NAFTA: Protector of National Intellectual Property Rights or Blueprint for Globalization - The Effect of Nafta on the First Sale Doctrine in Copyright Law

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NAFTA: PROTECTOR OF NATIONAL INTELLECTUAL PROPERTY RIGHTS OR BLUEPRINT FOR GLOBALIZATION? THE EFFECT OF NAFTA ON THE FIRST SALE DOCTRINE IN COPYRIGHT LAW*

I. INTRODUCTION

CBA v. Record Store, a Hypothetical

CBA Records, Inc. ("CBA") is a United States company that manufactures compact discs and cassette tapes for sale in the United States and abroad. In anticipation of increased business dealings between the United States and Mexico as a result of the North American Free Trade Agreement ("NAFTA"), CBA authorized Grupo Musica, S.A., a Mexican company, to produce and sell certain recordings exclusively in Mexico under a licensing agreement.

Some time later, a CBA employee in the United States was browsing in a local record store and noticed a CBA compact disc that was manufactured in Mexico. Upon further investigation, it was determined that a third party had bought several thousand recordings from Grupo Musica in Mexico, brought them into the United States, and sold them to various retail outlets around the country. CBA sued the retailer and the third party importer (collectively "Record Store") for copyright infringement, under 17 U.S.C. §§ 106(3) and 602(a).

Record Store's defense is based on 17 U.S.C. § 109(a), commonly known as the "first sale doctrine." Under this doctrine, once a legally manufactured, copyrighted product is placed on the market for the first time with the copyright owner's authority, that owner's subsequent distribution

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1. 2 MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT § 8.12 [B], at 8-140 (1995).
rights in the product are extinguished, and he or she cannot control any future sales of that physical copy of the product.²

CBA believes that the first sale doctrine applies only to products manufactured in the United States. It asserts that because the recordings at issue were made in Mexico, they have not been "lawfully made" for purposes of United States law, and the first sale defense does not avoid liability for copyright infringement. Record Store maintains, however, that because the United States and Mexico have entered into a free trade agreement (NAFTA), that agreement governs and should act to expand the first sale territory to allow the defense regardless of the place of manufacture, as long as the manufacture was authorized and was within the NAFTA territories. Record Store cites recent European case law that reached this result. In the European Community, the Treaty of Rome was found to override national law so that a first sale in one member state was found to act as a first sale in any other member state.³

This Comment analyzes whether NAFTA could affect the first sale defense in United States copyright law. Part II reviews United States copyright statutes and recent case law regarding the exclusive distribution right and the first sale doctrine. Part III explains how the European Community has dealt with the issue. Part IV introduces the concept of free trade agreements, explains the various types of agreements and their underlying principles, and analyzes the differences between the treaty establishing the European Community and NAFTA, to suggest possible resolutions to the problem posed in CBA v. Record Store.

II. UNITED STATES LAW

A. The Distribution Right and the First Sale Doctrine

United States copyright law has its roots in the Constitution of the United States, which provides Congress with the power "[t]o promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries."⁴

Congress has specified five exclusive rights for authors or owners of copyrighted works, one of which is the exclusive right to distribute copies

of the work to the public by sale or rental. These rights are contained in Title 17 of the United States Code, otherwise known as the Copyright Act. Any distribution which has not been authorized by the copyright owner is, therefore, an infringement of the copyright and subject to legal action under this title.

The Copyright Act distinguishes ownership of a copyright in a work from ownership of the material object in which the work is embodied. "Transfer of ownership of any material object [such as a phonorecord or compact disc] . . . does not of itself convey any rights in the copyrighted work [the performance] embodied in the object." Thus, the copyright owner retains his or her rights when the work is sold, even though he or she no longer owns the actual physical copy. The owner of the physical copy, in turn, is entitled to sell or otherwise dispose of the item without the permission of the copyright owner. In other words, once the copyright owner consents to the sale of a particular physical copy of his or her work, and it is sold for the first time, the distribution right has been extinguished, and the copyright owner loses exclusive control over that particular copy

6. 17 U.S.C. § 106 states:
   Subject to sections 107 through 120, the owner of copyright under this title has the exclusive rights to do and to authorize any of the following:
   (1) to reproduce the copyrighted work in copies or phonorecords;
   (2) to prepare derivative works based upon the copyrighted work;
   (3) to distribute copies or phonorecords of the copyrighted work to the public by sale or other transfer of ownership, or by rental, lease, or lending;
   (4) in the case of literary, musical, dramatic, and choreographic works, pantomimes, and motion pictures and other audiovisual works, to perform the copyrighted work publicly; and
   (5) in the case of literary, musical, dramatic, and choreographic works, pantomimes, and pictorial, graphic, or sculptural works, including the individual images of a motion picture or other audiovisual work, to display the copyrighted work publicly.

7. 17 U.S.C. § 501(a) states:
   Anyone who violates any of the exclusive rights of the copyright owner as provided by sections 106 through 118 or of the author as provided in section 106A(a), or who imports copies or phonorecords into the United States in violation of section 602, is an infringer of the copyright or right of the author, as the case may be.

9. 17 U.S.C. § 109(a) states:
   Notwithstanding the provisions of section 106(3), the owner of a particular copy or phonorecord 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 or phonorecord.

of the product. This is called the first sale doctrine, which acts as a limitation on the exclusive distribution right conferred by section 106(3)\textsuperscript{10} and is often raised as a defense to a charge of copyright infringement.\textsuperscript{11}

The first sale doctrine thus provides that the distribution right may be exercised with respect to the initial sale of copies or phonorecords of a work, but may not be invoked so as to prevent or restrict their resale.\textsuperscript{12}

Without this provision, the exclusive distribution right of § 106(3) would, for example, prohibit the unimpeded disposition of copyrighted products in the stream of commerce and would go so far as to prevent the sale of used books at garage sales or second-hand bookstores. To compensate for the loss of control, the copyright owner factors in the cost of subsequent transfers when charging for the first sale.\textsuperscript{13}

Although this rule is statutory, it “finds its origins in the common law aversion to limiting the alienation of personal property.”\textsuperscript{14} There is, however, an economic reason for the rule as well. The question underlying the first sale doctrine is whether or not the sale or other disposition of the copyrighted product has been sufficient to compensate the copyright owner for its use.\textsuperscript{15}

\section*{B. The Importation Right and the First Sale Doctrine}

The situation changes when a subsequent sale of the copy crosses international borders. At that point, it seems that the copyright holder may maintain some continued control further down the chain of distribution. Section 602(a) of the Copyright Act specifies that the unauthorized importation into the United States of copies or phonorecords of a work that

\begin{itemize}
\item \textsuperscript{10} 17 U.S.C. § 106(3) (1994).
\item \textsuperscript{11} 2 Nimmer & Nimmer, supra note 1, § 8.11[B], at 8-134.
\item \textsuperscript{12} Id. § 8.12[B], at 8-137, 8-138. The “sale of a copy or phonorecord (or other transfer of title) will vitiate the copyright owner’s power to prevent not only further sales, but also further physical disposition of such copies or phonorecords even if such further disposition does not involve a transfer of title.” Id. at 8-139, 8-140.
\item \textsuperscript{13} Donna K. Hintz, Comment, Battling Gray Market Goods With Copyright Law, 57 ALB. L. REV. 1187, 1194-95 n.46 (1994) (quoting ROBERT A. GORMAN, FEDERAL JUDICIAL CENTER, COPYRIGHT LAW 80 (1991) (citations omitted)).
\item \textsuperscript{15} Sebastian Int’l, 847 F.2d at 1096-97 (quoting Burke & Van Heusen, 233 F. Supp. at 883-84).
\end{itemize}
have been acquired outside the United States is an infringement of the exclusive distribution right of section 106(3).\(^{16}\)

Some consider section 602 to provide potential plaintiffs a weapon against the gray market.\(^{17}\) "Gray market goods" are authorized authentic goods but are "available in this country outside of their normal channels of distribution."\(^{18}\) These genuine products are meant for sale abroad, having been manufactured either in the United States and then exported, or manufactured abroad by the copyright owner's licensee.\(^{19}\) Third parties,
not distributors authorized by the manufacturer, then buy and import the goods into the United States for resale without the copyright holder's consent. A common term for the importation of gray market goods is "parallel" importing; once the gray market goods arrive in the United States, they compete directly with the authorized domestic goods. "The controversy over gray market goods centers on whether manufacturers should have to compete against imports of their own products." 

