R (22 May 2014) EC para. 5.310–513 (interpretation of Article 2.1. TBT Agreement cannot be readily adopted in the interpretation of Article XX GATT chapeau); see also EC – Measures Affecting Asbestos and Asbestos-Containing Products, WT/DS135/AB/R (12 March 2001) para. 80.

[37] While the TBT Agreement does not include a general exception clause, Article XX GATT nevertheless influences by means of preambular language in the TBT Agreement the interpretation of treatment no less favourable in Article 2.1. TBT, allowing one to assess whether treatment less favourable and unequal conditions of competition can be justified by legitimate policy goals and regulatory distinctions; United States – Measures concerning the Importation, Marketing and Sale of Tuna and Tuna Products (Article 21.5 DSU), WT/DS381/AB/RW (20 November 2015) para. 7.30.

[38] Id. 286 ('adopting measures allowed under TRIPS hence does not guarantee their consistency with GATT'), see also id. 308–320.

The integration of IP in the WTO multilateral trading system is not a formality and it does not lack implications for rights and obligations.[39] Squaring open trade and exclusive rights may lead to challenges of traditional perceptions and notions, just as it was seen above that the integration of IP in EU law and the single market substantially altered perceptions, in particular in the field of exhaustion.[40] It therefore is necessary to assess all pertinent provisions transgressing the TRIPS Agreement, to which we turn first.

C. THE TRIPS AGREEMENT

I. *Exhaustion (Article 6)*

The TRIPS Agreement of the WTO incorporates the substantive provisions of the Paris and Berne Conventions and sets minimal standards for the protection of IP in its different forms. It entails provisions on registration and enforcement of rights which Member States need to respect in domestic civil, administrative, and penal procedures.[41] In respect of exhaustion or rights, standards defined in Article 6 are minimal and essentially reflect an agreement to disagree. Efforts by Switzerland and the United States to anchor mandatory national exhaustion failed to the benefit of policy space of Member States in regulating exhaustion and thus the parallel importation of IP-protected products. Likewise, efforts to adopt international exhaustion by Australia, Brazil, India, and New Zealand equally failed.[42] Countries thus have remained free to operate exhaustion doctrines as they wish, even among different forms of IP.

Such policy space is secured by a carve-out from WTO dispute settlement. It was agreed that '[f]or the purpose of dispute settlement under this Agreement ... [n]othing in this Agreement shall be used to address the issue of exhaustion of intellectual property rights'. It is important to note that Article 6 does not grant Members a right under international law to select whatever doctrine of exhaustion they prefer. Nor does it impose adopting a particular variant of exhaustion. The carve-out remains subject to specific obligations within Article 6 and within the TRIPS Agreement and other WTO agreements, to the extent that they affect parallel importation, as discussed below.

[39] Cottier (n 26).

[40] *Supra* (n 6).

[41] Thomas Cottier, The Agreement on Trade-Related Aspects of Intellectual Property Rights, in Patrick F. J. Macrory, Arthur E. Appleton, and Michael G. Plummer (eds.), *The World Trade Organization: Legal, Economic and Political Analysis* Volume I 1041–1120 (New York: Springer 2005).

[42] See Daniel Gervais, *The TRIPS Agreement: Drafting History and Analysis* 112 (London: Sweet and Maxwell 2nd ed. 2003); Luis Mariano Genovesi, The TRIPS Agreement and Intellectual Property Rights Exhaustion, in Carlos M. Correa, *Research Handbook on the Protection of Intellectual Property under WTO Rules*, vol. I 216–225 (Cheltenham: Edward Elgar 2010).

The first exception to this carve-out was made within Article 6 for issues relating to Article 3 and 4, that is, national treatment and MFN treatment. Panels and the Appellate Body have jurisdiction to assess claims regarding unequal applications of exhaustion between domestic and foreign rightholders as well as those of different countries. They cannot assess otherwise the lawfulness of exhaustion under the TRIPS Agreement. The recognition of de facto discrimination in WTO law and under the TRIPS Agreement also includes neutral configurations of regulations which, however, in practical effect disadvantage foreign rightholders.[43] For example, an exhaustion regime which would allow domestic rightholders to import parallel traded goods without extending the privilege to foreign nationals and foreign-controlled companies is contrary to Article 6. National treatment issues, however, are unlikely to occur. Under national and regional exhaustion, rightholders trading domestically are treated less favourably than those trading with third countries, as domestic trade is subject to exhaustion while foreign trade is privileged, subject to more stringent rights under national or regional exhaustion within the overall framework.

More importantly, differential treatment of rightholders from different countries is inconsistent with Article 6. This raises the question of privileged treatment within a customs union or a free trade agreement commensurate to Article XXIV GATT and Article V GATS. The TRIPS Agreement does not provide for an equivalent of preferential trade exceptions, but defines in Footnote 1 'nationals' to include all natural and juridical persons domiciled within the separate customs territories (customs union) and irrespective of their nationality in the passport. It treats the Union, in other words, as a single entity for the purpose of the agreement. It allows applying international exhaustion among the Members of the union while applying national exhaustion to the rest of the world.

The same is true for the introduction in 2017 of regional exhaustion in the Eurasian Economic Union.[44] The European Court of Justice in *Silhouette* treated regional exhaustion as a mandatory rule, implying national exhaustion vis-à-vis third countries.[45] Rightholders within the European Union or the Swiss-Lichtenstein Customs Union[46] can be privileged in relation to foreign rightholders or companies domiciled abroad. At the same time, the footnote does not extend to free trade agreements, which by definition do not entail a single external tariff and do not

[43] European Communities – Protection of Trademarks and Geographical Indications, WT/DS174/R (15 March 2005) para. 7.185–7.204.

[44] Eurasian Economic Commission (EEC), Intergovernmental Council will permit 'parallel' importation for individual types of goods to the EAEU, 26.4. 2017; http://www.eurasiancommission.org/en/nae/news/Pages/26-04-2017.aspx (accessed 2 March 2020).

[45] Case C-355/96 *Silhouette International Schmied GmbH & Co KG v. Hartlauer Handelsgesellschaft*, [1998] ECR I 4799, ECLI:EU:C:1998:374.

[46] *Traité entre la Suisse et la Principauté de Liechtenstein concernant la réunion de la Principauté de Liechtenstein au territoire douanier suisse*, 29 March 1923 (RS 0.631.112.514); www.admin.ch/opc/fr/classified-compilation/19230011/index.html (accessed 2 March 2020).

qualify as separate customs territory. Early non-application of regional exhaustion to a European Free Trade Association free trade partner in *Polydor* thus is still in line with WTO law.[47] Privileges among Members, such as extending regional exhaustion to the Protocol 28 of the Agreement on the EEA[48] or introducing unilaterally regional exhaustion in the case of Switzerland, could therefore be challenged before the WTO.[49]

In *Maglite*, the EEA Court held that the doctrine of regional exhaustion of the EEA does not extend to third country relations but leaves EFTA States free to operate their own doctrines of exhaustion.[50] Hence, Article 6 TRIPS may partly explain why regional exhaustion has not been included in free trade agreements and modern comprehensive cooperation agreements – such as the Comprehensive Economic and Trade Agreement (CETA), the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTTP) and in preparations for the Transatlantic Trade and Investment Partnership (TIPP) between the European Union and United States.[51] The extension from national exhaustion to regional exhaustion would need to be extended to all rightholders of WTO Members under the MFN clause of Article 4 of the TRIPS Agreement, resulting in international exhaustion.

Finally, the question arises whether the carve-out of Article 6 only applies to international dispute settlement before the WTO or to judicial dispute settlement in general. The provision of Article 6 and the prohibition to address the issue of exhaustion does not extend to domestic courts, the application of the TRIPS Agreement potentially under a doctrine of monism and direct effect, or when taking considerations of exhaustion into account in the process of consistent interpretation of domestic law in line with obligations under international law.[52] Article 6 is relevant both in recognising the fundamental principle in the first place and in recognising the policy space granted. Importantly, the provision before domestic courts stands on the same footing as other provisions of the WTO, in particular GATT and GATS, which enjoy the same position in domestic law as the TRIPS Agreement. A domestic court thus would need taking into account, on par, all of WTO law.

[47] Case 270/80 *Polydor Ltd and RSO Records Inc. v. Harlequin Records Shops Ltd and Simons Records Ltd*, [1982] ECR 329, ECLI:EU:C:1982:43.

[48] OJ L 1, 3.1.1994, pp. 194–196.

[49] Thomas Cottier, Rachel Liechti, *Ist die einseitige statuierte regionale Erschöpfung im schweizerischen Patentrecht mit dem WTO-Recht vereinbar?* Rechtsgutachten erstattet dem Institut für Geistiges Eigentum Bern (5 October 2007); www.ige.ch/fileadmin/user_upload/andere/Juristische_Infos/d/j10071d.pdf, (accessed 2 March 2020).

[50] Case E-2/97 *Mag Instruments Inc. v. California Trading Company Norway*, Advisory Opinion (3 December 1997), [1997] EFTA Ct. Rep. p. 127.

[51] *Supra* (n 7).

[52] See Thomas Cottier, The Role of Domestic Courts in the Implementation of WTO Law: The Political Economy of Separation of Powers and Checks and Balances in International Trade Regulation, in Amrita Narlikar, Martin Daunton, and Robert M. Stern (eds.), *The Oxford Handbook on the World Trade Organization* 607–631 (Oxford: Oxford University Press 2012).

II. *Trademark Rights Conferred (Article 16)*

While Article 6 TRIPS addresses exhaustion, other provisions of the same agreement are otherwise important to the underlying issue of parallel trade and reimportation, bringing about a second exception to the carve-out. In defining the scope of trademark protection, Article 16(1) provides that '[i]n case of the use of identical sign for identical goods or services, a likelihood of confusion shall be presumed'. The provision facilitates combating counterfeiting and places the burden of proof on the defendant to rebut the presumption. In the case of parallel importation of original and identical products that are placed on the market abroad by the same multinational company and its subsidiaries, it can be readily demonstrated that there is no likelihood of confusion – in fact, that there is no confusion at law. As a consequence, trademark protection cannot be invoked, and the importation of such goods cannot be barred even under a doctrine of national or regional exhaustion. The particular configuration of importation of identical products placed on different markets by the same company and its subsidiaries therefore result in effect in applying the doctrine of international exhaustion in trademark law. The effect is in line with the International Law Association (ILA) recommendation to apply international exhaustion in trademark law[53] and a widespread practice to this effect in many countries.

