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# LEGAL BOUNDARIES OF INTELLECTUAL PROPERTY COMMERCIALIZATION IN THE EUROPEAN INTERNAL MARKET

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**NYILATKOZAT**

Alulírott, _____**Osman Buğra Beydoğan**_____ (név), büntetőjogi felelősségem tudatában kijelentem, hogy a Debreceni Egyetem Marton Géza Állam- és Jogtudományi Doktori Iskolában a doktori fokozat megszerzése céljából benyújtott, __**Legal Boundaries of Intellectual Property Commercialization in The European Internal Market**___ című értekezésem saját önálló munkám, a benne található, másoktól származó gondolatok és adatok eredeti lelőhelyét a hivatkozásokban (lábjegyzetekben), az irodalomjegyzékben, illetve a felhasznált források között hiánytalanul feltüntettem.

Kijelentem, hogy a benyújtott értekezéssel azonos tartalmú értekezést más egyetemen nem nyújtottam be tudományos fokozat megszerzése céljából.

Tudomásul veszem, hogy amennyiben részben vagy egészben sajátomként mutatom be más szellemi alkotását, vagy az értekezésben hamis, esetleg hamisított adatokat használok, és ezzel a doktori ügyben eljáró testületet vagy személyt megtévesztem vagy tévedésben tartom, a megítélt doktori fokozat visszavonható, a jogerős visszavonó határozatot az egyetem nyilvánosságra hozza.

Debrecen, 10.05.2021

aláírás

**SUPERVISOR'S OPINION**

**on Mr. Osman Bugra Beydogan's dissertation to be submitted for final defense**

*Debrecen, 10 May 2021*

Mr. Osman Bugra Beydogan dissertation focuses on questions and challenges of Intellectual Property Rights (IPR) commercialization in the EU Internal Market. The protection of intellectual property rights and their trade-related aspects are among the most contested issues in international trade negotiations and also a key issue from the point of view of EU economic law. The importance of the research topic is thus undeniable, both in the international context and from a European perspective.

The underlying research problem, which is analysed by Bugra's dissertation in several dimensions, arises from the tension between the (political and economic) interests of ensuring the proper functioning of the EU internal market (free trade and undistorted competition) on the one hand and those of maintaining intellectual property rights on the other. The work itself is based on the hypothesis that the establishment of an EU IPR regime is not initiated by a 'classic' IP law interest but rather determined by market-oriented policy goals, in particular by the efforts to complete the Internal Market.

On the basis of this conception, a detailed analysis is devoted to the conceptual framework itself, in particular aiming at explaining the term "intellectual property" as a specific subject to trade relations in market economies, and exploring the *sui generis* characteristics of intellectual property rights as compared to classic property rights. Such a conceptual foundation serves as a theoretical framework for the further parts of the thesis, exploring the nature and challenges of the conflict between IP rights and the fundamental principles of the internal market in light of the exhaustion doctrine, as well as in particular areas like copyright, trademark and related rules of EU competition law. The key findings are strongly built on the analysis of the relevant jurisprudence of the Court of Justice of the European Union which was essential in developing legal doctrines in seeking the balance between the two conflicting interests, and also contributed to the evolution of the normative legal framework for the protection of IP rights at the EU level.

The final conclusions of the dissertation are well-founded and are based on a creative and individual approach of the author towards the research topic, which characterized the whole analysis, starting from building up the conceptual and theoretical framework.

All in all, Bugra's work is convincing about his ability to identify the main research problems of the examined topic, to carry out in-depth research and to communicate the research result to the scientific community at a very professional level. The individual and complex approach of the research theme proves the novelty of the present work. As the supervisor of the research, I certainly support the acceptance of the dissertation for the final defense.

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## Contents

# INTRODUCTION

*i) Aim and Scope*

This dissertation explores from a legal perspective the notion of intellectual property commercialization in the EU, vis-à-vis the dynamics of the European Internal Market. The said market is identified by the primary legal sources of the Union as a *"highly competitive social market economy"*, envisaging an area "*without internal frontiers in which the free movement of goods, persons, services and capital is ensured".* The two pillars, i.e. free movement and undistorted competition, comprise a setting that almost intrinsically contradict the quiddity of IP rights which are cyclically exclusive-exclusionary-monopolistic and by, default, territorial. While this conceptually frames the tension between the Internal Market and national IP rights; reconciliation thereof is central to the European integration insofar as the Internal Market represents the very ground of the integration as such.

Both territorial and exclusive-exclusionary quiddities of IPRs, individually and cumulatively engender detrimental results to cross-border trade and undistorted competition, hence at very least potentially contradicting the very essence of the Internal Market. The author thus argues that these detrimental results transpire from what this study identifies as intellectual property commercialization. Along the same lines, the creation of a European Intellectual Property regime above the national ones has been necessitated by what this study conceptualizes as intellectual property commercialization and in which continuum the general interest is often preferred to that of IP right holder. To that end, the author argues, what emerges from this equilibrium is the law of policy, particularly that of integration as a single borderless market, instead of a classic law of intellectual property. And the latter concept is of dynamic nature interrelated to the advancements and progress in technology and creative industries resulting not only in novel types of subject matter but also in novel ways of commercializing thereof. Correspondingly, the understanding of IP commercialization under the principles of the Internal Market is not only of historical interest but it is also of present and future value. This is particularly because defining the legal limits of intellectual property commercialization is hinged upon a sustainable balance between IP protection, free movement and competition rules; therefore, as far as the integration is at the stake, that balance proves to be an ongoing task which is as essential in the present at least as it was in the past. Moreover 'commercialization' terminologically deserves a particular attention in the context of intellectual property and free movement insofar as the regional exhaustion model (Community exhaustion) -now being the settled mechanism of reconciling the interest of IP protection and

that of free movement- finds its aim at liberating "further commercialization" of the corporeal goods from the territorial trait of IP rights. However the fact remains that the semantic range of commerce, thus that of commercialization, covers a greater area than mere trade of goods, albeit without a clear cut contextual definition. The dissertation therefore explores this archaic clash with the postulate that conflict as such emerges not from the statics of IPRs but from commercialization thereof. Having assumed an understanding of intellectual property commercialization greater than mere trade in corporeal goods, the author sets about defining limits of IPR holder's right to commercialize the intellectual property in the European Internal Market, contending that the limits as such are collectively drawn by the free movement principle and competition rules of the Union.

In selection of this particular scope, there appear several points that attracted the author's interest and that also represent the merits of the underlying analysis. These might be summarized as follows: (i) Construction of European IP law, rather than being a part of the original agenda of the European integration,[1] was a result of the necessity compelled by the practical reverberations of the national rights on the intra-Union trade and, by extension, on the achievement and sustainment of the integration which aims to fuse the national territories into one single market.[2] These reverberations, ensue from what can be conceptualized as IP commercialization. Correspondingly, the EU law and *acquis* on intellectual property that we can speak of today has emerged from, shaped by and, in the future, will likely follow the pattern dictated by the reconciliation of this practical clash. (ii) That reconciliation, which we believe is an ongoing process much like the European integration itself on the axis of functioning of the Internal market, is realized through (or resulted in) divergence from the classic dogmatic methods of intellectual property laws. This, while representing the Europeanization element of intellectual property laws, ensued not on the axis of legal theory but rather motivated by policy. (iii) Purposive solutions that has been centered around the jurisprudence of the Europe judiciary that has been enhanced towards legal certainty and a balanced approach instead of an absolute free movement fanaticism.

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[1] Roger J. Goebel, *The Interplay Between Intellectual Property Rights and Free Movement of Goods in the European Community*, 4 Fordham Intell. Prop. Media & Ent. L.J. 125, 126 (1993); PÉTER MEZEI, COPYRIGHT EXHAUSTION LAW AND POLICY IN THE UNITED STATES AND THE EUROPEAN UNION 24 (Cambridge University Press 2018); PAUL TORREMANS, HOLYOAK AND TORREMANS INTELLECTUAL PROPERTY LAW 123 (Oxford University Press 2019)

[2] Stefan Enchelmaier, *Intellectual Property, The Internal Market and Competition Law* (In JOSEF, DREXL ED., RESEARCH HANDBOOK ON INTELLECTUAL PROPERTY AND COMPETITION LAW 405, Edward Elgar Publishing 2008)

*ii) Notes on Methodology*

On account of methodology, we have approached the particular matters, including the very essence -the fundamental clash- underlying the peculiarity of the EU IP law which emerged from what we conceptualized as IP commercialization, from a historical perspective and built up to the present state of affairs. This shall involve a legal analysis of the primary law of the Union insofar as it conceptualizes the foundations and functioning of the Internal Market, the free movement principle and the competition rules; and that of the secondary substantive law of the Union on intellectual property. It is however crucial to note that the jurisprudence of the European Court of Justice (hereinafter ECJ, Court of Justice or the Court) and the General Court has functioned as a bridge and middleman between the primary law and secondary law in this particular field. Generally speaking, on the axis of broad provisions of the primary law, doctrinal and interpretative accumulation actually transpired from the case law and were subsequently codified into the secondary law, prime example being the Community exhaustion. Furthermore, it is that jurisprudence that provides the brief concepts of primary and secondary law with their actual and extensive context, so much so that, up until recent, a number of important areas on intellectual property law have been almost exclusively governed by this jurisprudence at the Union level.[3] To that end, the jurisprudence in this field is as crucial, at least, as the substantive law. Along the same lines, as a general formative statement of this dissertation, we purport that the European IP law that we can speak of today has been created by means of case law which almost exclusively emerged from the practical clash of the principles of internal market and intellectual property rights which, in turn, collectively defined the limits of IP commercialization from a legal perspective. It is this very background that contains the reason why this dissertation has undertaken the case study as the most significant instrument of the intended exploration. It needs to be noted that the extensive set of case law we utilized throughout the dissertation is not approached in a summative manner, instead, each case is brought under individual legal analysis which sequentially accumulated into a collective and holistic scrutiny such as to represent the constituents of the particular legal phenomenon we set about analyzing. It is equally important to note that, given the highly economic and policy-centric nature of the domain the study concerns, the legal analysis as such cannot strictly be confined to the premises of law and jurisprudence. Therefore, these legal analyses shall also ponder upon the expression and realization of policy and

[3] For example, Union-wide exhaustion of patens was not codified up until Unitary Patent Regulation (1257/2012) which has not yet come into force by the time this study was completed.

economic intents through legal instruments and through the interpretation thereof; the prospect which complements our hypothesis that the EU IP law above that of the Member States is not created through an IP law interest but rather compelled by the necessities for effectuating the policy goals, the most significant one of which is the Internal Market. In order to expose this landscape not only in specific and extreme interest areas but also in a holistic sense that comprises the entire IP protection – Internal Market equilibrium, we have paid particular attention to the selection of case law. Instead of resorting to an extreme exemplification of the jurisprudence, we made this selection to the most holistic extent possible; that way, we were able to engage in particular discussions while capturing, in a greater detail, the general motives of the law and practice in the respective fields.

On many occasions, as far as falls relevant to the foundations of our subjects of analysis, we also revisited and comprehended the teleology and objective behind the bodies of law from a universal perspective and we, in turn, evaluated the particular reverberations and significance of these general prospects in respect to the Internal Market, in consideration of the peculiar dynamics of the latter. To that end the study exhibits occasional transitions from a pure legal doctrinal comprehension to a legal-economic one which is flagrantly necessitated by the understanding of intellectual property in the Internal Market. On a final note, it is important to highlight that the dissertation may be typified as an exploratory study in the light of its general objective, that is the exploration of the legal notion of intellectual property commercialization in the European Internal Market.

