

# Copyright Law Update: Costco v. Omega

November 8, 2010

 09-0234\_BANNER\_IPadvisory\_R1-small.gif

## Supreme Court Hears Arguments in *Costco v. Omega*

by Steve S. Chang and Rajit Kapur

### Background

On November 8, 2010, the U.S. Supreme Court heard oral arguments in *Costco Wholesale Corp. v. Omega, S.A.*, a case that could have far-reaching implications on a copyright holder's ability to control the downstream distribution of imported goods.

In the case, Swiss watch manufacturer Omega S.A. sought to control the distribution and pricing of its watches in different countries, and employed a rather unconventional use of copyright to limit importation of genuine Omega watches into the United States. In particular, Omega placed a small copyrighted logo on the back cover of its "Seamaster" watches, so that it could treat the unauthorized importation of the watches by others as an illegal importation of a copyrighted work.

The U.S. Copyright Act, at 17 U.S.C. 602(a)(1), restricts the unauthorized importation of copies of a copyrighted work, and Omega sought to use this restriction to prevent Costco, which was purchasing Seamaster watches from overseas dealers at reduced prices, from subsequently importing the watches into the U.S. and selling them for less than other U.S. retailers. According to the doctrine of copyright exhaustion, however, which is codified in §109(a) of the Act, "the owner of a particular copy ... lawfully made under this title ... is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy ..." Because the watches imported by Costco were originally made and sold by Omega to a distributor in Paraguay, Costco raised this copyright exhaustion clause as a defense, and the trial court granted Costco summary judgment. On appeal, the Ninth Circuit reversed on the grounds that §109(a) did not supersede §602(a)(1), and that applying this exhaustion or "first-sale" defense to copyrighted works manufactured overseas would amount to impermissible extraterritorial application of U.S. law.

Since the Supreme Court agreed to hear the case, numerous *amici* briefs were filed on behalf of manufacturers, importers, libraries, music recording associations, and other entities concerned with how the Court's decision would affect future use of imported copyrighted works.

### Oral Argument

The oral argument discussion with and questions from the bench mainly focused on what it meant to be “lawfully made under this title,” as the term is used in §109(a), since that section grants the owner of such a copy the right to sell or otherwise dispose of the copy however they see fit. The following provides some of our observations from the questioning and argument.

### **Justice Scalia**

Justice Scalia focused his inquiry on the language (or absence thereof) in the Copyright Act. To Omega, Justice Scalia asked where there was any textual support for Omega’s argument that “lawfully made under this title” should be interpreted to mean “lawfully made in the U.S. under this title.” Omega did not cite specific textual support, but responded with its position that something made in Switzerland by a Swiss manufacturer is not made under any U.S. title at all, since U.S. law does not govern Swiss manufacturing. So the manufacturing of the watches in this case, according to Omega, was neither lawful nor unlawful “under this title.” Scalia then turned his textual analysis to Costco, asking if Costco was also adding language to the text. Specifically, Scalia asked whether Costco was suggesting that “lawfully made under this title” should be interpreted to mean, for foreign-made goods, that the goods “would have” been considered lawfully made “if this title had been applicable” at the place of manufacture. This one appeared tougher for Costco to counter, and afterwards it appeared that Justice Scalia might not have bought into Costco’s position.

### **Justice Breyer**

Justice Breyer sought a simple solution. He posited that there were hundreds, thousands even, of contracts and contractual obligations out there between various manufacturers, distributors and retailers, and that it would be onerous to expect each purchaser of an imported good to sort through all of the applicable contracts to determine if an imported good were indeed “lawfully made” outside of the U.S. (and thus legally imported). He asked why the test could not just be whether there had been a sale at all by the copyright holder. Neither side appeared to provide him with a reason that his test was unworkable. That, and the question itself, appeared to suggest a leaning towards Costco’s position.

### **Justice Sotomayor**

Justice Sotomayor challenged Omega’s efforts to distinguish the Supreme Court’s decision in *Quality King*<sup>[1]</sup>. In *Quality King*, the copyright owner manufactured the copyrighted good, shipped them overseas, and the goods were subsequently imported back into the U.S. The Supreme Court held that this was an exhaustion, and Omega now attempts to distinguish that case on the grounds that the goods in that case were made in the U.S., and therefore made “under this title.” Justice Sotomayor, however, challenged Omega’s counsel to identify specific language from the *Quality King* decision that relied on the place of manufacture in determining whether it was “under this title” for purposes of exhaustion. Omega’s response did not say there was such explicit language, but noted that the decision itself included Justice Ginsburg’s brief concurrence (which acknowledged that their decision did not resolve cases in which the manufacturing was done abroad), and that Omega’s position today is consistent with the rest of *Quality King*.

### **Justice Ginsburg**

Justice Ginsburg asked counsel for Costco whether §602(a)(1) would have any purpose at all if §109(a) provided a defense for the importation in this case. Costco’s response was to note that §602(a)(1) would still be the proper remedy in situations that did not implicate first sales. Piratical copies, for example, would be blocked by §602(a)(1) and not §109(a).

### **Conclusion**

Time will tell how the Supreme Court decides this case. With Justice Kagan’s recusal, and the balanced questioning discussed above, there appeared to be a fairly evenly matched set of opinions in the room, and the possibility of a 4-4 split remains.

---

[1] 45 USPQ2d 1961 (U.S. 1998)

**Posted: November 8, 2010**