The provision, however, also explains why multinational companies, while using the same trademark in different countries, modulate the physical property of products – such as coffee or chocolates – in terms of quality and composition in order to establish a likelihood of confusion, based upon which market segmentation and effective price differentiation can be achieved.[54] While Article 16 TRIPS introduces international exhaustion for identical products by the back door, so to speak, it is important to note that this merely amounts to a minimal standard which can be overcome by more stringent protection. Thus, the doctrine of regional exhaustion in EU law overrides the effect of Article 16 and allows companies to prevent and bar parallel trading into the European Union even of identical products under trademark law.[55]

Even within the European Union, protection goes further and undermines the regional exhaustion of rights. The Court of Justice ruled that the scope of trademark protection includes the aura of the environment of sales, thus barring the sale of luxury products to discount stores even by third parties.[56] It is examined below whether regional exhaustion and restrictive use are also consistent with GATT rules.

[53] ILA Res. No 2/2000 International Trade Law, London 25–29 July 2000, in particular para. 8. The recommendation was based upon the Report by F. M. Abbott *supra* (n 12).

[54] See also Section D.II.4.g. in this chapter.

[55] Freytag (n 1) 222–226.

[56] Case C-58/08 *Copad SA v. Christian Dior couture SA*, [2009] ECR I 3421, ECLI:EU:C:2009:260.

Yet, to the extent that domestic law does not settle the matter, parallel imports cannot be banned in accordance with Article 16 TRIPS, given the direct effect or consistent interpretation of domestic law.

III. *Patent Rights Conferred (Article 28)*

The minimal scope of patent rights under the TRIPS Agreement explicitly includes the importation of products. It was argued that the right to import inherently amounts to a doctrine of national exhaustion in patent law as minimal standards which cannot be undermined.[57] That point of view ignores that the right to import is subject to Footnote 6 of the TRIPS Agreement, which refers to the application of Article 6. Thus, the right to import is effective under doctrines of national and regional exhaustion but void whenever a country opts for international exhaustion in patent law.[58] Therefore, an obligation to national exhaustion cannot be established under the TRIPS Agreement.

IV. *Compulsory Licensing (Articles 31 and 31bis)*

Article 31(f) TRIPS Agreement limits compulsory licensing to predominantly serve the domestic market. The provision does not allow for export licensing, and exports to third countries where the product is protected can be stopped by the rightholder. Legally, such trade is not parallel trade as the product is not original and the rightholder has not consented to the licence and to marketing. Legally, rights are not exhausted. In result, the TRIPS Agreement allows one to fully bar the exportation of such products. An exception to this exists for trade in pandemic drugs. The implementation of the 2001 Doha Declaration on the TRIPS Agreement and Public Health brought about an elaborate and restrictive system of trading under compulsory licensing of pandemic pharmaceuticals, allowing the exportation of medicines under patent protection to developing countries in need.[59] Article 31bis of the TRIPS Agreement imposes strict conditions prohibiting the re-exportation of such products and thus bans trading of such products, with a view to securing adequate supplies within countries in need and avoiding price undercutting on third markets. The ban on trade is essentially based upon the fact that these transactions are based upon compulsory licensing to which the rightholder has not consented. Rights therefore are not exhausted, and trade restrictions are justified.

[57] Joseph Straus, Implications of the TRIPs Agreement in the Field of Patent Law, in Karl Friedrich Beier and Gerhard Schricker (eds.), *From GATT to TRIPs – The Agreement on Trade-Related Aspects of Intellectual Property Rights, 18 IIC Studies 192* (Weinheim: VHC 1996).

[58] See also Freytag (n 1) 219–221.

[59] Abbott, Cottier, and Gurry (n 1) 274–287.

V. *Control of Anti-competitive Practices (Article 40)*

WTO law and the TRIPS Agreement do not yet entail substantive standards on anti-trust and competition law. Article 40 of the TRIPS Agreement, however, carves out domestic law to restrict 'specifying in their legislation licensing practices or conditions that may in particular cases constitute an abuse of intellectual property rights having an adverse effect on competition in the relevant market'. The TRIPS Agreement and its standards, including Article 6, cannot be invoked to limit the scope of anti-trust rules defined in domestic law. Parallel imports and the exhaustion of IP rights may thus be addressed both in rules relating to voluntary licensing – as well as other conditions unrelated to licensing. The latter include the possibility of regulating parallel traded goods and reimportation, with a view to avoiding market segmentation and price differentiation and resulting, in effect, in the adoption of international exhaustion – which amounts to a third exemption from the carve-out of Article 6 TRIPS. It is recalled that the case law introducing regional exhaustion into EU law based upon the free movement of goods in the 1970s[60] was substantially founded on competition law. As discussed, *Grundig/Consten* addressed market segmentation based upon domestic trademark law – which, at the time in France, was based on national exhaustion.[61] While regional exhaustion was confirmed in the case law,[62] qualifications subsequently emerged in the field of pharmaceuticals because strong regulatory government involvement in the sector precluded free trade.[63] In *Sot Lelos/GlaxoSmithKline*, the Court held that the refusal to supply wholesalers in order to prevent parallel imports amounts to an abuse of dominant position under Article 82 EC (102 TEFU), unless it can be demonstrated that the volume ordered substantially surpasses the past volumes required to mainly supply

[60] Case 78/70 Deutsche Grammophon Gesellschaft mbH v Metro-SB-Großmärkte GmbH & Co KG. [1971] ECR 487, ECLI:EU:C:1971:59 (copyright); Case 15/74 *Centrapharm BV and Adrian Peijper v. Drug Sterling Inc.*, [1974] ECR 1147, ECLI: EU:C:1974:114 (patents); Case 119/75 *Terrapin (Overseas) Ltd. v. Terranova Industrie CA Kapferer & Co* [1976] ECR1039, ECLI:EU: C:1976:94 (trademarks).

[61] *Supra* (n 6).

[62] Case 19/77 *Miller International Schallplatten GmbH v. Commission* [1978] ECR131, ECLI: EU:C:1978:19; Joined Cases 32/78, 36/78 to 82/78 *BMW Belgium and Others v. Commission* [1979] ECR2435, ECLI:EU:C:1979:191.

[63] Opinion of Advocate General Jacobs 28 October 2004 (denying direct consumer benefits by pharmaceutical parallel trade due to state intervention) in case C-53/03 *Syfait and Others v. GlaxoSmithCline plc* [2005] ECR I-4609, ECLI:EU:C:2004:673, ECLI, EU:C:2005:333 (jurisdiction of completion authority to seek preliminary ruling denied). See Josef Drexl, Healing with Bananas – How Should Community Competition Law Deal with Restraints on Parallel Trade in Pharmaceuticals? in Josef Drexl, Reto. M Hilty, Laurence Boy, Christine Godt, and Bernard Remiche (eds.), *Technology and Competition – Contributions in Honour of Hanns Ullrich* 291 (Brussels: Larcier 2009); Andreas Heinemann, Intellectual Property Rights and Market Integration, in Steven Anderman and Ariel Ezrachi, *Intellectual Property and Competition Law: New Frontiers* 303–322 (Oxford: Oxford University Press 2011).

domestic markets.[64] Protection of parallel imports here is partly based upon protecting the single market of the European Union and partly based upon consumer welfare by allowing for lower prices, to the benefit of hospitals and health insurance. Accordingly, restrictions on parallel imports in pharmaceuticals were found justified if research funding suffers and price reductions are not passed on to consumers.

For similar reasons, the courts also endorsed the possibility of dual pricing in licensing agreements and thus restricting parallel trade. In doing so, the Court of First Instance (the General Court) relied on the rather economic approach of the Chicago School by justifying the implied restrictions to competition, whereas the European Court of Justice upheld the protection of competition as an institution and relied upon exceptions of Article 81(3) EC (Article 101(3) TEFU) to this effect.[65]

The problem arose in the first place due to regional exhaustion which no longer allows barring parallel trade within the Union. The quantitative test introduced in the pharmaceutical sector, given strong government intervention and price controls, amounts de facto to a limitation of regional exhaustion. It seeks to prevent parallel trading and does not affect independent parallel trade effectively taking place. Beyond the Union, and in relation to third countries, there is no need for such restrictions due to regional exhaustion and the possibility to bar parallel imports in the first place. But the test adopted to rely upon existing market shares and the possibility to refuse excess supplies, with a view to limiting parallel trade, amounts to trade restrictions – which is of interest also from the point of view of rules on trade in goods, in particular GATT 1994. It may offer a less intrusive measure than banning imports outright under national or regional exhaustion.[66] We should also note that the arguments made relating to innovation and welfare are independent of the geographical scope of exhaustion. They may also be applied, and even more so, under the doctrine of international exhaustion.

D. THE GENERAL AGREEMENT ON TARIFFS AND TRADE (GATT 1994)

I. *Quantitative Restrictions and National Treatment (Articles XI and III:4)*

Import restrictions on parallel trade in original products placed on markets abroad amount to quantitative restrictions, which in principle are outlawed by Article XI of the GATT: 'No prohibitions or restrictions other than duties, taxes and other charges, whether effective through quotas, import or export licences or other

[64] *Sot. Lélos kai Sia EE and Others v. GlaxoSmithKline AEVE Farmakeftikon Proïonton, formerly Glaxowellcome AEVE*, Joint Cases C-468/06 to C-478/06, [2008] ECR I 71 39, ECLI:EU:C:2008:504.

[65] Joint Cases 501/06, C-513/06, C-515/06 *GlaxoSmithKline Services and Others v. Commission and Others* [2009] ECR I 09291, ECLI:EU:C:2009:610.

[66] Section D.II.4.f. in this chapter.

measures, shall be instituted or maintained . . .'. Restrictions imposed at the border upon importation by measures enforced by customs authorities fall under this provision. Certain exemptions exist relating to agricultural products in Article XI (2). To the extent that regulations addressing parallel importation operate within Members upon importation, for example injunctions or damages awarded, they fall under the provision of national treatment in Article III(4) of the GATT, including border measures under the Note to Article III.

