



NORTH CAROLINA JOURNAL OF INTERNATIONAL LAW AND COMMERCIAL REGULATION

Volume 11 | Number 2

Article 2

Spring 1986

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Benjamin I. Cohen

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Recommended Citation

Benjamin I. Cohen, *Grey Market Imports and the International Location of Manufacturing*, 11 N.C. J. INT'L L. & COM. REG. 171 (1986).
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Grey Market Imports and the International Location of Manufacturing

*Benjamin I. Cohen**

Manufacturers have frequently used independent dealers to distribute their products, assigning to each dealer an exclusive geographic area. A dealer may seek to maintain a minimum price in its area. Occasionally, however, an ultimate consumer residing in one distributor's territory buys goods from another distributor at a lower price. The proliferation of such "transshipments" has led to efforts either by the former distributor or by the manufacturer to prevent distribution across territorial lines. These efforts have in turn led to litigation under the antitrust laws, following attempts by manufacturers to "discipline" offending distributors,¹ and to legislation in the form of "fair trade" laws.²

Several recent judicial and administrative decisions have forced both the courts and the President to confront the problems posed by transshipments in the international context and to decide under what circumstances, if any, the United States should prohibit the transshipment of goods from other countries into the United States. These international transshipments are called "grey market" imports. Part I of this article summarizes the current case law. Part II reviews the development of the pertinent legislation and judicial decisions concerning "grey market" imports. Part III presents an economic analysis of the roles U.S. customs law might play in this area.

* Ph.D. Harvard University; J.D. Yale University. The author is an attorney in the Division of International Antitrust, Bureau of Competition, Federal Trade Commission. This article reflects only his personal views and does not constitute the views of the Commission or of any individual Commissioner.

¹ See, e.g., *Monsanto Co. v. Spray-Rite Serv.*, 104 S. Ct. 1464 (1984) (terminated dealer must present evidence other than complaints from other dealers to show that termination was pursuant to an illegal agreement between manufacturer and other dealers); *Continental T.V. v. GTE Sylvania*, 433 U.S. 36 (1977) (legality of terminating a dealer should be judged under "rule of reason" when nonprice restriction is involved); *United States v. General Motors*, 384 U.S. 127 (1966) (collaboration of some Chevrolet dealers and General Motors to enforce agreement that Chevrolet dealers would not deal with discounters violates Sherman Act); *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911) (agreements between a manufacturer and its wholesalers and retailers that specify minimum prices at which latter may sell violate both common law and Sherman Act).

² See *infra* notes 57-66 and accompanying text.

Part IV reviews the evolving legislative approach to transshipments within the United States. Part V argues that banning grey market imports will encourage manufacturing to locate in foreign countries and concludes that the U.S. government should adopt the same neutral stance towards international transshipments that it has adopted towards domestic transshipments. This stance would force manufacturers and dealers to rely on private contract and tort actions to control all transshipments.

I. Recent Case Law

Recent administrative and judicial decisions illustrate the different fact patterns in which attempts to ban imports of genuine trademarked goods can occur. *El Greco Leather Products Co. v. Shoe World*,³ for example, involved an effort by a U.S. company, El Greco Leather Products Co. (El Greco), to enjoin Shoe World, a chain of 92 retail shoe stores, from importing shoes that were manufactured in Brazil by an independent Brazilian company bearing El Greco's U.S. trademark, "CANDIES." The dispute arose when El Greco refused to accept certain shipments of Brazilian-made shoes. Some of the shoes in these shipments were authorized to bear the "CANDIES" trademark by El Greco's Brazilian agent. Shoe World purchased the rejected shoes from a Brazilian firm and sold them in the United States.⁴ The court denied El Greco's motion for an injunction prohibiting sales of the shoes in the United States, holding that section 526 of the Tariff Act of 1930⁵ did not apply because El Greco had not purchased its trademark from a foreigner.⁶

In *Certain Alkaline Batteries*⁷ a U.S. battery manufacturer sought an order banning importation of batteries bearing its trademark that were manufactured by a foreign wholly owned subsidiary. Duracell

³ 599 F. Supp. 1380 (E.D.N.Y. 1984).

⁴ *Id.* at 1384.

