

Parallel Imports under Ukrainian Law



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The parallel market, also quite often referred to as the grey market¹, is the name given to the market that develops in goods sold outside of their authorized channels of trade. Parallel importing is, in its turn, a term generally used to identify a non-counterfeit product imported from

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another country without the permission of the intellectual property owner². For example, if a manufacturer of fragrances sells a perfume in the United States and in France, and a third party purchases a large quantity of the fragrance in France and imports it for resale in the United States, this is a parallel market transaction.

The practice of parallel importing occurs in the main for three reasons:

(i) *Preference*. Different versions of a product are produced for sale in different markets e.g. Cosmopolitan Magazine (Russian Edition) is officially sold in Russia and Cosmopolitan Magazine (Ukrainian Edition) is officially sold in Ukraine. But some distributors in Ukraine also sell Cosmopolitan Magazine (Russian Edition) as there is a market demand for the latter.

(ii) *Price*. Generally there are price differentials in how goods are sold in different markets. Companies, either the manufacturer or the distributor, set different price points for their products in different markets. Parallel importers ordinarily purchase products in one country at a price (P1) which is cheaper than the price at which they are sold in a second country (P2), import the products into the second country, and sell the products in that country at a price which is usually between P1 and P2. This price differential allows the goods to be resold in the more expensive market at a profit.

(iii) *Shortage*. Quite often official distributors are not able to fully satisfy market demand for goods. In some mar-

kets consumers should wait for certain products to enter the market for some period of time or due to the quotes of the products allocated by the producer demand significantly outstrips supply.

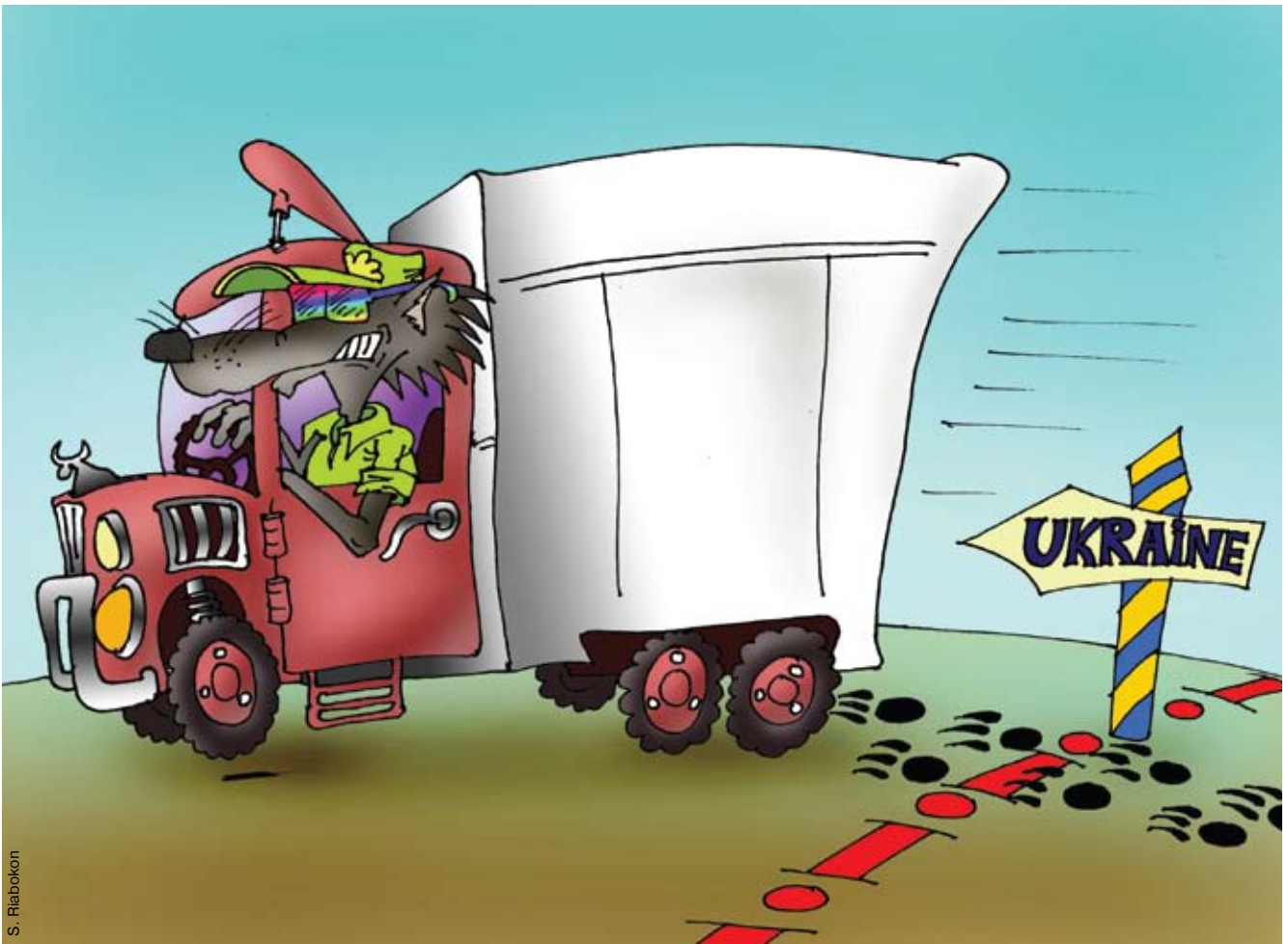
At present there is no consensus among producers, distributors and importers regarding the effect of parallel imports on their businesses. Official distributors complain that parallel import squeezes out them from the Ukrainian market and significantly impedes their sales and their major concern is brand image/reputation (especially for luxury goods) and product liability claims that may occur in respect of parallel imported products. It should be noted that some official distributors are still not concerned with parallel imports. For example, distributors of autos may benefit significantly from providing consumers with after sales services and spare parts (which, as a rule, parallel importers are not able to maintain). In addition, sometimes producers are lukewarm to problems of their official distributors as generally parallel imports do not affect their sales volumes worldwide and they do not want to make any efforts in this respect. Parallel importers believe, in their turn, that official distributors try to hinder parallel import to eliminate competition from the respective market segment and to make excess profits.