These rules apply irrespective as to whether goods imported are protected or not by IP rights. Hence, it is not necessary that measures applied to imported and domestic products are fully identical.[67] Substantive or procedural measures applying partly or exclusively to imported products, but not to domestically traded products, are dealt with as a violation of national treatment if they treat imported products less favourably than domestic like and competing products.[68] The doctrines of national and regional exhaustion, granting extended rights to rightholders, deploy such effects, whereas they are absent under international exhaustion, which treats imported and domestically traded products alike and does not entertain border measures focusing on the importation of products.

Matthew Kennedy submits a different view. He argues that IP protection (cum national or regional exhaustion) is controlled by Article III(4) GATT alone. Domestic regulation covers all laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation and distribution of imported and domestic like products. Domestic IP laws implementing the TRIPS Agreement, including Article 6, correspond to that description, including border enforcement under the Ad Article III Note, which may be taken to exclude the application of Article XI.[69] Kennedy applies the approach taken by the Panel on Sec 337 Trade Act to parallel importation. Seizure of goods applies to both imported and domestic products as 'consignments imported through unauthorised channels can ultimately be of either origin, as can the products that the right holder authorises for supply of the domestic market', leaving WTO Members to adopt exhaustion rules according to Article 6 TRIPS.[70]

[67] Note Ad Article III; European Economic Communities – Measures –Affecting Asbestos and Products Containing Asbestos, para. 891–8.92; 894–895, WT/DS/135/R (18 September 2000) (issue not appealed); India – Measures affecting the Automotive Sector para. 7.224, 2.296 WT/DS/R146R/WT/DS175/R (21 December 2001): 'In support of the conclusion that while Article III:4 and XI:1 deal with "imported products" and "importation" respectively, . . . the Panel wishes to note that it sees merit in the proposition that there may be circumstances in which specific measures may have a range of effects. In appropriate circumstances, they may have an impact both in relation to the conditions of importation of a product and in respect of the competitive conditions of imported products on the internal market within the meaning of Article III:4. This is also in keeping that the same measure may be covered by different provisions of the covered Agreements.' (para. 2.296) (issue not appealed).

[68] United States – Section 337 of the Tariff Act of 1930, L/6439 (16 January 1989), 36 Suppl. 346.

[69] Kennedy (n 32), 234–238.

[70] Id. at 236 referring to Bayle (n 13), Abbott (n 12), and Bronckers (n 30).

This approach allows for reconciling GATT and TRIPS rules, thereby avoiding tension and conflict. However, from the trade angle, it does not consider the fact that the seizure of parallel imports at the border, or upon importation, is based upon an extended scope of IP protection (right to import) which does not apply to domestic products, which affects the conditions of competition between foreign and domestic products. Under exhaustion in any of the variants, there is no right to ban the parallel trade of products first sold on the domestic market and traded parallel to authorised channels. Whether or not Article XI GATT applies to such bans and seizures, we therefore find that national and regional exhaustion grants treatment that is less favourable to imported like products and thus is contrary to Article III(4) GATT.

II. *Protection of Intellectual Property Rights (Article XX(d))*

Violations of the prohibition of import restrictions and of national treatment may be justified under the provision of Article XX GATT. Additional exemptions, besides Article XI:2, exist in Article XXI (discussed below) and the Agreement on Safeguards for temporary relief. Import restrictions of products protected by IP rights – such as patent, trademarks, geographical indications, or copyright – may in particular take recourse to Article XX(d) of the General Agreement:

> Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures:
>
> . . .
>
> (d) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement, including those relating to customs enforcement, the enforcement of monopolies operated under paragraph 4 of Article II and Article XVII, the protection of patents, trade marks and copyrights, and the prevention of deceptive practices;

It will be argued that the ban on parallel trade under national or regional exhaustion (permitted under Article 6 TRIPS) readily meets the test of Article XX(d) GATT. National and regional exhaustion form part of the domestic rules and regulations to be enforced, and the ban on parallel trade is necessary to implement the rule. The analysis under Article XX(d), however, is more complex and not limited to the rule of national or regional exhaustion, but extends to the objectives and rules of the overall domestic system of IP as informed by international law, in particular the TRIPS Agreement.[71] Article XX(d) entails a complex process of weighing and

[71] See also Kennedy n 32 at 240.

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balancing pertinent factors and interests at stake which transgress the specific rule on exhaustion.[72]

In assessing exceptions invoked under Article XX GATT, jurisprudence of panels and the Appellate Body first examine two requirements of the subparagraphs invoked, namely, scope and necessity or relatedness, and turn to the so-called 'chapeau' in the third step.[73] We therefore start with the analysis of paragraph (d), which in particular invokes the protection of IP and the prevention of deceptive trade practices. There are essentially two tests to comply with. First, the measures and regulations at hand must serve laws and regulations which are themselves compatible with the General Agreement. Second, the measures taken must be necessary. The Appellate Body set out the requirements in *Thailand – Cigarettes* as follows:

> 177. A Member will successfully discharge that burden and establish its Article XX (d) defence upon demonstration of three key elements, namely: (i) that the measure at issue secures compliance with 'laws or regulations' that are themselves consistent with the GATT 1994; (ii) that the measure at issue is 'necessary' to secure such compliance; and (iii) that the measure at issue meets the requirements set out in the chapeau of Article XX. Furthermore, when Article XX(d) is invoked to justify an inconsistency with Article III:4, what must be shown to be 'necessary' is the treatment giving rise to the finding of less favourable treatment. Thus, when less favourable treatment is found based on differences in the regulation of imports and of like domestic products, the analysis of an Article XX(d) defence should focus on whether those regulatory differences are 'necessary' to secure compliance with 'laws or regulations' that are not GATT-inconsistent.[74]

We note that the first requirement entails two components. First, laws and regulations must not be inconsistent with the provisions of GATT 1994. Second, the measure must be designed to secure compliance with such provisions, entailing an assessment of aptitude or capacity and thus the relationship of the two elements. Overall, Article XX(d) uses a three-step test. This essentially reflects an operation of the principle of proportionality, even though the term has not been explicitly used in WTO jurisprudence.[75]

1. Laws and Regulations Not Inconsistent with the Agreement

Until recently, the provision of Article XX(d) was rarely referred to and used, and the requirement to secure compliance with laws and regulations not inconsistent with

[72] For a detailed discussion see Henning Grosse Ruse-Khan (n 31) 305–319.

[73] United States – Import Prohibitions of Certain Shrimp and Shrimp Products, WT/DS58/AB/R (12 October 1998) paras. 115–121.

[74] Thailand – Customs and Fiscal Measures on Cigarettes from the Philippines WT/DS/371/AB/R (17 June 2011) para. 177.

[75] See Thomas Cottier, Roberto Echandi, Rachel Liechti-McKee, Tetyana Payosova, and Charlotte Sieber, The Principle of Proportionality in International Law: Foundations and Variations, 18 *Journal of World Investment & Trade* 628–672 (2017).

the GATT Agreement gave rise to confusion. How can this requirement be squared with the fact that the measure itself has been found inconsistent with Articles XI or III:4 of the GATT? In *Thailand – Cigarettes*, the Panel equated the measure found inconsistent under Article III to be relevant here and obviously engaged in erroneous circular reasoning,[76] while Thailand failed to properly identify the relevant measure to be realised by means of a rule inconsistent with Article III GATT, resulting in the failure of the defence.[77] In *Columbia – Textiles*, the Panel simply used its analysis under Article XX(a) on public morals and failed to complete the necessity test under Article XX(d). The finding was reversed by the Appellate Body.[78]

The measure imposed and found inconsistent with Article XI or III(4) needs to be distinguished from the laws and regulations which it implements. In the present context, consistency or inconsistency do not relate to the doctrine of national or regional exhaustion, or the ban on parallel importation, but to the laws and regulations which the doctrine of national or regional exhaustion and the ban of parallel imports serve to implement and realise. This point is sometimes misunderstood and also leads to the said circular reasoning in the literature.[79]

The rules at stake pertain to the domestic order. They may form part of international law as applied domestically, but cannot be those of others, for example partners of a free trade agreement.[80] Rules and regulations relate to conduct of kinds of actors, private or public, and encompass a broad range of measures.[81] The Appellate Body considers the list of areas addressed to be illustrative and thus open-ended.[82] In the case of IP, these are the rules relating to the scope of protection granted under domestic law to products protected as well as the very purpose of granting exclusive rights in these respective fields. Laws and regulations are not limited to specific functions but encompass the entire field subject to compliance. The Appellate Body held in *India – Certain Measures Relating to Solar Cells and Solar Modules*, referring to *Argentina – Financial Services*:

[76] Thailand – Customs and Fiscal Measures on Cigarettes from the Philippines WT/DS/371/AB/R (17 June 2011) para. 167.

[77] Id. para. 179.

[78] Columbia – Measures Relating to the Importation of Textiles, Apparel and Footwear, WWT/DS461/AB/R (7 June 2016) para. 5.133.

[79] E.g. Chang-Fa Lo, (n 29) at 80, ('[C]oncerning the exception under GATT Article XX:(d), although prohibiting parallel importation is about laws and regulations relating to the protection of patents, literally speaking it might not be easy to argue that such laws and regulations are not inconsistent with the provisions of the GATT 1994. It has already been indicated above that the prohibition of parallel importation is literally inconsistent with the provisions of Article XI.').

[80] Mexico – Tax Measures on Soft Drinks and other Beverages, WT/DS308/AB/R (6 March 2006) para 75, 77.

[81] India – Certain Measures Relating to Solar Cells and Solar Modules, WP/DS465/AB/R (16 September 2016) para. 6.6.

[82] Id. para 5.106

> 5.110 The Appellate Body has stated that a "measure can be said 'to secure compliance' with laws or regulations when its design reveals that it secures compliance with *specific rules, obligations, or requirements* under such laws or regulations". It is important, in this regard, to distinguish between the specific rules, obligations, or requirements with respect to which a measure seeks to secure compliance, on the one hand, and the objectives of the relevant 'laws or regulations', which may assist in 'elucidating the content of specific rules, obligations, or requirements' of the 'laws or regulations', on the other hand. The 'more precisely' a respondent is able to identify specific rules, obligations, or requirements contained in the relevant 'laws or regulations', the 'more likely' it will be able to elucidate how and why the inconsistent measure secures compliance with such 'laws or regulations'. Thus, in assessing whether an instrument constitutes a 'law or regulation' within the meaning of Article XX(d), a panel should also consider the degree of specificity or precision with which the relevant instrument lays down a particular rule of conduct or course of action within the domestic legal system of a Member, as opposed to simply providing a legal basis for action that may be consistent with certain objectives.[83]

Applied to the field of IP, and to competition in a broader sense, it follows that law and regulations are not limited to specific provisions but envisage compliance with the system of IP as a whole, entailing all its relevant components in the domestic law at hand. It is not a matter of exclusively focusing on the purpose and scope of patents, trademark copyright and other forms in isolation but rather of taking into account the broader purpose of these rights within the overall system of economic law. This includes the goals and principles providing their foundations as well as offering the balance of the interests of the different stakeholders involved – and which the principle of exhaustion is supposed to serve. This is the landscape which also provides the background for assessing the aptitude (or capacity) and necessity of the measure which was found to be inconsistent in the first place with the provisions of the GATT Agreement.