⁵ Tariff Act of 1930, ch. 497, § 526, 46 Stat. 741 (codified at 19 U.S.C. § 1526 (1982)). Section 526 provides, in pertinent part:

[I]t shall be unlawful to import into the United States any merchandise of foreign manufacture if such merchandise, or the label, sign, print, package, wrapper, or receptacle, bears a trademark owned by a citizen of, or by a corporation or association created or organized within, the United States, and registered in the Patent and Trademark Office by a person domiciled in the United States, under the provisions of sections 81 to 109 of Title 15, and if a copy of the certificate of registration of such trademark is filed with the Secretary of the Treasury, in the manner provided in section 106 of said Title 15, unless written consent of the owner of such trademark is produced at the time of making entry.

⁶ *El Greco Leather Products Co.*, 599 F. Supp. at 1401. See also *Parfums Stern, Inc. v. United State Customs Serv.*, 575 F. Supp. 416 (S.D. Fla. 1983) (U.S. importer financially linked to foreign manufacturer cannot bar imports of perfume).

⁷ *Certain Alkaline Batteries*, 225 U.S.P.Q. (BNA) 823, disapproved by President Reagan pursuant to 19 U.S.C. § 1337(g) (1982), 50 Fed. Reg. 1655, reprinted in 225 U.S.P.Q. (BNA) 862, appeal dismissed sub nom. *Duracell, Inc. v. United States Int'l Trade Comm'n*, 778 F.2d 1578 (Fed. Cir. 1985) [hereinafter cited as *Duracell*].

Inc. (Duracell US), a Delaware corporation, manufactured batteries in the United States bearing its U.S. registered Duracell trademark. Duracell US had a wholly owned U.S. subsidiary, Duracell International, which, in turn, owned all of the Belgian corporation, N.V. Duracell S.A. (Duracell Belgium). Duracell Belgium manufactured batteries in Belgium with the Belgian-registered Duracell trademark owned by Duracell International.⁸ Duracell US, invoking 19 U.S.C. § 1337,⁹ sought an order banning imports of foreign Duracell batteries. The International Trade Commission (ITC) unanimously held that although the foreign batteries were not inferior to domestic batteries, the importation of foreign batteries violated 19 U.S.C. § 1337.¹⁰ Three Commissioners also found a violation of section 42 of the Lanham Act.¹¹ These three ITC Commissioners ordered that all foreign Duracell batteries be excluded from the United States. Two ITC Commissioners dissented concluding that there should be an exclusion of only those foreign Duracell batteries that did not have labels clearly indicating that Duracell US did not sponsor, authorize, or guarantee them when sold in the United States.¹² The President, pursuant to 19 U.S.C. § 1337(g)(2), then disapproved the ITC's determination.¹³ The appeal by Duracell was dismissed.¹⁴

President Reagan, in rejecting the ITC recommendation,¹⁵ said that the ITC finding of a violation conflicted with recent decisions by

⁸ *Id.* at 825.

⁹ 19 U.S.C. § 1337 (1982) provides, in pertinent part:

Unfair methods of competition and unfair acts in the importation of articles into the United States, or in their sale by the owner, importer, consignee, or agent of either, the effect or tendency of which is to destroy or substantially injure an industry, efficiently and economically operated, in the United States, or to prevent the establishment of such an industry, or to restrain or monopolize trade and commerce in the United States, are declared unlawful.

¹⁰ *Duracell*, 225 U.S.P.Q. at 824.

¹¹ Lanham Act, ch. 540, § 42, 60 Stat. 440 (1946) (codified at 15 U.S.C. § 1124 (1982)). Section 42 provides in pertinent part:

[N]o article of imported merchandise which shall copy or simulate the name of the [sic] any domestic manufacture, or manufacturer, or trader, or of any manufacturer or trader located in any foreign country which, by treaty, convention, or law affords similar privileges to citizens of the United States, or which shall copy or simulate a trademark registered in accordance with the provisions of this chapter or shall bear a name or mark calculated to induce the public to believe that the article is manufactured in the United States, or that it is manufactured in any foreign country or locality other than the country or locality in which it is in fact manufactured, shall be admitted to entry at any customhouse of the United States.