*iii) Underlying Concepts*

The Internal Market denotes one grand and denationalized area in respect *inter alia* to commerce of which intellectual property is the major part.[4], while sub-elements of that multinational unit remain to be sovereign nations: the Member States. Free movement (four freedoms) are defining element of that market and are of constitutional importance. It goes without saying, the creation of such a market (Common Market and later Internal Market) and sustainment thereof, at the outset, is the foundational aim of the Union[5] and represents the mold of the entire European integration. That mold is held together by the free movement principle and undistorted competition environment. Consequently, free movement principle on the one

[4] See the discussion on the 1st chapter purporting that intellectual property is practically almost a pure commercial matter

[5] See: Art. 2 of the Treaty of Rome and Art. 3(3) TEU

hand and undistorted competition on the other hand appear as the integrating factor in the EU and are ongoing tasks of the European project: the values that need to be protected at all costs.

Much like the characteristics of the Internal Market, intellectual property rights -a notion dating back at least to the 15th century[6]- might likewise be expressed in two factors. IPRs in the broadest sense connote *exclusive* and *territorial* legal rights associated with creative effort or commercial reputation;[7] moreover, notwithstanding the underlying philosophy, the rights are, at least, quasi-proprietary in nature.[8] Besides the individual interest of those who are in possession of intellectual property rights, the states granting the rights do have particularly interest in granting those which can be identified as intellectual property theory and which normally is liable to vary from one state to another.

*By status* territorial nature of the rights reverberates on the underlying intellectual property *by effect*. This denotes physical or otherwise counterparts (the corporeal goods or services) of the intellectual property being subject to discretion of the right holder within the national boundaries where the associated IP rights are protected. This *inter alia* includes the exclusive rights to incorporate the underlying intellectual property into goods and services, exclusive right to sell, import and export such goods or provide such services which are recognized and exercisable along the national borderlines. To that end, national rights deploy territorial restrictions such as to impede what a free trade regime objectifies; furthermore, the former relies on proprietary rights in doing so.

Against this background sacrifices are inevitably to be made in order to reconcile the two poles apart: the interest of the IPR holder -the subjective interest- and that of free trade embodying free movement -the objective interest-. If sacrifice is made from the latter, the market integration is endangered; if, however, IP protection were to be compromised, the right to property comes into question. Between these two extremes, the reasonable -yet difficult-

[6] For a detailed account of origin of IPRs, see: Frank D. Prager, *A History of Intellectual Property from 1545 to 1787*, 26 J. Pat. Off. Soc'y 711 (1944)

[7] DAVID BAINBRIDGE, RESEARCH HANDBOOK ON INTELLECTUAL PROPERTY AND COMPETITION LAW 3 (Pearson Education 8th ed. 2010)

[8] From the perspective of fundamental rights, the protection afforded to intellectual properties is likened to classical property rights. In that respect the European Charter of Fundamental Rights (Art. 17) reads:

> "1. Everyone has the right to own, use, dispose of and bequeath his or her lawfully acquired possessions. No one may be deprived of his or her possessions, except in the public interest and in the cases and under the conditions provided for by law, subject to fair compensation being paid in good time for their loss. The use of property may be regulated by law in so far as is necessary for the general interest.
>
> 2. Intellectual property shall be protected."

task is to fine-tune the two interests such as to destroy neither the internal market nor the intellectual property rights of those who trade on that market.[9] Yet the primary law of the Union offered very little substantive material to the help of reconciliation of this tension.

Free movement of goods is realized*, inter alia,* by prohibiting the quantitative restrictions on imports and exports and measures having equivalent effect.[10] A derogation from the latter provision has been enabled on grounds of public morality, public policy or public security; the protection of health and life of humans, animals or plants; the protection of national treasures possessing artistic, historic or archaeological value; or *the protection of industrial and commercial property*.[11] However this is subject to the express proviso that such a derogation shall not constitute a means of arbitrary discrimination or a disguised restriction on trade between Member States.[12] Surrounding this framework, there exists the provision of the Treaty ensuring non-interference with the systems of property ownership in the Member States.[13] It has fallen to the European judiciary to make the best of these limited legal bases in striking such a balance, compelling it to become interpretative and inventive. It is a little doubt the foremost invention of the European judiciary is the creation of a regional exhaustion model which represents the medium of the said reconciliation to the present. However, as the old saying goes, *"Rome wasn`t built in a day"*; the Community exhaustion was achieved gradually with the leverage of the earlier doctrines of existence/exercise of the rights and specific subject matter. With the former, the Court drew a rather abstract distinction between the existence of the national IP rights and their exercise in order to go around the Treaty provision (Art. 345 TFEU) ensuring the property ownership so that it would have an ample maneuver room in restricting the exercise of IP rights. Accordingly, the derogation from free movement on the grounds of 'protection of industrial and commercial property' is confined to existence of the rights, while their exercise might be restricted as far as Treaty provisions on free movement and competition so requires. Devoid of any limitation to restrictions as such, the question inevitably arose as to the extent to which the exercise can be limited before the IP rights cease to exist. The Court subsequently devised the notion of specific subject matter whereby it created the core area of IP prerogatives whose exercise is not to be restricted by the Union law:

[9] DAVID T. KEELING, INTELLECTUAL PROPERTY RIGHTS IN EU LAW: FREE MOVEMENT AND COMPETITION LAW 3 (Courier Corporation 2003) The two other pillars of ensuring free movement of goods, i.e. prohibition of custom duties and charges having equivalent effect, as well as prohibition of discriminative taxation are less relevant in the context of the present analysis.
[10] Article 34 and 35 TFEU
[11] Id. Art. 36 (emphasis added)
[12] Id.
[13] Id. para. 345

an area whose exercise is linked to the existence of the rights which was in turn utilized in determining the limits of exhaustion. However, this timeline infers a gradual departure from legal uncertainty, the fact remains that the early doctrines were utilized purposively by the Court which engaged in interpreting from a policy-based perspective instead of a classic IP law perspective.[14] The purpose, as noted by many scholars, appeared to be to consistently favor the interest of free movement to the largest possible extent, interpreting the derogations rather strictly.[15]

It goes without saying the most definitive, and also utopian[16], way of reconciling this contrast would reside at the removal of the territorial trait of intellectual property rights for once and forever. And it is true that solid attempts were put towards that direction: i) territorial quiddity, to the extent that it affects the trade between the Member States, is for the most part wrecked down by the Community exhaustion; ii) harmonization of national laws circumvented some of the issues arising from the discrepancies of the national laws such as in the case of the duration of copyright protection; iii) creation of Union wide IPRs also significantly expansive.[17] Therefore territoriality, one might conceive, is not of much of an issue as it once was. This observation would be only partially true firstly because the unitary intellectual property rights are not necessarily exclusive modality of protection thus national right continue existing with all their territoriality; secondly the coping mechanism, i.e. Community exhaustion, is a brief formula (putting on the market + by or with consent of the right holder + in the Union) whose context has been discovered for several decades but has yet to be discovered in relation to all realities of the commerce in the internal market. Moreover, the interest of the right holder in protecting various aspects of the underlying intellectual property does not necessarily holistically exhaust after initial sale. This is of particular relevance to trademarks essentially protecting *inter alia* the reputation and goodwill built around the mark and conveying the commercial origin of the goods. Though it is reasonable to conceive that

[14] ANNETTE KUR ET. AL., EUROPEAN INTELLECTUAL PROPERTY LAW: TEXT, CASES AND MATERIALS 459 (Edward Elgar Publishing 2019)

[15] Guido Westkamp, *Intellectual Property, Competition Rules, and the Emerging Internal Market: Some Thoughts on the European Exhaustion Doctrine*, 11 Marq. Intell. Prop. L. Rev. 291, 293 (2007); Jarrod Tudor, *Intellectual Property, the Free Movement of Goods and Trade Restraint in the European Union*, 6 J. Bus. Entrepreneurship & L. Iss. 1, 99 (2012); Goebel, *supra* note 1, at 127; This is also spelled out in the Court`s jurisprudence, see: C-46/76 Bauhuis v The Netherlands, para. 12

[16] David Keeling, *Intellectual property rights and the free movement of goods in the European union,* 20 Brook. J. Int'l L. 127, 129 (1993)

[17] Intellectual property rights with unitary effect in the EU include design rights (Regulation 6/2002 on Community design), trademarks (Regulation 2017/1001 on the European Union trade mark), plant variety rights (Regulation 2100/94 on Community plant variety rights) and still-anticipated Unitary patent (Regulation 1257/2012 implementing enhanced cooperation in the area of the creation of unitary patent protection)

such interests should be protected even after the initial sales, the possibility of so doing is hinged upon the existence of 'legitimate interest' to oppose further commercialization[18]; an elusive concept that needs to be provided with an actual and dynamic content. These accounts also, all together, represent the ongoing relevance of a query to discover the limits of IP commercialization with reference to free movement principle.

Above considerations relate to intrinsic contrast of intellectual property and free movement and in most cases transpire on the axis of what has been offered (or put on the market) under intellectual property rights. Moreover, a certain degree of anticompetitive effect comes intrinsic to IP rights.[19] And this practically appears as an impediment to what can be offered under that intellectual property right. Such effect is not effectively mitigated by the theoretical and deontological pro-competitive objectives ascribed to IP protection. Although it is true that competitive advantage is rooted in the very objective of intellectual property right; the degree to which this effect is justifiable with a view to the competition rules describing the internal market model is humbler than the degree that IP protection is capable to produce. Relying on independency of national rights (bundle theory) different configurations of assignments or licenses may be used as a method of market sharing such as to affect the intra-Union trade. Secondly, they may erect barriers to entry and create market power when there are no close substitutes on the demand or supply side of the market.[20]

Consequently, these rough outlines sufficiently exhibit the essence of the problem: intellectual property rights, mostly owed to territorial quiddity, is liable to clash both characteristics of the internal market, sometimes simultaneously.

*iv) Structure of the Analysis*

Firstly, and as a preliminary matter, the dissertation explores the notion of intellectual property commercialization from a general legal perspective, with the acknowledgment of the vast continuum of 'commercialization' whose outer lines are in continuous evolution and in which realm not necessarily every stage exhibits a legal matter for the purposes of intellectual property law. From a contextual perspective, we purport, the legal account of intellectual property commercialization is to be mapped out in two layers manifesting three general modalities. The first layer shall concern commercialization of goods and services which

[18] Trademark Dir. Art. 15(2) [formerly Dir. 89/104 Art. 7(2)]
[19] Pro-competitive effects thereof, however is discussed in the relevant chapter below.
[20] VALENTINE KORAH, INTELLECTUAL PROPERTY RIGHTS AND THE EC COMPETITION RULES 1 (Bloomsbury Publishing, 2006)

incorporate the underlying intellectual creations, to which we shall continue referring as corporeal goods and services.[21] Second layer shall center around commercialization of intellectual property rights (IPRs) *per se* as a quasi-proprietary legal identity in relation to which protection and the possibility of enforcement are afforded by the law. The latter layer is premised upon the 'property object' dimension and the concordant transactional function of intellectual property rights. From the inner periphery transactional function denotes the right of disposition and of determining the use of IPRs as well as promissory transactions. Correspondingly, commercialization of the rights as such is represented by intellectual property licensing and assignment on the one hand, and by their collateralization and instatement as capital share to commercial companies.

