

LSUC Continuing Legal Education Program of February 28, 2008

Euro-Excellence Inc. v. Kraft Canada Inc., 2007 SCC 37
(Supreme Court of Canada, July 26, 2007)

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FACTS

Kraft Foods Belgium SA (“KFB”) and Kraft Foods Schweiz AG (“KFS”) are the manufacturers of Côte d’Or and Toblerone chocolate bars, respectively. The packaging of these chocolate bars included artwork consisting of copyrighted logos that function as trade-marks and depict an elephant and “bear within mountain” respectively. In what the trial judge found to be “an interesting strategy in an effort to thwart Euro-Excellence's distribution of these chocolate bars in Canada”,² KFB and KFS gave exclusive copyright licenses to Kraft Canada Inc. (“KCI”) for the artwork. These copyrights and licenses were duly registered.

For a time, Euro-Excellence (“EE”) had been the authorized exclusive distributor of Côte d’Or chocolate bars in Canada. However, the contractual arrangement ended and EE became a parallel importer of both brands of chocolate bars.

Canadian trade-marks law would not have been effective to block parallel importation of the genuine Côte d’Or and Toblerone chocolate bars in question.³ Instead, KCI, along with KFB and KFS, sued EE pursuant to s. 27(2)(e) of the Canadian *Copyright Act* for secondary infringement arising from importation of the chocolate bars on the basis of KCI’s copyright rights as an exclusive licensee of the artwork in question.

The trial judge awarded damages of CDN \$300,000 and granted an injunction that allowed EE to continue to import the chocolate bars, provided that the art work in question was obscured by a “cover up” effected with non-removable stickers.

¹ Note: The author of this comment was Counsel for the Intervener, Retail Council of Canada (“RCC”), in the hearing before the SCC. RCC supported the Appellant, but on the basis of different submissions, largely concerning the hypothetical maker requirement. Any views expressed in this article are solely those of the author.

² *Kraft Canada Inc. v. Euro Excellence Inc.* (F.C.), [2004] 4 F.C. 410, 2004 FC 652, para. 4.

³ *Smith & Nephew Inc. v. Glen Oak Inc. et al.; Beiersdorf Ag, Necessary Party* (1996) 68 C.P.R. (3d) 153.

The Federal Court of Appeal largely upheld⁴ the trial judgment, although it remitted the matter on the question of the calculation of damages.

At this point, the case was attracting considerable attention and numerous prominent Canadian law firms were advising on their websites that copyright law offered the potential to “thwart” parallel importation in circumstances where trade-marks law would be ineffective. The Defendant obtained leave to appeal to the Supreme Court of Canada (“SCC”). The appeal was heard on January 16, 2007 and the Court rendered its judgment on July 26, 2007.

HELD

The SCC allowed the appeal⁵ with costs throughout, with two of the nine Justices dissenting. Amongst the seven Justices who allowed the appeal, there were interesting disagreements on important issues.

The Reasons for Judgment were written by Rothstein, J., with Binnie and Deschamps JJ. concurring. There were concurring reasons and additional comments by Fish, J. These four justices held that there was no secondary copyright infringement because there was no “hypothetical primary infringement.” These Justices concluded that, according to the statute, which includes a “hypothetical maker”⁶ requirement in s. 27(2)(e), KFB and KFS could not infringe their own copyright in Canada if they were to hypothetically manufacture in Canada. This is because they are the copyright owners and a copyright owner cannot infringe its own copyright. Therefore, it followed that the secondary infringement remedy is not available to exclusive licensees when the goods are made abroad by the copyright owner/licensor. In a separate concurrence, Justice Fish agreed with all of this and went on to note, *inter alia*, the nominal consideration for the exclusive license. He clearly expressed scepticism arising from the trial judge’s finding that:

the sole purpose of [Kraft Belgium and Kraft Schweiz] registering copyright in Canada and then assigning rights to Kraft Canada Inc. was to mount the very attack upon [Euro-Excellence] which is currently before this Court (Kraft Canada Inc. c. Euro Excellence Inc., [2004] 4 F.C.R. 410, 2004 FC 652, at para. 44 (emphasis added)).⁷
(emphasis is by Justice Fish)

Justice Fish added “Without so deciding, I express grave doubt whether the law governing the protection of intellectual property rights in Canada can be transformed in this way into an instrument of trade control not contemplated by the *Copyright Act*.”

Thus, four Justices agreed on the main issues concerning hypothetical primary infringement and

⁴ *Kraft Canada Inc. v. Euro Excellence Inc.* 2005 FCA 427.

⁵ *Euro-Excellence Inc. v. Kraft Canada Inc.*, 2007 SCC 37.