¹² These two ITC Commissioners found no violation of either § 42 of the Lanham Act or § 526 of the Tariff Act of 1930, and based liability only on violations of § 32(1) of the Lanham Act, 15 U.S.C. § 1114 (1982), and the Fair Packaging and Labeling Act, *id.* §§ 1452-1453.

¹³ 50 Fed. Reg. 1655 (1985).

¹⁴ *Duracell, Inc. v. Int'l Trade Comm'n*, 778 F.2d at 1578.

¹⁵ 50 Fed. Reg. 1655 (1985).

the United States District Court for the District of Columbia¹⁶ and the Court of International Trade.¹⁷ Both courts upheld the validity of Customs regulations, issued under section 42 of the Lanham Act and section 526 of the Tariff Act of 1930, permitting such imports.¹⁸ These regulations¹⁹ prohibit a person other than the owner of the U.S. trademark from importing foreign manufactured articles bearing a genuine trademark when the foreign trademark and the U.S. trademark are not owned by the same person or firm or by persons or firms subject to "common ownership or control."²⁰ Because Duracell US and Duracell Belgium are under common ownership or control, the regulations permit anyone to import Duracell Belgium batteries.

Two recent judicial decisions rejected claims that these Customs regulations are inconsistent with section 526. *Vivitar Corp. v. United States*²¹ was a declaratory judgment action by Vivitar (Vivitar US), a California corporation. Vivitar US licensed foreign firms to manufacture photographic items using the Vivitar trademark; the foreign firms then sold the items to the wholly owned foreign subsidiaries of Vivitar US, which marketed the items outside the United States. The United States Court of International Trade, in a decision affirmed by the United States Court of Appeals for the Federal Circuit, held that customs regulations permitting sales within the United States of Vivitar trademarked products marketed by its foreign subsidiaries were not unreasonable interpretations of section 526.²²

Coalition to Preserve the Integrity of American Trademarks v. United

¹⁶ *Coalition to Preserve the Integrity of American Trademarks (COPIAT) v. United States*, 598 F. Supp. 844 (D.D.C. 1984), *rev'd*, 790 F.2d 903 (D.C. Cir. 1986).

¹⁷ *Vivitar Corp. v. United States*, 593 F. Supp. 420 (Ct. Int'l Trade 1984), *aff'd*, 761 F.2d 1552 (Fed. Cir. 1985), *cert. denied*, 106 S. Ct. 791 (1986).

¹⁸ The President also stated there should be no change in U.S. policy until the Cabinet Committee on Commerce and Trade had completed its analysis of the issue, including a review of data submitted by the public pursuant to a request by the Customs Service and the Patent and Trademark Office. 49 Fed. Reg. 21,453 (1984) (extended at 49 Fed. Reg. 29,509 (1984)).

¹⁹ 19 C.F.R. § 133.21(c)(1)(2) (1985).

²⁰ *Id.* "Common ownership or control" is illustrated by two recent cases, *Bell & Howell: Mamiya Co. v. Masel Supply Co.*, 548 F. Supp. 1063 (E.D.N.Y. 1982), *vacated and remanded*, 719 F.2d 42 (2d Cir. 1983), and *Osawa & Co. v. B & H Photo*, 589 F. Supp. 1163 (S.D.N.Y. 1984). Both cases involved the efforts by Osawa & Co. (Osawa), a U.S. company, to prevent other companies from handling Mamiya cameras. Mamiya cameras are made in Japan by a Japanese company, Mamiya Camera Co. (Mamiya), which owns the Japanese trademark. J. Osawa & Co. (Osawa Japan) owns 3% of Mamiya's stock. Osawa Japan and Mamiya agreed that Osawa Japan is the exclusive distributor for Mamiya cameras outside Japan. Osawa Japan owned all of the stock of Osawa & Co. (USA), which in turn owns 93% of Osawa's stock. Osawa Japan and Osawa agreed that Osawa is the exclusive distributor in the U.S. for Mamiya cameras and Osawa owned the U.S. Mamiya trademark. Customs determined there is no common ownership or control between Mamiya and Osawa and banned imports of Mamiya cameras by firms other than Osawa. *See also* 49 Fed. Reg. 29,509 (1984).

²¹ 593 F. Supp. at 420.

²² *Id.* at 434-36.

