

## **Asian Patents Attorney Association**

Hong Kong - Anti-Counterfeiting Committee Report

60th & 61st Council Meeting

### **Party II - Specific topic: legal and practical measures to prevent parallel imports**

#### **A. What are parallel imports?**

Parallel imports are genuine products that are originally made and destined for one country but are subsequently imported into another country or territory without the consent of the intellectual property owner ("IP owner") or its exclusive licensee(s) in the place of sale.

Usually, the goods are bought in markets where the price is lower and sold in markets where the price of the same goods is, for various reasons, higher. The importers stand to make significant profits from the regional differences in retail pricing, and are able to take advantage of the "goodwill" in the brand, which is generated by marketing campaigns of the manufacturer or authorised distributor.

Parallel imports can be a problem for IP owners who wish to control the sale of goods developed for use in a particular market. Multi-national companies may need to price their products at levels appropriate to local economies and to control distribution networks to protect brand image and product quality. Parallel imports can have the effect of disrupting distribution chains, and can adversely affect sales of the local licensee(s).

The issue of parallel importation has become a topical issue in Hong Kong and has recently seen high profile enforcement actions taken by Hong Kong enforcement authorities against Chinese nationals entering Hong Kong under tourist visas and engaging in work as parallel import traders shifting goods to Mainland China. The actions led to high profile arrests of over a hundred traders found working in Hong Kong in breach of their conditions of stay visa status.

Whether or not parallel imports should be restricted is a controversial issue which currently leads to much debate in Hong Kong. As the law stands today, the legal position varies with the different intellectual property rights. It is the purpose of this article to give a brief summary of the legal position vis-à-vis different IP rights and identify some of the measures available to prevent parallel imports.

#### **B. Control of parallel imports by IP laws**

In summary, parallel imports in Hong Kong may attract liabilities for infringement of trade marks, copyright, patents, and/or registered designs of the IP owner. Where false representations have been made by the parallel importer in relation to the products, it may also result in criminal liability for false trade description(s). There are separate pieces of legislation dealing with these liabilities. In addition, an IP owner may also take action against the parallel importer under the common law for passing off. A detailed outline of the legal positions is provided below.

##### **1. Trade marks and the doctrine of exhaustion**

The doctrine of exhaustion refers to an IP owner losing his rights against a parallel importer after first use (usually the first sale in the market) of the rights. The trade marks law in Hong Kong has taken an international approach to this doctrine. Under section 20 of the *Trade Marks Ordinance* (Cap 559), once the trade marked goods is released anywhere in the world by the trade mark owner or with its consent, the trade mark owner cannot complain if the goods are subsequently imported into the local market in Hong Kong.

This provision, however, is subject to the proviso that the condition of the products has not been changed or impaired after they have been put on the intended market, and that the use of the trade mark in relation to those goods is not detrimental to the distinctive character or repute of the trade mark.

The type or degree of differences there must be between the domestic goods and the parallel imported goods bearing the same trade mark before the IP owner is entitled to take action against the parallel importer will vary case to case. The relevant test seems to be whether the quality of the goods is changed or impaired such that sale of the goods in Hong Kong would adversely affect the reputation and goodwill of the trade mark concerned. Obvious examples would be where the imported products are actually defective or rejected goods in the intended market, or where the quality of the product has deteriorated through the importation process.

It was said in the legislative debate that the rationale for adopting the international approach to exhaustion is to maintain Hong Kong's status as a free port and to encourage competition to ensure the widest availability of goods at the best prices for consumers. It was believed that the proviso would provide sufficient protection for the reputation of established trade marks and safeguard consumers against deception.

## **2. Copyright**

The provisions in the *Copyright Ordinance* (Cap 528) relevant to parallel imports is rather complicated, and has been the subject of several amendments since 2001. As a result of the latest amendments which came into force on 6 July 2007, the law in relation to parallel imports has been relaxed in certain ways. For instance, the liabilities for business end-users have been abolished, and the period for criminal sanctions in relation to the prohibited acts has been shortened. The current legal positions can be summarized as follows:

- a) Trading in any form of copyright work, except for computer software products, which is parallel imported can be subject to civil liabilities;
- b) Criminal sanctions will also be imposed if the parallel imported copies are imported within 15 months (as opposed to the 18 months under the old law) from the date when the work was first published anywhere in the world. An 'infringing copy' is defined for the purposes of the criminal provisions of the Copyright Ordinance as being a copy which, if made in Hong Kong, would be an infringement of the copyright in the work or a breach of an exclusive license agreement and it has been or is proposed to be imported into Hong Kong within 15 months at the first day of publication of the work (in Hong Kong or elsewhere);
- c) Business end users are allowed to import and possess parallel imported works for their own use in the business. However, the following acts are still prohibited:
  - (i) sell, hire or distribute, or import for sale, hire or distribution copies of copyright works (except computer software) which are parallel imported; and
  - (ii) use movies, television dramas, musical sound recordings or musical visual recordings which are parallel imported for playing or showing in public.
- d) Parallel imports for purely educational purposes or for library use is allowed.

The new law also provides several defences to a person who does any of the prohibited acts mentioned above. However, the provisions have been drafted in such a way that no particular situation is clear-cut. This has generally resulted in both retailers and right holders being more conscientious in their dealings and a form of self-regulation has occurred.

### 3. Patents

Under the Patents Ordinance (Cap 514), the proprietor of a Hong Kong registered patent has the exclusive right to import into Hong Kong, put on the Hong Kong market and stock any product which is the subject of the patent or any product obtained directly by means of a process patent. Any person who carries out any of the above acts, without the consent or authorisation of the patent owner, would be liable for patent infringement.

The accepted position is that where a patent owner or his agent has sold the patented article without limitations, the patentee has lost the right of free disposition of that article. Hence, the subsequent purchaser can import and sell the goods into Hong Kong or elsewhere.

However, if there are restrictive conditions imposed by the patent owner in relation to the disposal of the patented article and if the person acquiring the patented goods was aware of the restrictions at the time of acquisition, any dealing with the goods may constitute infringement of the patent. For example, if the patent owner's products are marked that the sale, distribution or exportation of the product outside of a particular country is prohibited, then the importation of the product into Hong Kong, or putting it on the market in Hong Kong, by a third person would potentially amount to an infringement of the patent owner's rights.

### 4. Registered Designs

The law in relation to registered designs is governed by the *Registered Designs Ordinance* (Cap 522) (the "Design Ordinance"). There is no provision specifically dealing with parallel imports bearing registered designs. However, the proprietor of a Hong Kong registered design has the exclusive right to import into Hong Kong for sale, or for trade or business, goods in respect of which the design is registered.

The exercise of such rights by a person, without the consent of the registered owner, would constitute infringement of the registered design. In the same way as patents, the issue is whether the registered design owner has expressly or impliedly consented to the importation of the goods. To determine whether there is such consent, it is necessary to take into account any limitations the IP owner may have imposed on the subsequent sale, distribution or exportation after first release onto the market.

### 5. Passing-off

Passing off is a common law tort which can be used to enforce unregistered trademark rights. The tort of passing off protects the goodwill and reputation of a business from misrepresentations that causes damage to goodwill and reputation.

To bring an action against the importer or trader of the parallel imported goods, the IP owner needs to show misrepresentation by the importer or trader which may cause confusion and damage to the brand owner and also unauthorized import.

In the context of parallel imports, examples which would give rise to an action in passing off include misrepresentations that the parallel imported goods in question are "officially authorized" rather than "genuine". Such misrepresentations may be explicit or implicit.

For instance, Pringle, an internationally-known retailer and manufacturer of woollen and cashmere garments, successfully sued a retailer who sold parallel imported "Pringle of Scotland" products in Hong Kong for passing off. In that case, the Hong Kong retailer made representations to create an impression that the parallel imported products sold were the same as the official "Pringle of Scotland" products sold at department stores in Hong Kong, contrary to the fact.

## **6. False trade**

The *Trade Descriptions Ordinance* (Cap 362), may provide a limited remedy against parallel imports. The legislation provides that it is an offence for any person to give in the course of trade any false indication that any goods supplied by him are of a kind supplied to any person. Further, it is an offence for any person to make, in the course of trade or business, a false representation to any other person that a particular seller is connected with or endorsed by any individual or body.

Thus, if a person falsely represents that the goods he supplied are imported through official dealers or he is directly authorised by the IP owner contrary to the case, he commits an offence of false trade descriptions and would be liable for prosecution.