Since gray market goods are being resold, rather than put on the market initially, "gray marketeers" can argue, in reliance on the first sale defense of section 109, that the rights of copyright holders do not extend to this "aftermarket." The central issue, then, is whether the "first sale doctrine" applies to such goods.

The interplay between the importation right and the first sale doctrine has received some attention in the literature. At first glance, the two policies appear to clash. How can a product which the copyright owner has authorized to be placed on the market, thereby extinguishing the owner's distribution rights, become infringing merely because it crosses a national border somewhere down the line of subsequent sales?

When a copyright owner first consents to the sale of his or her work, he or she still wishes to prevent unauthorized reproduction. Any attempt to control further distribution of copies already released into public channels, however, does not supplement that intangible right; rather, it is only a device to control the disposition of the tangible personal property that embodies the copyrighted work. "[A]t this point, the policy favoring a copyright monopoly for authors gives way to the policy opposing restraints of trade and restraints on alienation." The Copyright Act attempts to balance authors' monopoly interests in the control and exploitation of their writings with society's interest in the free flow of ideas, information, and commerce. Ultimately, the Copyright Act regards financial reward to the owner as secondary to society's interests.

21. SOBEL, supra note 19.
23. Id. at 1188-89.
27. Sebastian Int'l, 847 F.2d at 1095 (citing Sony Corp. of Am. v. Universal City Studios, Inc., 464 U.S. 417, 429 (1984)).
28. Id.
One interpretation of the interplay between the first sale doctrine and the importation right is that the latter is distinct and separate from the distribution rights conferred by section 106(3). As such, it would not be subject to limitation by the first sale defense of section 109(a), and copyright owners would be free to prevent unauthorized importation of copyrighted goods. Some United States District Courts have read section 602(a) in this way, but this reading does not represent a unanimous view and the trend seems to be against it.

The United States Court of Appeals for the Third Circuit preferred to harmonize sections 602(a) and 109(a) such that the import prohibition, rather than adding to the exclusive rights of section 106(3), serves only as a specific example of those rights still subject to the first sale limitation. This way, "once transfer of ownership has cancelled the distribution right to a copy, the right does not survive so as to be infringed by importation."

The latter interpretation, "if expansively construed, threatens to render the importation right 'virtually meaningless.'" Because of the territorial nature of copyright, however, United States courts have begun to recognize an additional distinction based on where the goods were made. The result in the Third Circuit has been that the first sale doctrine acts as a defense to a charge of copyright infringement, permitting unauthorized importation of copyrighted goods, only when those goods were manufactured in the United States. In other words, the first sale shield against liability for copyright infringement applies only to copies legally made and sold abroad under a territorially restricted license. If the goods were manufactured abroad, they would be outside the scope of section 109(a).

29. Id. at 1097.
30. Id.
32. Kernochan, supra note 31, at 1417 (citing Sebastian Int'l, 847 F.2d at 1093).
33. Sebastian Int'l, 847 F.2d at 1097.
34. Id. at 1099. This latter scenario, however, would apply only "when what is in issue is not the importing of copies produced and sold abroad under a territorially restricted license." Kernochan, supra note 31, at 1417-18.
35. 2 NIMMER & NIMMER, supra note 1, § 8.11[B], at 8-134 (quoting Columbia Broadcasting Sys., 569 F. Supp. at 49).
36. Sebastian Int'l, 847 F.2d at 1099.
Thus, in the hypothetical case *CBA v. Record Store*, the defendant Record Store cannot assert the first sale defense under United States law because the recordings were produced in Mexico. Therefore, CBA would prevail. A closer look at the cases will expand upon this discussion.

**C. The Cases**

Cases addressing the applicability of copyright law to the problem of gray market goods fall into two groups,\textsuperscript{38} based on whether or not the goods were originally manufactured in the United States.\textsuperscript{39} The first group includes cases which permitted re-entry of goods originally made in the United States, based on the first sale doctrine.\textsuperscript{40} The second group of cases prohibited the importation of copyrighted goods when the goods were manufactured abroad.\textsuperscript{41} Cases in the second group have assisted copyright owners in their battle against gray marketeers "because the courts ruled that section 602(a) importation rights are not limited by the first sale doctrine when goods, lawfully manufactured abroad, are imported without permission."\textsuperscript{42}

1. **Domestically Manufactured Goods First Sold in the United States**

"To the extent that goods are manufactured in this country, shipped abroad, and subsequently reimported, they are subject to the first sale defense and outside the scope of the importation bar."\textsuperscript{43} Courts have thus refused to allow the importation to be enjoined, often taking into consideration the financial benefits already received by the copyright holders from the initial sale of their goods.

While authentic Ralph Lauren products were in the custody of the customs service at ports awaiting entry into the United States, the copyright holders sought a preliminary injunction preventing entry because defendant

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39. *Id*.


43. 2 *Nimmer & Nimmer, supra* note 1, § 8.12(B), at 8-152 n.67.
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consignees were attempting to import the goods without the copyright holder’s permission.\textsuperscript{44} The \textit{Cosmair v. Dynamite Enterprises}\textsuperscript{45} court refused to grant the injunction, finding that the plaintiffs failed to establish a "substantial likelihood of success on the merits,"\textsuperscript{46} because the first sale doctrine of section 109(a) could be used to limit plaintiffs' claim of copyright infringement since the products had originally been made in the United States.\textsuperscript{47}

Similarly, Neutrogena Corporation, a major United States manufacturer of personal care products, shipped some of its products to a distributor in Hong Kong.\textsuperscript{48} Facts indicate that this distributor then sold the products to a third party, who sold the products to another party, who in turn shipped the products back to the United States.\textsuperscript{49} Several days after the products arrived at the port of entry, the United States Customs officials notified Neutrogena that a shipment of goods were received and appeared to be (and in fact were later determined to be genuine) Neutrogena products.\textsuperscript{50} Neutrogena sued the United States, through the United States Customs Agency, to restrain the entry of the Neutrogena products.\textsuperscript{51}

The court denied the injunction, stating that the first sale defense may be applicable here as it was in \textit{Cosmair}, especially when the goods were manufactured in the United States and sold to the defendant by a third party. The court further found it unlikely that the plaintiff would be irreparably harmed by the sale of plaintiff’s authentic products:

By no means can it be said that the sale of plaintiff’s authentic goods will affect or damage plaintiff’s good will or reputation. Additionally, if defendant has properly acquired title to the products, defendant’s right to alienation will be stifled by a restraining order. Finally, the public interest will not be infringed upon if the injunction is not issued.\textsuperscript{52}

The Third Circuit in \textit{Sebastian International, Inc. v. Consumer Contacts (PTY) Ltd.}, came to the same conclusion when it vacated an order

\textsuperscript{45} Id.
\textsuperscript{46} Id. at 347.
\textsuperscript{47} Id. at 346-47. Although there was a question of whether the sale was actually completed in the United States, the court nonetheless found the facts sufficient for § 109(a) to limit the application of § 602(a). Id. at 347.
\textsuperscript{49} Id.
\textsuperscript{50} Id.
\textsuperscript{51} Id.
\textsuperscript{52} Id. at 1903.
by a district court issuing a preliminary injunction against a similar infringement. 53 Sebastian International, Inc. ("Sebastian") is a California corporation that manufactures and markets personal care beauty supplies. Sebastian's products carry copyrights for the text and artistic content of their labels. Sebastian contracted with the defendant to distribute its products to professional hair styling salons in South Africa, but not elsewhere. Sebastian shipped products to the defendant in South Africa, who then reshipped them back to the United States. 54

The court found that under the first sale doctrine, when the plaintiff made and then sold its copies, it relinquished all further rights to sell or otherwise dispose of those copies. 55 "Unquestionably that includes any right to claim infringement of the [section] 106(3) distributive rights for copies made and sold in the United States. With respect to future distribution of those copies in this country, clearly the copyright owner already has received its reward through the purchase price." 56 The Third Circuit thus held that the first sale doctrine of section 109(a) supersedes the import right of section 602(a) where a domestic manufacturer first exports its materials and then attempts to invoke the copyright laws to enjoin a third party from importing the copyrighted goods. 57

2. Foreign Manufactured Goods

Several cases before the Ninth Circuit involved goods manufactured outside of the United States. The court has consistently held in these cases that the first sale doctrine is not a defense. In BMG Music v. Perez, 58 the plaintiffs produced, manufactured, distributed, and sold phonorecords in the United States. In addition, they owned copyrights in sound recordings embodied within those phonorecords. The plaintiffs sued Perez, alleging that he violated the Copyright Act by purchasing plaintiffs' copyrighted sound recordings manufactured abroad and exporting them to the United States where they were sold. 59

54. Id.
55. Id. at 1098-99.
56. Id. at 1099.
57. Id.; see Parfums Givenchy Inc. v. Drug Emporium, Inc., 38 F.3d 477, 482 (9th Cir. 1994), cert. denied, 115 S.Ct. 1315 (1995).
59. Id. at 319.
Perez contended that he was protected by the first sale doctrine. The court disagreed, concluding that the first sale doctrine does not provide a defense to infringement under 17 U.S.C. § 602 for goods manufactured abroad, because the words "lawfully made under this title" in section 109(a) grant first sale protection only to copies legally made and sold in the United States. The court reasoned that construing the first sale doctrine of section 109(a) as superseding the prohibition on importation of section 602 would render section 602 virtually meaningless. "Copyright owners would no longer have an exclusive right to distribute copies or phonorecords of works manufactured abroad, an interest clearly protected by section 602."