*States*²³ was a declaratory judgment action by a group of U.S. corporations that owned trademarks registered in the United States and licensed foreign firms to manufacture goods such as fragrances and cosmetics, watches, tires, fine crystal, cameras, photographic equipment, binoculars, and electronic goods using those trademarks. The United States District Court for the District of Columbia found that Customs regulations allowing sales within the United States of products manufactured by the foreign licensee and bearing, without authorization, the registered U.S. trademark were consistent with section 526.²⁴

These two decisions summarize a century of judicial, legislative, and administrative grappling with the importation of items made in foreign countries and bearing the same trademark as an item sold in the United States pursuant to authorization by owners of the U.S. trademark.

II. Legislative and Judicial History

The first U.S. statute²⁵ dealing with the grey market issue prohibited importation of foreign merchandise that "copied or simulated" a domestic trademark. This provision was reenacted in section 27 of the Trademark Act of 1905.²⁶

In *Fred Gretsch Mfg. Co. v. Schoening*²⁷ the exclusive U.S. agent of a German manufacturer of violin strings, which had registered the manufacturer's trademark in the United States, sought to prevent another firm from importing into the United States violin strings purchased abroad from the German manufacturer. The court held that section 27 of the Trademark Act of 1905 did not apply because the chief purpose of the section was to protect the public from articles "which are not genuine."²⁸

Five years later, the Second Circuit Court of Appeals addressed a similar claim in *A. Bourjois & Co. v. Katzel*.²⁹ A. Bourjois Co., a U.S. firm, purchased from a French manufacturer of face powder the manufacturer's U.S. business, including the trademark "Java." Bourjois bought the face powder in France, repackaged the powder, and sold it in the United States under the "Java" trademark. Bourjois brought suit to stop another company from buying the same face powder in France and selling it in the United States in the original

²³ 598 F. Supp. at 844.

²⁴ *Id.* at 851-52.

²⁵ Act of Mar. 3, 1871, ch. 75, 16 Stat. 580.

²⁶ Trademark Act of 1905, § 27, ch. 592, 33 Stat. 724 (codified at 15 U.S.C. § 1224 (1982)).

²⁷ 238 F. 780 (2d Cir. 1916).

²⁸ *Id.* at 782.

²⁹ 275 F. 539 (2d Cir. 1921), *rev'd*, 260 U.S. 689 (1923).

French package.³⁰ The court rejected Bourjois' claims and refused to certify the question to the Supreme Court.³¹

Congress reacted to *Katzel* by enacting section 526 of the Tariff Act of 1922.³² The legislative history of the Act indicates that Congress intended the section to overrule *Katzel*.³³ Senator McCumber, one of the amendment's sponsors, stated that its purpose was to protect U.S. firms that had purchased trademarks from foreigners, but it did not protect the U.S. agent of a foreign manufacturer from competing imports.³⁴ Congressional debate did not mention *Gretsch*.³⁵

Meanwhile, the Supreme Court reversed the lower court decision in *Katzel* holding that the Trademark Act of 1905 did apply.³⁶ The Court said that plaintiff's trademark "was sold and could only be sold with the good will of the business that the plaintiff bought."³⁷ Thus, the Trademark Act was designed, in part, to protect plaintiff's investment in the goodwill of the business.³⁸

The implications of *Katzel* are illuminated by *Prestonettes v. Coty*,³⁹ decided the following year. In *Prestonettes* the Supreme Court held that Coty, the French owner of a U.S. trademark, was not entitled to an injunction prohibiting Prestonettes, a U.S. firm, from buying Coty's perfumes and toilet powders in Europe and repacking them for sale in the United States. Injunctive relief was denied because Prestonettes' label clearly indicated that Prestonettes was not connected with Coty and had repacked Coty's products.⁴⁰ The Court distinguished *Katzel* by stating that Prestonettes' label would ensure that "the public . . . is likely to find . . . out" if Prestonettes' product is inferior to Coty's.⁴¹

Thus, by 1924 the Supreme Court had identified two factors to be weighed in deciding whether to restrict competition by barring grey market imports: reducing consumer confusion and protecting the firms' goodwill investment. The law barred transshipments of merchandise manufactured in a foreign country bearing an authorized trademark if a U.S. firm had purchased, in an arms length transaction, the right to be the exclusive U.S. distributor and to own the U.S. trademark. The law did not bar transshipments of foreign merchandise bearing an authorized trademark if the U.S. distributor and

³⁰ *Id.* at 540.