While the matter of object and purpose of IP rights in the context of para (d) has not yet been addressed in WTO jurisprudence, the European Court of Justice in applying similar restrictions under then Article 30 EEC Treaty (now Article 36 TFEU) held, in *Merck/Stephar*, as follows: 'It must be stated that in accordance with the definition of the specific purpose of the patent, which has been described above, the substance of the a patent right lies essentially in according the inventor an exclusive right of first placing the product on the market'.[84] The Court thus concluded that the importation of pharmaceuticals first marketed in a country short

[83] India – Certain Measures Relating to Solar Cells and Solar Modules, WP/DS465/AB/R (16 September 2016) para. 5.110, 5.111, referring to Argentina – Measures Relating to Trade in Goods and Services, WT/DS453/AB/R (14 April 2016) 6.203, fn 495 to para. 6.203, fn 505 para 6.208 (footnotes omitted).

[84] Case 187/80 *Merck & Co Inc. v. Stephar BV and Petrus Stephanus Exler*, [1981] ECR 2063 para. 9, ECLI:EU:C:181:180.

of patent protection into a Member granting such protection does not amount to a violation of the patent right. Article 36 TFEU does not entail the requirement of laws and regulations not inconsistent with the agreement. Applying the findings of the court to Article XX(d) GATT, it would read that the measure imposed – namely, banning importation – does not serve the purpose and scope of patent rights as recognised by the agreement.

The question is whether GATT law equally limits the function of patents and other rights to the right to define the first sale. We do not think so. The European Court of Justice ruled prior to the advent of TRIPS Agreement and prior to the harmonisation of patent law in the EU. The very purpose of patent law, and indirectly also of trademark and copyright law, is to reward for investments made and to allow appropriate compensation, which are necessary to incentivise investments in light of market failures otherwise existing in non-rivalrous and non-exclusive information markets. Borrowing from competition law, we also include the function of consumer welfare in this equation, which is inherent to the goals of IP. In assessing the functions of IP, the principles and objectives in Article 7 of the TRIPS Agreement, binding upon Members, must be taken into account as relevant context. That includes the promotion of technological innovation and the transfer and dissemination of technology 'to the mutual advantage of producers and users of technological knowledge and in a manner conducive to social and economic welfare, and to balance rights and obligations'. In addition, the principles set out allowing Members 'in formulating or amending their laws (not necessarily limited to IPRs) adopt measures necessary to protect public health and nutrition and to promote the public interest in sectors of vital importance to their socio-economic and technological development' need to be taken into account. Implicitly, this agenda also relates to human rights and the Sustainable Development Goals (SDGs). These measures also include appropriate disciplines against the abuse of IP rights (Article 8:2 TRIPS). A more complete mission statement would include product differentiation, preventing consumer deception (trademarks) and the promotion of cultural diversity and values (copyright). Finally, it should be added that combating counterfeiting and the use of IP without consent amounts to the major purpose of IP, albeit outside the realm of parallel trade in original goods.

The protection and enforcement of IP in domestic law must serve all these ends, which places IP in the broader framework of international economic law. It is not limited to defining the first sale of a protected product. Nor is it limited to the protection of investment, but serves the purpose of a multitude of goals fostering consumer welfare – which needs to be taken into account in balancing the partly competing interests at hand.

It would seem that these objectives and goals all are in line with the provisions of the GATT Agreement, as it broadly recognises the protection of IP rights in Article XX GATT and in Article IX recognises marks of origin as well as non-trade related concerns. Moreover, the objectives are in line with the TRIPS Agreement, the very

purpose of which is to provide such protection and define the scope of rights in greater detail. Whatever the regulation of parallel trading, it should support the goals and objectives set out above.

Under the rules of Article 31(3)(c) of the Vienna Convention on the Law of Treaties, the provisions of the TRIPS Agreement need to be taken into account in interpreting the notion of 'not inconsistent with this Agreement'. We therefore conclude that – unlike the limitation on first sale in EU law – the protection of investment and of consumer welfare is not inconsistent with the agreement and restrictions of trade compatible with the first condition under Article XX(d) GATT. We thus turn to the requirement of necessity of such measures.

2. Not Incapable to Secure Compliance with Laws and Regulations

Further specifying the requirements of Article XX(d), the Appellate Body held in *Korea – Various Measures on Beef* that the measure must be one 'designed' to secure compliance with the laws and regulations that are not inconsistent with some provisions of GATT 1994:

> 157 For a measure, otherwise inconsistent with GATT 1994, to be justified provisionally under paragraph (d) of Article XX, two elements must be shown. First, the measure must be one designed to 'secure compliance' with laws or regulations that are not themselves inconsistent with some provision of the GATT 1994. Second, the measure must be 'necessary' to secure such compliance. A Member who invokes Article XX(d) as a justification has the burden of demonstrating that these two requirements are met.[85]

In *India – Certain Measures Relating to Solar Cells and Solar Modules*, the Appellate Body elaborated on the requirement that the design must be capable of securing compliance with laws and regulations found consistent with GATT:

> 5.58 As to the first element of the analysis contemplated under Article XX(d), the Appellate Body has stated that the responding party has the burden of demonstrating that: there are 'laws or regulations'; such 'laws or regulations' are 'not inconsistent with the provisions of' the GATT 1994; and the measure sought to be justified is designed 'to secure compliance' with such 'laws or regulations'. An examination of a defence under Article XX(d) thus includes an initial, threshold examination of the relationship between the challenged measure and the 'laws or regulations' that are not GATT-inconsistent so as to determine whether the former is designed 'to secure compliance' with specific rules, obligations, or requirements under the relevant provisions of such 'laws or regulations'.[86]

[85] Korea – Measures affecting Imports of Fresh, Chilled and Frozen Beef, WT/DS/161/AB/R, WT/DS169/AB/R (11 December 2000) para. 177.

[86] India – Certain Measures Relating to Solar Cells and Solar Modules, WP/DS465/AB/R (16 September 2016) para. 5.58.

It is thus a matter of demonstrating a relationship between the measure challenged and the laws and regulations not inconsistent with GATT 1994, and assessing whether the measure is not itself 'incapable' to secure compliance with such laws and regulations – before necessity can be assessed. Capability and necessity thus amount to two elements otherwise assigned to the principle of proportionality in international and domestic law, but not deployed in WTO law.

The doctrine of exhaustion of IP rights clearly serves the purpose of defining the scope of rights and bringing about legal security in commerce related to products protected by IP. The issue before us is whether the same holds true for its geographical variants of national and regional exhaustion (both found to contravene Articles XI or III GATT), which enlarge the scope of rights compared to the domestic realm. Rightholders enjoy enlarged powers to control markets. The ban on parallel imports thus affects the balance of rights and obligations within the system of IP protection and its different forms to which laws and regulations in the present context relate. It was seen that all its objectives need to be taken into account and cannot be limited to the protection of investment and innovation. The dissemination of technology and consumer interests equally need to be considered.

Clearly, the right to ban parallel imports on the basis of national and regional exhaustion is capable of strengthening the position of rightholders – which explains the strong support for the right among industry. It is a different question whether banning parallel imports is equally capable of serving other goals and objectives of IP protection and of maintaining an overall balance between rightholders and users within the system. Resulting market segmentation and price differentiation may weaken the dissemination of products and of technology and potentially hamper consumer interests. At the same time, they may benefit consumer and public interests through fostering research capacities and output. The answers depend upon empirical studies on parallel importation.

It is interesting to observe the resemblance between the analysis here and the one undertaken under competition law to assess the limitations to sell or of a dual pricing system, both limiting parallel trade by selling restrictions.[87] All pertinent interests need to be considered in the examination and equation, and much will depend upon the finding regarding whether national or international exhaustion are equally beneficial for consumers and the public at large. It is at this stage that the economic analysis of parallel importation needs to be considered. Empirical studies have been scarce, and the field remains a somewhat grey area. The theoretical literature, led by Keith Maskus and Mathias Ganslandt, shows a complex configuration which strongly depends on the particularities of a sector and regulatory environment, including trade and transportation costs, and which does not lend itself to conclusions one way or another as to whether the prohibition of parallel

[87] Section C.V. and D.II.4.f. in this chapter.

trade is capable of producing welfare effects.[88] Parallel trade often takes place on the wholesale level, allowing for differentiated pricing in retail.

Much also depends on the findings regarding whether parallel trade produces these effects for consumers and the public at large and whether gains are passed on to society, for example in public health and insurance, or instead are substantially pocketed by parallel traders who free-ride and undermine the research capacities of rightholders. A ban might not be suitable to produce such effects in the context of regional integration. In the context of the European Union, national exhaustion of rights was – and will be – found unable to secure the goals of market integration and the creation of corresponding welfare effects, despite resisting industry interests. Empirical studies in pharmaceutical trade have confirmed this finding.[89]

A ban may be suitable among jurisdictions of great divergence and difference in economic and social development. In 1999, the National Economic Research Associates report on trademark exhaustion concluded that the introduction of international exhaustion in the European Union would have vastly divergent effects on different sectors.[90] The point is that the test of capacity and aptitude of a ban on parallel importation needs to be assessed on a case-by-case basis. The findings imply

[88] For a survey published in 2016 see Keith E. Maskus Economic perspectives on exhaustion and parallel imports, in Calboli and Lee (n 1) 106–124; Mathias Ganslandt and Keith E. Maskus, Intellectual Property Rights, Parallel Imports and Strategic Behavior, Research Institute of Industrial Economics, IFN Working paper No 704 (2007); Keith Maskus, Parallel Imports, 23 *The World Economy: Global Trade Policy* 1269–1284 (2000); Keith E. Maskus and Chen Yongmin, Parallel Imports in a Model of Vertical Distribution: Theory, Evidence and Policy, 7 *Pacific Economic Review* 319–334 (2002); Keith E. Maskus and Chen Yongmin, Vertical Price Controls and Parallel Imports: Theory and Evidence, 12 *Review of International Economics* 551–570 (2004); Kamal Saggi, Market Power in the Global Economy: The Exhaustion of Intellectual Property, 123(567) *The Economic Journal* 131–161 (2013), particularly focusing on interests to trade with developing countries and the impact of national and international exhaustion on export incentives of firms.