This result was reiterated most recently in Parfums Givenchy, Inc. v. Drug Emporium. "Amarige" is a perfume that is produced in France by Parfums Givenchy, S.A. and sold in the United States by Givenchy USA, its wholly owned subsidiary and owner of the United States copyright to the perfume box design. Third parties lawfully bought the perfume abroad, imported it into the United States without the authorization of either Parfums Givenchy, S.A. or Givenchy USA, and sold it to Drug Emporium, a discount retail chain, which retailed the perfume in the original copyright protected packaging.

Givenchy USA sued Drug Emporium for copyright infringement, alleging unauthorized importation under 17 U.S.C. § 602(a). Drug Emporium's defense was that the first sale doctrine of 17 U.S.C. § 109(a) protected it from liability because, as a lawful purchaser of a "lawfully made" copy, it is entitled to resell the copy without the copyright holder's authority.

The Ninth Circuit found that to resolve this case, it needed to determine the relationship between the first sale doctrine and the importation right of section 602(a). Drug Emporium contended that section

60. Id.
61. Id.
63. BMG Music v. Perez, 952 F.2d 318, 319 (9th Cir. 1991), cert. denied, 505 U.S. 1206 (1992). See also Columbia Broadcasting Sys., 569 F. Supp. at 49. The BMG Music court distinguished Sebastian Int'l, where the goods were originally manufactured and sold in the United States, declining to rule based on its facts because those facts were not before this court.
64. 38 F.3d 477.
65. Id. at 479.
66. Id. at 480.
67. Id.
109(a) supersedes section 602(a). In its view, "a lawful sale abroad of United States copyrighted foreign goods would terminate the exclusive right of the United States copyright holder to import and distribute those goods in the United States, in the same way that a lawful domestic sale terminates the exclusive distribution rights of domestically manufactured materials."68

The court acknowledged the important policy considerations on both sides of the issue because of the gray market implications.69 Nevertheless, the court allowed copyright holders the right to bar importation of a specific copy, "unless and until there has been a 'first sale' in the United States."70 The court reasoned that section 602(a) in effect gives section 106(3) an extraterritorial scope, "ensur[ing] that a United States copyright owner will gain the full value of each copy sold in the United States by preventing the unauthorized importation of copies sold abroad from being used as a means of circumventing the copyright owner’s distribution rights in the United States."71 The rule set forth in BMG Music, that the statutory language in section 109(a), “lawfully made under this title,” grants first sale protection only to copies made and sold legally in the United States, was essential to preclude rendering section 602 "virtually meaningless."72

The court found no first sale because the perfume had been manufactured abroad and the defendant purchased it abroad. Therefore, the foreign purchase could not trigger section 109(a) so as to allow subsequent unauthorized sales in the United States. The first sale, for purposes of section 109(a), occurred when Drug Emporium placed the perfume on the market in the United States after importing it. Therefore, the defendant infringed the United States copyright when it imported and sold the perfume without authorization by the copyright holder.

In summary, the question of whether the first sale doctrine acts as a defense to allegations of copyright infringement by unauthorized importation into the United States turns on the question of where the goods were made and first sold. If made and first sold in the United States, then the defense applies, and unauthorized importation from abroad back into the United States will not infringe the copyright. If made abroad, the first sale

68. Id. at 481.
69. Drug Emporium, 38 F.3d at 481 n.6.
70. Id. at 481 (emphasis omitted).
71. Id. at 481 (citing Parfums Givenchy, Inc. v. C & C Beauty Sales, Inc., 832 F. Supp. 1378, 1390-91 (C.D. Cal. 1993)).
72. Id.
doctrine is no defense, and the unauthorized importation will be a copyright infringement.\footnote{73}{Although the distinction between the applicability of the first sale doctrine to foreign versus domestically manufactured goods appears firm, it has been called into question by the Third Circuit. In a footnote, the \textit{Sebastian} court indicated "some uneasiness" with the construction of the phrase in section 109(a), "lawfully made under this title," to describe goods made in the United States, "because it does not fit comfortably within the scheme of the Copyright Act. When Congress considered the place of manufacture to be important, as it did in the manufacturing requirement of section 601(a), the statutory language clearly expresses that concern." \textit{Sebastian Int'l, Inc. v. Consumer Contacts (PTY) Ltd.}, 847 F.2d 1093, 1098 n.1 (3d Cir. 1988). In dictum if not in holding, therefore, \textit{Sebastian} calls into question the continued interpretation of the phrase as meaning legally made and sold in the United States. 273. 2 \textit{Nimmer \& Nimmer}, supra note 1, at § 8.12[B], 8-152 n.67. This creates a possibility that, in at least the Third Circuit, the first sale doctrine may be found to apply also to foreign-manufactured goods. Hintz, \textit{supra} note 7, at 1207.\textit{}}

Thus, returning to the hypothetical, and according to United States law, as described in this section, Record Store's first sale defense would fail because the recordings were manufactured in Mexico, not in the United States. Therefore, they have not been "lawfully made" for purposes of United States law.

The cases described above did not involve countries which are members of the newly organized NAFTA. Record Store contends that because the United States and Mexico have entered into this free trade agreement, the agreement governs and should act to expand the first sale territory to allow the defense, regardless of place of manufacture, as long as the manufacture was authorized and within NAFTA territory. Record Store cites recent European case law, under which this was indeed the result.\footnote{74}{In Europe, the treaty establishing the European Economic Community was found to override national law, and a first sale in one member state was found to act as a first sale in any other member state.\textit{75} We turn now to the events in the European Community.\textit{}}

We turn now to the events in the European Community.

\section*{III. THE EUROPEAN COMMUNITY}

\subsection*{A. The Structure of the Agreement}

The European Community ("EC") or as it is presently known, the European Union, was originally founded in 1957 by the Treaty Estab-
lishing the European Economic Community ("EEC Treaty"). Its aim was to establish a common market:

[t]o promote throughout the Community a harmonious development of economic activities, . . . a high degree of convergence of economic performance, a high level of employment and of social protection, the raising of the standard of living and quality of life, and economic and social cohesion and solidarity among Member States.

For these purposes, Article 3 of the EEC Treaty provides for the following activities:

(a) the elimination, as between Member States, of customs duties and quantitative restrictions on the import and export of goods, and of all other measures having equivalent effect;

(b) a common commercial policy;

(c) an internal market characterized by the abolition, as between Member States, of obstacles to the free movement of goods, persons, services and capital;

. . . .


The TEU does not override, but rather amends the EEC Treaty. TEU, art. G. One of the things the amendment did was to delete the term "Economic" from the name "European Economic Community." TEU, art. G.A(1). It did so "to reflect the change in scope of the Treaty to include new provisions which are not exclusively economic in character." JACQUELINE DUTHEIL DE LA ROCHERE, RIGHTS OF INDIVIDUALS UNDER EEC LAW 23 n.2 (class materials prepared for the Tulane Institute of European Legal Studies, Summer, 1994). The remainder of this Comment includes quotes from and references to the EEC Treaty provisions, some of which have been amended by the TEU. Those amended provisions are hereinafter referred to as EEC Treaty, amended by the TEU.

The EC changed its name to the "European Union" following the signing and entry into force of the Maastricht Treaty on European Union in November of 1993. TEU, art. A. For consistency (the European cases presented in this Comment were decided by the ECJ before the name was changed to the "European Union," and the Court therefore speaks in terms of the "EC"), the term "European Community" or "EC" will be used throughout this Comment instead of "European Union" or "EU."