We shall consequently purport that intellectual property commercialization neither in a general sense nor in a legal sense is confined to squeezing money out of intellectual creations. Nor is the legal notion of commercialization is confined to IP-related transactions; quite the contrary IP-based commercial behavior might just as well land on the legal realm. This is particularly apparent on the face of competition laws.

On the second chapter, we shall lay the background to the problem in a greater detail. Initially the territoriality principle apprehended from a historical perspective drawing on the non-statutory nature of the exclusivities which appeared as a reward or courtesy from the sovereign to the innovators; correspondingly the validity of those exclusivities be limited to the area of sovereignty. Secondly, we shall follow the traces of territoriality towards the recent times, enfolding the reasons why the IPRs are bound to remain territorial. This is followed by an outline of the other characteristic feature of the IPRs, namely the exclusivity, thus exhibiting while *territoriality* is the defining element of the legal identity afforded to the IPRs, *exclusivity* depicts the contextual or functional nature thereof. It shall be exhibited that the grand total of these two characteristics practically tends to isolate the national markets to the detriment of international trade, thus relating directly to the commercialization of incorporeal goods, most visibly in the context of parallel trade activities. On that note we shall identify the particular challenge, posed by the obvious tension between the territorial exclusivities and free trade, in the Internal Market vis-à-vis the free movement principle; the tension we shall address as the conflict in nature.

[21] The term "corporeal goods" is used, with reference to the goods incorporating IPRs, by: Abdulqawi A. Yusuf & Andres Moncayo von Hase, *Intellectual Property Protection and International Trade - Exhaustion of Rights Revisited*, 16 World Competition 115 (1992)

In the ensuing chapter we shall analyze the initial doctrines that the European Court of Justice devised in order to reconcile that conflict in nature. The early doctrines, namely existence/exercise of rights and the doctrine of specific subject matter, are important at least on three ends: (i) They have been a footstone to the creation of a regional exhaustion model; (ii) They are clear demonstration of the policy-based development that characterizes the IP law of the Union; enfolding, in particular, that the IPRs are not apprehended with a pure IP law interest -in fact it can be said that hardly any IP law interest was initially involved- but they were rather re-constructed for the interest of the particular market model through a plainly interpretative approach. Not surprisingly, it is noted that *"Intellectual property lawyers often deem the jurisprudence regarding the interface of intellectual property and the principle of free movement of goods as an unswerving interpretation of the proprietary scope of territorial intellectual property rights"*[22] (iii) Specific subject matter continues to be a reference point in determining the limits of exhaustion as well as, in general, that of the derogations from free movement under Art. 36 TFEU.

In the fourth chapter the principle of exhaustion is extensively analyzed to the effect that it represents the main instrument of managing the identified conflict in nature as well as the element of Europeanization of IP law. We shall firstly embark on a conceptual approach towards the general premises of exhaustion principle, exposing the function thereof in liberalizing the subsequent commercialization of corporeal goods following the initial sales by the right holder. This shall be followed by the formulation of the regional exhaustion modality as follows from the jurisprudence of the Court. We shall in turn fragmentally explicate the elements, i.e. putting on the market, consent, and the geographical scope, that effectuate the exhaustion. In that, various settings, such as licensing and assignment, whereunder the goods are marketed and their interfaces with exhaustion shall be scrutinized in the light of different relationships that may exist (or be absent) between the right holder and the entities that engage in actual commercialization. Of particular importance to this realm, we shall focus *inter alia* on marketing under compulsory licenses, voluntary and involuntary assignments and marketing in breach of licensing agreements.

These general accounts are followed, in the ensuing chapters, by specific considerations for (i) Copyright (Chapter 5) with regards to inexhaustible prerogatives such as rental and lending rights, rights in performances and in communication of the work to the public, which

[22] Westkamp, *supra* note 15, at 293

denote unique ways of commercialization of certain type of copyright protected work without depending on distribution of a physical subject. In that, a particular emphasis shall be put on the -possibility- of exhaustion of rights in digital realm, a trending topic of the present decade; (ii) Trademarks (Chapters 6 and 7) in relation respectively to the exhaustion in case of repackaging of trademarked products and the use of other`s trademark for advertising in relation to the further commercialization of the products and to other related commercial activities. The discussions in respective sections prove a distinct importance on several ends. Firstly, they reveal the expansion of the scope of exhaustion beyond the exclusive distribution right such as to cover, subject to certain conditions, the exclusive right to affix the mark and to use thereof in advertising. Secondly, the latter implies and re-affirms that the exhaustion principle is not confined simply to further trade but also covers certain aspect auxiliary to further trade, thus better identified as commercialization. Lastly, they surface certain benefits of the economic approach that been taken towards IPRs, particular example being the recent and enhanced recognition of the prestige (or aura of luxury) of the mark as a legitimate interest that deserves protection on the end of the right holder even after the initial sales.[23]

The final subject of analysis (Chapter 8) is devoted to the interface of the IP protection with the competition rules of the Union which we shall define as the external denominator of the legal boundaries of intellectual property commercialization in the Internal Market. We shall initially explicate the convergence of the two bodies of law on theoretical and deontological objectives and their divergence as regards practical and actual reverberations. We shall, in turn, go on to identify particulars of that divergence to the extent that it contradicts foundations of the Internal Market. This facade of the divergence, the dissertation proposes, is not circumvented by the exhaustion doctrine; in that, we shall identify interrelated but distinct demesnes over which the exhaustion principle on the one hand and competition rules on the other hand may have an impact. Accordingly, while the exhaustion ensures the market integrity in relation to what is offered under an IP right competition rule look out for the market integrity in relation to what can be offered and more. Subsequently, the general treatment of IPRs under the competition rules shall be discussed. Finally, a number of typified IP transactions and IP-based conducts were analyzed in relation to the competition rules. These include the selective distribution systems for the corporeal goods whereunder restrictions on online sales is particularly emphasized; the refusal to license an IP right *vis-à-vis* abuse of a dominant position

[23] To that effect see: Case C-59/08 Copad and Case C-230/16 and Coty Germany

followed by specific considerations for standard essential patents (SEPs); patent pooling arrangements and finally reverse payment settlements (pay-for-delay arrangements).

# CHAPTER 1

# FROM INTANGIBLES TO INTELLECTUAL PROPERTY

# DELINIATING IP COMMERCIALIZATION*

## 1. Introduction

The intellectual property realm is one of the central proximities where the law and economics are most entangled. In order create an IP law and practice and for interpretative undertakings in that context, the knowledge of multidisciplinary elements that form the overall characteristics of intellectual property is a prerequisite. In dealing with this prerequisite, we build upon the stance that the intangibles, unlike tangible capitals, are the essential and perpetual source of value in view of the fact that they are inexhaustible. Clearly however, not every intangible encapsulates the same intensity of value, in this way, the term "intangibles" in itself is too ambiguous to be a reference point in the making and operation of law and practice. Therefore, it is necessary to establish the position of intellectual property rights among intangibles. In this connection, we are going to emphasize that, besides other features, the major determinant that differentiates the intellectual property rights from the other sorts of knowledge assets is the legal identity that the former is provided with by the IP laws. Correspondingly, we argue that this identity is not quite reflective of a classical sense of proprietary rights despite being called so. It rather exhibits *sui generis* characteristics. In view of the value embedded in them and that of the property-right-like legal identity they are backed up with, IP rights not only enable the controlling of the dissemination of value, thus creating a competitive advantage, but they also form a sort of currency to the extent that they have transactional power. All considered, we purport IP rights are the subject of business and commerce but have very little to do with individuals, regardless of the fact that they are, in essence, created by individuals. This reveals, first, that in most instances intellectual properties are manufactured for commercial purposes, therefore they are purposively and intrinsically subjected to commerce. To that end, they are naturally and actively commercial. Secondly, even if not initially created for commercial purposes, the monopolistic and exclusionary effect of intellectual property rights confers certain commercial value, at least to the extent that it

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prevents the others from exploiting the underlying intellectual property (i.e. inventions, distinctive signs used in the course of commerce, designs, literary and artistic works and the like) for commercial purposes.

Having taken this wide array of economic and commercial connotations into the equation, we suggest IP rights encapsulate both static (potential) and kinetic (dynamic) commercial importance. Frankly however, not every step of the commercialization continuum is identified as, or results from a legal matter; even if it is a legal matter, it does not necessarily always fall in the domain of intellectual property law. The wide continuum of commercialization also entails pure business industrial aspects which do not clearly interest the focus area of IP laws. Equally clear, on the other hand, IP law is not the only legal disciple that finds itself in interaction with this wide continuum; for instance, while the economic effect created in that course might attract competition law, the legal instruments of commercialization comprise the subject matter of contract law. Consequently, the legal aspects of intellectual property commercialization tend to blend in with (or melt into) the broad definition of commercialization. With a view to this proposition, we shall try to set the scene for a legal doctrinal analysis by conceptualizing intellectual property commercialization. Having argued that intellectual property commercialization has to refer to more than just squeezing out some money from one`s ideas, we attempt to define the scope of intellectual property commercialization for the purposes of legal scrutiny and from a legal perspective, to which we tend to ascribe a two-layer meaning. To begin with, the economic potential of information assets and the particular gravity of intellectual property needs to be highlighted.

## 2. Intangibles as the Fundament of Value Creation

At the North end of the world where nature is not particularly generous in giving out to its inhabitants the building materials, igloos came to rescue of humankind and became the ultimate way of survival against blizzards and brutal winter conditions. As the snow blocks act like good insulators, the interior temperature could be kept at survivable level with body warmth only. Hence, igloos proved efficient in counteracting cold. Nevertheless, as the raw material of these shelters, namely snow, is fairly delicate and at the end of the day this makes the shelter quite fugacious especially when the temperature alterations towards positive occur. Further, the humidity created inside the shelter by the human respiration will form a thin layer of ice on the inner face of walls, as a result of which the whole insulation function will be impaired. In a nutshell, the life of the shelter, in the best scenario, is unlikely to exceed several

weeks. In the wake of such a prospect, it is probable that a question is aptly posed: whether an already-built igloo or the constructional knowledge as to the making of it is more valuable? In most instances, the answer would conceivably be the latter.

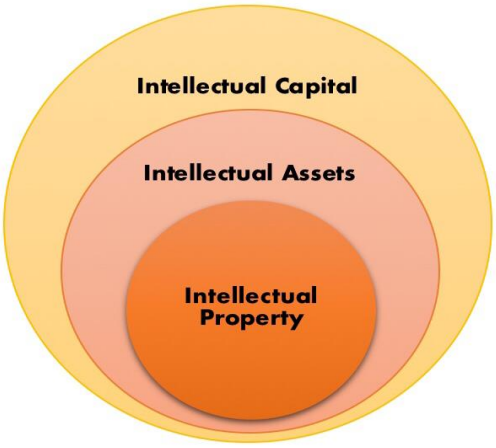
Regarding the value, the appearance of which in the above example is a snow house, there is the one-time value on one hand and a perpetual source of value on the other. This simple and rather primitive analogy is however viable in most cases where the value of intangibles and physical substance compete, especially at business level as we sought to discuss later.

With that being said, in an attempt to perceive the power of intangibles within the frame of value creation, pinning down true characteristics of the intangible in question likely be vital. To this end, an often-overlooked nuance between information and knowledge has primarily to be taken into consideration. *Information* pertains to facts provided or learned by something or someone mostly in the form of raw data, whereas *knowledge* features a subset of information and pertains to information and skills acquired with the help of education, experience, etc.[24] In a scrutiny of the power of intangibles and their evolution into intellectual properties, we believe, taking "knowledge assets" in a broader sense and "intellectual assets" in a relatively narrow sense as reference points, rather than "information assets", is plausible. This is mainly because intangibles, at least those which are eligible for intellectual property quality, are seldom in the form of raw information -the value of which is arguable-, but they are rather compounds of information, skills and experience. Moreover, the latter postulate is also consistent with the creation of literary and artistic works which has a lot to do with skills and experience.

