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The Saga of *Omega v. Costco Wholesalers Corp.*

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In an effort to control after-market (grey market) sales of its Swiss-made watches, Omega places a U.S. copyrighted design (“the Omega Globe Design”) on the backside of its watch cases. Omega hoped doing so would let it control third party imports to the United States by suing the unauthorized seller for copyright infringement. Seven years after it first sued Costco for copyright infringement, Omega is now back at the Ninth Circuit.

Omega makes its watches in Switzerland and distributes them globally through a network of authorized distributors and retailers. The Omega Globe Design was three millimeters in size and was inscribed on the backside of certain of Omega’s watches. Costco obtained the watches outside the United States where Omega had originally sold them to authorized distributors. Costco, then, sells these grey market watches in the United States at a significant discount.

Omega sued Costco in 2004 for copyright infringement for the unauthorized importation of watches bearing the U.S. copyrighted Omega Globe

Design. At the district court, Costco moved for summary judgment that it was entitled to the first sale defense. Costco argued that Omega’s authorized sale of the watches bearing the copyrighted Globe Design exhausted Omega’s ability to use its U.S. copyright to control future sales, even though those initial sales were outside the United States. Costco also alleged copyright misuse. Omega moved to strike Costco’s affirmative defense of copyright misuse. Judge Hatter, of the Central District of California, granted Costco’s motion for summary judgment “without explanation,” and did not decide the copyright misuse issue on the grounds that Omega’s motion to strike the defense was mooted. Omega appealed to the Ninth Circuit.

The Appeal to the Ninth Circuit and the Supreme Court “Affirmance”

On appeal, the Ninth Circuit considered whether Omega’s authorized initial sale outside of the United States exhausted Omega’s U.S. copyright. The Ninth Circuit ruled that the third party importation and sale of a watch bearing a copyrighted design that

was both made and first sold outside of the United States by the U.S. copyright owner, was an infringement of the U.S. copyright. *Omega v. Costco Wholesale Corp.*, 941, F.3d 982 (9th Cir. 2008), *aff'd*, 131 S. Ct. 565 (2010) (per curium).

The Ninth Circuit reasoned that Costco's infringement depended on the relationship of three sections of Title 17 (The Copyright Act of 1976): 17 U.S.C. §§ 106(3), 109(a), and 602(a). *Id.* Section 602(a) states that importation into the United States without the authority of the owner of a copyright under Title 17 is an infringement of the copyright owner's exclusive right to distribute copies. Section 106(3) states that the owner of the copyright under Title 17 has the exclusive right to distribute copies of the copyrighted work in the United States. However, Section 109(a) of Title 17 provides that "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..." (emphasis added). Section 109(a) represents a codification of what is often called the "first sale doctrine" which holds that after a copyright owner authorizes the sale of a particular copy, they may not thereafter exercise control over that copy. *Id.* at 985.

Omega argued that Title 17 was not extraterritorial. Consequently, because copies of the design were not made in the United States, they were not made under "this title." *Id.* Costco countered that the copies were lawfully made under Title 17 based on an argument that Omega did not violate Title 17 when it made the copies. Costco also argued that in *Quality King Distributors, Inc. v. L'anza Research Int'l, Inc.*, 523 U.S. 135 (1998) the Supreme Court had held that when a copyright owner makes or sells a copyrighted work anywhere, it exhausts the U.S. copyright in that copy. Omega disputed that interpretation.

The Ninth Circuit agreed with Omega. They reasoned that *Quality King* did not directly overrule prior precedent holding that foreign made goods did not exhaust U.S. copyrights when sold outside the United States by the U.S. copyright owner. The Ninth Circuit explained that *Quality King* involved a situation where the copyrighted works were made by the copyright owner in the United States before they were exported for foreign sale. They concluded that it was manufacturing in the U.S. in *Quality King* that exhausted the copyright, not a foreign sale. *Id.* at 985-86.