### **C. The Enforcement Agencies**

There are a number of agencies that may assist in the prevention of parallel imports in Hong Kong.

#### **1. Public agencies**

##### **1.1 The Customs and Excise Department (the "Customs")**

The Customs may help to control parallel import of goods by clamping down on false trade descriptions, such as the sale of parallel imported goods as "authorised products". The Customs adopts a risk-profiling approach and conducts targeted inspections on high-risk shops. In 2010, the Customs has conducted 709 of such inspections. Consumers and rights owners may also file complaints for the Customs to follow up and conduct investigations. In 2010, the Customs had received four complains and conducted investigations into all four cases.

To protect tourists and consumers, the Customs had further set up a quick response team in March 2009. The response team is on duty around the clock, ready to arrive at case scenes quickly and attend to consumer complaints immediately. The Customs will follow up and conduct investigation upon receiving the complaints.

The Customs is also responsible for criminal investigation and prosecution of copyright infringement activities. Moreover, it may help prevent parallel imports by using its power of enforcement under certain packaging and labelling laws. For example, in Hong Kong, toys and children's products that do not bear the required warnings and caution statements in both English and Chinese will be subject to investigation and even seizure by the Customs.

##### **1.2 The Consumer Council**

The Consumer Council provides assistance to the Customs in resolving consumer disputes by mediating between consumers and traders, and provides advice on consumer matters.

At present, the Consumer Council has in place a name-and-shame mechanism under which the names and addresses of traders which have engaged frequently in unfair trade practices or have committed offences under the Trade Descriptions Ordinance are disclosed through press releases and on the Consumer Council's website for public information.

##### **1.3 Other authorities**

Some examples are:

- a) The Director of Food and Environmental Hygiene may assist in the prevention of parallel imports by using its power of enforcement under the relevant food labelling laws. Inspections may be conducted by the Director to seize parallel imported food which does not have on its package the required list of ingredients, allergens, additives, statement of special conditions for storage or instructions for use and information of manufacturer.

- b) The Director of Electrical and Mechanical Services may help prevent parallel imported electrical products which do not comply with the safety requirements set by the Electricity Ordinance and Electrical Products (Safety Regulations). The powers of the Director include, *inter alia*, ordering the parallel importer to accept a return of the product and refund the purchaser any sum paid for the product, and requiring the importer to make public the specific hazardous defects in the products.

## **2. Private agencies**

Private agencies and investigators may be engaged to conduct market surveys and provide sighting on potential actionable parallel imports. They may also be engaged to purchase samples at suspected or known parallel importers to check the quality of the goods and whether the traders make false representations as part of the sale process.

### **D. Public education**

Public education plays an important role to create awareness on the risks of parallel imported products. In particular, public awareness highlighting potential risks of parallel imports include:

- manufacturing process standards overseas are not always as stringent as those in Hong Kong, particularly when it comes to food and drugs. Such parallel imported goods may be inferior in terms of quality, compared to goods either produced locally or specifically manufactured for the Hong Kong market.
- parallel imported goods may have been altered or modified by the retailers. Such alternations are not subject to strict quality control and may result in health risks to the consumers who purchase them.
- parallel imported goods may not have access to the after-sale services and warranties available for the local authorized products.

### **E. Impact of internet on parallel imports**

The advent and advancement of digital technology and Internet in recent years has led to the boom in online shopping. For consumers, the market of online shopping and parallel imports have effectively merged, and it has become easier for consumers to access and purchase goods originally destined for foreign markets. In such a context, the battle against parallel imports has become more difficult. Typically online traders of parallel imported goods are located outside of Hong Kong, complicating investigations and collection of evidence and in many jurisdictions, the mere export of local goods by a parallel importer, say to Hong Kong, would not contravene local laws. Accordingly, it is especially important that detailed investigations are conducted against the parallel importer to understand the nature of their business operations and its goods to enable full assessment of available legal actions that can be taken.

### **F. Concluding remarks**

Hong Kong has always been proud of its tradition as a free market. Hong Kong's economic success has been largely built on its reputation as a free port and by a commitment by the Government to not intervene and put restrictive barriers to access of Hong Kong markets. However, IP owners should monitor actively the nature of the parallel imports in the market and take advantage of measures available to restrict and limit parallel imports in Hong Kong.