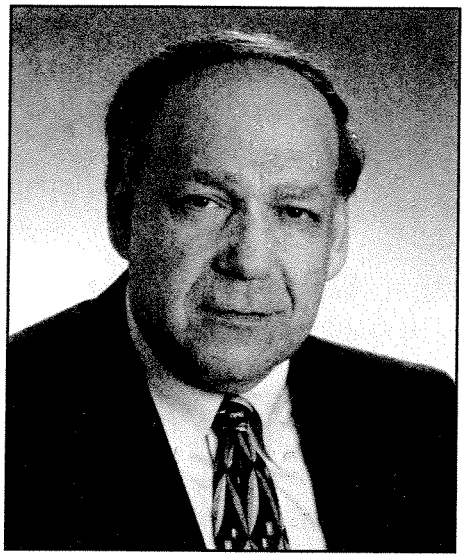
Ninth Circuit Report



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COPYRIGHT FIRST SALE DOCTRINE DOES NOT APPLY TO GOODS WHICH ARE PURCHASED OUTSIDE THE UNITED STATES AND IMPORTED INTO THE UNITED STATES

Omega S.A., v. Costco Wholesale Corporation ___ F.3d ___ (9th Cir. September 3, 2008)

OMEGA MANUFACTURES WATCHES in Switzerland and sells them throughout the world and in the United States. Each watch has on the back an "Omega Globe Design" which has been copyrighted in the United States, no doubt with the view to use the copyright to keep out foreign goods such as those at issue here.

Discount store Costco purchases watches on the "gray market" from ENE Limited, a New York company, which purchased the watches from authorized Omega watch dealers overseas. Although Omega authorized the initial foreign sale of the watches, it did not authorize the importation of the watches into the United States or the sales made by Costco, and filed this copyright infringement in the Central District of California. The parties filed cross motions for summary judgment, with Costco arguing that the "first sale doctrine" under 17 U.S.C. § 109(a) applied to provide a defense to any copyright infringement.

The First Sale Doctrine

The first sale doctrine of Copyright Act § 109(a) provides: "Notwithstanding the provisions of section 106(3), the owner of a particular copy...lawfully made under this title, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy...."

Section 602(a) of the Copyright Act prevents importation of copies of copyrighted works into the United States, without the authority of the owner of copyright: "Importation into the United States, without the authority of the owner of copyright under this title, of copies...of a work that have been acquired outside the United States is an infringement of the exclusive right to distribute copies...under section 106, actionable under section 501." Further, section 106(3) of the Copyright Act gives a copyright owner control of distribution. It states: "Subject to sections 107 through 122, the owner of copyright under this title has the exclusive rights...to distribute copies...of the copyrighted work to the public by sale or other transfer of ownership, or by rental, lease, or lending." The question here is the interplay between the three sections, the first sale doctrine, the exclusive right to distribute, and the right to prevent importation, which rightfully belong to the copyright owner.

The District Court granted summary judgment to Costco applying the first sale doctrine.

In its 1998 decision *Quality King Distributors, Inc. v. L'anza Research International, Inc.*,[1] the Supreme Court held the first sale doctrine to provide a defense allowing a defendant to sell copyrighted goods which had been manufactured in the United States, shipped outside the United States, and then ultimately imported back and sold into the United States without the consent of the copyright owner. In this case, the Omega watches were actually manufactured and obtained abroad from an authorized foreign distributor, then brought in through importation into the U.S. by ESS, and then sold here by Costco.

The Court noted that before *Quality King* was decided by the Supreme Court, Ninth Circuit precedent was clear that the first sale provision § 109(a) provided no defense against a claim of infringement for importation of goods which had been made outside the United States, unless the goods had already been first sold in the United States with the permission of the copyright owner.

The defendant, Costco had argued, and the District court had held, that prior Ninth Circuit decisions had been implicitly overruled by the *Quality King* decision of the Supreme Court. For example, the Ninth Circuit had previously held in *BMG Music v. Perez*,[2] that the first sale doctrine provided no defense against a claim of unlawful importation under 602 (a) against foreign-manufactured imported goods. As the court there said, the words "lawfully made under this title" in

§ 109(a) "grant first sale protection only to copies legally made and sold in the United States," and the copies at issue there were made and first sold abroad. The Ninth Circuit in *Omega* noted that the rational for this interpretation was twofold: First, "a contrary interpretation would impermissibly extend the Copyright Act extraterritorially, [and] second, the application of § 109(a) after foreign sales would 'render § 602 virtually meaningless'"... because importation is almost always preceded by at least one lawful foreign sale that will have exhausted the distribution right on which § 602 is premised.

Another prior case, *Denbicare U.S.A. Inc. v. Toys "R" Us, Inc.*,[3] involved copies made in Hong Kong and voluntarily sold in the United States by the US Copyright owner, applied the first sale exception to infringement, because the goods imported by third parties into the United States prior to the defendants purchase and resale of them, although foreign made, had been voluntarily sold within the United States. The U.S. sale had "exhausted the exclusive rights of distribution."

With this as a background, the Ninth Circuit considered the effect of the Supreme Court's decision in *Quality King*, and held that the *Quality King* decision did not overrule such cases as *BMG Music* and *Denbicare,* since the goods in *Quality King* had been manufactured inside the United States. Justice Ginsburg, in her concurring opinion in *Quality King* specifically recognized that *Quality King* involved only domestically manufactured copies and, as she noted, "the Court did not address the effect of § 109(a) on claims involving unauthorized importation of copies made abroad. We do not today resolve cases in which the allegedly infringing imports were manufactured abroad."

Since the *Omega* watches sold by Costco were manufactured abroad and never sold in the United States, the court held the application of the first sale doctrine inapplicable, and thus that the decision in *Quality King* had not changed the rule.

The Ninth Circuit wrestled with the question whether the reasoning of *Quality King*, that applied § 109 to foreign-made goods, would violate the presumption against the extraterritorial application of U.S. law, and should change the result, and concluded that it did not. The court noted that in the *Quality King* decision's only direct language on the issue was Judge Ginsburg's concurring opinion, citing a copyright treatise for the proposition that "lawfully made under this title" means "lawfully made in the United States."

The Court concluded that its general rule that § 109(a) refers "only to copies legally made...in the United States," is not clearly irreconcilable with *Quality King*, and, therefore, remains binding precedent. Under this rule, the first sale doctrine is unavailable as a defense to the claims under §§ 106(3) and 602(a) because there is no genuine dispute that *Omega* manufactured the watches bearing the copyrighted Omega Globe Design in Switzerland.

Critics of the Ninth Circuit decision in *Omega* have suggested that applying the first sale doctrine to copyrighted goods manufactured in the United States, exported, and then imported into the United States, would encourage trademark owners concerned about "gray market goods" or "parallel imports," to shift their manufacturing sources outside the United States. While this may be the result, the decision falls naturally from the law in the Ninth Circuit, not overruled by *Quality King*, and, time will tell whether this interpretation of the law will cause any shifts in manufacturing outside the United States. ▪

Endnotes

1. *Quality King Distributors, Inc. v. L'anza Research International, Inc.,* 523 U.S. 135 (1998).
2. *BMG Music v. Perez*, 952 F.2d 318 (9th Cir. 1991).
3. *Denbicare U.S.A. Inc. v. Toys "R" Us, Inc.*, 84 F.3d 1143 (9th Cir. 1996). The author was counsel to the defendant Toys "R" Us, Inc. in this case.

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