It goes without saying that the Ukrainian state authorities are interested in restricting parallel imports as the parallel imported goods quite often do not comply with effective applicable standards and their import results in significant losses of state budget due to non-payment of the relevant taxes and customs duties.

Therefore, opinions on the impact of the parallel market vary by region and industry and, as a result, opinions

¹ The synonymous term grey import is sometimes substituted. The latter term is generally used to suggest that the trade, while not exactly "black market", is not entirely lawful either. In the present article we will use the term parallel import.

² http://en.wikipedia.org/wiki/Parallel_import



on the legitimacy of parallel importation vary by jurisdiction. The legal warfare against parallel imports takes the form of litigation and sometimes efforts at legislation, depending on the jurisdiction³. At one time or another trademarks, copyrights, patents, coding and trade secrets have all been used. Although the legal landscape for the parallel market has become more difficult in the last few years, the business is likely to continue for the foreseeable future.

The aim of this article is not to analyze the legality of parallel trade; we will mainly focus on general review of measures and remedies aimed at restricting it, that may be used by producers and official distributors in Ukraine in the following main areas: intellectual property rights, competition law, related to Ukraine's accession to the World Trade Organization and to be applied by producers and/or official distributors, etc.

Intellectual property rights protection remedies

Ukrainian legislation in the field of intellectual property rights protection (IP rights) was significantly amended in order to comply with the high standards set out in the *WTO Agreement On Trade-Related Aspects of Intellectual Property Rights*. This part of the article provides a general overview of the extent to which the owners of IP rights may use these rights to restrict parallel imports in Ukraine that became available due to Ukraine's accession to the WTO.