77. Corbet, supra note 75, at 327.
78. EEC Treaty, amended by the TEU, supra note 76, at art. 2.
79. Previously, this section read "the establishment of a common customs tariff and of a common commercial policy towards third countries." EEC Treaty, supra note 76, at art. 3(b).
(g) a system ensuring that competition in the internal market is not distorted;
(h) the approximation of the laws of Member States to the extent required for the functioning of the common market.80

Two of these fundamental principles, Freedom of Movement (mentioned in Article 3(c)) and Freedom of Competition between Member States (mentioned in Article 3(g)), are particularly relevant to intellectual property, and are given specific effect in various other EEC Treaty provisions.81 Articles 30 through 34 attempt to guarantee freedom of movement of goods within the Community by abolishing (gradually, according to a specified timetable) quantitative restrictions between Member States.82 Articles 85 and 86 regarding Rules on Competition prohibit agreements or concerted practices, or abuses by parties with a dominant market share, which affect trade between Member States so as to restrict competition within the common market.83

80. EEC Treaty, amended by the TEU, supra note 76, at art. 3.
81. Corbet, supra note 75, at 329.
82. Article 30: “Quantitative restrictions on importation and all measures with equivalent effect shall . . . be prohibited between Member States.” EEC Treaty, supra note 76, art. 30, at 26.
Article 34: “Quantitative restrictions on exportation and any measures with equivalent effect shall hereby be prohibited as between Member States.” Id. art. 34.1 at 28.
83. Article 85.1 states:
The following shall be deemed to be incompatible with the Common Market and shall hereby be prohibited: any agreements between enterprises, any decisions by associations of enterprises and any concerted practices which are likely to affect trade between the Member States and which have as their object or result the prevention, restriction or distortion of competition within the Common Market, in particular those consisting in:
(a) the direct or indirect fixing of purchase or selling prices or of any other trading conditions;
(b) the limitation or control of production, markets, technical development or investment;
(c) market-sharing or the sharing of sources of supply;
(d) the application to parties to transactions of unequal terms in respect of equivalent supplies, thereby placing them at a competitive disadvantage; or
(e) the subjecting of the conclusion of a contract to the acceptance by a party of additional supplies which, either by their nature or according to commercial usage, have no connection with the subject of such a contract.

EEC Treaty, supra note 76, art 85.1, at 47-48.
Article 86 states:
To the extent to which trade between any Member States may be affected thereby, action by one or more enterprises to take improper advantage of a dominant position within the Common Market or within a substantial part of it shall be deemed to be incompatible with the Common Market and shall hereby be
The Court of Justice of the European Communities ("ECJ") was established in Luxembourg to "ensure observance of law and justice in the interpretation and application of this Treaty," resulting in a new area of case law. The most abiding and significant outcome has been that when the treaty has conflicted with national law, the treaty has taken precedence. The ECJ has declared that "the primacy of Community law, particularly regarding principles as fundamental as those of the free movement of goods and freedom of competition, prevails over any use of a rule of national intellectual property law in a manner contrary to those principles."

B. The Distribution Right and the First Sale Doctrine in Europe: Specific Subject Matter of Copyright and the Doctrine of Exhaustion

Corresponding to the exclusive rights granted by statute to United States copyright owners, the ECJ speaks in terms of the "specific subject matter" of intellectual property. This includes: (1) the exclusive right to manufacture, reproduce or perform the work (which includes the right to prevent unauthorized reproduction); and (2) the right to first publication, i.e., to put the product on the market for the first time.

The second right embodies the first sale doctrine, which, as explained above, "generally limits a copyright owner's right to control distribution of a given copy of a work once that copy is 'first' sold. The distribution right
of that one copy is then said to be, to some degree, [extinguished, or in European terms,] 'exhausted.'

Before the formation of the EC, the exhaustion of the distribution right, "and the first sale that triggered that exhaustion, [were seen to occur] in only one country at a time. Consequently, the relevant market was . . . national in scope." This is similar to the state of the law in the United States. The EEC Treaty, however, sought to unite several long-established national markets into a single common market and to encourage Community-wide free movement of goods. Territorial restrictions would directly conflict with this principle. Intellectual property rights asserted under the law of a Member State have therefore come into direct conflict with the objectives of the EC by threatening to hinder the free movement of goods.

The solution to the conflict involved performing a delicate balancing act between two provisions of the Treaty. Article 36 creates an intellectual property exception to the free movement of goods principle. On one hand, Article 36 allows restrictions on the movement of goods when justified by a need for the protection of industrial and commercial property. "Industrial and commercial property" has been deemed to include intellectual property rights, including copyrights. On the other hand, the Treaty provides a mechanism to ensure its own supremacy, stating that "[s]uch prohibitions or restrictions shall not, however, constitute either a means of arbitrary discrimination or a disguised restriction on trade between Member States."

In a series of cases, the ECJ has taken the position that once an owner of an intellectual property right consents to market his or her product in one EC Member State, under Community law that right is exhausted.

91. Corbet, supra note 75, at 333.
92. Id. at 334.
93. Id. at 334.
94. EEC Treaty, supra note 76, art. 36 at 29.
95. Article 36 reads: "The provisions of Articles 30 to 34 inclusive shall not be an obstacle to prohibitions or restrictions in respect of importation, exportation or transit which are justified on grounds of . . . the protection of industrial and commercial property . . . ." Id.
96. Corbet, supra note 75, at 334; see also Case 78/70 Deutsche Grammophon Gesellschaft mbH v. Metro-SB-Grossmärkte GmbH & Co., 1971 E.C.R. 487, 500 (1971) (where the Court proceeded on the "assumption that those provisions [industrial and commercial property] may be relevant to a right related to copyright."). Id.
97. EEC Treaty, supra note 76, art. 36, at 29.
The owner cannot thereafter use it to restrain the parallel importation of that product into another EC Member State. 99

The outcome, in general, has transformed the definition of the relevant market in a way that yields to the EEC Treaty's principle of the free movement of goods. Where it once was the national territory in which the first sale of the copy or product occurred, and the location of the first sale would trigger the exhaustion of the right to control further distribution of that copy or product in that country, the relevant market is now the Community. "Thus, any party marketing a copy or product which has already been first sold on the Common Market can raise the . . . [d]efense of Community-wide exhaustion against a holder of rights suing to control distribution in the . . . EC." 100

C. The Cases

The leading cases defining the free movement of copyrighted goods within the EC are commonly known as Deutsche Grammophon, 101 Dansk Supermarked, 102 and GEMA. 103 In these cases the Treaty was found to override national copyright laws because the copyright holder had consented to distribution and to the resulting exhaustion of that right. 104

In Deutsche Grammophon, 105 the plaintiff, a West German record producer, produced and sold phonorecords within the Federal Republic of Germany directly to retailers who, as part of the agreement, had to sign an undertaking to maintain a certain price for the records. Defendant Metro refused to sign the undertaking. As a result, Deutsche Grammophon ("DG") broke off business relations with Metro. 106

Meanwhile, DG also exclusively licensed the distribution of the phonorecords by other entities in the common market, including its subsidiary in France, where DG records were sold at a lower price. Some

99. Id. at 858-59.
100. Corbet, supra note 75, at 335-36.
106. Id. at 489-90.
DG records, pressed by DG in Germany and supplied to the Paris subsidiary, were sold and resold until they ended up with Metro, who turned around and sold them to retail customers in Germany at a price below that fixed by DG. 107  

DG applied to the German courts and obtained a provisional injunction prohibiting Metro from distributing the records, based on German national copyright law. 108 Metro's unsuccessful protest and ensuing appeal eventually reached the ECJ. Metro's defense included the contentions that (1) DG's distribution rights in the records had been exhausted by the delivery to the French subsidiary, and (2) the license agreement between DG and the French subsidiary divided the market, making interstate trade more difficult, which, together with the price fixing, infringed Articles 85 and 86 of the EEC Treaty. 109  

The issue decided by the Court of Justice, simply put, was whether the German national law conflicted with the Treaty. 110 The court found that it did. 111 Rejecting an anti-competition argument (Article 85) in favor of an analysis relating to the free movement of goods (Article 30), the court weighed the two counterparts of Article 36 112 and found that a copyright holder's attempt to prohibit the sale of his or her goods in one Member State, when he or she has consented to their sale in another Member State, solely because this marketing has not occurred in the territory of the first Member State, conflicts with the provisions regarding the free movement of goods as well as the essential aim of the Treaty to integrate the national markets into one uniform market. 113 It does so by using national laws to maintain the isolation of the national markets, thereby dividing the market and causing arbitrary discrimination or disguised restrictions in trade between the Member States, as prohibited by Article 36. 114 The ECJ thus determined that there was "Community-wide exhaustion of [the copyright] relative to the phonorecords which were 'placed on the market by the [owner of the right], or with his [or her] consent, in another Member State.'" 115  

