



Supreme Court to Examine Application of Copyright Law's First Sale Doctrine to Importation of Gray Market Goods

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by [Uli Widmaier](#), [Trademark Attorney](#)

Does copyright law's first sale doctrine apply to imported goods manufactured abroad that are not intended for the United States market? That is the question on which the Supreme Court recently granted *certiorari* in *Costco Wholesale Corp. v. Omega, S.A.*, No. 08-1423 (Apr. 19, 2010). Costco purchased genuine Omega "Seamaster" from an entity that acquired the watches outside the U.S. and imported them into the U.S. without Omega's authorization. Costco ultimately sold the watches to consumers at 35% below the price Omega normally charged in the U.S. To stop this practice, Omega engraved a small design on the back of these watches, registered it with the U.S. Copyright Office, and then sued Costco for copyright infringement in the Central District of California, alleging violations of Sections 106(3) and 602(a) of the Copyright Act, 17 U.S.C. §§ 106(3), 602(a). The district court entered summary judgment in Costco's favor, but the Ninth Circuit Court of Appeals reversed. *Omega S.A. v. Costco Wholesale Corp.*, 541 F.3d 982 (9th Cir. 2008).

Applicable Law

The resolution of the dispute turns on three provisions of the Copyright Act. Section 106(3) of the Act grants copyright holders—here, Omega—the exclusive right to distribute copies of a work by sale or other ownership transfer. Section 602(a) further specifies that "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." Yet the first-sale doctrine, codified in Section 109(a) of the Copyright Act, limits this exclusive right to distribute under Sections 106(3) and 602(a). Section 109(a) provides that "[n]otwithstanding 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."



PATTISHALL
McAULIFFE
NEWBURY
HILLIARD &
GERALDSON LLP • 311 South Wacker Drive, Suite 5000 • Chicago IL 60606 • T (312) 554-8000 • F (312) 554-8015 • www.pattishall.com

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The specific question the Supreme Court will have to decide, then, is this: What precisely does the phrase "lawfully made under this title" in Section 109(a) mean? Everyone agrees that copies manufactured in the U.S. by or on behalf of the copyright owner are "lawfully made under this title." Further, Section 109(a) also exempts copies legitimately manufactured in the U.S. that are then exported, purchased abroad by a third party, reimported, and sold in the U.S. without authorization by the copyright owner. In other words, the U.S. sale of reimported copies does not constitute copyright infringement under Section 602(a). See *Quality King Distributors, Inc., v. L'anza Research International, Inc.*, 523 U.S. 153 (1998).

But what about Omega's "Seamaster" watches, which were manufactured by Omega in Switzerland? Are copies manufactured abroad by a U.S. copyright owner "lawfully made under this title"? If so, Section 109(a) permits their unauthorized reimportation and sale in the U.S. If not, Section 109(a) does not apply, and Costco's actions constitute copyright infringement under Section 602(a).

Competing Interpretations of Section 109(a)

The Ninth Circuit has a longstanding rule that unauthorized importation and sale in the U.S. of U.S.-copyrighted foreign-manufactured goods without the copyright owner's authorization constitutes copyright infringement, and the decision below is a straightforward application of that precedent. See 541 F.3d at 985-6. The Ninth Circuit also concluded that *Quality King* did not overrule that line of precedent because the copies in *Quality King* were manufactured in the U.S. *Id.* at 987-90. The court's interpretation of Section 109(a) as being limited to domestically manufactured copies, while excluding copies manufactured abroad, is based on two concerns. First:

the application of Sec. 109(a) to foreign-made copies would impermissibly apply the Copyright Act extraterritorially. . . . To characterize the making of copies as 'lawful . . . under [Title 17]' would be to ascribe legality under the Copyright Act to conduct that occurs entirely outside the United States, notwithstanding the absence of a clear expression of congressional intent in favor of extraterritorially.

Id. at 988. Second, "the application of Sec. 109(a) after foreign sales would render Sec. 602 virtually meaningless as a tool against unauthorized importation of nonpiratical copies because importation is almost always preceded by at least one lawful foreign sale that will have exhausted the distribution right on which Sec. 602(a) is premised." *Id.* at 986 (citations and quotation marks omitted).

What is the counterargument to the Ninth Circuit's findings? In its petition for *certiorari*, Costco claims that Section 109(a)'s phrase "lawfully made under this title" simply means made pursuant to, or in compliance with, the Copyright Act. Thus, Costco argues:

because Omega is the U.S. copyright holder, any copies that it makes [anywhere] are necessarily in compliance with 17 U.S.C. Sec. 106(1), which provides the U.S. copyright holder with an exclusive right to make or authorize copies. As a result, any copies made by Omega are

'lawfully made under this title' and, therefore, subject to the first-sale doctrine.

Petition for Writ of Certiorari, *Costco v. Omega* (2010) (No. 08-1423), at 9-10. Costco also points out that at least two other provisions in the Copyright Act—Sections 110 and 1004(b)—use the phrase "lawfully made under this title" in a way that comports with Costco's interpretation but contradicts the Ninth Circuit's interpretation. *Id.* at 10-11.

