

## **Report Q205**

in the name of the Canadian Group  
by Bruce E. MORGAN

### **Exhaustion of IPRs in cases of recycling and repair of goods**

#### **Questions**

##### **I) Analysis of the current statutory and case laws**

###### *1) Exhaustion*

*In your country, is exhaustion of IPRs provided either in statutory law or under case law with respect to patents, designs and trademarks? What legal provisions are applicable to exhaustion? What are the conditions under which an exhaustion of IPRs occurs? What are the legal consequences with regard to infringement and the enforcement of IPRs?*

#### **Exhaustion**

In Canada, exhaustion of IPRs is not provided in statutory law, but has received limited equivalent recognition in case law with respect to patents, designs and trade-marks, under the concept of "implied license".

#### **Patents**

Section 42 of the Canadian Patent Act provides that "the patentee has the exclusive right of making, constructing and using the invention and selling it to others to be used...". Canadian case law has construed this section to grant an implied licence to a purchaser from the patentee of a patented article to freely use and/or resell the article in the ordinary course of trade. Although there is no established Canadian law on point, it is assumed that the vendor of an article which uses the vendor's patented process impliedly licenses the use of the article to practice the process.

The patentee/vendor may place contractual restrictions on use or resale, but the restrictions must be drawn to the attention of the purchaser. A purchaser without notice of restrictions therefore has an implied license, and to that extent, the rights are exhausted.

#### **Industrial Designs**

Designs are exhausted by placing into commerce an article to which the design has been "applied". Importation of an article to which a design, protected in Canada, has been applied in a foreign country is infringement (Section 11 Industrial Designs Act) unless a license has been granted by the owner. License may be implied if the owner of the design authorized its foreign application.

#### **Trade-marks**

Once a product, bearing a trade-mark, has been placed into commerce, the trade-mark owner's rights are exhausted within Canada. Contractual restrictions may limit the rights of a licensee or distributor.

2) *International or national exhaustion*

*Does the law in your country apply international exhaustion for patents, designs or trademarks? If yes, are there any additional conditions for international exhaustion compared to regional or national exhaustion, such as a lack of marking on products that they are designated only for sale in a specific region or country or the non-existence of any contractual restrictions on dealers not to export products out of a certain region? What is the effect of breach of contractual restrictions by a purchaser?*

Canada generally recognizes national exhaustion, characterizing it as “implied licence”. The origin of products in other jurisdictions is problematic. Importation of a patented article or an article made directly or indirectly by a patented process where the goods do **not** originate with the Canadian IPR owner is contrary to Canadian case law (Saccharine Doctrine). However, grey goods/parallel imports are a different situation. Where the goods originate in a foreign jurisdiction, but are from the Canadian patent holder, then there is an implied licence, and they may be imported into Canada, used and resold here, unless there is a known contractual limitation to the contrary.

The same applies to industrial designs.

Section 27 of the Copyright Act makes it an act of infringement to import a work if the importer should have known that making the work in Canada would infringe copyright. Section 27.1 is more specific in relation to grey goods importation of books, and requires the consent of the copyright owner to avoid infringement.

In contrast, trademark law in Canada has extended to recognize international exhaustion. While trademarks are infringed by importation of trademarked goods which did not originate with the Canadian trademark owner, grey goods having common trademark ownership may be imported under an implied licence. Consequently, where there are different owners in Canada and another country, of the same trademark, importation into Canada from that other country can still constitute infringement.

*If your law does not apply international exhaustion, is there regional exhaustion or is exhaustion limited to the territory of your country?*

Canada does not recognize International exhaustion for patents or designs. Furthermore, there is no regional exhaustion in the NAFTA territories. Exhaustion is limited to the Canadian territory.

For trade-marks, where the owner in both Canada and in a foreign jurisdiction is the same, international exhaustion will apply and the foreign trademarked goods of the owner can enter Canada without restriction (parallel importation is permitted).

*In case your country applies regional or national exhaustion, who has the burden of proof regarding the origin of the products and other prerequisites for exhaustion and to what extent?*

The party asserting implied or express license (i.e. exhaustion) bears the evidentiary burden, while the ultimate burden of proof of infringement remains with the IPR owner.

3) *Implied license*

*Does the theory of implied license have any place in the laws of your country? If so, what differences should be noted between the two concepts of exhaustion and implied license?*

Canada recognizes the concept of an implied license. Such implied license is subject to express contrary terms, such as contractual limitations, in a license or a sale, which may clearly deny exhaustion by limitations of further use or sale including export/import.