107. Id. at 490.  
108. Id. at 503.  
109. Id. at 490-91.  
111. Id. at 500.  
112. Id.  
113. Id.  
114. Id.  
115. Corbet, supra note 75, at 336.
The GEMA cases\textsuperscript{116} concerned differences in rates of authors' royalties collected in the various Member States. Records had been manufactured and marketed in various Member States with the copyright holders' consent. The requisite licenses had been granted by those owners, and royalties had been paid on the basis of distribution in the country of manufacture. The records were then imported into Germany, where royalty rates were higher.\textsuperscript{117} GEMA, a German collecting society attempting to protect the distribution rights of the authors it represented regarding the imported records, sought damages for infringement of those rights in the form of the difference in the amount of royalties paid in the other states and the higher royalty in force in Germany. The question in these cases did not concern the prohibition of imports as such, but rather the legality of the additional royalty.\textsuperscript{118} The German national court ordered the payment.\textsuperscript{119}

The ECJ held that such a payment was incompatible with the operation of the common market and the aims of the Treaty and was therefore precluded by Articles 30 and 36 of the Treaty:

\begin{quote}
[N]o provision of national legislation may permit . . . [a company] which is responsible for the management of copyrights and has a monopoly on the territory of a Member State by virtue of that management to charge a levy on products imported from another Member State where they were put into circulation by or with the consent of the copyright owner and thereby cause the Common Market to be partitioned. Such a practice would amount to allowing a private . . . [company] to impose a charge on the importation of sound recordings which are already in free circulation in the Common Market on account of their crossing a frontier; it would therefore have the effect of entrenching the isolation of national markets which the Treaty seeks to abolish.\textsuperscript{120}
\end{quote}

The court felt that the existence of disparities between national laws cannot justify measures that are incompatible with the Treaty and impede

\textsuperscript{117} Id. at 149-150.
\textsuperscript{118} Id. at 154.
\textsuperscript{119} Id. at 150.
\textsuperscript{120} Id. at 163-64.
the free movement of goods within the Common Market. These disparities continue to exist in the absence of any harmonization and are capable of distorting competition between Member States.

In *Dansk Supermarked*, Imerco, a Danish company, ordered a special edition set of china dishes from a United Kingdom manufacturer to sell in Scandinavia in honor of the company's fiftieth anniversary. Imerco chose the designs and imposed very high standards of quality. As a result, approximately twenty percent of the dishes were found to be unacceptable. Imerco agreed to let the United Kingdom manufacturer sell the rejected sets in the United Kingdom, but prohibited their resale in Denmark.

Dansk Supermarked, also a Danish company, bought these sets through a reseller who had purchased them in the United Kingdom and sold them in its supermarkets in Denmark. Imerco took the matter to the national court which, based on a national Danish law, prohibited Dansk Supermarked from selling the sets. Dansk Supermarked appealed, claiming that the Treaty took precedence over the Danish law and made it impossible for Imerco to prevent parallel imports.

The case was referred to the ECJ to determine whether goods which have been lawfully marketed in one Member State with the consent of the company entitled to sell them, may be prohibited from being marketed in another Member State under an agreement between that company and the manufacturer. The answer was no. The court held that the exception in Article 36 to the free movement of goods, while justified for the purpose of safeguarding rights which constitute the specific subject matter of industrial and commercial property, is limited to the content of that

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The basic objectives of joint collective societies were accepted as legitimate. It is proper for individual members, such as composers, authors and publishers, to protect their interests against major music users, namely broadcasting organizations and record companies, by assigning rights to a joint association to enforce rights and to collect royalties. Nevertheless, these associations may not enforce anticompetitive arrangements if they go beyond what is required "for the association to carry out its activity on the necessary scale."

Corbet, *supra* note 75, at 355 (citations omitted).


123. *Id.* at 183-84.

124. Imerco relied on national provisions for the protection of both the copyright (in the design and production of the dishes) and the trademark (the right involved in affixing its name to the product). *Id.* at 198.

125. *Id.* at 184.

126. *Id.* at 196.

127. The "specific subject matter" of copyright consists of the exclusive right to manufacture and reproduce the work and the right to put the copy on the market for the first time. *See supra* part III.B.
specific subject matter. This in turn, is exhausted when a product has been lawfully distributed on the market in another Member State by the actual proprietor of the right or with his or her consent.\textsuperscript{128}

Returning once again to the hypothetical case of \textit{CBA v. Record Store}, where Record Store's first sale defense would fail under United States law, it would probably prevail if we were to set the case in Europe. If one imagines for a moment that CBA is a French company and its licensee, Grupo Musica, is a German company, it would not matter in which country the recordings were manufactured and first put on the market. A first sale in Germany would cause Community-wide exhaustion of the distribution right so that the French copyright holder could not assert a copyright infringement claim against the German company.\textsuperscript{129}

In North America, the question is whether the potential exists for NAFTA to be interpreted as having a similar effect vis-à-vis national copyright laws of the United States, Canada, and Mexico, as the EEC Treaty has had in Europe. The logical analysis the court would have to apply to answer this question can be expressed in the following syllogism: The overriding effects of the EEC Treaty upon the national laws of its Member States have caused an expansion of the first sale territory to the boundaries of the entire Community. NAFTA is a free trade agreement similar to and organized for the same objectives as the EEC Treaty. Therefore, NAFTA should have a similar effect upon its member territories.

To determine whether this conclusion is valid, the truth of the underlying premises must first be ascertained. Regarding the major premise, a review of relevant European case law demonstrated that the stated effect—expansion of the first sale territory—has in fact occurred.\textsuperscript{130} Settling the truth of the minor premise necessitates an understanding of the nature of free trade agreements in general, and then a comparison of NAFTA with the EEC Treaty both in terms of their underlying principles and their specific provisions regarding the protection of intellectual property.

\textsuperscript{128} Dansk Supermarked, 1981 E.C.R., at 196. 
\textsuperscript{129} Leigh, supra note 98, at 858-59. 
\textsuperscript{130} See supra part III.C and notes 101-04.
IV. THE NORTH AMERICAN FREE TRADE AGREEMENT

A. An Introduction to Free Trade Agreements

The most important international economic agreement in the history of world trade is the General Agreement on Tariffs and Trade ("GATT"), with well over one hundred signatories. GATT was developed in a series of conferences between 1946 and 1948, and "was intended to reverse the protectionist and discriminatory trade practices that had multiplied during the pre-war depression years." In combination with the World Bank and the International Monetary Fund, GATT was designed to help advanced industrial countries achieve the objectives of raising standards of living, ensuring full employment and stable exchange rates, developing the full use of the resources of the world, and expanding the production and exchange of goods.

GATT is "not a single agreement, but is a series of over one hundred agreements, protocols, and . . . tariff schedules." The central core of the GATT system is the commitment by each country to limit its tariffs, or customs taxes, on similar items within a specified ceiling. This commitment is based on GATT's two main underlying principles of non-discrimination among countries. Under the Most Favored Nation principle ("MFN"), each member of GATT is obligated to treat other GATT members at least as well as it treats any other country with regard to imports or exports. The National Treatment principle requires that each country treat imports no worse than domestically produced goods, under its own internal taxation or regulatory measures. In other words, it

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134. GATT, supra note 131, pmbl. at 194.
135. JACKSON & DAVEY, supra note 133, at 296.
136. Id.; GATT, supra note 131, at art. 2. The GATT also seeks to limit non-tariff barriers to trade such as quotas or import or export licenses. See GATT, supra note 131, at arts. 11, 16.
137. GATT, art. 1 states in pertinent part:

With respect to customs duties . . . and with respect to all rules and formalities in connection with importation and exportation . . . any advantage, favor, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties.

GATT, supra note 131, at art. 1.
should not afford greater protection to its own domestic production.\footnote{138} Under these non-discriminatory trade principles, trade and world wealth have exploded tremendously since World War II.\footnote{139}

Exceptions were written into the original treaty with developing countries in mind, allowing for means by which smaller, less wealthy countries could group together to increase their own economic strength. Two of these exceptions are customs unions and free trade areas. They were not seen as very significant exceptions at first, but have in fact affected the entire concept of world trade, particularly since the massive trade unit of the European Community ("EC") was formed.\footnote{140}

The customs union and free trade area are now the two most important types of modern trade agreements.\footnote{141} Although both promote free trade among their members, each has its own distinct qualities. The customs union, also known as a common market, combines political and economic objectives.\footnote{142} The EC is one example.\footnote{143} As discussed more fully above, the EC's purposes and underlying principles, besides the elimination of quantitative restrictions, include a common external commercial policy, freedom of movement, and freedom of competition between Member States.