Remarkably, as Costco admits, no circuit split exists on this issue. Nevertheless, Costco points out that many district courts have been troubled by how to read Section 109(a). In support of that contention, on September 28, 2009, Costco filed a supplemental brief to inform the Supreme Court of a September 22, 2009, decision by the U.S. District Court for the Southern District of New York in *Pearson education v. Liu*, 656 F. Supp. 2d 407 (S.D.N.Y. 2009). In *Pearson*, the district court held that the language of Section 109(a) means that "'lawfully made under this title' refers not to the place a copy is manufactured, but to the *lawfulness* of its manufacture as a function of U.S. copyright law." *Id.* at 412 (emphasis in original). The court also noted that the Ninth Circuit had "never explained how Sec. 109(a)'s text supports a distinction based on where a first sale occurred." *Id.* at 414. Nevertheless, the court stated it felt itself bound by strong *dicta* in *Quality King*, which it understood to agree with the Ninth Circuit's interpretation. Therefore, the *Pearson* court—contrary to its own reading of the statute—followed that interpretation. Remarkably, however, the court labeled its decision "*dubitante*," meaning doubtful, so as to signal the legal uncertainty perceived by the court. *Id.* at 416. This may have influenced the Supreme Court's decision to grant *certiorari* in the *Omega v. Costco* case.

Policy Implications

At heart, this dispute is about a narrow issue of statutory construction. What is its practical relevance? Why, other than to resolve a thorny issue of statutory interpretation, did the Supreme Court grant *certiorari*? One possibility is that the Court was swayed by the policy implications raised by Costco and its *amici*. The *amicus curiae* brief filed by the Retail Industry Leaders Association, Amazon.Com, Inc., Target Corporation, Gamestop Corp., Movie Gallery, Inc., Quality King Distributors, Inc., and the National Association of Chain Drug Stores explained as follows:

As product manufacturing increasingly moves offshore, a substantial percentage of the products retailers offer for sale in the United States are produced and first sold abroad and imported. . . . Retailers need confidence that lawfully-produced goods they purchase from importers and distributors can be resold in United States commerce free from claims of copyright infringement.

Similarly, consumers have the right to purchase goods at discount prices free of constraints on their property rights. . . . The principles underlying the first sale doctrine are of vital interest to suppliers, retailers, and their customers. Therefore, in support of the proper interpretation of the first sale doctrine by the Petitioner Costco, the *amici* submit this brief to inform the Court of the potentially destructive

impact of the Ninth Circuit's decision upon modern commerce, and to urge the Court to grant certiorari in this important case.

Brief for Retail Industry Leaders Association et al. as Amici Curiae Supporting Petitioner, *Costco v. Omega* (2010) (No. 08-1423), at 4-5. Making the application of the first sale doctrine turn on the location where the copies were (legitimately) manufactured, these *amici* argue, cripples the global marketplace. As eBay, Inc., puts it in its amicus brief, "eBay's customers buy and sell a wide variety of goods manufactured domestically and abroad. These buyers and sellers need confidence that lawfully produced and purchased goods may be resold free from unknown and unknowable claims of copyright infringement." Brief for eBay, Inc. as Amicus Curiae Supporting Petitioner, *Costco v. Omega* (2010) (No. 08-1423), at 2.

The United States, despite filing an *amicus curiae* brief against the Court granting *certiorari*, largely agrees with these policy concerns:

Taken together, the decision below and this Court's ruling in *Quality King* create the anomalous result that a copyright holder can exercise its statutory right to bar unauthorized importation *only* when the relevant copies are made abroad. That differential treatment of domestic- and foreign-manufactured goods has no evident policy justifications, and it could at least in theory provide an artificial incentive for outsourcing. There is no reason to suppose that Congress anticipated and intended that result.

Brief for the United States as Amicus Curiae, *Costco v. Omega* (2010) (No. 08-1423), at 18-19.

Summary

Will the Supreme Court confirm the Ninth Circuit's reading of Section 109(a), which would have the effect of strengthening copyright owners' power to control the unauthorized importation of their goods? Or will the Supreme Court find that "lawfully made under this title" simply means made in compliance with the U.S. Copyright Act, regardless of where the manufacture of the article in question takes place? The intellectual property bar is watching this case with great interest.

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Uli Widmaier is a partner with [Pattishall, McAuliffe, Newbury, Hilliard & Geraldson LLP](#), a [leading intellectual property law firm](#) based in Chicago, Illinois. [Pattishall McAuliffe](#) represents both plaintiffs and defendants in [trademark](#), [copyright](#), and [unfair competition trials and appeals](#). The firm advises its clients on a broad range of domestic and international intellectual property matters, including [brand protection](#), [Internet](#), and [e-commerce](#) issues. Uli's practice focuses on domestic and international [trademark](#), [copyright](#), [trade dress](#), and [Internet](#) law and litigation.