However, given the advancements in information technologies, science and with the world immensely digitalized in various realms, the conception of intangibles *inter se* embodies more ambiguity than ever. With this being the case, the hierarchical connection between intellectual capital, intellectual asset and intellectual property should necessarily be demonstrated. Intellectual capital, among others, forms the broadest term including the knowledge, information as well as intangible factors of other sorts. As Poltorak & Lerner put it, intellectual capital is what an enterprise is left with after all of its tangible assets has been

[24] Ian Lurie, *Information is free. Knowledge is not*, PORTENT (5 Jan. 2021), https://www.portent.com/blog/random/information-is-free-knowledge-is-not.htm

stripped off.[25] Accordingly, the total sum of knowledge in an enterprise including those possessed by the employees and existing information, regardless of their value, will collectively constitute the intellectual capital of the entity in question. Intellectual assets, on the other hand, present a subset of intellectual capital factors that are identified, captured, and documented so that they are enabled for access.[26] In addition, it is necessary to note that the knowledge assets, of which we previously made mention, may more conveniently be deemed a part of intellectual assets insofar as they are cleared of trivial information and as they are subject to inter-organization sharing and transfer. In the same vein, knowledge assets could be adequately described as a set of knowledge that has a present or future value possessed by an individual enterprise.[27] Finally the narrowest and most valuable subset of this intangible chain consists of intellectual properties which also delineate our main domain of scrutiny. This category of intangibles differentiated from the broader sense of intellectual assets by the legal protection attributed to them under applicable laws.




Although intangibles of any hierarchical level are pertinent to value creation, thus greatly important to business, it is suggested that the aim concerning intangibles is often to convert them into a more valuable subsequent subset of intangibles, consequently to generate intellectual property out of intellectual capital.[28] Accordingly, the value created by intangibles gradually increases in every subset as moved from the outer periphery of the circle towards the center. Through this flow, value creation normally occurs in each and every level. The magnitude and intensity of the value created will inherently vary depending on the level it is created at. Nevertheless, value in most cases will be determined by domestic and global market forces over the time. As such, sometimes

[25] ALEXANDER POLTORAK & PAUL LERNER, ESSENTIALS OF INTELLECTUAL PROPERTY XXVI (John Wiley & Sons 2011)
[26] Id.
[27] This description has been based on and put forward in the light of "information asset" definition of Arena & Carreras suggested in CRISTOPHER ARENA & EDUARDO CARRERAS, THE BUSINESS OF INTELLECTUAL PROPERTY 42 (Oxford 2008)
[28] POLTORAK & LERNER, *supra* note 25, at XXVIII.

relational databases, for instance, may be of more significant value than a computer software with a limited area of use.[29]

With the significant shift of the economic tendency from a product-driven one to a knowledge-based one, not only are intangibles *per se* of tremendous value but they are also the very foundation of value. Monetary and tangible assets (i.e. hard assets), in a way, serve as auxiliary factors to reify the intangibles into profit-generating goods and services. Accordingly, they are used to make, use and sell products and services based on intellectual property.[30] In this sense, intangible assets function as a bridge between hard assets and intellectual properties.[31] It is necessary, however, to note that despite financial capitals being less important than social and human capital for achieving, and especially for sustaining, a competitive advantage -as a sort of emergence of value-, they are often crucial for acquiring or establishing the resources that are needed to exploit opportunities[32], especially when rather traditional businesses are at issue.

Putting their significance in conjunction with corporate elements aside, the very nature of intangibles is apt to portray a perpetual foundation of value. In the most simplified fashion, this may be said to stem from following qualities:

(i) Knowledge, unlike material assets, resides in the human brain. Thus, the value attributed to it is not owed to a physical substance. As long as the mental capacity of humankind exists, so does the knowledge that is of value.

(ii) Owing to the lack of physical substance, intangibles are excluded from depletion. Hence, knowledge cannot run out due to overwhelming use.

(iii) They are easily transformed, modified, built upon and compounded with other knowledge without requiring substantial investments. Also, new knowledge may make a near obsolete technology current.[33] This makes intangible assets cumulatively valuable.

(iv) It is also knowledge that can yield tangible property so long as the materials are available.

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[29] ARENA & CARRERAS, *supra* note 27.
[30] RUSSELL PARR, INTELLECTUAL PROPERTY; VALUATION, EXPLOITATION, AND INFRINGEMENT DAMAGES 40 (John Wiley & Sons 2018)
[31] Id.
[32] Michael Hitt, et al., *Creating Value for Individuals, Organizations, and Society*, 25(2) Academy of Management Perspectives 57, 75 (2011)
[33] ARENA & CARRERAS, *supra* note 27, at 56.

(v) The worth of all goods and services produced based on certain knowledge holistically are embedded in the value of the original knowledge. Therefore, it is pointedly more value-intense than the products -including the services- generated.

As a result of these traits, knowledge and intangible asset-based businesses can create much more wealth than traditional financial assets-based businesses, because outgoings which are costs in traditional businesses turn into investments in knowledge businesses and create future revenue- generating assets.[34]

On the other hand, the value created does not necessarily accrue only to businesses but it may also cater to customers and, in a wider perspective, to the society. Accordingly, it is possible to behold the value created by the medium of intangibles both on the micro and macro level. As regards to performance on the micro level, such elements of intangible capitals as brand value, management skills, reputation, intellectual properties along with know-how, R&D activities, inter-organizational relations, process quality etc. collectively figure an indicator for the creative and innovative strength as well as potential of a given business, therefore, determine its market value[35] possibly greater than its book value. Meanwhile, products and services as well as customer relations quality of which have been enhanced with the help of said intangible capitals, eventually resulting in satisfaction, will form the benefit of customers from the value created.

Where the value creation at the macro level is concerned, knowledge-based industries and businesses have their significant impact on fostering innovation and competition which, in turn, leads to employment, improvement in gross national product -inasmuch as they are more wealth-intense than conventional businesses and industries- and results in a greater per-capita income.[36] Also, the law regulating intellectual property often amounts to a potent policy tool for the governments, through which they seek to shape economic and at some instances social dynamics in the global market which is more knowledge-based now than ever. The recent joint analysis report[37] disclosed by the European Patent Office (EPO) and the European Union Intellectual Property Office (EUIPO) pertaining to economic performance of IP rights intensive

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[34] JUERGEN H. DAUM, INTANGIBLE ASSETS AND VALUE CREATION 6 (John Wiley & Sons 2003)
[35] ANNETTE KUR & THOMAS DREIER, EUROPEAN INTELLECTUAL PROPERTY LAW; TEXT, CASES AND MATERIALS 9 (Edward Elgar 2013)
[36] Id.
[37] *IPR-intensive industries and economic performance in the European Union: Industry-Level Analysis Report, September 2019,* EUIPO (12 May 2020) https://euipo.europa.eu/tunnel-web/secure/webdav/guest/document_library/observatory/documents/IPContributionStudy/IPR-intensive_industries_and_economicin_EU/WEB_IPR_intensive_Report_2019.pdf

industries in the EU mirrors a stream of macro impacts and economic contribution of knowledge-based industries.[38] Accordingly; IPR-intensive industries are shown to have generated 29.2% of all jobs in the EU during the period 2011-2013. When indirect jobs are taken into account, the total share of IPR dependent jobs rises to comprise 39% of all jobs. The worth of economic activities conducted by IPR-intensive industries amounted to 45% of EU GDP. In the same vein, U.S. Patent and Trademark Office (USPTO) reported that, in 2014, IP-intense businesses figured 38.2% of total U.S. GDP, meanwhile supporting 45.5 million jobs that amounted to 30% of all employment.[39]

Consequently, as far as intangibles present the foundation of creating value in variety of realms and on distinct levels, intellectual property rights constitute the most advanced and legally institutionalized reflection of intangibles.

### 3. Intellectual Properties Through the Lens of the Concept of Property

Historically, intellectual property rights have often been explained and justified through the theories of material (or classical) property. In this way, they are extensively modeled after property rights in tangible goods.[40] Indeed, the rights of both types veritably present similarities. Accordingly, the former one establishes the rights over the physical goods pertaining to the determination of its use, whereas the latter vests the same authority in its owner, in the context of intangibles. Therefore, just like it is the case in classical property, intellectual properties can be bought, sold, assigned and put up as collateral and inherited, thanks to the legal quasi-property identity ascribed to them. This is where IP rights approximate material property rights the most. In this fashion, physical attribution, or dependency on a material substance, seems to be the distinction between the two types of rights. This is unlikely to be falsified. As is well known, intellectual properties are shaped by the intellectual capacity and creativity, and outcome of these facilities in intangible and legally protectable form. They lack physical substance, thus do not have weight or height; they are odorless and tasteless; all in all, they are immaterial. However intellectual creations, in order to be the subject of IP protection, have to be expressed or externalized in a convenient medium.[41] Depending on the

[38] In the said report, IPR-intensive industries have been defined as the ones that have an above-average use of IPR per employee, in comparison to other IPR-using industries.

[39] *Intellectual Property and the U.S. Economy: 2016 Update*, USPTO (May 14 2020), https://www.uspto.gov/sites/default/files/documents/IPandtheUSEconomySept2016.pdf

[40] KUR & DREIER, *supra* note 35, at 2

[41] Externalization or expression for that matter should mean for the intellectual creation to be carried beyond the state of mere (and abstract) thought and be made somehow discernable. This is, of course, with the express note

type of the creation, this expression or externalization may, for instance, be a composition of colors, a poem, a song, a distinctive packaging, a machinery prototype or otherwise objectively discernable output. Differently from classical property, however, intellectual properties exist independently from the medium they have been reified into; thus, they are subjected to a distinct legal regime than the material good they are embedded in.

Another crucial divergence becomes apparent in the context of continuity of the rights. Property rights on material goods -save for the exceptions stemming from specific laws e.g. expropriation- are sustained as long as the owner retains the ownership intention. Thus, such property rights are not time-limited. Conversely, protection by intellectual property rights pertains to a definite time. Copyrights, for example, are protected for the lifetime of the author and another (minimum) 50 years after the author`s death (*post mortem auctoris*) as pursuant to the Berne Convention.[42] Patents are granted for 20 years; designs are often protectable for 5 years and renewable 4 times, thus 25 years in total; meanwhile, utility models and trademarks enjoy protection of 10 years, which can be renewed indefinitely.[43]

In addition, the absolute exclusionary effect of classical property rights does not necessarily encompass the concept of intellectual property. In other words, IP rights, unlike material property rights, are concerned with striking an optimal balance property interest (exclusionary) and non-property (access) interest.[44] Said quality thus, underlies the rationale of definite time protection, and is also quite apposite to functions of IP rights on a macro level, as later discussed in connection with justification theories of IP rights. By limiting the

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that the (minimum and maximum) thresholds of expression or externalization shall vary according to the intellectual creation at issue and the IP right claimed thereupon. For example, in regard to copyright, the transition from mere idea to a copyright-worthy expression of the said idea (i.e. work for the purposes of copyright law) requires a somewhat permanent and discernable fixation (See: TORREMANS, *supra* note 1 at 198.) For the purposes of trademark law, the signs and indicators that can comprise a trademark must be capable of being objectively represented in the relevant registry and in a way that is identifiable by the authorities and the public. As far as patents are concerned the idea-externalization transition has at least two facades: the invention must be susceptible for industrial application and it should be capable of being represented in a patent application. On the other hand, if, externalization of an invention is made such as to disclose it to the public before the filing of an application, this might give rise to an absolute ground of refusal [to that effect see: Article 54(2) of the European Patent Convention]. Likewise, the use of a trademark before the registration might entail different legal results such as priority right or protection being afforded to unregistered marks under certain conditions.