4) *Repair of products protected by patents or designs*

*Under what conditions is a repair of patented or design-protected products permitted under your national law? What factors should be considered and weighed? Does your law provide for a specific definition of the term "repair" in this context?*

Although there is limited Canadian case law, Canada has recognized the distinction between repair of a product (which is permitted) and remanufacture (which is not permitted). In the patent case of *Rucker v. Gavel* (1985) 7 C.P.R. (3d) 294, the Federal Court of Canada examined the question of manufacture or repair where a purchaser of a patented article (blow-out preventer) arranged to have the article "repaired" by a third party, when the article was worn out and no longer functional. The "repair" constituted total disassembly of the article, discard of some worn or damaged components and remanufacture of a new article utilizing some old components plus a new flexible mounting. In theory, the "repaired product" was returned to the original purchaser with their old incorporated in the repaired product. Occasionally, however, some new components were required as replacement parts. The Court followed English authorities and held that it is a question of fact in each case whether the work which has been done "may be fairly termed repair or manufacture, regard being had to the exact nature of the patented invention." Elongation of life of a patent article is fair, but obtaining a substantially new article by retaining only some subordinate parts of an old article is not fair. In *Rucker*, the Court held that it was substantially a remanufacture of the BOP packing element as while only some or all of the original teeth were retained, all other aspects of the element were new manufacture.

The term "repair" has not been defined in Canadian statute, but the meaning is ascertained from case law. Repair, as distinguished from remanufacture, must be determined with due consideration as to the nature of the invention.

5) *Recycling of products protected by patents or designs*

*Under what conditions is a recycling of patented or design-protected products permitted under your national law? What factors should be considered and weighed? Does your law provide for a specific definition of the term "recycling" in this context?*

Canada has no statutory provisions pertaining to recycling of patented or design protected articles, nor has there been case law determination of "recycling" except by analogy to "repair" as enunciated in the *Rucker* decision.

6) *Products bearing trademarks*

*Concerning the repair or recycling of products such as reuse of articles with a protected trademark (see the examples hereabove), has your national law or practice established specific principles? Are there any special issues or case law that govern the exhaustion of trademark rights in your country in case of repair or recycling?*

Section 19 of the Canadian Trade-marks Act gives the owner of the trade-mark the exclusive right to use the trade-mark in Canada in respect of the registered wares or services. It is infringement if a person sells, distributes, or advertises wares or services in association with a confusing trade-mark. It is actionable to depreciate the goodwill in a trademark to use another person's registered trade-mark. From this, it appears that it is not an infringement to repair and recycle articles bearing the registered trade-mark which were previously sold by a trade-mark owner in the ordinary course of trade. There is an implied license that articles entering the stream of commerce by the trade-mark owner or with the owner's approval may continue to be used or sold. Nonetheless, it may be considered depreciation of goodwill contrary to Section 20 of the Trade-marks Act if a third party repairs or recycles a product bearing a trade-mark. This is not simply resale in the ordinary stream of commerce, but is deemed to be use of the trademark by the third party because "at the time of transfer of the property

in the repaired or recycled wares, the trade-mark is still marked on the wares themselves". Furthermore, as the trade-mark owner no longer has control of the character or quality of the repaired or recycled product the goodwill is clearly subject to potential depreciation, i.e. for example Coca Cola bottles refilled with inferior, and possibly deleterious, product.

7) *IPR owners' intention and contractual restrictions*

- a) *In determining whether recycling or repair of a patented product is permissible or not, does the express intention of the IPR owner play any role? For example, is it considered meaningful for the purpose of preventing the exhaustion of patent rights to have a marking stating that the product is to be used only once and disposed or returned after one-time use?*

Canada recognizes implied licenses to a purchaser of a patented article. Canada also recognizes express licenses or contractual limitations at the time of sale of a patented product, but mere intention is not relevant unless expressed contractually. Consequently, an express license or condition of sale restricting a product to single use would ordinarily be recognized by Canadian Courts. This is particularly true where there is a public benefit of such restriction (i.e. disposable syringes not capable of satisfactory decontamination after use). However, the limitations must be drawn to the purchaser's attention in order to be effective, and a purchaser without notice is not bound. Clear marking on the product may be sufficient notice, such as "shrink wrap" conditions.

- b) *What would be conditions for such kind of intentions to be considered?*

Intentions must be express, such as contractual limitations.

- c) *How decisive are other contractual restrictions in determining whether repair or recycling is permissible? For example, if a license agreement restricts the territory where a licensee can sell or ship products, a patentee may stop sale or shipment of those products by third parties outside the designated territory based on his patents. What would be the conditions for such restrictions to be valid?*

Canadian Courts will enforce contractual limitations unless they offend public morality, are unconscionable, or are contrary to law, such as the Canadian Competition Act. Canadian case law recognizes that licenses may be restricted, including restrictions by territorial jurisdiction, specific product, or duration. Where a licensee breaches a clearly enunciated territorial restriction, the Courts would normally recognize such restriction and enforce it unless contrary to law.