Countries within the common market "eliminate essentially all internal tariff barriers and coordinate their external policies to create a uniform tariff policy for goods coming from countries that are not within the common market."\footnote{144} GATT defines a customs union as:

the substitution of a single customs territory for two or more customs territories, so that (i) duties and other restrictive regulations of commerce . . . are eliminated with respect to substantially all the trade between the constituent territories of the union . . . and (ii) . . . substantially the same duties and other regulations of commerce are applied by each of the

\footnotesize{138. See id., at art. 3.}
\footnotesize{139. Round Table Discussion: The North American Free Trade Agreement: In Whose Best Interest?, 12 J. INTL. L. Bus. 536, 537 (1992).}
\footnotesize{140. Id.}
\footnotesize{142. Id. (citing D. LASOK & J.W. BRIDGE, LAW AND INSTITUTIONS OF THE EUROPEAN COMMUNITIES 385-86 (4th ed. 1987)).}
\footnotesize{143. Id. at 100 (citing CROOKELL, supra note 141, at 21).}
\footnotesize{144. Id. at 99-100 (citing CROOKELL, supra note 141, at 21-22).}
members of the union to the trade of territories not included in the union.\textsuperscript{145}

Each individual state "surrenders some of its sovereign power to regulate trade across its borders by conforming to the trade policies of the common market."\textsuperscript{146} The result is a single market. "Harmonization of trade regulation is the hallmark of this type of trade agreement."\textsuperscript{147}

A free trade area is the second type of modern trade agreement.\textsuperscript{148} GATT defines a free trade area as "a group of two or more customs territories in which the duties and other restrictive regulations of commerce . . . are eliminated on substantially all the trade between the constituent territories in products originating in such territories."\textsuperscript{149} Countries in a free trade area "have the same economic goals as members of a common market, such as efficient access to a larger market; a free trade area, however, fulfills these goals primarily through economic means."\textsuperscript{150} Members maintain their own distinct tariffs and regulations on non-members' imported goods, while the agreement ensures easy trading access between the member states' markets.\textsuperscript{151}

Like GATT, a key provision of a free trade area agreement is national treatment. "National treatment requires each state to subject imported goods to the same regulations which apply to domestically produced goods,"\textsuperscript{152} thereby preventing discriminatory regulation of goods in the free trade area based on country of origin.\textsuperscript{153} NAFTA is an example of a free trade area,\textsuperscript{154} and like GATT, requires national treatment.\textsuperscript{155}


\textsuperscript{146} Strong, \textit{supra} note 141, at 100 (citing LASOK & BRIDGE, \textit{supra} note 142, at 33).

\textsuperscript{147} \textit{Id.} at 100 (citing DERRICK LOYATT & ALAN DASHWOOD, THE SUBSTANTIVE LAW OF THE EEC 21 (1987)).

\textsuperscript{148} \textit{Id.} at 100 (citing CROOKELL, \textit{supra} note 141, at 19).

\textsuperscript{149} GATT, \textit{supra} note 145, at art. 24.8(b).

\textsuperscript{150} Strong, \textit{supra} note 141, at 100.

\textsuperscript{151} \textit{Id.} (citing CROOKELL, \textit{supra} note 141, at 28-29).

\textsuperscript{152} \textit{Id.} at 100 (citing CROOKELL, \textit{supra} note 141, at 22).

\textsuperscript{153} See GATT, \textit{supra} note 131, at art. 3.

\textsuperscript{154} Strong, \textit{supra} note 141, at 101 ("Other free trade agreements which have been negotiated in compliance with GATT standards include the 1960 European Free-Trade Area, the 1965 U.K.-Ireland Free-Trade Agreement, the 1983 Australia-New Zealand Closer Economic Relations Agreement, and the 1986 United States-Israel Agreement."). \textit{Id.} at 101, n.55 (citing CROOKELL, \textit{supra} note 141, at 19).

B. Comparing NAFTA and the EEC Treaty

1. Structure of the Agreement

As stated above, a free trade area is defined in GATT as a group of two or more customs territories, whereas a customs union is defined as the substitution of a single customs territory for two or more customs territories. The ECJ has stated the purpose of the EEC Treaty as seeking "to create a single market reproducing as closely as possible the conditions of a domestic market."5

It appears that the EC, much more so than a free trade area, is akin to a single unit of government. Besides the establishment of a common customs tariff and of a common commercial policy towards other countries, the EEC Treaty also lists, among its objectives, types of activities that make it more than just a trade agreement, such as "the strengthening of economic and social cohesion" and common policies in various other "spheres." As a political unit, the influence of the EC upon the domestic laws of its Member States is potentially greater than the influence of a free trade area such as NAFTA upon the domestic laws of its constituent parties.

The EEC Treaty created its own judicial system to ensure the uniform interpretation and application of its provisions throughout the EC. "In addition, article 100 of the Treaty creates a legal basis for the harmonization of differing national laws. . . ." NAFTA, on the other hand, lacks any such provision. Although resolving to "contribute to the


156. GATT, supra note 145, at art. 24.8.


158. Strong, supra note 141, at 99-100.

159. EEC Treaty, amended by the TEU, supra note 76, at art. 3(j).

160. Mentioned are the sphere of transport, the social sphere, the sphere of the environment, the sphere of development cooperation and the spheres of energy, civil protection and tourism. Id., amended by the TEU, supra note 76, at arts. 3(f), (i), (k), (q) and (t).

161. Leigh, supra note 98, at 861.

162. Id.
harmonious development and expansion of world trade and provide a catalyst to broader international cooperation," NAFTA does not cede United States sovereignty. "Even if a [United States] practice were found by a NAFTA dispute settlement panel to violate the NAFTA, the [United States] would not be required to change such practice." 

One case brought before the ECJ in which the court refused to apply the rule of Community-wide exhaustion of distribution rights involved a similar comparison of a common market and a free trade area, suggesting that the EC law regarding Community-wide exhaustion of rights would not apply to free trade areas. In *Polydor Ltd. and RSOP Records Inc. v. Harlequin Record Shops Ltd. and Simons Records Ltd.*, the defendant imported copyrighted works from Portugal, a country at that time outside the EC, and retailed them in the United Kingdom at lower prices without the copyright holder's consent. The defendant raised Community law as a defense, based on the free trade agreement between the EC and Portugal, proposing that the court's interpretation of the EEC Treaty govern the interpretation of comparable provisions in the EC-Portugal agreement. This defense was rejected; the court did not consider a similarity of terms sufficient reason to transport the EC case law to the provisions of the EC-Portugal agreement for two reasons.

First, the EC-Portugal agreement does not have the same purpose as the EEC Treaty which "seeks to create a single market reproducing as closely as possible the conditions of a domestic market." One construction considered by the ECJ is that the EC-Portugal agreement more closely resembles the convention establishing the European Free Trade Association ("EFTA"), which shares the objective of establishing a free trade area between the contracting parties. The exhaustion doctrine has no equivalent under the EFTA Convention. "Moreover, prior to the *Polydor* judgment, the supreme courts of two EFTA countries, Austria and Switzerland, had refused to read the exhaustion doctrine into the free trade

163. NAFTA, *supra* note 155, pmbl.
165. *Id*.
168. *Id.* at 332.
169. *Id.* at 348.
170. *Id.* at 349; Leigh, *supra* note 98, at 860.
agreements between their countries and the Community. 172 This argument easily applies to a comparison of the EC and NAFTA.