⁶ or “hypothetical infringer”, in the Court’s words

⁷ 2007 SCC 37 at para. 55.

the construction of the statutory provisions relating to exclusive licensees.⁸

Three other Justices concurred in the result,⁹ in an opinion written by Bastarache, J. They disagreed with Rothstein, J.'s position on the hypothetical maker analysis and the inability of an exclusive licensee to sue its licensor (and thus third parties) for copyright infringement. These three Justices, however, found there to be no infringement on the basis that the “merely incidental presence of the copyrighted works on the wrappers of the chocolate bars does not bring the chocolate bars within the protections offered by the *Copyright Act*.”¹⁰ Justice Bastarache suggests¹¹ that using the copyright in a logo on a package of a product not protected by copyright goes beyond the “legitimate economic interests” meant to be protected by the *Copyright Act*. Justice Bastarache also noted the existence of the doctrine of “*abus de droit*” and “copyright misuse”,¹² but left these issues for another day.

Justice Abella (with Chief Justice McLachlin concurring) dissented on the basis that the language of the Act caught the transaction in question, that an exclusive licensee could avail itself of the legislation and that the Court should not create an exception to the legislation based upon incidental use.

Rothstein, J., along with his concurring colleagues, disagreed with Bastarache, J. with respect to the concepts of incidental use and “legitimate economic interests.”

COMMENT

The key to the judgment by Rothstein, J. and his concurring colleagues is the hypothetical maker requirement that arises in commonwealth copyright regimes (such as Canada's) that derive from the 1911 UK copyright statute. The 1911 UK *Copyright Act* and its descendants, such as Canada's, created the possibility of secondary infringement for importation of copies legitimately made abroad that would have infringed copyright if, hypothetically, they had been made in the country into which they are imported, i.e. if they had been made in Canada in this instance.

It is important to understand that the application judge¹³ was heavily influenced by an Australian

⁸ 2007 SCC 37 para. 50.

⁹ Bastarache J. (LeBel and Charron JJ. concurring).

¹⁰ 2007 SCC 37 para. 57.

¹¹ 2007 SCC 37 para. 85. He states: *In particular, if a work of skill and judgment (such as a logo) is attached to some other consumer good (such as a chocolate bar), the economic gains associated with the sale of the consumer good must not be mistakenly viewed as the legitimate economic interests of the copyright holder of the logo that are protected by the law of copyright.*

¹² 2007 SCC 37 para. 97-98.

¹³ This matter was brought as an “application”, which is an unusual and truncated procedure based upon affidavit evidence and the rules and procedure designed for judicial review. Euro-Excellence tried unsuccessfully to have the application

decision¹⁴ that he found to be “persuasive.”¹⁵ This was unfortunate because that decision was based upon a statute that differed in fundamentally material respects from the applicable Canadian law. The Australian case was based upon the “hypothetical maker” of the imported product being the importer under the Australian statute, which will catch virtually all parallel importers. Thus, the Australian decision was, at best, irrelevant. On the other hand, the Canadian law deems the “hypothetical maker” to be the “actual maker” – in this case, the two European Kraft companies in Belgium and Switzerland. The 1997 amendments merely confirmed prior Canadian case law as set forth in the landmark 1960 *Clarke, Irwin*¹⁶ decision of Justice Spence of the Ontario High Court, as he then was.

The reasons of Rothstein, J. and his three concurring colleagues can be seen as carefully construing the statute as they found it. In fact, Rothstein, J. expressly points out it is for Parliament to rewrite the law, if Parliament wishes: “If Parliament decides that this result is problematic, it can amend the *Copyright Act*. In the meantime, this Court must apply the Act that Parliament has given us.”¹⁷

While there are some interesting splits and there is no clear majority within the SCC on some very important issues here, the result is that 7 of the 9 Justices ruled against Kraft’s “strategy” of using copyright in packaging elements to block parallel imports in the circumstances of this case. The splits within the Court quickly caused several observers to suggest that a strategy based upon an outright assignment (rather than an exclusive license) might succeed. Indeed, Kraft itself was quick to note this possibility in the media on the same day as the decision.¹⁸

However, simply changing or creating paperwork and calling the resulting document an assignment rather than an exclusive license may not necessarily avail a potential plaintiff seeking to get around the result of the SCC’s judgment. This is for several reasons.

For starters, if the assignment is a true assignment, there could also be tax and corporate law issues. In any event, there could be serious issues as to whether any particular assignment is an actual “assignment” for relevant purposes under the *Copyright Act*. Such issues could arise not only by virtue of the construction of the alleged assignment but the circumstances and context in which it is allegedly made. In some circumstances, it could conceivably be a complete sham.

converted to an action, which would have enabled full discovery and *viva voce* evidence, and presumably a much fuller and more adequate record, considering the issues at stake. *Kraft Canada Inc. et al. v. Euro Excellence Inc.* 25 C.P.R. (4th) 224.

¹⁴ *Bailey & Co. Ltd v Boccaccio Pty Ltd.*, (1986) 84 FLR 232.

¹⁵ 2007 SCC 37 para. 66.