[42] Fifty years of protection after the lifetime of the author is set as a lower limit, meaning the signatory countries have flexibility to impose longer protection periods. In most cases, especially in the EU, protection is presently granted for the lifetime of the authors and an additional 70 years.

[43] Trademarks are maintainable indefinitely provided that the renewals take place in every 10th year, nevertheless, this requires an action, hence they are circumstantially indefinite rather than indefinite in nature.

[44] KUR & DREIER, *supra* note 35.

exclusivities by time, this enables the opportunity to build upon previous knowledge thus preserves the intellectual productivity as well as the progress in sciences and arts.

At the end of the day, having regard to disharmonious features of the two concepts we strive to exhibit, the property metaphor may not always be feasible to explain the notion of IP rights, and it is suggested that it may be even misleading.[45] With this being the case, it is necessary to bear in mind that IP rights have their unique characteristics, and without regarding them, the conventional understanding of proprietary rights is unlikely to suffice to elucidate this realm.[46]

**4. Why More Commercial Than Tangible Assets?**

A possible answer to this question lays in the cognition that we earlier strived to exhibit in the context of value creation. That is, flowing from the fact that intangibles are the primary foundation of innovation not only on the micro level but also in the wider perspective. Correspondingly, intellectual properties, with the protection they enjoy and the resulting propertization effect, entail a much more significant and institutionalized economic potential in comparison to other intangible assets. As Arena and Carreras articulate: if knowledge is the basis of value creation in today`s economy, then intellectual property is one of its primary currencies and the means of extracting that value.[47]

Nevertheless, it cannot be overstated that the archaic theories striving to justify and pin down the rationale of intellectual property rights have been largely based on individual artistic and inventive activities and often on their flourishing impact on artistic and scientific progress. A more rational perception of intellectual property rights, however, indicates the fact that they are rather business tools in the micro, and policy tools on the macro level than a sophisticated fashion of rights given to individuals so as to award their intellectual and creative endeavors. Indeed, the majority of creative works are today extensively business oriented, hence, carried out within commercially organized settings, conceptualized as innovative and creative businesses.[48]

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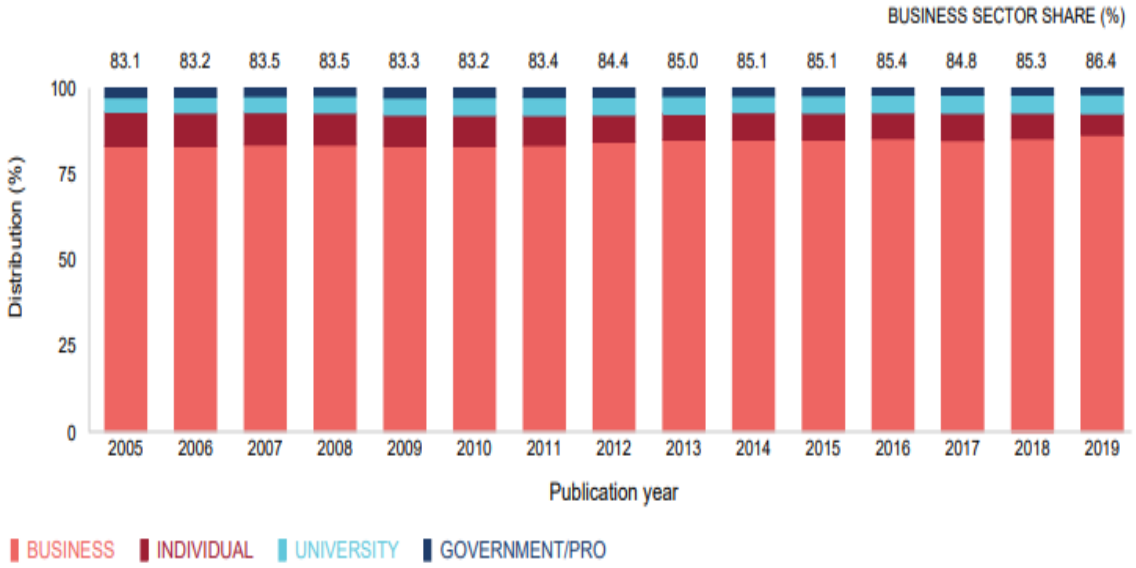
[45] Id.
[46] SAMI KARAHAN et al., FIKRI MULKIYET HUKUKUNUN ESASLARI 4 (Seckin 2013)
[47] ARENA & CARRERAS, *supra* note 27.
[48] Moreover, regardless of whether the business activity is identified as innovative/creative or conventional, commercial reputation and goodwill could -to a certain degree- be substantiated by intellectual property, particularly apparent in the case of trademarks. Information on the commercial origin of the goods and services as well as the reputation and goodwill that associates with that origin is conveyed by trademarks.

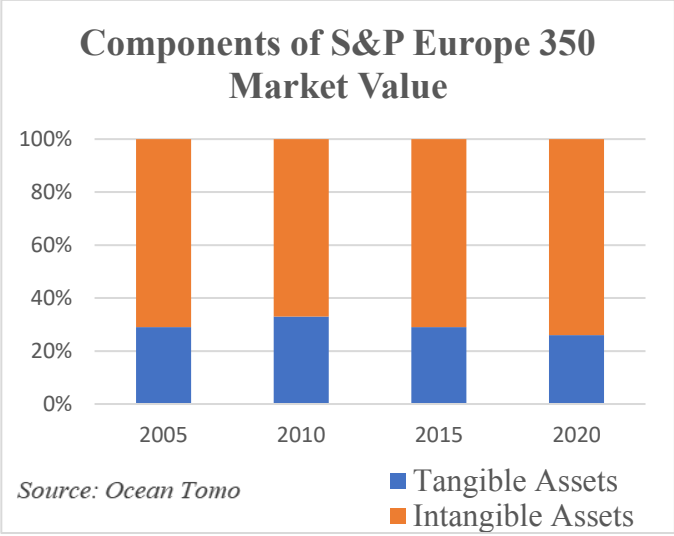



The statistical data above[49], delivered by the World Intellectual Property Organization (WIPO), regarding patent applications by the type of applicant corroborates to this proposition. Accordingly, in 2019, 86.4% of the patent applications under Patent Cooperation Treaty (PCT) has been filed by businesses, meaning, individuals remain as a minor stakeholder in terms of patents. This is the case for trademarks as well. Though trademarks, in principle, can be owned by individuals, due to their core function, they hardly associate with individual ownership.

As we pointed earlier, knowledge is an inexhaustible source of value creation, not exclusively but extensively at a business level. This is the case not only for IP-intensive businesses but also for rather traditional material-property oriented businesses. Take the example of Coca-Cola®, though the said company engages in rather conventional, non-IP-intense production, by the end of 2020, the price-to-book ratio has been realized as 12,67.[50] That means the current market value of the company is more than eleven times greater than its book value. This positive gap has been mostly created by the trademarks of the company. Regardless of whether it is traditional or IP-intense, businesses of various types today, somewhat, have to lean towards intellectual properties in so far as the wealth and the capitalization is extensively centered around intangibles.

[49] *Patent Cooperation Treaty Yearly Review 2020: The International Patent System,* WIPO, (6 May 1021) https://www.wipo.int/edocs/pubdocs/en/wipo_pub_901_2020.pdf

[50] Coca-Cola Co Price to Book Value on 31 December 2020
based on YCHARTS data (26 Jan. 2021) *https://ycharts.com/companies/KO/price_to_book_value*




Approvingly, the study suggested that this tendency is increasingly continuous.[51] Accordingly, in 2020 intangible assets of 350 leading European companies comprised 74 percent of market value, leaving the hard assets far behind at the rate of 26 percent *(See the chart on the left)*.

Hence, those without access to intellectual property will stagnate for a while in low-profit commodity businesses and eventually fade out of existence.[52] This is also inevitable taking into account the fact that the value emerges not only from the possession of the knowledge but arises more significantly from the exclusion of the others. The power of intellectual properties, correspondingly, resides in the fact that they are the major instruments through which the rights holders are able to control the dissemination of the knowledge and the value. In terms of intellectual assets -in which IP rights are embedded-, the question "who owns the knowledge" is of explicit importance. What is more important however is the question of "who is deprived of the knowledge". Competitive strength and value arise rather from whom the information is concealed from than who possesses it, namely monopoly.

Most evident, and perhaps the ultimate, way of successfully remaining competitive in business resides in opening up to new markets and keeping up with demands in it, in the meantime offering as broad a product range as possible. Nevertheless, as we are to detail throughout this study, the execution of these strategies will often amount to substantial investments, thus to costs, meanwhile still accommodating serious risks. This very point is also where intellectual properties serve as the most efficient business tools. Companies are seeking to expand product lines, increase market share, minimize new product development costs, expand market opportunities internationally, and reduce business risks. Companies are also seeking to create corporate value for investors. All of this is accomplished by exploiting

[51] *Ocean Tomo Intangible Asset Market Value Study*, OCEAN TOMO INTELLECTUAL CAPITAL EQUITY, (6 May 2021) https://intellisys.fi/wp-content/uploads/2020/09/Ocean-Tomo-Intangible-Asset-Market-Value-Study-IAMV-Report_08_01_17.pdf ; *Ocean Tomo Releases Intangible Asset Market Value Study Interim Results for 2020* , OCEAN TOMO INTELLECTUAL CAPITAL EQUITY, (6 May 2021) https://www.oceantomo.com/insights/ocean-tomo-releases-intangible-asset-market-value-study-interim-results-for-2020/

[52] PARR, *supra* note 30, at 5.

patents, trademarks, trade secrets, and copyrights.[53] In the simplest example, companies desiring to enter new markets often resort to licensing their trademarks so as to get their products produced in the target market by another manufacturer or get their services provided by another provider that already exists in the target market, thus avoiding the investment in manufacturing and possibly distribution infrastructure in the targeted market. Various businesses also quite commonly form an IP-based enterprise and pool their relevant IP rights, mostly their patents, so as to easier generate more advanced or unprecedented products and which they would not be able to come up with on their own.

Finally, the proprietary characteristics of intellectual property rights is a big help for them to substitute the currency in the business sphere, or be the currency itself. Appropriately, by means of sales, leasing and collateral, they are interconvertible with monetary currency (transactional characteristic). Further, with the recent tendency, intellectual properties are gathered in the portfolios of intellectual property merchant banks, which establish an IP exchange market of sorts through which IP rights are even bought and sold by means of auctions.

**5. Delineating Commercialization**

Commercializing is a means of extracting the value encapsulated in intellectual property rights, by linking them to products or processes.[54] As far as IP rights are concerned, commercialization is often perceived as squeezing money out of them or converting them into money. This postulate is partially relevant; converting them into money firstly, by manufacturing/offering and marketing the IP protected goods and services and secondly by selling (assigning) the making available to others (licensing) the rights themselves are certain forms of commercializing. It is crucial, however, to note that the said aspects pertain respectively to trade of IP-incorporating goods/services and the transactional feature of IP rights. Commercialization activities certainly involve making money from intellectual outcomes, though the activities with such orientation are more accurately be defined as monetization.