- d) *Are there any other objective criteria that play a role besides or instead of factors such as the patentee's intention or contractual restrictions?*

Other objective criteria – statutory limitations, such as Canadian Competition Act can impose restrictions on price maintenance, tied selling. Similarly, International obligations of WTO or NAFTA may have limiting implications.

- e) *How does the situation and legal assessment differ in the case of designs or trademarks?*

The foregoing legal assessment is assumed to apply equally to designs, although there is no case law or statutory limitation thereon. Trade-marks would not normally be restricted in the aftermarket, but contractual restriction may apply to licensees using the mark.

8) *Antitrust considerations*

*According to your national law, do antitrust considerations play any role in allowing third parties to recycle or repair products which are patented or protected by designs or which bear trademarks?*

The Canadian antitrust law, the Competition Act, does not authorize third parties to recycle or repair products.

9) *Other factors to be considered*

*In the opinion of your Group, what factors, besides those mentioned in the Discussion section above, should be considered in order to reach a good policy balance between appropriate IP protection and public interest?*

Canadian law has endeavoured to structure a balance between fair reward to a patentee or trade-mark owner, and competition in the marketplace. On occasion, for policy reasons, statutory intervention has limited an IPR holder's rights, such as Section 21.01 of the Canadian Patent Act, permitting third parties to manufacture patented pharmaceuticals in Canada for export only. This was intended to assist in providing pharmaceuticals for humanitarian purposes in countries with public health problems, and was a moral policy decision imposed statutorily. In today's economy, where undue exploitation of resources is to be discouraged and environmental protection encouraged, statutory intervention to define repair and recycling rights may be appropriate.

10) *Interface with copyrights or unfair competition*

*While the present Question is limited to patents, designs, and trademarks as noted in the Introduction above, does your Group have any comments with respect to the relationship between patent or design protection and copyrights or between trademarks and unfair competition relative to exhaustion and the repair and recycling of goods?*

In the environment of products, Canadian copyright protection is limited to designs for those useful products manufactured to an extent fewer than 50 in number. Beyond that range, copyright protection no longer applies (Section 64(2)), and resort to industrial design protection is necessary. With respect to trade-marks, improper use of another's trade-mark may result in depreciation of goodwill. Also Section 7(e) of the Trade-marks Act prohibits anyone from doing any act or adopting a business practice contrary to honest industrial commercial usage in Canada.

11) *Additional issues*

*In the opinion of your Group, what would be further existing problems associated with recycling and repair of IPR-protected products which have not been touched by these Working Guidelines?*

The most significant issue in repair or recycling would be the issue of quality control. Counterfeiting is a major International issue today, and the equivalent situation arises where a product, bearing a legitimate trade-mark, may be refilled with sub-quality product, or repaired with inferior materials, but purchased by consuming public assuming a quality consistent with the original trade-marked product.

With respect to articles subject to patent or design protection, the exclusivity arising from the design or patent protection may lead consumers to anticipate size or quality standards. Such standards may not be met by a remanufactured/repaired or recycled product. Issues of that regard may be resolved by requiring clear labelling that the product has been remanufactured or recycled with materials different from the original manufacturer. Consumer protection legislation may be required to put appropriate conditions on such labelling.

**II) Proposals for uniform rules**

The Canadian Group has not developed any such proposals.

### **Summary**

Canada has no statutory or case law policy of exhaustion of IPR's. However, licenses are implied when goods bearing an IPR are placed into commerce by the IPR owner. Such implied license may be countered by express contractual restrictions.

### **Résumé**

L'épuisement des droits de propriété intellectuelle en cas de réparation ou de recyclage des produits.

Le Canada n'a pas de politique en droit ou en jurisprudence quant à l'épuisement des droits de propriété intellectuelle. Cependant, une licence implicite est présumée quand des marchandises portant un droit de propriété intellectuelle sont placées dans le commerce par leur propriétaire. Une telle licence implicite peut être contrée par des restrictions contractuelles expresses.

### **Zusammenfassung**

Die Erschöpfung von Rechten des Geistigen Eigentums in Fällen des Recyclings oder der Reparatur von Waren

Kanada hat keine gesetzlichen oder rechtssprechenden Leitlinien für die Erschöpfung von Rechten des Geistigen Eigentums. Lizenzen sind jedoch impliziert, wenn rechtstragende Waren von den Rechteinhabern in den Verkehr gesetzt werden. Solche implizierten Lizenzen können durch ausdrückliche vertragliche Einschränkungen entgegengesetzt werden.