¹⁶ *Clarke, Irwin & Co. Ltd. v. C. Cole & Co. Ltd.*, (1960) 33 C.P.R. 173 at p. 179-180

¹⁷ 2007 SCC 37, para. 50.

¹⁸ <http://www.bloomberg.com/apps/news?pid=20601082&sid=aWoawFLpz8Kc&refer=canada>

Now, with this judgment, there is also the strong possibility that a future defendant will raise the doctrines of copyright abuse or misuse, if the circumstances so warrant. There is nothing in the judgment to suggest that all nine Justices would not be open to arguments on the abuse and misuse doctrines. The latter, in particular, figured prominently in questions from the bench. It is clearly now on the Court's radar screen. Likewise, any non-arms length assignment, particularly one based upon nominal consideration, could be viewed with great scepticism if its real purpose is essentially that of achieving market segmentation with respect to goods not themselves protected by copyright.

Finally, anyone who believes that the next decision of the SCC, if this issue gets revisited, or even of a lower court can be predicted on the basis of the arithmetic of this SCC decision¹⁹ could be very surprised. The Supreme Court works in mysterious ways, but we do know that simple arithmetic is not one of its main guiding principles. In any event, even the arithmetic is not that simple in this instance, as a close reading and rereading will reveal. For example, the conclusions about exclusive licenses reached by Bastarache, J. and his two colleagues were arguably *obiter dicta* in their reasoning because they allowed the appeal on another basis, i.e. that their conclusions on incidental use rendered s. 27(2) inapplicable in this instance.

What's Next?

The decision does, admittedly, reflect an unusual degree of disagreement by recent standards in Canada's highest court.²⁰ However, this is not altogether surprising, given the importance and complexity of the issues. Sir Hugh Laddie describes the question of when a parallel import is an infringing copy as "one of the most difficult topics in copyright law."²¹ Accordingly, the decision is not "fractured" as Professor Scassa suggests,²² but merely reflects the inherent difficulties of the subject matter. These difficulties were no doubt exacerbated by the fact that the SCC was presented with a less than ample factual record resulting, presumably in part at least, from the treatment of this proceeding as an application and not as an action in the Courts below. The Courts below were also given irrelevant case law and not presented with all of the necessary and useful law and arguments that eventually were provided in the SCC.

What is entirely clear, however, is that seven of the nine Justices, for their various reasons, ruled against Kraft's "strategy" of using copyright law to "thwart" the parallel importation of chocolate bars. Some of these justices laid down explicit hints for even further reasons why a similar case might fail in the future.

¹⁹ G. Bloom, S. Burshstein, et al, *Canadian Copyright, Design and Related Jurisprudence* - 2007, LSUC *Intellectuals Property Annual Year in Review*, January 17 and 18, 2008. Tab 2 §23.1.

²⁰ Far more serious disagreements took place not so long ago, where it was sometimes not entirely clear even who won and who lost.

²¹ Sir Hugh Laddie et al, *The Modern Law of Copyright and Designs*, Third Edition, London, 2000, §32.27, p. 1545.

²² See Prof. Teresa Scassa, *Are Intellectual Property Rights Out of Control?* LSUC Year in Review, January 18, 2008.

In the aftermath of the SCC decision, at least two lawsuits have been launched by the same law firm that unsuccessfully represented Kraft in the SCC. One is a rematch against Euro-Excellence²³ itself, as Kraft promised in its media statement. Another involves Cuban cigars.²⁴ Both involve purported assignments rather than exclusive licenses and both are at very early stages and are being contested. Both have been commenced as applications rather than actions, an unusual tactic for matters of potentially great complexity potentially requiring a great deal of *viva voce* evidence.

The doors have now been opened to new issues such as copyright abuse or misuse, or the argument that copyright law cannot be used to limit free trade in articles not protected by copyright. Other arguments are also open. Current and future potential plaintiffs contemplating the use of copyright law to bar parallel imports of consumer products not protected by copyright may wish to be careful about what they wish for.

Legislative Intervention?

While some may wish for legislative intervention that would provide further clarification and more certainty, it seems unlikely that this will happen soon, given that the overall outcome in the SCC is consistent with the law as it had been generally understood prior to the decisions below. Any such amendment would be very complex and controversial, as the Australian experience shows,²⁵ and hopefully unnecessary in Canada given the difference between our statute and the Australian statute with respect to the “hypothetical maker” requirement. However, had the SCC gone the other way, there would have been intense pressure for immediate legislation to restore free trade in articles not themselves protected by copyright. Moreover, if lower courts are somehow persuaded to come to a different overall result than the one reached by the SCC, one can certainly expect pressure for an immediate amendment to restore the *status quo ante* of free trade and competition in the Canadian marketplace, unimpeded by assertions of copyright in mere elements of packaging material.

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²³ Federal Court of Canada T-2103-07.

²⁴ Federal Court of Canada T-1926-07.

²⁵ Australia eventually amended its legislation 12 years later to undo the result in ***Bailey v. Boccaccio***.