Conversely, commercialization consists of a greater area of activities, in a way forming a superset that covers a cluster of activities including monetization. Nearly any type of activity

[53] Id.
[54] ARENA & CARRERAS, *supra* note 27, at 59.

aimed at making a commercial use of the intellectual property in question may be roughly identified as commercialization. Thus, its scope may be defined as the process of bringing intellectual property to the market in order to be exploited.[55] WIPO, in its Guide on Intellectual Property Commercialization[56], defined its scope as *"a continuum of activities and actions that provide for the protection, management, evaluation, development and value-creation of ideas, inventions, and innovations to implement them in practice. Prototypes and implemented processes lead to the development of products and services by entrepreneurs, startups, existing companies as well as governments resulting in economic and societal benefits"*. Clearly adopting a broader concept of commercialization, emphasis has been put both on micro (or business) level and macro (social) level functions of IP rights. In this direction, attributing the concept of commercialization solely to monetizing is very likely to remain shallow, and it would not properly lead to merited scrutiny as to legal aspects of it.[57] Admittedly on the other hand, a great deal of the activities involved in the continuum of commercializing intellectual property rights may not have a direct contact with the realm of intellectual property law. Although intellectual property rights are existentially linked to the intellectual property laws whereunder they acquire their actual identity, once they came into existence their management and exploitation is driven by the business strategies of the right-holder, whereby a wide array of commercial choices and sub-elements such are those regarding manufacturing, marketing, competition etc. become determinant. Consequently, the term of intellectual property commercialization is often perceived to have fallen in the scope of business and economics than that of intellectual property law and that is even more so when the corporate aspects are at the stake.

Therefore, the highly commercial nature of intellectual property and rights attributed thereto tend to inhibit the possibility of setting a sharp divide between the legal and commercial aspects of intellectual property rights. As a matter of fact, it is *per se* arguable whether such a divide can possibly be drawn between those aspects. Furthermore, when the task is to identify the implications of intellectual property commercialization for the purposes of law and

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[55] *Fact Sheet Commercialising Intellectual Property: Licence Agreements,* EUROPEAN IPR HELPDESK (26 Jan. 2021) https://www.iprhelpdesk.eu/sites/default/files/newsdocuments/Fact-Sheet-Commercialising-IP-Licence-Agreements.pdf

[56] Gary N. Keller, *Guide on Intellectual Property (Ip) Commercialization*, WIPO COMMITTEE ON DEVELOPMENT AND INTELLECTUAL PROPERTY (CDIP) 18 (15 may 2020) https://www.wipo.int/edocs/mdocs/mdocs/en/cdip_16/cdip_16_inf_4.pdf

[57] Quite contrary to this broad understanding of commercialization propounded in this document, respective paragraph of executive summary containing this definition starts with following postulate that clearly indicates the monetization: "Commercialization of intellectual property (IP Commercialization) is making money out of one's ideas."

jurisprudence, this elusive divide represents a particular challenge. Last but not the least, it is also phonetically eccentric when the commercialization of the rights -which are in fact readily commercial in nature- is spoken off.

Having acknowledged the magnitude of the scope of the term of 'commerce' hence that of 'commercialization', intellectual property commercialization may nevertheless be somewhat identified in respect to those aspects that coincide the domain of intellectual property law.

## 6. Identifying the Concept of Intellectual Property Commercialization from the Legal Perspective

From the outset, the legal relations and status emerging from the commercialization continuum defines the borderlines of the legal perception of intellectual property commercialization. Clearly however this definition also indicates an ambiguously vast domain. Alternatively, the definition could be relatively narrowed down to 'the interface with intellectual property laws of the process of making intellectual property and IP rights a subject of commerce'. In either case, no distinct and crystal-clear concept *prima facie* outstands. Nevertheless, these definitions maintain two potential connotations. Firstly, for a relation or a status involved in the intellectual property commercialization continuum it has to be of a prevalent legal nature. That is to say, pure commercial matters such as product development, manufacturing, business strategies, marketing choices etc. usually do not represent any specific or direct province for intellectual property law. Secondly, with regards to the dissociation of intellectual property rights from the goods or services on which they are embodied, commercialization of intellectual property also entails two different facets. We shall roughly address these two aspects as (i) commercialization of intellectual property (i.e., the inventions, distinctive signs indicating the commercial origin, works of art, designs etc.) by incorporating them into commercially viable products, processes or services and offering them in the market; (ii) commercialization of intellectual property rights and briefly describe these below.

Prior to that however, it is imperative for our purposes to elucidate the differential between the intellectual property (IP) and the intellectual property rights (IPRs) on a theoretical plane. The former term (IP) refers to the outcome or product of the human intellect such as inventions; literary and artistic works; designs and signs (e.g. symbols, names, images or

combination thereof) used in commerce.[58] In order for such intellectual property to be susceptible for legal protection they must be somehow externalized such as to carry them beyond mere abstract concepts [59]; they must comply with (and fit into) the other criteria set out by the intellectual property law under which protection is sought and -when necessary- comply with the formal procedures are fulfilled.[60] This is when intellectual property rights (IPRs) come into the scene: the latter term, therefore, hand entails the exclusive rights that are granted by law to its proprietor in respect to these intellectual properties. These legal rights are organized in bundles (i.e. patents; trademark rights; copyright and related rights; design rights etc.) which embody several exclusive prerogatives.[61] On that note, an invention, a work of art, a design or a sign used in commerce will respectively be the subject of patent rights, copyright and related rights, design rights and trademark, given that they conform with the substantive requirements.

Although, at the outset, this divide does not necessarily seem to be of a vital importance; in fact, the use of intellectual property (IP) for intellectual property rights (IPRs) and vice-versa is often only a matter of preference and is intended to address the same phenomena, it nevertheless comes useful in exhibiting different facets of commercialization.

### 6.1. Commercialization of Intellectual Property (IP)

As was highlighted above, in the rudimentary sense intellectual property commercialization is perceived as the venture of making money from intellectual creations. Plausibly, the latter most commonly transpires by way of incorporating these creations -which are incidentally protected or protectable under intellectual property rights- onto goods and marketing them thus making profit. Likewise, a similar pattern may apply to services as far as the underlying intellectual outcome is susceptible to being provided as a service.

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[58] *What is Intellectual Property?*, WIPO, (6 May 2021) https://www.wipo.int/about-ip/en/

[59] Visit note 41 above.

[60] The general principle in pursuant to Article 5(2) of Berne Convention is a formality-free protection for copyright. Further, under different jurisdictions, unregistered trademarks and designs may occasionally avail of intellectual property protection.

[61] For instance, in respect to patents, the exclusive right of making, using, offering for sale, selling or importing invention covered by the patent;
In respect to trademarks, exclusive right of using in the protected sign in the course of trade, in relation to goods or services, that of offering the goods or putting them on the market, importing or exporting goods bearing that sign etc.;
As regards copyright and related rights, exclusive right of distribution, reproduction, communication to the public, exclusive rights in performances, moral rights etc.

Therefore, with reference to the distinction we laid above, what is visibly commercialized through this pattern is not the intellectual property rights as such but rather the intellectual property, more particularly the goods and services that correspond to (or embody or incorporate) the underlying intellectual property. Accordingly, the definition of intellectual property commercialization from a legal perspective that follows from this pattern may be: The exercise of intellectual property rights in the context of commerce, specifically by way of trading goods and providing services that incorporate the IP in question. Thereby the focus is said to be around the goods and services that incorporates the intellectual property. Evidently this shall lead to an immense area of activity, even more so once it is conceived that almost every fashion of goods or services that are commercially available embody at least one intellectual property and that the more technology gets involved in the products, the bigger the number of embedded intellectual properties gets. In the same vein, the legal aspects of commercialization shall cover the vast area of relations arising from the exercise and the breach of the commercial nature of exclusivities that are part of IP rights. These relations primarily pertain to manufacturing (the breach of which results in counterfeit products), imports and exports (parallel import cases being probably the largest battlefield over which international trade and IP rights clash) and distribution of the goods or services that embody the relevant IP rights. Insofar as each specific type of intellectual property right confers different exclusivities on its holder, the relations and disputes arising from their exercise and breach and correspondingly the actual scope of the legal aspects of intellectual property will inherently vary. Nevertheless, the definition and the breadth of legal aspects of intellectual property commercialization of this fashion may be confined to 'the legal relations and the disputes that are originating from the exercise and breach of intellectual property rights in the context of trade of goods and provision of services that incorporate intellectual properties.'

### 6.2. Commercialization of Intellectual Property Rights (IPRs)

The second modality of intellectual property commercialization is largely constructed upon the transactional value of intellectual property rights. This follows that the value embedded in the intellectual property prerogatives also serves, as it were, as a corporate currency.

Accordingly, this manner of commercialization activities, which could also plausibly be addressed as IP right transactions, take the intellectual property rights as their subjects, instead of the goods or services on which IP rights embodied. In other words, this modality

pertains to making profit from the intellectual property rights themselves rather than incorporating the IP protected substance into goods and services and commercially benefiting therefrom.

On an analogy, commercialization of IP rights amounts to a peculiar type of commerce, the subject commodity of which consists of intellectual property rights i.e. patent rights, design rights, trademarks, copyrights etc. Such transactions tend to take various forms, although these are not of limited number, the foremost types are briefly pinned down below:

(i) IP rights assignment: IP assignment refers to the transactions that transfer the ownership (title) of IP rights such as patents, design rights, trademarks, copyright and related rights from their present owner (assignor) to another party (assignee); hence the latter becomes the new owner of the intellectual property right at stake. In a way, intellectual property assignment creates a legal impact that is equivalent to sales of IP rights insofar as it transfers the title from one party to another and is typically made in return for an agreed pecuniary consideration.

(ii) IPR licensing: Connotes the agreements on the basis of which the IP right holder (licensor) authorizes a third party (licensee) to exploit the intellectual property for a limited time and on the agreed terms; and he/she in return receives the agreed consideration. The parties to the agreement enjoy a great deal of liberty in determining the scope of the license and it is not necessarily holistic. That is to say the authorization granted by the right holder may be limited to certain prerogatives among the bundle of rights covered by that particular IP right (such as right to reproduce the copyrighted material, or right to distribute); or the whole bundle of rights recognized for that specific type of intellectual property may be licensed.[62] Also, the limits to the scope of license may be set by other factors such as geographical limitations, field of use, right to sub-license etc. Furthermore, the consideration that is accorded to the licensor is not necessarily monetary; it might also be in the form of another commercial benefit, or quite often it is a cross license.