Second, the EC-Portugal agreement, unlike the EEC Treaty, did not provide for a mechanism to ensure the uniform interpretation and application of its provisions in the territories of the contracting parties. 173 NAFTA, like the EC-Portugal agreement, also lacks such a mechanism. NAFTA in fact, defers to domestic law, at least in the case of enforcing its intellectual property provisions. 174

Polydor was a private company invoking the provisions of a treaty. While this has not been unusual with regard to the EEC Treaty, the Polydor court’s silence on the issue of whether the EC-Portugal agreement could be invoked by private parties in the first place 175 brings up a subtle but interesting point of comparison between the EEC treaty and NAFTA. Trade agreements have traditionally provided mechanisms for the resolution of government to government disputes rather than those of private individuals. The EEC Treaty differs from trade agreements because it specifically provides that its provisions may be invoked by individuals. 176 NAFTA also departed from the traditional role of free trade agreements when it became the first such agreement “to address the resolution of international commercial disputes between private parties.” 177 The United States had proposed that NAFTA, the most comprehensive free trade agreement it had entered, address the resolution of private commercial disputes. Concerns of the United States were that “where there is a perception in the business community that commercial disputes with foreign partners are difficult or costly to resolve, it may discourage [United States] businesses from entering commercial relationships with traders and investors in those countries, thus reducing exports of [United States] goods and services.” 178

This first glance at the structure of the two agreements reveals that the EEC Treaty, for the most part, appears to have created much more of a

172. Leigh, supra note 98, at 860-861.
173. Id. at 861. Polydor, 1982 E.C.R., at 349.
174. See discussion infra part IV.B.3.
175. Leigh, supra note 98, at 861. This restraint may have been inspired by the increasingly controversial notion of reciprocity. “The Court was advised by several intervening member states and the EEC Commission that a unilateral grant of direct effect to the Agreement (and international agreements generally) would impair the Community’s maneuverability in defending its interests and those of its member states through international negotiation.” Id.
176. EEC Treaty, amended by the TEU, supra note 76, at art. 173.
178. Id. at 4.
single unit of member states than has the NAFTA, suggesting that NAFTA may not be able to exert a similar influence upon the domestic laws of its member states. A look at the underlying objectives of the two agreements, however, reveals a striking similarity.

2. Objectives of the Agreements

The elimination of quantitative restrictions is a goal of both the EEC Treaty and NAFTA. The starting point for all trade agreements is the goal of reducing barriers to trade. Under GATT, tariffs are maintained in trade between contracting parties;\(^\text{179}\) the MFN principle only requires that tariffs be kept equal for like products and under a certain ceiling.\(^\text{180}\) Tariffs are not to be eliminated, whereas in the common market this is an express goal. The Treaty provides for the "elimination, as between Member States, of customs duties and quantitative restrictions in regard to the importation and exportation of goods, as well as of all other measures with equivalent effect."\(^\text{181}\)

The corresponding provision of NAFTA reveals language close to that of the EEC Treaty, providing that each country "shall progressively eliminate its customs duties on originating goods."\(^\text{182}\) NAFTA provisions will phase out all North American tariffs within a decade.\(^\text{183}\) "GATT . . . approves of such free trade areas as a deviation from the most favored nation treatment."\(^\text{184}\)

Two of the EC's fundamental principles, Freedom of Movement and Freedom of Competition between Member States, were discussed above as being particularly relevant to intellectual property issues in the EC.\(^\text{185}\) Indeed, the EC case law, which has changed the landscape of the exhaustion defense to copyright infringement claims, has been based on EEC Treaty Articles 30 and 36, which deal with the free movement of goods.\(^\text{186}\) Virtually all decisions in the ECJ, in which the Treaty pre-

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179. Strong, supra note 141, at 103.
180. Id.
181. EEC Treaty amended by the TEU, supra note 76, at art. 3(a); see discussion supra part III.A.
182. NAFTA art. 302(2) states: "Except as otherwise provided in this Agreement, each Party shall progressively eliminate its customs duties on originating goods in accordance with its Schedule to Annex 302.2." NAFTA, supra note 155, at art. 302(2).
184. Id.
185. See discussion supra part III.
186. Strong, supra note 141, at 117.
vailed over national laws concerning exhaustion of rights, are due to the "supremacy" of that principle.\(^\text{187}\)

It has been said that NAFTA "does not establish any principles of free movement of goods that would require signatories to allow parallel importing."\(^\text{188}\) A closer look at the text of NAFTA, however, reveals that it does address this basic goal. NAFTA Article 102.1(a) lists as an objective of the Agreement to "eliminate barriers to trade in, and facilitate the cross-border movement of, goods and services between the territories of the Parties."\(^\text{189}\) In addition, Article 102.1(b) seeks to "promote conditions of fair competition in the free trade area . . . ."\(^\text{190}\)

A comparison of the text of the two agreements leads to the conclusion that, at least in their objectives, they are quite similar. Both seek to eliminate trade barriers and to encourage fair competition and the free movement of goods between their territories.

3. Enforcement of Intellectual Property Rights

The major difference between the two agreements is that NAFTA contains express provisions regarding intellectual property.\(^\text{191}\) In the EC, intellectual property rights began merely as an exception to the provisions

\(^{187}\) Corbet, \textit{supra} note 75, at 330.


\(^{189}\) NAFTA art. 102 states:

\(\text{(1)}\) The objectives of this Agreement, as elaborated more specifically through its principles and rules, including national treatment, most-favored-nation treatment and transparency, are to:

\(\text{(a)}\) eliminate barriers to trade in, and facilitate the cross-border movement of, goods and services between the territories of the Parties;

\(\text{(b)}\) promote conditions of fair competition in the free trade area;

\(\text{(c)}\) increase substantially investment opportunities in the territories of the Parties;

\(\text{(d)}\) provide adequate and effective protection and enforcement of intellectual property rights in each Party's territory;

\(\text{(e)}\) create effective procedures for the implementation and application of this Agreement, for its joint administration and for the resolution of disputes; and

\(\text{(f)}\) establish a framework for further trilateral, regional and multilateral cooperation to expand and enhance the benefits of this Agreement.

\(\text{(2)}\) The Parties shall interpret and apply the provisions of this Agreement in the light of its objectives set out in paragraph 1 and in accordance with applicable rules of international law.

\(^{190}\) \textit{Id.}

\(^{191}\) NAFTA, \textit{supra} note 155, at arts. 1701-09.
dealing with the elimination of quantitative restrictions and the free movement of goods. In addition, the specific subject matter of copyright, consisting of the exclusive right to reproduce the work and the right to put the product on the market for the first time has been largely defined by case law. NAFTA, on the other hand, includes express provisions for the enforcement of intellectual property rights as well as sections delineating the subject matter of its copyright protection.

NAFTA contains specific sections for copyright, trademark and patent Articles 1705 (regarding copyright) and 1706 (regarding sound recordings) provide to authors (or producers of sound recordings) the right to authorize or prohibit, inter alia, "(a) the importation into the Party's territory of copies of the work made without the right holder's authorization; (b) the first public distribution of the original and each copy of the work by sale, rental or otherwise."
Most notable is the inclusion of a provision in NAFTA embodying the first sale doctrine. We also see, as in the United States Code, a juxtaposition of the first sale doctrine with the importation right. Clearly, the territoriality of the importation right of subsection (a) is national, and can be seen as a multilateral extension of the United States' importation right of 17 U.S.C. § 602(a). Subsection (b) does not explicitly address territoriality. However, it does address the first sale and is therefore open to interpretation. One may infer territoriality from the proximity of the subsections and a desire for consistency. On the other hand, the omission of a territorial definition for the first sale provision could also facilitate application of the European model of territorial expansion.

Subsection (a) prohibits the importation of copies "made" without the right holder's authorization. It does not address the issue of copies "re-sold" without authorization. Therefore, referring back to the hypothetical, recordings made and first sold in Mexico with CBA's authorization, then imported into the United States without CBA's authorization, might slip through the cracks of NAFTA's copyright provisions.

In general, however, NAFTA is seen as "a watershed in the history of protection of intellectual property rights . . . vastly increasing the level of protection afforded to holders of such rights." It is viewed by some as a United States initiative creating high standards of intellectual property protection and enforcement. Indeed, one of the major objectives of NAFTA is to "provide adequate and effective protection and enforcement of intellectual property rights in each Party's territory."

NAFTA begins its section on intellectual property with the following statement regarding the nature and scope of obligations: "Each Party shall provide in its territory to the nationals of another Party adequate and effective protection and enforcement of intellectual property rights, while ensuring that measures to enforce intellectual property rights do not

198. NAFTA, supra note 155, art. 1705, ¶ 2(b).
199. Id.
200. Id. at 1705, ¶ 2(a).
201. Notably, supra note 155, at arts. 1705.2, 1706.1, also provides that putting the original or a copy of a computer program or a sound recording "on the market with the right holder's consent shall not exhaust the rental right." Prohibitions on the concept of exhaustion are therefore addressed in the NAFTA, but their conspicuous omission in relation to the import right, whether or not intentionally done, has opened a door to the possibility of exhaustion of distribution rights on the level of the trading block as a whole.
202. Levy & Weiser, supra note 188, at 270.
203. Id.
204. NAFTA, supra note 155, at art. 102.1(d).
themselves become barriers to legitimate trade.”