³¹ *Id.* at 544.

³² Ch. 356, § 526, 42 Stat. 975 (codified as amended at 19 U.S.C. § 1526 (1982)).

³³ H.R. REP. NO. 1223, 67th Cong., 2d Sess. 158 (1922).

³⁴ 62 CONG. REG. 11,604 (1922).

³⁵ *Id.*

³⁶ *Katzel*, 260 U.S. at 691.

³⁷ *Id.* at 692. See also *A. Bourjois & Co. v. Aldridge*, 263 U.S. 675 (1923) (per curiam).

³⁸ See *Katzel*, 260 U.S. at 692.

³⁹ *Prestonettes v. Coty*, 264 U.S. 359 (1924).

⁴⁰ *Id.*

⁴¹ *Id.* at 369.

owner of the U.S. trademark was financially related to the foreign manufacturer.⁴²

Efforts to control grey market imports might be viewed by some as an attempt by manufacturers or their exclusive U.S. distributors to protect "monopoly" profits rather than an endeavor to preserve manufacturer and distributor "goodwill." It is therefore not surprising that the Department of Justice has periodically become involved in the issue of grey market imports. Given the complexity of the problem, it is also not surprising that the Justice Department's position has vacillated.

In *United States v. Guerlain, Inc.*⁴³ the Government alleged that each of three defendant U.S. corporations had violated section 2 of the Sherman Act⁴⁴ by registering the trademark of French toilet goods with the United States Treasury, in an attempt to prevent the importation of the French toilet goods by others. The Government prevailed in the district court, and the defendants appealed to the Supreme Court. The Government then asked the Supreme Court to vacate the judgment and remand so that the complaint could be dismissed.⁴⁵ The Government advised the district court that the Executive Branch had decided that any possible conflict between the Sherman Act and section 526 was better resolved through legislation.⁴⁶

In 1983 the Justice Department filed an *amicus* brief on behalf of Bell & Howell: Mamiya Co. in *Bell & Howell: Mamiya v. Masel Supply Co.*,⁴⁷ maintaining there was no conflict between a ban on grey market imports of cameras and federal antitrust policies.⁴⁸ Two years later the Antitrust Division of the Department of Justice filed comments with the Department of Transportation on the question of a proposed rule to require that original manufacturers of foreign vehicles put a numerical stamp on certain parts of the car. While agreeing that the rule would reduce the number of cars stolen, the Justice Department suggested that importers, as well as original manufac-

⁴² An earlier analysis of this topic, urging Congress to reconsider the wisdom of section 526, apparently did not consider that section 562 did not bar transshipments when the U.S. trademarks and the foreign trademark were owned by related companies. Dam, *Trademarks, Price Discrimination and the Bureau of Customs*, 7 J.L. & ECON. 45, 48 n.14, 49 (1964).

⁴³ 155 F. Supp. 77 (S.D.N.Y. 1957), *prob. jurisd. noted sub nom* Lanvin, Parfums, Inc. v. United States, 355 U.S. 951, *cert. denied*, 357 U.S. 924, *vacated and remanded sub nom*. Guerlain, Inc. v. United States, 358 U.S. 915 (1958), *dismissed*, 172 F. Supp. 107 (S.D.N.Y. 1959).

⁴⁴ 15 U.S.C. § 2 (1982).

⁴⁵ *Guerlain, Inc. v. United States, Parfums Corday, Inc. v. United States, and Lanvin Parfums, Inc. v. United States*, 358 U.S. 915 (1958) (consolidated cases dismissed).

⁴⁶ *Guerlain, Inc. v. United States*, 172 F. Supp. 107 (S.D.N.Y. 1959) (on remand, motion to dismiss granted).

⁴⁷ 719 F.2d at 42.