(iii) IPR pooling: Collective exploitation of intellectual properties are desirable to right holders on many ends. Particularly in innovative industries, obtaining a commercial access to various existing technologies in the field could often appear as a tedious and costly process. To that end, holders of patents tend to enter into pooling arrangements whereunder they put their

[62] With the exception of moral rights to literary and artistic works due to their non-economic quiddity.

patented technologies under each other`s disposal, thus reducing transaction cost and the risk of patent blocking between themselves; while having easier access to a cluster of essential technology in the respective industry. At the same time, with the possibility of collectively excluding the third parties from exploiting the pooled technology or that of implementing selective terms of licensing, the pool members avail themselves of the opportunity of an oligarchical competitive advantage. Similarly collective management of literary and artistic management could contribute into easier monitoring the use of the protected work and enforcement of exclusive rights covering them. Indeed, it is noted that copyright and related right could scarcely be managed individually in the contemporary prospect due to the immense number of users seeking access to protected works in different places and different times[63]; add to the ease of dissemination of these works in the digitalized world. By authorizing the collecting societies to license the work, the right holders are provided with better access to a wide range of users while utilizing the possibility of more effective negotiation of terms and more systematic monitoring of the use of work. Also, on the end of the users seeking access to work -especially commercial users such as radio stations, broadcasters, cinemas etc.-, it is imperative to be able to obtain licenses from a one stop shop.[64] Therefore, much like in the case of patent pooling, collective managements of literary and artistic works provides the both ends of the deal with considerable advantages. Finally, it is necessary, from the view point of intellectual property commercialization, to note that pooling arrangements, which can take various forms, involve different layers. First layer is the actual licensing transactions that transpire within the pool and licensing to the third parties; a clear appearance of commercialization. However, a second layer of commercialization could be identified to be the pooling arrangement itself. This is because firstly because an authority to license or sub-license in respect to third parties is occasionally preemptively left to the pools; and secondly because pooling arrangement itself amounts to a promissory undertaking to license the intellectual property right to the pool members. On that note, pooling arrangement and licenses concluded under that arrangement represent a form of wide-scale of commercialization.

(iv) Franchising: Although franchising infers a business model, it has its roots in intellectual property licensing. The contractual settings of franchising are centered around the core business which is in possession of a cluster of intellectual property rights and seeks to expand (franchisor) and a third party (however typically a multiple number of third parties)

[63] MIHÁLY FICSOR, COLLECTIVE MANAGEMENT OF COPYRIGHT AND RELATED RIGHTS 17 (WIPO 2002)
[64] DANIEL GERVAIS (ED.), COLLECTIVE MANAGEMENT OF COPYRIGHT AND RELATED RIGHTS 3 (2nd ed. Wolters Kluwer 2010)

who seeks to benefit from the said business model, good reputation and intellectual properties of the core business (franchisee). Accordingly, the franchisor authorizes the franchisee to use its intellectual properties, that emblematically being trademark, know-how and copyright; furthermore, it undertakes the duty of providing assistance and training as to the said business model, meanwhile retaining supervision and control over the performance of the franchisee. The franchisee on the other hand, gets under the duty of paying the franchisor the agreed consideration and providing the preset quality standards, while replicating the business model of the franchisor, in a way acting as an extension of the core business, building upon its well-founded reputation, customer portfolio and intellectual property value.

(v) Joint ventures and Spin-offs: Joint ventures refer to the initiatives that are aimed at collaboratively bringing into the market, hence commercializing, the knowledge assets that are owned by different parties. Collaboration in this context may be organized contractually or by establishing a separate entity that is to undertake the collective project in question.[65] The main benefit to each participant is likely to be the allocation of the risk entailed and collective and accumulated benefit from the knowledge assets, that include intellectual property rights, that the collaborators bring into the joint venture. Accordingly, each party will be able to derive significant economic benefits from the commercialization existing intellectual properties of one another as well as from the intellectual properties that are resultant from the joint venture as such. The parties, having been able to avail themselves of the experience, expertise, technology and more importantly the intellectual properties of one another, will undoubtedly have a less costly and more rapid access to the end result/product.

Moreover, universities and research organizations are the fundamental sources of innovation technology and knowledge in general. Such intellectual outcomes and knowledge assets not only possess significant corresponding economic value but they also retain immense potential for the scientific, industrial and intellectual -likewise cultural- progress of the society. For that reason, the necessity of paving a way for transfer of knowledge from universities to industry and to the public becomes apparent. Spin-off is the mechanism that facilitates intellectual property commercialization in the said direction. It refers to a brand-new corporation that is created by the parent organization -which may be universities, research organizations or another corporation- so as to bring its innovation into the market. Thus, spin-

[65] ROBERT GOLDSCHEIDER & ALAN GORDON (eds.), LICENSING BEST PRACTICES: STRATEGIC, TERRITORIAL, AND TECHNOLOGY ISSUES 212 (John Wiley & Sons 2006)

offs serve as a mediator and an effective means of technology transfer between the research environment and industrial sector.[66]

(vi) Collateral function: Over the discussions above we have extensively referred to the economic and commercial value embedded in intangible assets in general and in intellectual property rights in particular. Value of the latter is captured, institutionalized, protected and enforced by intellectual property laws, to which they owe their very existence. Therefore, although the actual worth varies depending on the type of intellectual property right and on the intellectual property in question as such, the presence of certain value is objective. This follows that, once there is objective economic value attributed, they are susceptible to use as collateral to secure financing, typically under a lending agreement. Accordingly, on the occasion that intellectual property rights are used as collateral, the borrower promises the rights of his intellectual property -such as a patent, trademark, copyright, or design rights- if he/she fails to repay his loan.[67] This connotes a capitalization of the potential and predictable value of intellectual property rights for commercial purposes, hence commercialization thereof. It is also observed that, although its full potential has yet to be realized, securitization of intellectual property rights tends to gain incremental importance as the global economies persistently grow closer to knowledge-based models.[68]

(vii) Capital function: Founding capital of commercial entities such as limited liability companies and joint stock companies is not necessarily comprised only of cash capital but also *inter alia* in-kind capitals could be brought by the shareholder as capital contribution. Prerequisite for in-kind contribution to qualify as founding corporate asset is subsumed under the headers of economic value, negotiability (transmissibility) and monetizability. Capitalization of the objective value embedded in intellectual property rights, by the same token as in abovementioned collateral function, may also, depending on the jurisdiction, qualify in-kind capital in the context of commercial entities. This evidently forms a method of commercialization of intellectual property rights through capitalization thereof.

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[66] *Fact Sheet Commercialising Intellectual Property: Spin-offs*, EUROPEAN IPR HELPDESK FACT SHEET, (15 May 2020), www.iprhelpdesk.eu/sites/default/files/newsdocuments/Fact-Sheet-Commercialising-IP-Spin-offs.pdf

[67] Brian Jacobs, *Using intellectual property to secure financing after the worst financial crisis since the Great Depression*, 15 Marq. Intell. Prop. L. Rev. 449, 451 (2011)

[68] Dov Solomon & Miriam Bitton, *Intellectual property securitization*, 33 Cardozo Arts & Ent. LJ, 125, 127 (2015); Jacobs, *supra* note 61, at 463.

## 7. Conclusion

In the light of the grounds we strived to lay, it may be articulated that: knowledge is the main foundation of value; IP rights are the fixation or instrumentalization of value; whereas commercialization equates to the extraction of value. In a way knowledge encapsulates the existing and potential value and the wealth likewise, whereas tangibles no longer present the capital and wealth, quite contrarily they remain rather primitive in this equation.

Intellectual properties present the most advanced and possibly the most qualified form of intangible assets as they are backed up and institutionalized by the IP laws. In this sense, IP laws figure the set of principles through which a certain balance is intended to be struck. As much as IP rights are the source of monopolistic powers of the right-holder, they have a number of more sophisticated goals which often contrast the monopolistic interest of right-holders. Said -more sophisticated- objectives of IP laws are most apparent in macro level. In this context, monopoly IP rights built upon has to be limited in favor of artistic and inventive progress and of a fair accession to the knowledge and of competition. Limitations -of finiteness- of these rights, along with lacking physical substance, is the most marked point where they steer away from the proprietary concept, therefore IP right do not fully exhibit the characteristics of property rights in classical meaning.

Admittedly, in most instances, creative activities are hardly engaged in with the sole impetus of inventive or artistic pleasure but they are rather carried out on professional level, typically within a contractual relation. Naturally, the end products of these creative activities end up being a part of the aim of profit making, thus, more of a corporate subject anything else. In this connection, intellectual property rights are primarily business tools that subsist the main instrument to control the dissemination of the precious knowledge and the values created arduously, thus they are guarantors of competitive strengths of the businesses under the possession of which they remain. And they are of course key elements to implement various business strategies as specific regards to market accessions and mitigation of R&D costs. Further, intellectual property rights subsist the currency itself that is used in business and commerce owing to the capacity of being bought, sold and put as collateral. That may be called the transactional function of IP rights.

Finally, as far as commercializing these rights is concerned, the terminology of commercialization should be well defined. Although commercializing is often defined as making money out of them, this is only one component of a wider continuum. Hence, this

continuum pertains to bringing intellectual properties into the market to be exploited[69] which certainly encapsulates their statutory and contractual legal aspects as well. Consequently, having put the legal aspects of intellectual property commercialization in main focus, the scope of the term should be perceived in two layers. Firstly, the commerce in goods and services that incorporate intellectual properties, hence come to interface with IP rights. Secondly, it connotes the legal vehicles of commercializing; (i) the sales or assignment of IP rights; (ii) other business contracts that do not alter the ownership of the intellectual property rights but are aimed at commercial exploitation thereof; principally but not exclusively, intellectual property licensing, franchising as well as commercial initiatives which entail legal transaction such as establishing joint ventures and spin-off companies; (iii) legal transactions in the center of which stands the transactional value (can also be referred to as negotiability, commodity value or currency aspect) of intellectual property rights, for instance, securitizing the external financial support by using the IP rights as collateral or bringing intellectual property rights into the companies as capital.

On the final note it may be maintained that although intellectual property and the rights attributed to them are majorly commercial in nature and their economic/commercial reverberations are occasionally more profound than legal ones, their existence is nevertheless inextricably dependent to IP laws that create the identity of intellectual property. Correspondingly commercial and legal aspects of intellectual property very frequently come into the scene simultaneously. Having accepted 'commercialization' as a large continuum that covers almost every step taken with a view to bring into commercial use or open up to public whatever being commercialized, corresponding legal aspects are, admittedly, ambiguously ample. Nevertheless, in the light of above discussion we tend to suggest intellectual property commercialization should not be perceived as narrow as mere act of making money from intellectual property, meanwhile as far as it is seen from the intellectual property law stand point it should also not entail the entire continuum that knowledge-based industries commence, especially those that pertain to pure business strategies and concerns and pure industrial matters even though various other legal status and relations might naturally emerge therefrom.

[69] *Commercialising Intellectual Property: Licence Agreements*, EUROPEAN IPR HELPDESK FACT SHEET (15 May 2020), https://www.iprhelpdesk.eu/sites/default/files/newsdocuments/Fact-Sheet-Commercialising-IP-Licence-Agreements.pdfs

# CHAPTER 2

# CONFLICT IN NATURE: TERRITORIAL EXCLUSIVITIES VS. FREE MOVEMENT OF IP PROTECTED SUBSTANCE; IMPLICATIONS OF IP TERRITORIALITY FOR THE EU INTERNAL MARKET*

## 1. Introduction

From the universal perspective, a two-factor definition largely encapsulates the idiosyncrasy of intellectual property rights: territorial exclusivities over the creative outcomes of human intellect. On that note, territoriality of intellectual property rights and exclusionary effect they create collectively comprise the canvas when any matter of intellectual property law is to be scrutinized.

Territoriality in simple terms connotes the rights being limited, in effect, to the territory of the granting state. This therefore follows that initial grant of the rights, the area to which they extend and their enforcement are bound to follow the territorial patterns. Territoriality in a bigger landscape also infers the sovereignty of each state in crafting its intellectual property laws in a way to correspond to its economic, social and policy goals. The result is that intellectual properties are mostly granted protection only on national basis, in the way that the legislation of respective state desires.

Secondly, exclusivities indicate to the very reason behind the identification of the rights on intangibles as intellectual property rights, in which terminology certain attention must be paid to the analogy to proprietary rights. Although remarkable and merited contention exists as to whether 'property' falls relevant to intangibles, this analogy is justifiable to the extent -at least- that IP rights throughout the term of protection create an effect, that is exclusivity, analogous to classical proprietary rights.[70] The common thread of exclusionary nature is definitive of intellectual property rights on account that they authorize the right holder to exclude others from using the underlying intellectual property.