[89] 'The most frustrating feature of parallel imports for researchers is that data about them are extremely scarce and hard to locate', Maskus in Calboli and Lee (n 1) at 109; see for empirical data Matthias Ganslandt and Keith E. Maskus, *Parallel Imports of Pharmaceutical Products in the European Union, World Bank, Policy Research Paper* 2630 (Washington: The World Bank 2001), finding that prices of drugs subject to competition from parallel imports increased less than those of other drugs between 1995 and 1998, examining the impact of moving to regional exhaustion by Sweden upon joining the EEA. Roughly three-quarters of the effect is attributed to parallel imports and one-quarter to prices lowered by manufacturing firms. Tomaso Duso, Annike Herr, and Moritz Suppliet, *The Welfare Impact of Parallel Imports of Parallel Imports: A Structural Approach Applied to the German Market for Oral-Anti-diabetics, Düsseldorf Institute for Competition Economics*, Discussion Paper No 137 (Düsseldorf: Düsseldorf University Press 2014) found that parallel imports of oral anti-diabetic drugs at the time reduced the price of patented drugs by 11 per cent and did not have a significant effect on generic drugs. Parallel imports reduced the profits of original German producers by 37 per cent per year, but only a third of it is appropriated by the importers.

[90] 'Our analysis shows that the consequences of change are complex, and may vary considerably both between sectors, and between products within a sector. In our analysis, we have attempted to identify those factors that are likely to be important for different sectors', National Economic Research Associates (NERA) and SJ Berwin & Co, The Economic Consequences of the

that both national and regional exhaustion are conceptually overbroad as they also entail configuration where they are not capable of enforcing the laws and regulations of the domestic IP system.

For cases where the capacity of restrictions on parallel trading to secure compliance with the overall IP system, its rights, objectives, and principles is affirmed, we turn to the third test of necessity.

3. Necessary to Secure Compliance with Laws and Regulations

Necessity in terms of Article XX(d) GATT amounts to a demonstration that the measure is (i) indispensable to achieve the goals of said laws and regulations and (ii) that no reasonably available less intrusive alternative exists. In WTO case law, the burden of proof to show that the measure is not necessary lies with the claimant, challenging the ban on parallel trade and thus of national or regional exhaustion.

Necessity in the case law entails a process of balancing different interests and of assessing whether the measure is well calibrated to the cause and purpose. Interests of rightholders need to be balanced with public interests in securing adequate supplies at reasonable costs and in fostering competitive relations. For example, in pharmaceuticals, the interests of rightholders to recuperate investment and to fund research and innovation, shared with the health system and consumers, need to be balanced against the financial constraints of the health system and the interest of consumers and hospitals to foster competition and to have access to less expensive medication – which supports parallel traded original and generic products.

The Appellate Body held in *Korea – Various Measures on Beef* that balancing and weighing of these factors results in a determination of whether or not the measure is indispensable. The spectrum ranges from necessity in terms of indispensability to the quality of making a contribution to secure compliance with laws and regulations, taking into account the importance of public interests at stake:[91]

> 164 In sum, determination of whether a measure, which is not 'indispensable', may nevertheless be 'necessary' within the contemplation of Article XX(d), involves in every case a process of weighing and balancing a series of factors which prominently include the contribution made by the compliance measure to the enforcement of the law or regulation at issue, the importance of the common interests or values protected by that law or regulation, and the accompanying impact of the law or regulation on imports or exports.[92]

Choice of a Regime of Exhaustion in the Area of Trademarks: Final Report for DG XV of the European Commission, 8 February 1999, at 109.

[91] Korea – Measures affecting Imports of Fresh, Chilled and Frozen Beef, WT/DS/161/AB/R, WT/DS169/AB/R (11 December 2000) para. 161–162.

[92] Id. para. 164.

In *Argentina – Financial Services*, the Appellate Body recalled that in balancing these factors, the trade restrictiveness of the measure and the importance of laws and regulations to be enforced need to be considered. The analysis cannot be limited to an assessment of whether or not the measure involves some restrictions on trade.[93]

As a practical matter, is it up to the defendant to convincingly demonstrate that national or regional exhaustion is indispensable to – or at least contributes to – a secure return on investment as well as consumer welfare and other non-trade concerns mentioned above. Such demonstration can be readily provided in combating counterfeited and pirated products, as rights are not exhausted in the first place. Similarly, necessity can be demonstrated in the case of importation of products made under compulsory licensing for which IP does not allow for exportation, with the exception of pandemic drugs. Necessity is more difficult to demonstrate in the case of banning the import of original products.

Article 6 TRIPS is relevant in the context and needs to be considered in assessing necessity under Article 31(3)(c) of the Vienna Convention on the Law of Treaties. It has to be taken into account because it could inform the application and interpretation of Article XX(d) and the necessity test. WTO Members using national or regional exhaustion will argue that the ban on parallel imports is indispensable to enforce IP rights as defined in domestic law, which entails market segmentation and price differentiation. It will also be argued that GATT and TRIPS do not exclude the national and regional exhaustion of IP rights and that Article 6 TRIPS explicitly allows for these as a matter of policy space. But Article 6 TRIPS does not prejudice the answer. Neither is there a right and a requirement for Members to use these doctrines under international law, nor a prohibition to use them. As stated at the outset, Article 6 TRIPS does not consume the application of other WTO agreements, and exhaustion remains subject to the disciplines of other WTO agreements to the extent that they address parallel importation. In result, Article 6 does not dispense from demonstrating under Article XX(d) GATT that a ban on parallel importation is indispensable to secure the enforcement of IP protection.

The fundamental question therefore is whether any import restrictions are indispensable to protect the purpose of IP in terms of investment protection, advancing innovation, consumer welfare and the general interests of the public at large. If the restrictions are limited to protecting the right of first sale, as held in *Merck/Stephar* above,[94] it is evident from that logic that no restrictions are justified, resulting in the doctrine of international exhaustion. However, we look only at the right to first sale but also the system as a whole regarding the laws and regulations relating to IP. Hence, maximising rents by means of market segmentation, serving the dual goals of

[93] Argentina – Measures Relating to Trade in Goods and Services WT/DS453/A/R (14 April 2016) para. 6.234.

[94] *Supra* (n 84).

recuperating investment and making profit (with a view to fund research and further product development), must be balanced with public interests in terms of price competition, adequate supplies and access – all with a view to fostering consumer welfare.

Banning parallel trade amounts to the most restrictive trade measure available in terms of quantitative restrictions on importation. At the same time, it is unclear to what extent the measure, if enforced, contributes to welfare. Even in cases where the banning of imports shows such effects, it is doubtful that they outweigh the gains to the overall system of IP protection, innovation and the welfare of an economy. In addition, it should be noted that enforcement fully depends upon the initiative of the rightholder and is not enforced by government per se. This is yet another indication that the public interest at stake is of much lower weight than the trade restrictiveness of banning parallel importation in the first place.

Balancing these interests may result in different outcomes, depending on the industry and product involved. Again, recourse to economic analysis is required. The matter varies from case to case. Particular configurations may exist in the fields of pharmaceuticals and chemical products that are subject to regulatory approval and price controls, which need to be taken into the equation. There may be configurations where restrictions of parallel trade may be justified under the necessity test, making at least a contribution to the enforcement of laws and regulations. A ban on parallel trade found to be capable of securing compliance with IP protection is likely to pass the first test of necessity, as it makes at least a contribution to this effect, even though it is not indispensable to produce the welfare effects sought by laws and regulations. At the same time, the balancing test again shows and confirms that outright prohibitions of parallel imports under national or regional exhaustion, as applied to third countries, are overbroad as a matter of principle. They inherently include configurations where this requirement of necessity is not met. They per se do not stand the test of necessity under Article XX(d) in the abstract.

The second test of assessing whether reasonably less intrusive alternatives are available is more important in the present context. It is understood that – in line with the principle of proportionality – alternative measures inherently are deemed less intrusive than the measure challenged. The test faces the difficulty that the claimant needs to show what is good for another jurisdiction, while the government of the latter insists that the measure is necessary and respects the principle of proportionality – that is, no less intrusive instrument can effectively achieve the goals of law or regulation. We also note that in the field of environmental protection, a different and less stringent standard of relating to the environmental law and regulations applies under Article XX(g) GATT, which does not apply in the present context. For example, in *EC – Trademarks and Geographical Indications*, the Panel found that the possibility of reporting or inspection offers a reasonable and less intrusive alternative to the requirement of mandatory foreign government participation in

the protection of geographical indications (GIs). It is up to the claimant to demonstrate that a less intrusive alternative is reasonably available. It is important to note that the burden of proof to maintain the measure being imposed and challenged lies with the defendant.[95]

In the present context, it is a matter of assessing whether a ban on parallel importation that is found to be capable and which makes at least a contribution to enforcing laws and regulations relating to the overall IP system is necessary, in the sense that less intrusive alternatives to achieve such implementation of objectives, principles and rights of IP are not reasonably available. We recall that the ban on parallel importation amounts to quantitative import restrictions or a violation of national treatment and is thus in conflict with the fundamental principles of WTO law. We also recall the finding that a ban on parallel importation strongly depends upon the particular configuration and the context and that a general rule of national or regional exhaustion is overbroad.

The question is whether alternative measures need to be located within the regulatory world of IP itself, or whether governments, instead of authorising outright market segmentation, can and should refer to other public policy tools. In addition, the question arises to what extent answers can be found within the realm of private conduct, subject to disciplines of competition law and policy. We note that parallel trade is a problem mainly in areas subject to strong governmental intervention and regulation, in particular in the field of pharmaceuticals. These products are not solely subject to IP protection but rather a host of regulation, ranging from funding basic research and training to regulatory approval and price controls as well as competition law. It does not amount to a major shift to address ad hoc the problems of parallel importation by other and newer means, short of imposing a general ban on the basis of national exhaustion. The same applies for customs union operating regional exhaustion, in particular the European Union.