It is well known that IP rights give owners the right to prohibit third parties from carrying out certain activities. Therefore, the IP owner enjoys a bundle

of rights that may be used in order to restrict parallel imports⁴.

(i) Remedies available under the Civil Code of Ukraine

According to the *Civil Code of Ukraine*, in the event of infringement of IP rights, an owner or an authorized licensee⁵ is entitled to bring a claim before a court for the following remedies⁶: (a) recognition of IP rights; (b) termination of actions infringing IP rights; (c) indemnification of damages caused by act of infringement of IP rights; (d) application of immediate measures to prevent an act of infringement and to preserve relevant evidence (e.g. provi-

³ http://espinosaiplaw.com/wordpress/?page_id=5

⁴ C. Stothers, *Parallel Trade in Europe: Intellectual Property, Competition and Regulatory Law*, 2007, p. 27.

⁵ According to Ukrainian law only an owner or a person granted by an owner with rights to claim the infringed IP rights based on a license agreement (license) is entitled to claim for protection of infringed IP rights.

⁶ It is worth noting that special legislation in respect of particular IP rights objects shall be taken into account as well, while preparing claim to the court.

sional measures under the *Commercial Procedural Code of Ukraine*); (e) suspension of imports or exports into Ukraine of goods imported/exported with infringements of IP rights; (f) withdrawal from commerce of goods manufactured or entered into the channels of commerce with infringement of IP rights and destruction thereof; (g) publication in the mass media of information on the infringement of IP rights and content of the court decision in this respect, etc.

The major problem arising during use of the said remedies is that since parallel importers import non-counterfeit goods, it may be difficult to substantiate before the court occurrence of infringement of IP rights because of the principle of “exhaustion of rights”. For instance, the *On Protection of Rights to Trademarks for Goods and Services Act of Ukraine* provides for that the exclusive right of a trademark owner to prohibit other persons from unlawful use of the registered trademark shall not cover, *inter alia*, the use of the trademark with respect to goods, being branded with the said trademark, that have been entered into the channels of commerce by the trademark owner or upon its consent⁷, i.e. the right of an owner to the trademark for certain goods shall be regarded as exhausted if such goods are legally sold directly by the trademark owner or by any official/authorized distributor with the consent of the latter.

(ii) Border measures⁸

(a) *Protection of intellectual property rights on the initiative of an owner or an authorized licensee*

For this purpose either an owner, or an authorized licensee of IP rights to a trademark, shall submit to the State Customs Service of Ukraine an application on assistance in protection of IP rights to the trademark⁹. Within the next 30 days the State Customs Service of Ukraine shall adopt a decision on registration of the trademark in the customs register of IP rights and notify

the applicant of such registration. After the applicant places a deposit or bank guarantee in the amount of EUR 5,000 the State Customs Service of Ukraine registers the trademark in the customs register of IP rights and provide the applicant with the respective certificate.

The said registration allows customs agencies, in the event that they define that those goods are imported with infringement of IP rights to the trademark¹⁰, to suspend customs clearance thereof with immediate notification of the authorized persons¹¹ of such suspension. Thereafter, within 15 days of suspension of import, the IP rights owner or authorized licensee shall bring to the court a claim for protection of rights to the trademark. Otherwise, the said goods will be allowed for import into Ukraine.

(b) *Protection of trademark on the initiative of customs agencies*

Customs agencies are entitled to suspend customs clearance of the goods into Ukraine at their own initiative even without registration of the trademark in the customs register of IP rights if: (i) there are justified grounds to believe that the goods are imported with infringement of IP rights; (ii) there is precise information on an owner or an authorized licensee of such IP rights. In the latter case, customs agencies shall notify the said persons on such suspension and they shall act as stated above.