The Ninth Circuit also relied on what it considered to be a presumption that the copyright laws are not intended to be applied extraterritorially. The Ninth Circuit held that applying the first sale doctrine to "foreign-made copies would impermissibly apply the Copyright Act extraterritorially" because characterizing copies made overseas as lawful under Title 17 would require ascribing legality under the Copyright Act to conduct occurring outside of the United States. *Id.* at 988. The Ninth Circuit further relied on Justice's Ginsberg's concurrence in *Quality King* that "lawfully made under this title 'means' lawfully made in the United States." *Id.* at 989.

The Supreme Court granted *certiorari* on the Ninth Circuit's decision. Justice Kagan recused herself from rendering a decision in this case due to her prior Justice Department involvement in briefing this matter before the Supreme Court, and thus only eight Justices remained. The Supreme Court announced that it was tied at 4-4 and therefore unable to reverse the Ninth Circuit. Accordingly, the Ninth Circuit's decision is "affirmed."

On Remand to the District Court

Back on remand at the district court, both parties

again moved for summary judgment. Costco moved for summary judgment for a finding of copyright misuse, and Omega moved for partial summary judgment to strike Costco's affirmative defense of copyright misuse. Judge Hatter granted summary judgment for Costco, finding that Omega is precluded for enforcing its copyright because it misused its copyright. *Omega v. Costco Wholesale Corp.*, CV 04-05443 TJH (C.D. Cal. Nov. 9, 2011) (Hatter, J.).

Judge Hatter noted that in the Ninth Circuit, the copyright "misuse defense prevents copyright holders [from] leveraging their limited monopoly to allow them to control areas outside of their monopoly." *Id.* at 3. However, he indicated that this did not preclude copyright misuse from applying to other situations. *Id.*

In his decision, Judge Hatter focused on "Omega[']s conce[ssion] that a purpose of the copyrighted Omega Globe Design was to control the importation and sale of its watches containing the design, as the watches could not be copyrighted." *Id.* at 3. Seemingly, based on this fact alone, Judge Hatter found that "Omega misused its copyright of the Omega Globe Design by leveraging its limited monopoly in being able to control the importation of that design to control the importation of its [] watches." *Id.*

Judge Hatter acknowledged that previous cases finding "copyright misuse [have] been limited to situations involving antitrust tying agreements and restrictive licensing agreements." *Id.* In fact, in both of the cases that Judge Hatter relied on in his decision to find copyright misuse, the underlying theory was that of a restrictive licensing agreement.

For example, in *Lasercomb America, Inc., v. Reynolds*, the copyright holder included language in the licensing agreements that restricted the licensee from developing "any kind of software" relating to the technology being licensed. 911 F.2d 970, 978 (4th Cir. 1990). Similarly, in *Practice Management Info. Corp. v. Am. Med. Assoc.*, the copyright holder included language requiring the licensee to use its software to the exclusion of all others. 121 F.3d 516, 520-521 (9th Cir. 1997). In both of these cases, copyright misuse had been based on the restrictive language in the licensing agreement.

Judge Hatter conceded that Omega did not engage in either an antitrust-type tying agreement or a restrictive licensing agreement. *Id.* However, he reasoned that "the contours of the doctrine of copyright misuse have yet to be defined." *Id.* He proposed that the above-mentioned cases adopted a broad rule for the application of copyright misuse and did not state that a tying agreement or a restrictive licensing agreement was a necessary element for finding copyright misuse. *Id.* Thus, Judge Hatter concluded that copyright "misuse could be applied to new situations as they arose." *Id.*

Further, Judge Hatter rejected Omega's argument that the multiple purposes of the copyrighted Omega Globe Design—one of which was to control the importation of its watches—was a defense to copyright misuse. *Id.* at 3-4. He concluded that "[w]hile the Omega Globe Design might have its own independent creative and aesthetic value, those aspects of the design are protected by its copyright and are not a defense to copyright misuse." *Id.* at 4. Accordingly, Judge Hatter entered judgment for Costco.

Conclusion

On December 9, 2011, Omega filed an appeal to the Ninth Circuit. It remains to be seen how the Ninth Circuit will rule and whether this case will ever come to an end.

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