4. Less Intrusive Policy Options and Instruments

It is submitted that a number of less intrusive measures are possibly available for addressing legitimate concerns. These tools may be employed in different sectors, essentially replacing a general ban on parallel importation. Without going through a GATT analysis, Frederick Abbott suggests a similar approach in addressing the complexities of the pharmaceutical market by trade policy and trade regulations tools.[96] Some are governmental, falling under the ambit of WTO law (a–c). Others pertain to contractual relations and the realm of competition law, which is not

[95] European Communities – Protection of Trademarks and Geographical Indicators WT/DS174/R (15 March 2005) para. 7.459.

[96] Frederik A. Abbott, Parallel trade in pharmaceuticals: trade therapy for market distortions, in Calboli and Lee (n 1) 145–165.

addressed in WTO law but is admissible under Article 40 TRIPS (d–f). While the first group entails governmental administration, the latter remains in the hands of operators and thus does not fundamentally alter allocation of powers in managing imports and exports.

Finally, in examining alternatives to national and regional exhaustion, today's realities of international online sales need to be taken into account. The aptitude and capability of banning parallel importation with a view to segmenting the markets, in the age of international online trading, is seriously questioned. The doctrine depends upon private action and does not involve public enforcement at the border or inside the country, except by courts of law and custom authorities acting upon private action. The original market of products is increasingly difficult to trace, and customs authorities are unable to stop consignments other than through random checking. Traditional tools, such as preliminary injunctions of courts, fail to work in online business. Alternative measures therefore may not only be less intrusive but also more suitable and capable than an outright ban on parallel trading.

a. import and export tariffs Members of the WTO are entitled to apply import and export tariffs to protect domestic production or needs, within the limits of bound tariffs in their respective schedules of commitment.[97] Members of the WTO can possibly reduce the problems caused by varying purchasing powers of different countries, which leads to price differentiation, by imposing applied tariffs on parallel imported products – with a view to protect domestic production and in particular research activities. The option of increasing trade costs has not been actively studied and used to this effect, as the reduction and elimination of product tariffs has been a major goal of multilateral trade negotiations and free trade agreements. Tariffs, of course, induce higher consumption prices and in effect burden domestic consumers. Tariffs therefore cannot be used in isolation, but may complement other measures, with a view to achieving an overall balance of interests by protecting the prices ranges of domestic research industries and eliminating undercutting imports by parallel traded products. At any rate, tariffs are less intrusive than the effects of national or regional exhaustion amounting to outright import restrictions. Countries facing the problem of shortage of supplies due to parallel exportation and sales of stock at higher pricing abroad may resort to export duties on such products. These measures are less intrusive alternatives compared with quantitative restrictions under the necessity test of Article XX(d) GATT. The options are not available within customs unions and free trade agreements under Article XXIV GATT, which bans the imposition of new tariffs and requires existing ones to be gradually dismantled.

[97] Thomas Cottier and Matthias Oesch, (n 15), 595–607.

B. LABELLING Parallel traded products are genuine and of equal quality. They are subject to the same technical standards and regulations under the TBT Agreement.[98] They are essentially the same, and consumers are not deceived. Producers may be required to label products by indicating market destinations and product characteristics in order to inform consumers and traders alike. The practice is well known in the distribution books under copyright protection, justifying different price levels. Labelling has been recognised under the TBT Agreement as a main alternative to quantitative restrictions and a viable alternative under the necessity test.[99] It entails both voluntary standards and mandatory regulation. In the end, consumers should decide what they buy, independently of the geographical origin of the product.

The law on labelling is essentially controlled by the TBT Agreement, and particular labels may be challenged under these provisions. Labelling of products traded in the original form may require informing consumers about the original destination for sale and consumption – and thus that the product is a parallel import (destined for sale and consumption in country X). The policy is of increasing importance in light of the online sales of products. Consumers ordering via the Internet should know about the origin and the markets of destination of products, in part to be sure that these products comply with the laws and regulations in force in the country of consumption. Labelling of regulated products often requires the repackaging of products for the purpose of parallel trade.

Pharmaceuticals are required to provide information in the language or languages of the country of importation, which may be different from the exporting country. Such requirements increase the costs and prices and may reduce the incentives to parallel trade in the first place. Particular provisions exist in the WTO for pharmaceutical products imported under Article 31bis of the TRIPS Agreement, restricting the re-exportation of products.

C. IMPORT AUTHORISATION AND LICENSING Governments may require import authorisation of products, in particular for pharmaceuticals, in relation to regulatory approval and marketing.[100] Article XIII provides the foundations for import licensing of products subject to quantitative restrictions or tariff quotas. The tool allows for calibrating applied tariffs and linking them to quantitative restrictions. This approach is clearly less intrusive than a flat ban on imports. Such prohibitions,

[98] See generally Thomas Cottier, Technology and the Law of International Trade Regulation, in R. Brownsword et al. (eds.) *The Oxford Handbook of Law, Regulation and Technology* 1017–1051 (Oxford: Oxford University Press 2017).

[99] E.g. United States – Certain Country of Origin Labelling (Cool) Requirements, WT/DS384/AB/R, WT DS386/AB/R (29 June 2012); Australia – Certain Measures concerning Trademarks, Geographical Indications and other Plain Packaging Requirements applicable to Tobacco Products and Packaging, WT/DS345/R, WT/DS441/R, WT/DS458/R, WT/DS467/R (28 June 2018).

[100] For the example of Switzerland see Cottier and Leber, *supra* (n 28).

considering MFN, are deemed lawful only to the extent that the restrictions are not selective but apply to all Members alike.

In allocating quotas, GATT law requires taking into account existing and prospective patterns and volumes of trade. The Agreement on Import Licensing Procedures sets out a number of provisions to ensure fair and equitable procedures both for automatic and non-automatic licensing by government authorities.[101] Importantly, the system is not limited to 'first come, first served' and existing patterns but also needs – in Article 5(j) – to be open for newcomers. While these rules mainly relate to the importation of agricultural products, it is conceivable to selectively apply them to sensitive parallel traded products with a view to managing overall supplies and striking a balance between domestic and imported products.

D. PRICE CONTROLS Members of the WTO are free to operate price controls over regulated products, in particular pharmaceutical and chemicals, applying to both domestic and imported products.[102] Neither GATT nor TRIPS address the issue. Excessive controls, which erode returns on investment, may undermine the protection of patents as well as trademark law, in particular in the case of generics, and give rise to non-violation complaints under Article XXIII(1)(b) GATT. Such complaints, however, have been suspended for the TRIPS Agreement under an extended moratorium.[103] Moreover, price controls have been in place for pharmaceuticals in most countries and fail the basic test for non-violation complaint, which protects legitimate expectations and requires a measure to be unexpected.[104] Moreover, even if non-violation were to be found, measures need not be withdrawn.[105] Governments thus are able to address the problem of price undercutting and excessive pricing by setting price ranges for products, whether domestically sold or imported, and whether patented or under trademark protection (generics).

E. IMPLIED LICENSING Implied licensing has been a traditional tool in common law for addressing parallel trade prior to the advent of national and regional exhaustion. Implied licensing presumes that the rightholder does not object to importation or reimportation, unless explicitly stated otherwise. It only applies to contractual

[101] See www.wto.org/english/docs_e/legal_e/legal_e.htm (accessed 2 March 2020)

[102] Governments use such controls mainly in pharmaceutical markets, see OECD, Pharmaceutical Pricing Policies in a Global Market 97–115 (Paris 2008), read.oecd-ilibrary.org/social-issues-migration-health/pharmaceutical-pricing-policies-in-a-global-market_9789264044159-en#page1 (accessed 2 March 2020).

[103] WTO, 'Non-violation' complaints (Article 64.2), www.wto.org/english/tratop_e/trips_e/nonviolation_e.htm (accessed 2 March 2020).

[104] Thomas Cottier and Krista Nadakuvaren Schefer, Non-Violation Complaints in WTO/GATT Dispute Settlement: Past, Present and Future, in Ernst- Ulrich Petersmann (ed.), *International Trade Law and the GATT/WTO Dispute Settlement System*, 145–183 (The Hague: Kluwer 1997).

[105] Article 26 (1)(b) DSU.

relations; furthermore, it is less intrusive than the doctrines of national or regional exhaustion but more restrictive than international exhaustion. It allows companies to discipline wholesale and retail within the international distribution system, subjecting contractual violations to sale restrictions and damages, subject to disciplines of competition law and policy. Licensing thus may deploy a deterrent impact on parallel trade without banning it. The shortcoming of implied licensing is that it is limited to contractual relationship. It does not extend to parallel traders outside the system of distribution, to whom no contractual relation exists, and for which rightholders need to be able to rely upon their IP rights. While licensing may thus be a relatively unintrusive option for parallel trade within contractual relations, it does not offer an alternative to addressing outside and independent traders – which led to the doctrine of exhaustion as applied within a country.[106]

F. RESTRICTIONS OF SUPPLY Companies seeking to limit parallel trade may reduce the supplies to destinations which may use those supplies to parallel export into other jurisdictions. Developing countries, fearing such effects in the pharmaceutical sector, partly refrained from adopting international exhaustion in patent and trademark law, as long as they do not yet dispose of effective disciplines in competition law or price controls. Restrictions of supply to wholesalers are not addressed by WTO law unless governments are directly or indirectly involved. These restrictions are subject to competition law and potentially amount to an abuse of a dominant position and the prohibition of cartels. Such measures are compatible with Article 40 TRIPS Agreement and may justify exceptions under Article XX(d) GATT and Article XIV GATS.

The case law of the European Court of Justice discussed calibrated restrictions of supplies in the wholesale supplies of pharmaceuticals, limiting in effect parallel trading in terms of government regulation, innovation and consumer welfare. It was seen that these factors may justify restrictions on a case-by-case basis, under Article 101(3) and Article 102 TEFU or by recourse to general regulation (block exemptions and guidelines).[107] Competition law and policy thus offers the potential for less intrusive and tailor-made answers to address the needs of specific sectors, compared with the doctrine of national and regional exhaustion. Problems relating to restrictions of digital trade, in particular the refusal to sell to foreign online customers or geo-blocking, may best be addressed with disciplines of competition law and policy.