At the same time, producers and official distributors shall bear in mind the following risks related to application of borders remedies. As parallel importers import non-counterfeit goods, it may be difficult to prove before the court that the goods are imported with infringement of IP rights (see for details above). Moreover, both customs agencies and parallel importers are entitled to claim an owner of IP rights or an authorized licensee for compensation for any injury caused by suspension of imports (es-

pecially in cases, when they will not be able to substantiate before a court that the goods are imported with infringement of IP rights).

(iii) Unfair competition protection remedies

The *On Protection Against Unfair Competition Act of Ukraine* stipulates that use of a trademark by a legal entity without permission of another legal entity started earlier to use such trademark (or similar trademark) in its commercial activities that result (or may result) in likelihood of confusion of consumers in the respect of commercial activities of the said legal entities shall be regarded as infringement of fair competition. For instance, the following actions may be regarded as unfair competition: while distributing goods, parallel importers actively use the trademark of the producer e.g. in promotion, advertising materials, in media, etc., without the relevant permission. In such case, an owner of the trademark or an authorized licensee is entitled to file an application to the Antimonopoly Committee of Ukraine¹². The Committee shall investigate the alleged infringement and, as a result, may impose a fine. In addition, an owner of the trademark or an authorized licensee is entitled to bring a claim before a court for indemnification by parallel importers of damages caused by unfair competition and/or for seizure of goods/materials with unlawful use of the trademark.

Remedies introduced or to be introduced by state agencies

Ukraine has been, on its path to WTO membership, gradually adopting its legislation to the standards and

¹⁰ E.g. by unauthorized importers - importers, information on which is not incorporated in Clause 6 of the application on assistance in IP rights protection or is incorporated in Clause 7 therein that includes information on importers importing counterfeit goods (pursuant to Annex of the *Order of Registration of Intellectual Property Rights Objects in Customs Register, Obtaining Information and Cooperation of Customs Agencies with Other Law Enforcement and Supervisory Bodies and Owners of Rights to Intellectual Property Rights Objects in case of Suspension of Customs Clearance of Goods by Customs Agency approved by the Resolution of the Cabinet of Ministers of Ukraine*)

¹¹ The list of authorized persons as well as contact details thereof, shall be inserted in the application on assistance in IP rights protection

⁷ Similar provisions are stipulated in the *On Protection of Rights to Industrial Designs Act of Ukraine, On Protection of Rights to Innovations and Utility Models Act of Ukraine*.

⁸ Set forth by the *Customs Code of Ukraine*. At the present time the respective remedy is mostly used for trademarks. Therefore, in order to avoid any misunderstandings herein we will refer to trademarks only.

⁹ The form of the said application as well as exhaustive list of documents to be submitted therewith is set forth in the *Resolution of the Cabinet of Ministers of Ukraine On Issues related to Registration of Intellectual Property Rights Objects in Customs Register, Obtaining Information and Cooperation of Customs Agencies with Other Law Enforcement and Supervisory Authorities and Owners of Rights to Intellectual Property Rights Objects in case of Suspension of Customs Clearance of Goods by Customs Agency*.

practices of WTO Members. Therefore, the relevant certification, registration procedures conducted by state authorities is gradually becoming more transparent and thus, there is a fall in corruption. State control procedures can also be used by producers and official distributors as an effective remedy against parallel import.

(i) Certification

Even though parallel importers import into Ukraine non-counterfeit goods, sometimes the latter may not comply with the applicable Ukrainian standards (e.g. cars destined for the USA and the Middle East, household appliances, mobile phones). Due to different "reasons" such unfit goods are allowed for import into Ukraine by customs agencies and then, are sold to final customers in Ukraine. It is worth noting that strengthening of certification regulations may be quite an effective remedy against parallel import.

Taking into account the above, it is highly advisable for official distributors and/or producers to actively cooperate with state agencies in charge of adopting new or improving effective certification legislation. Moreover, it is of crucial importance for official distributors and/or producers to monitor further application and compliance with certification regulations and to take appropriate measures in the event of breaches.