Thus, NAFTA defers to national laws for the enforcement of intellectual property rights, directing each Party to “ensure that enforcement procedures . . . are available under its domestic law.” It also includes the very significant caveat of non-interference with free trade objectives; the text goes on to say that “[s]uch enforcement procedures shall be applied so as to avoid the creation of barriers to legitimate trade and to provide safeguards against abuse of the procedures.”

This language is comparable to Article 36 of the EEC Treaty which provides the two part balancing test used by the ECJ in its exhaustion cases. On one hand, the first sentence of the EEC Treaty provision includes a national intellectual property exception to the free movement principle, analogous to the rights allowed by NAFTA Article 1705 regarding copyright, as discussed above. On the other hand, the second sentence of Article 36 states that the exceptions “shall not, however, constitute a means of arbitrary discrimination or a disguised restriction on trade between Member States.”

Thus, in both trade agreements we find the perennial balancing of the two objectives: protection of intellectual property and free trade. This balancing in the EC led to a result in which the ultimate principle of free trade prevailed. It is possible that a similar weighing of these objectives under NAFTA might have a similar result, the purpose of both agreements being the elimination of trade barriers and facilitation of movement between member states.

C. Could NAFTA Follow the European Model?

The EEC Treaty does not contain provisions for copyright protection, but (like NAFTA) it originally deferred to national law for enforcement. “[I]t should be noted that in the present state of Community law, which is characterized by a lack of harmonization or approximation of legislation governing the protection of literary and artistic property, it is for national
legislatures to determine the conditions and detailed rules for such protection.\textsuperscript{213}

Restrictions on the Community could be justified, according to Article 36, by the need to protect intellectual property rights, but “[n]o such justification would exist if the restrictions on trade imposed or accepted by the national legislation relied on by the owner of the exclusive rights or his [or her] licensee were of such a nature as to constitute a means of arbitrary discrimination or a disguised measure to restrict trade.”\textsuperscript{214}

Thus, both the EEC Treaty and NAFTA started out with the delegation of copyright protection to national law and the need to balance that with the objectives of free trade and free movement. In the EC, the Court of Justice found it necessary to place some limits on national protectionism.\textsuperscript{215} This same result may be obtained in the NAFTA trading block without overriding national laws by a more supreme agreement. We may see a trend to the convergence of member nation laws in a way that would maintain the high level of copyright protection that the United States and NAFTA seek to enforce. “Because the ‘virtues of free trade areas may be undermined by disharmonious economic conditions,’ free trade agreements tend to drive states to the eventual convergence of national laws.”\textsuperscript{216} This scenario involves “following NAFTA’s principles of free trade to their logical end by legalizing parallel importation within the trading block.”\textsuperscript{217}

The continued globalization of the marketplace calls for harmonization of national laws. A shift is required in the thinking of those charged with the protection of intellectual property.\textsuperscript{218} Instead of viewing the erosion of territoriality as an erosion of protection, it may be viewed as an

\begin{footnotes}
\item[213] Id.
\item[214] Id. at 96-97.
\item[215] See id. at 79.
\item[217] Id. at 306.
\end{footnotes}
expansion of that very same protection. NAFTA was written with a view toward raising the standards of intellectual property protection worldwide.\textsuperscript{219} It was "designed to bring Mexico and Canada into compliance" with United States standards for the protection of intellectual property.\textsuperscript{220} Therefore, those standards must be applied uniformly and with no partitioning of individual national markets, which not only places restrictions on free trade, but evidences discriminatory protection. At first glance, the expansion of the first sale territory appears to protect infringers rather than copyright owners by expanding the use of the first sale defense to a broader range of facts. But in effect, the application of United States law, allowing the defense for goods made domestically but not for goods made outside its national borders, does indeed act to partition national markets and evidence discriminatory protection.

In the EC, the expansion of the first sale territory represented "a move from a pre-EC doctrine of territoriality of intellectual property protection to a multidimensional doctrine of universality of intellectual property protection within the . . . trading block."\textsuperscript{221} The European experience of integration "provides an obvious basis for comparison with NAFTA."\textsuperscript{222} The ECJ's structure and case law have been described as models of indirect influence in the non-European setting.\textsuperscript{223} The ECJ has become a kind of standard by which other regional trading blocks measure their system's effectiveness; its case law has affected the decisions of non-European trading blocks and is of direct and indirect interest to non-member states as a source of comparative law.\textsuperscript{224} "ECJ case law on restrictions of parallel imports, specifically, has been the model for the United Nations' 'Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices.'"\textsuperscript{225} In addition, when NAFTA was being negotiated, Mexican President Carlos Salinas looked very carefully to the European reforms for examples of institutional progress without

\textsuperscript{219} Levy & Weiser, \textit{supra} note 188, at 270.
\textsuperscript{221} \textit{Id.} at 327.
\textsuperscript{222} \textit{Id.} at 320.
\textsuperscript{223} \textit{Id.} at 321 (citing Pieter VerLoren van Themaat, \textit{The Impact of the Case Law of the Court of Justice of the European Communities on the Economic World Order}, 82 \textit{MICH. L. REV.} 1422 (1984)).
\textsuperscript{224} Gonzalez, \textit{supra} note 216, at 321 (citing VerLoren van Themaat, \textit{supra} note 223, at 1425).
\textsuperscript{225} \textit{Id.} at 322 (quoting Fox, \textit{supra} note 216, at 4 n.12).
disintegration of political systems. He "perceived the global movement to regional trading associations as a response to the unification of Europe."227

V. CONCLUSION

NAFTA has left a palpable regulatory gap in the area of parallel imports.228 Its intellectual property provisions do not regulate the shipment of gray market goods; the parties chose to depend on each individual state's domestic intellectual property and unfair competition laws to resolve disputes over unauthorized importing and exporting.229 Consequently, there is room for a choice, which NAFTA member states will have to face when dealing with parallel imports, "between continuing to rely on national, territory-based intellectual property regimes to prohibit parallel imports, or following free trade to its logical conclusion by legalizing parallel importing within NAFTA trading block. This decision turns on the interpretive approach that the Member States adopt in relation to NAFTA."230

One view is that the omission of any explicit prohibition of parallel imports is unfortunate because national territoriality is important, and that "[t]o gain full benefit from their rights, right holders should be able to make, use, or sell the subject matter of their rights on a country-by-country basis. The practice of parallel importing and the concept of exhaustion of rights eliminate the ability to maintain this control."231 Since NAFTA contains nothing on exhaustion and does not, according to this view, "establish any principles of free movement of goods that would require signatories to allow parallel importing, . . . the territoriality of intellectual property rights remains a matter for national law, and the signatories are free to protect right holders by prohibiting parallel imports."232 Under

226. Id. at 320 (citing Jeff Silverstein, An Interview with President Salinas, BUS. MEX., Aug. 1992, at 18).
227. Id. at 320-21 (citing "We Had to React Quickly:" An Interview with Carlos Salinas, FORBES, Aug. 17, 1992, at 65).
228. Gonzalez, supra note 216; Levy & Weiser, supra note 188.
229. Id. at 307.
230. Id. at 329.
231. Levy & Weiser, supra note 188, at 285.
232. Id. at 286. Levy and Weiser believe that the "[t]erritoriality of intellectual property rights will have to be dealt with in future international agreements," and that NAFTA's approach is to ignore the issue. They believe, however, that "laying to rest the concept of exhaustion and explicitly prohibiting parallel importing would ensure a higher level of protection for intellectual property rights." Id.
this view, in our hypothetical, clearly CBA would prevail, as Record Store
could not assert the first sale doctrine as a defense.

The opposing view allows the importation of the recordings into the
United States, even though they were made in Mexico, based on the theory
that once placed into the stream of commerce (anywhere within the
NAFTA trading block), the United States copyright owner has extinguished
its exclusive distribution right. This view involves elevating the principle
of free movement of goods above national protectionism, resulting in the
expansion of the first sale territory, and the eventual legalization of parallel
importing.

The latter approach, however, does not necessitate the disregard of
national protectionism but seeks to expand the protection of intellectual
property to a global level by the harmonization and convergence of national
laws. The two policies, which at first seem in direct opposition to each
other, can be blended and both satisfied by changes in domestic laws
resulting in a high level of protection for authors and composers on a
global rather than merely national scale.

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