⁴⁸ Brief for United States of America, *Amicus Curiae* at 16, *Bell & Howell: Mamiya Co. v. Masel Supply Co.*, 719 F.2d 42 (2d Cir. 1983).

urers, be permitted to mark major parts so that the grey market in automobiles could be maintained.⁴⁹

III. Economic Analysis

In the domestic context, some consumers benefit, while others are hurt, by price discrimination.⁵⁰ There is no *a priori* effect of price discrimination on total output and hence on the "average" consumer.⁵¹ Congress, perhaps conscious of these mixed effects, made price discrimination illegal only when the effect "may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy or prevent competition."⁵² The Department of Justice recently said that "price discrimination has ambiguous or unpredictable welfare effects."⁵³

In the international context, appreciation of the dollar relative to other currencies⁵⁴ makes international transshipments more profitable to foreign exporters and domestic importers by increasing the difference between the prices of products in the United States and the prices of the same products in foreign countries.⁵⁵ Prohibitions of or limitations on grey market imports result in an international price discrimination that is distinguishable in effect from domestic

⁴⁹ Comments of U.S. Justice Dep't to Notice of Proposed Rulemaking: Performance Standards and Criteria for Selection of Covered Vehicles and Replacement Parts—Motor Vehicle Theft Law Enforcement Act of 1984, Docket No. T84-01 (June 14, 1985).

⁵⁰ "Price discrimination occurs when the same commodity is sold at more than one price, or when similar products are sold at prices that are in different ratios to marginal costs." E. MANSFIELD, MICROECONOMICS: THEORY AND APPLICATION 308 (4th ed. 1982).

⁵¹ P. SAMUELSON, FOUNDATIONS OF ECONOMIC ANALYSIS 45 (1965).

⁵² 15 U.S.C. § 13(a) (1982).

⁵³ Vertical Restraints Guidelines, 50 Fed. Reg. 6263 (1985) [hereinafter cited as Guidelines]. The Guidelines have been sharply criticized, but not on this particular point, as being "inconsistent with existing law and demonstrably unsound as a matter of policy." H.R. REP. NO. 113, 99th Cong., 1st Sess. 41 (1985).

⁵⁴ Between 1980 and 1984 the U.S. dollar appreciated by 58% relative to the weighted average of our major trading partners. ECONOMIC REPORT OF THE PRESIDENT 1985, H.R. DOC. NO. 19, 99th Cong., 1st Sess. 351.

⁵⁵ A simple example illustrates this point. Consider a French firm manufacturing an item in France for five francs per unit and selling it in France at eight francs per unit. Assume the firm incurs selling costs in the United States of one dollar per unit and faces a downward sloping demand curve, given by $p = 10 - q/2$, in which p is the dollar price in the United States and q is the quantity sold in the United States. Assume also that the firm believes that the price in France is independent of the price in the United States and that the firm wishes to maximize the profit (measured in francs) it makes on its U.S. sales. Finally, assume the current exchange rate is one dollar equals one franc. Profit on sales in the United States equals $10q - q^2/2 - q - 5q$. Using the formula, the result is that the profit-maximizing price in the United States is eight dollars from the sale of four units. Because the price in France is also eight dollars, there will be no transshipments. Now assume the exchange rate becomes one dollar equals two francs. The price in France becomes four dollars, and the firm's profit on sales in the United States (measured in francs) becomes profit equal to $20q - q^2 - 2q - 5q$. The profit maximizing price is now \$6.75 from the sale of 6.5 units in the United States. Because of the change in the rate of exchange, the difference between the U.S. price and the French price has grown to \$2.75, which might induce transshipments.

price discrimination on domestic consumers. When economic incentives to international transshipments exist, foreclosure of U.S. markets by means of U.S. customs law results in higher product costs to domestic consumers. Thus, unlike domestic price discrimination, international price discrimination injures all U.S. consumers.

Those who wish to ban grey market imports argue that such a ban would help solve the "free-rider" problem associated with certain products. To establish a market for its products, a manufacturer, distributor, or retailer must often provide product information to the consumer. Such information is disseminated at no cost to the consumer by a variety of means, including national advertising and retail sales promotions. Other distributors and retailers who have not invested in trademark development can offer trademarked products at lower prices, thereby receiving a "free ride." The inability of the firm initially providing the information to consumers to charge directly for that information can result in too little information being supplied and hence, too little consumption of the good. Forcing all consumers to pay for the information, by charging a higher price for the good, however, may also lead to too little consumption, because consumers who do not need the information may be deterred from buying the higher priced product. Thus, the net welfare effects on consumers of preventing "free-riding" are ambiguous in the absence of empirical information.⁵⁶