The option presupposes that a Member State of the WTO disposes of a workable system of competition law. Much progress has been made in recent years with the support of the International Competition Network.[108] Common disciplines were

[106] Section A
[107] *Supra* (n 62).
[108] International Competition Network, www.internationalcompetitionnetwork.org/ (accessed 2 March 2020).

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developed within comprehensive trade and cooperation agreements, in particular CETA between the European Union and Canada. However, the linkages discussed also support the case to bring back negotiations on minimal standards on competition law into the WTO and to explore and define the relationship between this body of rules and trade regulation.[109]

G. PRODUCT DIFFERENTIATION Finally, producers may revert to product differentiation mainly in the field of trademark-protected goods. By alternating the physical properties of a product, the presumption of consumer deception using the same trademarks for the same products allows for banning the sale of such products marketed abroad upon importation due to trademark protection under Article 16 TRIPS Agreement.[110] Such restrictions are not based upon national or regional exhaustion, but equally apply under the doctrine of international exhaustion due to the protection of consumers from deception. These restrictions, together with licensing and contractual relations, allow companies to partially segment markets and employ product differentiation in terms of physical qualities, restricting parallel trade if they wish to do so.

5. Chapeau of Article XX GATT

The chapeau of Article XX applies once the necessity test under Article XX(d) has been complied with (i.e. a ban on parallel trade is found justified). To the extent that such a ban is based upon the doctrine of national or regional exhaustion, the chapeau essentially addresses whether this amounts to an abuse of rights in a particular configuration at hand.[111] Outright prohibitions of parallel trade as applied *ergo omnes* should not pose a problem; complex regulations may treat different countries differently beyond the realm of Article XXIV GATT. Less likely, they will amount to a disguised restriction of trade, to the extent that the regulation is transparent and without a hidden agenda. It will be objected that a GATT approach lacks legal security and predictability, because it follows a case-by-case approach. In

[109] Robert D. Anderson, William E. Kovacic, Anna Caroline Müller, and Nadezhda Sporysheva, Competition Policy, Trade and the Global Economy: Existing WTO Elements, Commitments in Regional Trade Agreements, Current Challenges and Issues for Reflection, WTO Staff Working Paper ERSD-2018-12, 31 October 2018, pp. 57/58; https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3321116 (accessed 1 March 2020); Thomas Cottier, Competition and Investment: the Case for 21st Century WTO Law, in Katia Fach, Anastasios Gourgourinis, and Catherine Titi (eds.), *International Investment Law and Competition Law, Special Issue, European Yearbook of International Economic Law* 261 (Cham: Springer 2021); on previous work see WTO, Interaction between Trade and Competition Policy, www.wto.org/english/tratop_e/comp_e/comp_e.htm (accessed 1 March 2020).

[110] See Section C.II. in this chapter

[111] United States – Standard for Reformulated and Conventional Gasoline (WT/DS/2/AB/R (19 April 1996); United States – Import Prohibition of Certain Shrimp and Shrimp Products, WT/DS58/AB/R (12 October 1998); Cottier and Oesch (n 15), 451–462.

reality, however, it is a matter of assessing the problem in a number of controversial sectors, in particular pharmaceuticals and chemicals and other goods subject to regulatory approval. The jury is still out, and it is here that national and regional exhaustion is defended most ardently.

In many areas of patent law and other forms of IP, the test is likely to confirm that less intrusive measures than national or regional exhaustion offer well calibrated solutions. The continued application of national and regional exhaustion thus essentially amounts to an exception which may or may not be justified in complex regulatory areas under the necessity test. The GATT rules substantially undermine the operation of national and regional exhaustion in international law, and we concur with the view that overall, a general ban on parallel imports does not meet the necessity test.[112] Predictability can be readily achieved by adopting, on the basis of GATT rules, a doctrine of international exhaustion subject to specifically defined exceptions and recourse to different policy tools in addressing specific problems in specific sectors.

III. *National Security Exceptions (Article XXI)*

National security was not at the forefront of trade rules until recently. The evolution of the digital and cyber economy mean that the role of big data and artificial intelligence is increasingly interlinked with security interests. Governments are entitled to adopt measures for their essential security interest in case of a national emergency. The Panel in *Russia – Traffic in Transit* held that the notion is justiciable and the provisions do not offer a general carve-out.[113] Not any interest can be deemed to be essential and is subject to invocation in good faith.[114] In the first case ever assessed, the Panel recognised situations of armed conflict, latent armed conflict, heightened tensions of crisis or of general instability, which entitle governments to invoke national security.[115]

It is difficult to anticipate how this situation translates into IP and parallel trade of hardware falling under GATT rules. Potentially, the importation of goods can be blocked under embargo and economic sanctions, irrespective of IP, which inherently includes parallel importation. Importation may be also blocked in the context of cyber-technology due to the risk of manipulation of products sold and marketed abroad for security reasons. The potential of abusing national security for political and protectionist reasons is increasing. National security and trade are increasingly

[112] The analysis confirms the view expressed prior to the adoption of the TRIPS Agreement, see Abdulqawi A Yusuf and Andrés Moncayo von Hase, Intellectual Property Protection and International Law – Exhaustion of Rights Revisited, 16 *World Competition* 116, 129 (1992); Frederick A. Abbott (n 12); Genovesi (n 30) at 221, but subject to prevailing Article 6.

[113] Russia – Measures Concerning Traffic in Transit, WT/DS512/R (5 April 2019) para. 7.102–7.103.

[114] Id. 7.132.

[115] Id. 7.76–7.77.

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overlapping, with the latter dominated by the former in the age of cyber-warfare and the digital economy. It will be a matter of developing more precise rules in the field. Importantly, however, the provision operates independently of the geographical scope of exhaustion. It also applies to international exhaustion and offers a safeguard of last resort.

E. THE GENERAL AGREEMENT ON TRADE IN SERVICES

The GATS seeks liberalisation of services in four modes of cross-border trade: to consumers, for consumption abroad, for investment abroad through commercial presence and for investment abroad through the presence of natural persons. While MFN applies across the board, national treatment is limited to particular concessions granted in schedules of Members, often subject to further qualifications.[116] The relationship of GATS and schedules to IP has not been well explored. The same holds true for distribution services under Article III GATT. These issues may be relevant mainly in the field of copyright protection, which covers a number of important cultural and digital services.

The European Court of Justice held in *Coditel II* that cultural services and the right to control a performance is not subject to exhaustion.[117] The redistribution of bought electronic books made available to an electronic library for redistribution was held by the Court in *Tom Kabinet* to amount to a communication to the public by the library and thus not subject to exhaustion.[118] Exhaustion – let alone its geographical variants of national, regional and international exhaustion – increasingly seem outdated in services.[119] The problem of legal security in downstream markets thus needs to be addressed by prohibitions or licensing, which in turn are subject to disciplines and competition or anti-trust law safeguarded by Article 41 and the principles of non-discrimination, both MFN and national treatment under Articles 3 and 4 TRIPS Agreement.

Products resulting from services, however, are not necessarily excluded from exhaustion.[120] The European Court of Justice held in *Usedsoft* that the right of distribution of a copy of a computer program is exhausted if licensed with a right to use the copy for an unlimited period.[121] Problems relating to parallel trade thus cannot be excluded for resulting products in downstream markets. Such problems

[116] For a detailed analysis see Nicolas F. Diebold, *Non-Discrimination in International Trade in Services: 'Likeness' in WTO/GATS* (Cambridge: Cambridge University Press 2010).
[117] Case 262/81 *Cotidel v. Cine Vog Films* [1982] ECR 3381, ECLI:EU:C:1982:334.
[118] Case C-263/18 *Nederlands Uitgeversverbond et al. v. Tom Kabinet Internet BV et al.*, [Judgement of 19 December 2019], ECLI:EU:C:2019:1111.
[119] Cf. Reto M. Hilty, 'Exhaustion' in the digital age, in Calboli and Lee (n 1) 64–82.
[120] Westerkamp (n 1) pp. 49–50.
[121] Case C-128/11 *UsedSoft GmBH v. Oracle International Corp*, Judgment of 3 July 2012, ECLI: EU:C:2012: 407.

are not yet well known, partly because most countries apply international exhaustion in the field of copyright.

Regional exhaustion, however, in the European Union may lead to comparable problems encountered under GATT rules. The ban on parallel importation of a product protected under copyright, trademark or patent law may undermine the value of commitments made in the schedules of concessions. Operators of Members may be entitled to cross-border trade and establishment but may be barred from importing products put on the market under a licence or acquired as a third party in another Member. For example, a company offering music streaming in the United States may be barred from offering licensed works in the European Union due to regional exhaustion of copyright, fostering market segmentation and eliminating competition despite the right to cross-border trade in the field of related cultural services. Access to websites may be blocked, or certain jurisdictions excluded from online sales of services. Or, assuming that big data is proprietary information and protected by copyright, the flows and use of such data licensed to a subsidiary in a different jurisdiction could be barred from being used under regional exhaustion within the European Union. Proprietary information stored by a company in a cloud in a particular jurisdiction and licensed for use could thus be stopped and banned from being used in the European Union by a third party without the consent of the rightholder. This may force rightholders to store proprietary information within the European Union in order to secure access and use. The impact of IP protection on managing and harnessing big data remains to be explored.[122]

In the end, all of this could conflict with MFN obligations under Article II GATS and in sectors that are subject to schedules with national treatment obligations of Article XVII and Article VI. The latter provides that in scheduled sectors, 'each Member shall ensure that all measures of general application affecting trade in services are administered in a reasonable, objective and impartial manner'.

Under GATS, restrictions of national treatment and non-discriminatory market access may be justified under Article XIV GATS, which is modelled after Article XX GATT discussed above. Panels and the Appellate Body recognised the parallel structure and methodology with Article XX(d) GATT.[123] Interestingly, the provision does not entail an explicit reference to IP rights but is limited, in the present context, to measures necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this agreement, including those relating to (i) the prevention of deceptive and fraudulent practices. Panels and the Appellate Body recognised that the list is non-exhaustive.[124] Laws and regulations relating to IP

[122] Cf. World Bank, *Harnessing the Power of Big Data for Trade and Competitiveness Policy* (Washington DC 2017) does not address intellectual property issues.

[123] United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services, WT/DS285/AB/R (20 April 2005) para. 6.537; Argentina – Measures Relating to Trade in Goods and Services WT/DS453/AB/R (14 April 2016) para. 6205–6.209.