(ii) Cooperation with customs authorities in respect of indicative prices

According to the *Customs Code of Ukraine*, the Regulation of the Cabinet of Ministers of Ukraine *On Approval of Order of Conducting Control under Correctness of Customs Value Determination* customs agencies are empowered to control the correctness of customs value determination at different stages of customs clearance procedure. In addition, customs agencies are entitled to increase/decrease the declared customs value if the latter does not comply with customs values of identical or similar goods, for

which customs clearance has been completed; available information on the price level for certain goods or on direct production costs (e.g. costs for raw materials, components); information received from tax agencies, supervisory agencies, different financial institutions in respect of particular transactions, etc. Experts are of the opinion that introduction of the said regulation may be an effective measure to stop parallel import.

(iii) *Establishment of joint customs check points*, at which the imported goods will be checked jointly by customs agencies of Ukraine and of the respective foreign countries. Quite often parallel importers provide foreign customs agencies with invoices containing the actual price of goods, while Ukrainian customs agencies – with invoices containing undercut prices in order to avoid paying full amounts of VAT and applicable customs duties. Thus, establishment of joint customs check points may eliminate the said scheme.

(iv) Keeping joint statistical records

Foreign customs agencies and Ukrainian customs agencies will exchange information on export-import operations. As a result, Ukrainian customs agencies will have precise information on volumes and values of goods exported from a particular country. Thus, parallel importers will not be able to import goods without customs clearance procedures and with undercut prices.

(v) Industry-specific measures:

(a) *Parallel import of cars*. State agencies are currently developing amendments to relevant Ukrainian legislation in order to prohibit state automobile inspections from registering vehicles that do not comply with Ukrainian standards, or imported under inadequate prices or imported without payment of all mandatory taxes and fees, which may significantly impede parallel import.

(b) *Parallel import of mobile phones*. On 5 February 2009 the National Commission on Regulation of Telecommunication of Ukraine (the Commission) approved the *Order On Disposal of Radio Electronic Facilities and Radiating Devices in Ukraine* and the *Order On Provision of Permit for Import from Abroad into Ukraine of Radio Electronic Facilities and Radiating*

Devices. The said orders significantly amend the existing order of import into Ukraine and sale of radio electronic facilities and radiating devices, especially mobile phones. Moreover, the Commission is going to introduce accounting of IMEA codes of mobile phones. After the import of mobile phones into Ukraine, importers shall provide the Ukrainian State Centre of Radiofrequency State Enterprise (USCR) with a list of IMEI codes of imported mobile phones along with the invoice, import permit and customs clearance declaration. Then, the USCR shall include the said IMEI codes in the IMEI database. In addition, the mobile operators will render mobile services only in mobile phones included in the said IMEI database. There is no uniform attitude to the said orders. However, experts believe that such measures will be effective against parallel import¹³.

Remedies to be applied by producers and official distributors

It is worth noting that producers and official distributors are also able to apply effective commercial remedies against parallel import on their own, e.g. proper re-export restrictions in distribution agreements, high quality after sales services and warranty works, media campaigns, etc.

This overview of remedies available against parallel imports under Ukrainian law is aimed at showing that Ukrainian law provides the required minimum level of protection against parallel imports. However, a number of problems still exist in this field and a lot still needs to be done by the Ukrainian government. Notwithstanding the above, producers and official distributors should not neglect to study and apply all the above remedies when necessary. At the same time, prior to commencing the fight against parallel imports producers and official distributors shall, in order to win, develop a comprehensive strategy and system of remedies at different levels. It also goes without saying that the cornerstone of success in such a fight is common interest and joint efforts on the part of producers as well as official distributors. ■

¹² The requirements to such application as well as order of consideration thereof is envisaged in the *On Protection of Economic Competition Act of Ukraine*, in the Order of the Committee *On Approval of Temporary Rules on Consideration of Cases on Infringement of Antimonopoly Legislation of Ukraine*.

¹³ <http://www.kommersant.ua/doc.html?DocID=1143889&IssueId=7000075>