IV. Recent Legislation

Congress has vacillated between protecting firms from the "free-riding" of others and letting consumers buy from firms that offer lower prices and less services. In 1937 Congress passed the Miller-Tydings Act⁵⁷ to exempt state "fair trade" laws, permitting a manufacturer to enter into an agreement with a distributor stipulating the minimum price at which the distributor would sell the product, from the Sherman Antitrust Act. In 1952 the McGuire Act⁵⁸ extended the privity of state "fair-trade" contracts to "non-signer" distributors.⁵⁹ In 1975, however, Congress passed the Consumer

⁵⁶ See Novos & Waldman, *The Effects of Increased Copyright Protection: An Analytical Approach*, 92 J. POL. ECON. 236 (1984); Hirshleifer & Riley, *The Analytics of Uncertainty and Information—An Expository Survey*, 17 J. ECON. LIT. 1375, 1403-06 (1979). Cf. P. SAMUELSON, FOUNDATION OF ECONOMIC ANALYSIS, 42 (1965) (absent empirical information, no presumption is possible about effects of advertising, as compared to no advertising, on output and price). One economist claims "the empirical significance [of free-riding] appears modest." F. SCHERER, INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE 593 (1980).

⁵⁷ Ch. 690, 50 Stat. 693 (1937).

⁵⁸ Pub. L. No. 542, ch. 745, 66 Stat. 631 (1952).

⁵⁹ Nothing contained in this Act or any of the Antitrust Acts shall render unlawful the exercise or the enforcement of any right of action created by any statute, law, or public policy now or hereafter in effect in any State, Territory, or the District of Columbia, which in substance provides that willfully and

Goods Pricing Act,⁶⁰ which repealed both the Miller-Tydings Act and the McGuire Act, again making agreements to set minimum prices illegal under the Sherman Act. Congress noted that the Federal Trade Commission and the Department of Justice supported repeal and that "[o]pponents [of repeal] were primarily service-oriented manufacturers who claimed retailers would not give adequate service unless they were guaranteed a good margin of profit."⁶¹ In 1984 Congress enacted 18 U.S.C. § 2320,⁶² which imposes criminal sanctions on persons importing goods with a counterfeit trademark. Congress indicated that this new statute did not apply to grey market imports and "is not intended to be used . . . to facilitate or enforce any system of resale price maintenance."⁶³

For the last decade, therefore, Congress has decided that firms whose products are subject to "free-riding" must be their own policemen.⁶⁴ Neither state nor federal officials will enforce efforts by a domestic manufacturer to have its product sold above a uniform minimum price within the United States.⁶⁵ The Government could, of course, require sellers of grey market goods to tell consumers which, if any, U.S. warranties apply. New York has recently passed such legislation.⁶⁶

V. Conclusion

As a result of the repeal of domestic fair trade laws, U.S. law now favors the foreign over the domestic manufacturer when the foreign

knowingly advertising, offering for sale, or selling any commodity at less than the price or prices prescribed in such contracts or agreements *whether the person so advertising, offering for sale, or selling is or is not a party to such a contract or agreement*, is unfair competition and is hereby actionable at the suit of any person damaged thereby.

Id. § 2 (emphasis added).

⁶⁰ Pub. L. No. 94-145, 89 Stat. 801 (1975).

⁶¹ S. REP. NO. 466, 94th Cong., 1st Sess. 3, reprinted in 1975 U.S. CODE CONG. & ADMIN. NEWS 1569, 1571. The principal fair traded products were stereo components, television sets, major appliances, mattresses, toiletries, kitchenware, watches, jewelry, glassware, wallpaper, bicycles, some types of clothing, liquor, and prescription drugs. *Id.* Some of these products, such as toiletries and watches, are among those now involved in "grey market" imports.

⁶² Trademark Counterfeiting Act of 1984, Pub. L. No. 98-547, § 204(a), 98 Stat. 2770 (to be codified at 18 U.S.C. § 2320).

⁶³ S. REP. NO. 526, 98th Cong., 2d Sess. 3 (1984), reprinted in 1984 U.S. CODE CONG. & ADMIN. NEWS 449.