[124] Id.

protection therefore are subject to the same analysis made under Article XX(d) GATT, including the necessity test discussed above.[125]

Again, it would seem questionable that national exhaustion or regional exhaustion of IP rights, to the extent that exhaustion applies in the first place – such as in software – could be justified across the board as a matter of principle, which amounts to overbroad prescriptions, while restrictions may be justified on a case-by-case basis. Finally, it is important to note that national security exceptions under Article XIVbis may play an increasing role in areas related to the digital economy, and trade restrictions on IP-related products may be justified in defence of essential national security interests. For example, import restrictions on copyright-protected online software and updates of programs may be justified in these terms, even though a country operates international exhaustion in copyright law covering big data and digital trade. Overall, as under GATT, national and regional exhaustion is overbroad and may conflict with provisions of the GATS Agreement. On the other hand, the latter being stricter in scheduled sectors, undermines the operation of national and regional exhaustion and calls for tailor-made restrictions under Article XIVbis or the invocation of essential national security interests.

An entirely different issue here is the enforcement of such disciplines in the digital economy. It remains an open question as to how restrictions of electronic commerce induced by national or regional exhaustion can be effectively enforced.

F. PREFERENTIAL TRADE AGREEMENTS

Finally, we turn to the impact of Article XXIV GATT and Article V GATS allowing for the formation of the preferential trade agreements (PTAs). Such agreements privilege some states or separate customs territories and thus deviate from the MFN principle. Under the TRIPS Agreement Footnote 1, as discussed earlier, such privileges are limited to customs unions and separate customs territories, but do not extend to free trade agreements and agreements on comprehensive economic cooperation where Members keep their own external economic regime.[126] Under GATT, privileges relating to parallel trade can be extended, and limited, to customs unions as well as to free trade areas. Under GATS, they can be extended to all Members of an economic integration agreement, essentially eliminating all discrimination of service providers.

Both Article XXIV(5)(a) and (b) GATT and Article V(4) GATS provide that regulations within the PTA must not (on the whole, in customs unions) be more restrictive towards the rest of the world. To the extent that a country allows for parallel trade and international exhaustion prior to joining a customs union or a PTA, a return to limitations of parallel trade and regional exhaustion is inconsistent

[125] See Section D.II. in this chapter.
[126] See Section C.I. in this chapter.

with these provisions. The *Silhouette* ruling of the European Court of Justice, mandatorily imposing regional exhaustion to Austria and leaving international exhaustion behind, was inconsistent with this requirement.[127] Article XIV and Article V GATS thus further undermine the doctrine of mandatory regional exhaustion applied across the board by the European Union and EEA, unless the latter keeps international exhaustion in relation to third countries in accordance with the *Maglite* ruling.[128]

The discrepancy between GATT, GATS and TRIPS may explain why the doctrine of regional exhaustion, developed in the EEC, has not been extended to free trade agreements, with the exception of the EEA Agreement – which includes the EU Member States of Norway and Iceland. One would expect that regional integration amounts to a mainstay of modern economic trade agreements. In fact, the agreements remain silent or, in the case of the United States, positively prescribe national exhaustion of patents[129] or leave the issue entirely to the parties, such as in the 2020 United States–Mexico–Canada Trade Agreement (USMCA).[130]

Importantly, the privileges accorded under regional trade and integration agreements can only stand to the extent that national or regional exhaustion can be justified under Article XX GATT. Where it is found that the necessity test is not met in the first place, the operation of national or regional exhaustion is undermined and preferential rules cannot be justified under Article XXIV either. The configuration again, as a result, steers towards the adoption of international exhaustion as a general rule, while leaving national and regional exhaustion to more specific sectorial exceptions.

G. CONCLUSIONS

Both GATT and GATS undermine the operation of national and regional exhaustion in Article 6 TRIPS by means of rules applicable to the restrictions of parallel trading. These agreements do not regulate parallel trade amounting to international exhaustion but rather result in treating national and regional exhaustion as subject to

[127] *Supra* (n 45).

[128] *Supra* (n 50).

[129] For example, the United States – Morocco Free Trade Agreement, Chapter 15 Article 9(4) ('Each Party shall provide that the exclusive right of the patent owner to prevent importation of a patented product, or a product that results from patented process, without the consent of the patent owner shall not be limited by the sale or distribution of that product outside its territory.') footnote providing for exceptions under licensing agreements omitted. ustr.gov/sites/default/files/uploads/agreements/fta/morocco/asset_upload_file797_3849.pdf (accessed 3 March 2020).

[130] Article 20.11 of the Agreement between the United States of America, the United Mexican States and Canada 7/1/20 completely leaves exhaustion to the Parties: 'Nothing in this Agreement prevents a Party from determining whether or under what conditions exhaustions of intellectual property rights applies under its legal system'; ustr.gov/sites/default/files/files/agreements/FTA/USMCA/Text/20%20Intellectual%20Property%20Rights.pdf (accessed 9 June 2021).

the disciplines of Article XI, III and XX GATT – in particular the necessity test, and thus also result in the need to calibrate rules on parallel trade in line with the principle of proportionality. The impact of GATS on parallel trade is much less explored and remains unclear. It may be largely non-existent, to the extent that copyright is operated under international exhaustion or rights to not exhaust in the first place in the digital age. It may, however, cause problems under regional and national exhaustion. Rights to provide services under the four modes of the agreement and in schedules may tend to undermine national exhaustion, to the extent that the latter impedes these market access rights by limiting cross-border trade in services protected by IP rights.

A comprehensive analysis of WTO rules shows that the issue of exhaustion is not limited to Article 6 TRIPS Agreement. Article 16 TRIPS shows that even provisions within that agreement have a bearing on parallel trade. While states formally remain free to define the geographical scope of exhaustion as they wish and prefer, the application of the GATT Agreement – and potentially also the GATS Agreement – undermines the operation of national and regional exhaustion. As a practical result, the multilateral trading system undermines the operation of national and regional exhaustion and implies that these doctrines are used as exceptions where less intrusive regulations are not workable.

In particular, the necessity test of Article XX(d) GATT and of Article XIV GATS, applying the principle of proportionality, does not allow for uniform answers. Based on the economic analysis of welfare effects, the answers will vary from sector to sector, from right to right and even within one field. Assessments may also differ in light of the industry and regulations at hand. It needs to be examined to what extent one of the tools listed, or additional ones, may satisfy the regulatory purpose of IP protection at hand. It is possible that national or regional exhaustion will stand the test, if workable and less intrusive alternatives fail. It however no longer stands as a general proposition across the board.

A close analysis of WTO law, in particular GATT 1994, reveals that the doctrines of national and regional exhaustion are constitutionally overbroad.[131] They privilege rightholders in external relations on all accounts, and they go beyond the scope of rights in domestic commerce without assessing the welfare effects. Exhaustion is binary, either national or international in a particular case, and *tertium non-datur*, granting additional rights in one case but not the other. Such rigidity is hardly able to cope with the complex economic configurations in different sectors identified by

[131] The legal term 'overbreadth' originates in US constitutional law, relating to the first amendment of free speech. A law is void on its face if it 'does not aim specifically at evils within the allowable area of [government] control but ... sweeps within its ambit other activities that ... constitute an exercise' of protected expressive or associated rights, *Thornbill v. Alabama*, 310 US 88, 97 (1940); see Laurence L. Tribe, *American Constitutional Law* 710–718 (New York: The Foundation Press 1978) for further references. The doctrine is related to the principle of proportionality, as applied to legislation.

economists. A more nuanced approach is required in international economic law. An assessment under Articles XX GATT calls for a sectorial cost–benefit analysis, which may or may not justify the ban of parallel importation. The point is that under the text of necessity and proportionality, neither the test of capacity nor of indispensability can be met across the board, and in many configurations the concerns can be addressed by recourse to more specific trade instruments – entailing tariffs, labelling, import licences, price controls, restrictions of supply and product differentiation. These options often are not only less intrusive but also more capable to address modern regulatory challenges in parallel trade in the age of digital trade and climate change.

Today, tensions mainly arise in patent law. While there is a general trend in trademark and copyright to apply international exhaustion, the area of patent law – and in particular the pharmaceutical and chemical sector – remains conceptually controversial. The problem exists across the board for all forms of protection with the doctrine of regional exhaustion in the European Union. It is in patent and EU law that a more in-depth assessment and work on alternate and less intrusive regulations of parallel trade are warranted, which may eventually lead to the revision of Article 6 of the TRIPS Agreement. The adoption of international exhaustion in patent law by the US Supreme Court and by China pave the way to revisit national and regional exhaustion doctrines in domestic law and international agreements, taking into account WTO rules beyond the TRIPS Agreement. Technological developments will support this evolution. It would seem that the doctrine of national and regional exhaustion is increasingly ineffective in the age of digital economy and transboundary sales. Traditional tools of implementation in private law and border enforcement need to be redesigned for the digital age. Finally, the need for enhanced transfer of technology in renewable energy and sustainable agriculture, to address climate change mitigation and adaption, calls for rethinking the doctrine of national and regional exhaustion.[132] It is imperative to encourage dissemination of clean technology as a matter of common concern of humankind.[133]

We recall that Josef Kohler introduced the doctrine and notion of exhaustion in the process of nation building, without distinguishing between national and international exhaustion.[134] The doctrine was not meant to segregate markets beyond

[132] Cf. Keith E. Maskus and Ruth L. Okedji, Intellectual Property Rights and International Technology Transfer to Address Climate change: Risk, Opportunities and Policy Option, ICTSD Issue Paper no 23 (Geneva 2010); Agnieszka A. Machinika, TRIPS and Climate Change in the International Economic Order, in Hanns Ullrich, Reto M Hilty, Matthias Lamping, and Josef Drexl (eds.), *TRIPS plus 20: From Trade Rules to Market Principles* 415–443 (Heidelberg, New York, Dordrecht, London: Springer 2016) – but neither source addressing parallel importation for renewable technology dissemination.

[133] Thomas Cottier, (ed.), *The Prospects of Common Concern in International Law* (Cambridge: Cambridge University Press 2021).

[134] *Supra* (n 5).

national borders, implying international exhaustion. Geography no longer should matter in exhaustion. It is time to go back to the roots of the doctrine and to address regulatory challenges by appropriate means and 'clinical surgery'. We should simply talk about the exhaustion of rights in international economic law and leave fine-tuning of cross-border parallel trading to international trade regulations in different sectors of the economy.

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