⁶⁴ See, e.g., *Norman M. Morris Corp. v. Weinstein*, 466 F.2d 137 (5th Cir. 1972) (enjoining Weinstein from selling watches in the United States that he buys in Europe unless he makes it clear they are not guaranteed by Omega Watch Company and makes no false description or representation about any watch purporting to be an Omega watch).

⁶⁵ A U.S. manufacturer cannot bring a trademark infringement action against someone who buys an item in a low price area of the United States and sells it in a high price area of the United States. *Dam, supra* note 42, at 48. *Dam* wrote when state fair trade laws were still legal and did not discuss the consequences of their repeal.

⁶⁶ Assembly Bill No. 5971 (effective Oct. 22, 1985). See also *N.Y. Times*, June 22, 1985, at 52, col. 1.

manufacturer seeks to have a uniform minimum price within the United States. For example, consider firms *A*, *B*, and *C*, each making widgets with a separate trademark. Firm *A* manufactures widgets bearing its trademark in the United States and sells in both the United States and France. Firm *B* manufactures widgets bearing its trademark in France and sells in both France and the United States. Firm *C* manufactures widgets in both the United States and France. U.S. and French trademarks for firms *B* and *C* are owned by financially separate entities. Firms *A*, *B*, and *C* each try to set a uniform minimum price in the United States that is higher than the price in France. Suppose a U.S. retailer buys *A*'s widgets, *B*'s widgets, and *C*'s widgets in France and sells them in the United States below the price exclusive U.S. distributors seek to maintain. While firm *B*'s U.S. distributor and firm *C*'s U.S. distributor can each invoke the Customs regulations⁶⁷ and cease unauthorized imports, firm *A* and its U.S. distributor now have no remedy under U.S. law.

In the 1920s Congress was protectionist. It is doubtful that the Congress that originally passed section 526 in 1922 intended to favor foreign manufacturers over U.S. manufacturers. The Tariff Act of 1922, which raised tariffs, was based on a belief that "the quotations made by foreign producers for export sale of late have been so extremely low that they threaten the destruction of American industries and have consequently demoralized American trade."⁶⁸

It may be that the Congress that enacted section 526 in 1922 believed that a U.S. purchaser of a foreign trademark would be unable to obtain effective relief in foreign courts against a foreign seller who breached its contract with the U.S. purchaser. The development of international mechanisms for resolving international business disputes,⁶⁹ however, suggests that this rationale should no longer have much weight.⁷⁰

In conclusion, there is no reason to think that "free-riding" is a

⁶⁷ 19 C.F.R. § 133.21 (1985).

⁶⁸ S. REP. NO. 595, 67th Cong., 2d Sess. 2 (1922).

⁶⁹ See, e.g., *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 105 S. Ct. 3346 (1985) (Arbitration Act and Convention on the Recognition and Enforcement of Foreign Arbitral Awards require arbitration in Japan of antitrust counterclaim by Puerto Rican corporation against Japanese corporation); *Scherk v. Alberto-Culver Co.*, 417 U.S. 506 (1974) (U.S. company must submit to foreign arbitration its claim that a German citizen residing in Switzerland violated the Securities Exchange Act of 1934 when he sold certain companies and trademarks to U.S. company). For a comprehensive treatment of *Mitsubishi* and the Arbitration Act, see McClendon, *Subject-Matter Arbitrability in International Cases: Mitsubishi Motors Closes the Circle*, 11 N.C.J. INT'L L. & COM. REG. (1986).

⁷⁰ While there were historical reasons for limiting section 526 protection to U.S. firms purchasing their trademarks in an arms length transaction, there is little current justification for treating independent U.S. distributors differently from those owned by foreign firms. Occasionally independent distributors may be more efficient than a subsidiary; sometimes a firm may use both systems in the same market. Guidelines, *supra* note 53, at § 2.2. A wholly owned distributor may, however, make it easier for the foreign manufacturer to capture all the profits earned in the United States. By favoring individual distribu-

more serious problem for imported goods than for items manufactured solely in the United States. The original justification for section 526 having receded and with unforeseen effects now visible, Congress, having made state fair trade laws illegal, should reconsider the wisdom of section 526.

tors, section 526 reduces the adverse effects of price discrimination on the domestic economy.