* Certain parts of this section of the dissertation have been published in: O. Bugra Beydogan, *Territoriality of Intellectual Property Rights Foundations of IP Territoriality and Reverberations of Territorial Exclusivities on Trade*, 18(4) Gemt Yavdaltai Temtsekh Asuudal, 117-128, (2020)

[70] Comparison of classical proprietary rights and intellectual property has been touched upon in the earlier parts of this study.

Subject matter of intellectual property, on the other hand, is often substantially commercial in nature and they are in the center of commerce. Further, such subject matter undeniably becomes more intangible as the time and technology advances. The whole intellectual property scenery entails, as it were, an attempt to capture a very abstract and universally mobile (dynamic) phenomena with a territorially static set of rules.

The grand total of territoriality and exclusivity equals to the insulation of national markets. The control of use -including commercial use- being monopolistically left to the right holder, hence making its consent central to the commercial activities involving incorporating goods and services within the territory of protection, intellectual property rights by nature are impediment to international trade. Further, this is justified on grounds of 'proprietary' interest of the right holder. However, resulting market insulation is devastating for international trade in general and for free trade in particular.

In this section we shall focus on these two inborn qualities of the intellectual property rights. In that we intend to comprehend, in turn, the origins of intellectual property territoriality and the how the latter has been also placed in the foundations of contemporary intellectual property laws. Secondly, we tend to unfold what the exclusionary nature of intellectual property rights precisely entails. Subsequently we shall discuss the ramifications of territoriality and exclusivity from the view point of international trade in general and free trade in particular. Finally, we shall illustrate the exceptionally important connotations of the exercise of territorial exclusivities, namely intellectual property rights, for the European Internal Market, whereby the founding principle of free movement falls in a sharp contrast with intellectual property. The essence of the problem, we strived to describe in this regard is also the spring of the European intellectual property law that has been formed so far. Hence, our main purpose shall be to depict what may be called a constructive clash: the dichotomy of territorial exclusivities and free movements.

## 2. Territoriality of IP Rights

In this fragment of the study, we will scrutinize the territoriality principle which, in a way, appear to be an inborn quality of intellectual property rights. However, in the different stages of the evolution of rights the patterns from which the consequence of territoriality distilled are variable, the territorial idiosyncrasy has largely persisted to the current day.

## 2.1. The Early Background

The earliest antecedents of relatively systematic intellectual property rights are traced back to European Venice and of the 15th Century,[71] although privileges of non-exclusive nature have been in place in the same proximity at least a century earlier.[72] Nevertheless, the exclusive privileges in these examples were not necessarily hinged upon inventiveness or originality but rather on the effort invested and ingenuity of the grantee.[73] Secondly, there was no statutory foundation of such grants[74]. In the essence, the rights were not actually conferred upon the introducers of new and useful arts and technologies[75] as private individual rights, but rather as a result of the will of the sovereign or a curtesy therefrom. It quite naturally followed that the exclusivities were limited to the territory under the rule of the sovereign or a fragment of it. By the same logic, violation of the privileges by the others, in substance, amounted to a violation against the sovereign.

The actual foundations of intellectual property laws of the contemporary sense, on the other hand, are largely believed to have been formed by the English statutory laws of the 17th and 18th Century, respectively the Statute of Monopolies 1624 and the Statute of Anne 1710. The former, at the outset, aimed at discharging the existing monopolies and re-constructing the system of privileges. In that, it declared void all existing monopolies with the exception of inventions, subsequently stipulated a substantive framework in respect to requirements and duration of privileges stemming from the invention.[76] The Statute of Anne granted the authors who publish in the Kingdom of Great Britain a sole liberty of printing and reprinting their books for 14 years, which is extendable to additional 14-year periods during the lifespan of the author.[77] The two statutes are deemed to have laid the foundations of modern patent laws, insofar particularly as they have altered the complexion of the rights from a discretionary 'royal favors'[78] into private rights that are available to anybody as long as the substantive

[71] For a detailed account of the 15th Century Venetian patents see: Giulio Mandich, *Venetian Patents (1450-1550)*, 30 J. Pat. Off. Soc'y 166 (1948); though, contemporarily, the first known record of patent is traced back to 1421, Florence; see: Frank D. Prager, *Brunelleschi's Patent*, 28 J. PAT. OFF. Soc'y 109 (1946)
[72] Frank D. Prager, *A History of Intellectual Property from 1545 to 1787*, 26 J. Pat. Off. Soc'y 711, 713 (1944);
[73] MARTINE C. RIFE, INVENTION, COPYRIGHT, AND DIGITAL WRITING 155 (SIU Press 2013)
[74] Although the Venetian custom of granting monopolies as such has been later confirmed in a written pronouncement, that is the Venetian Patent Statute of 1474.
[75] LYDIA LUNDSTEDT, TERRITORIALITY IN INTELLECTUAL PROPERTY LAW 73 (Stockholm University 2016)
[76] STEPHEN P. LADAS, PATENTS, TRADEMARKS, AND RELATED RIGHTS: NATIONAL AND INTERNATIONAL PROTECTION. VOL. 1. 6 (Harvard University Press 1975)
[77] The Statute of Anne: The First Copyright Statute <www.historyofinformation.com/detail.php?entryid=3389>
[78] Prager *supra* note 66, at 716.

requirements are met. However, the fact remains that in either case the rights expand only to the territories of the sovereign state.

The early initiatives, regardless of whether non-exclusive and discretional privileges granted by the sovereign or the first statutory examples of regulating intellectual efforts boil down to a utilitarian stance. The intent of Venetian state in aiding the technology importers was to spread the knowledge of new arts and techniques to societal domain.[79] Similar societal goals, perhaps more specific ones, were among the motivations in respect to the Statute of Monopolies and the Statute of Anne.[80] Quite evidently the prime purpose concerned is incentivizing and incrementing the introduction of the novelties that are of value to society, insofar as such corresponded to societal needs. Also, with the knowledge falling into the public domain; industrial and cultural progress being gradually realized through the artistic and inventive novelties, the social welfare eventually advances. This also enfolds another connotation that the sovereigns of nations have historically attributed certain social functions to inventive and artistic activities, therefore, the promotion and facilitation of these play certain roles in socio-political balance. This is coherent with the general perception that the privileges of this sort, both in a rudimental and modern senses, served as a policy instrument. The very ability of administering or customizing the borderlines of such privileges in early times and of intellectual property laws in modern times is undoubtedly central to attaining a great scale of policy objectives. In that, countries can design their intellectual property laws in a manner that facilitates the achievement of specific societal goals including encouraging the development of domestic industries, realization of the development agenda and protecting public health.[81] They were used as a means of public policy regulation to control and monitor industries.[82] It however needs to be highlighted that the society in the center of the utilitarian stance, and whose benefit is looked after in the context of industrial and cultural progress, obviously, denotes the society that is present within the territory of the sovereign rather than a global one.

At the end, having in mind the origin of privileges, that being the will of the sovereign authority, both non-exclusive privileges as far precursors and the earliest evidencable

[79] Id. 714
[80] Chris Dent purported that 'It is likely that one of the underlying motivations for the Statute of Monopolies was to encourage employment, as a major concern of the Parliament in the 1620s was the economy.' See: Chris Dent, *Generally inconvenient: The 1624 statute of monopolies as political compromise*, 33 Melb. UL Rev. 415, (2009); Similarly, the societal goal of the Statute of Anne was given in itself as 'encouragement of learning'.
[81] Emmanuel K. Oke, *Territoriality in Intellectual Property Law: Examining the Tension between Securing Societal Goals and Treating Intellectual Property as an Investment Asset*, 15(2) SCRIPTed. A Journal of Law, Technology & Society 316, 316 (2018)
[82] LUNDSTEDT, *supra* note 75 at 73

antecedents of intellectual property rights were of territorial nature. Even up to present day, this nature has hardly changed.

### 2.2. Towards the Modern Day

The emergence of the first statutory intellectual property laws, and reconstruction of the underlying concept as private rights as opposed to discretionary privileges, coincide the era where the nation-states tendency began. Accordingly, each nation is sovereign in the sense that it is solely competent to regulate and govern domestic matters within its own borders, correspondingly, domestic actions, principally legislative and administrative ones, have no effect abroad (extraterritorial effect) unless the respective foreign state permits.[83] Application of national laws therefore was bound to follow and to remain within the same territorial pattern, which evidently was the case for intellectual property laws as well.

The regulatory sovereignty also amounted to a good deal of flexibility to tailor overall legislative complexion of the countries, independent of what the views of other sovereign states are as regards the same areas. As far as regulation in the IP sphere is concerned, such a maneuvering room retains an exceptional importance. IP legislations are likely to be, and factually are, tailored to attain the basic policy objectives reflective of specific interest of the respective country, ranging from societal objectives such as promoting industrial and cultural progress and creative potentials, facilitating the access to knowledge, advancing the social welfare all the way to the economic objectives in a way to correspond to the selection of development agenda, such as incentivizing domestic production, controlling the competition environment in the market. Among all policy goals, as Pila & Torremans noted, economic self-interest has always -and even more strongly in the recent times- been the foremost determinant of domestic intellectual property laws and policies.[84] This has a great deal to do with the exact positioning of the country on the development scale, that subsequently represents an infallible parallelism to the market pattern of the country, in specific regards to whether it is the exporter or the import of the products of inventive and creative industries.

In most of the cases, states did not seem to have any interest in protecting the rights of foreigners in their countries, quite the contrary such protection would potentially impede the

[83] KUR & DREIER, *supra* note 35 at 12;
To that end territoriality is a general principle beyond intellectual property rights, SEE: PAUL TORREMANS (ED.), COPYRIGHT LAW: A HANDBOOK OF CONTEMPORARY RESEARCH 461 (Edward Elgar 2007).
[84] JUSTINE PILA & PAUL TORREMANS, EUROPEAN INTELLECTUAL PROPERTY LAW 30 (Oxford University Press 2019)

opportunity from benefiting from the new foreign inventions, or at best, attribute extra costs thereto.[85] In retrospect, more notably in early times of statutory laws, even those countries, which are today representing the leading exporters of creative and inventive industries, effectively endorsed so-called free-riding as a means of development. Thus, the lack of any protection accorded to non-national innovation has been made advantage of. This is even more so when the country in question stands on the underdeveloped end of the scale. An alike pattern can also be consistently seen to reappear in international realm as far as multilateral IP arrangements are concerned. Underdeveloped countries typically tend to accord lower standard of IPR protection so that technology importations would be less costly, whereas developed countries advocate for higher standards thereof thus the value created through IP is improved.

As one may effortlessly see, this freedom did not solely relate to delineation of what is protectable and what level of protection shall be provided but it also enabled a selective attitude as regards the beneficiary of protection, which is particularly relevant when the protection is sought abroad. Nevertheless, the fact remained that trading activities were in incremental growth and they have been widely liberalized from the territorial limitations as such. Already from early times on, in response to market related needs, and somewhat in the interest of justice, private rights of foreigners have started being respected on the mutual recognition basis.[86] Intellectual property rights however stalled, given that such recognition of foreign rights would have amounted -as we referred above- firstly to compromising the advantages of free-riding on foreign innovations; and secondly to a serious sacrifice from the policy tool function of national intellectual property laws. Despite such unwelcome connotations for the granting state, the factuality surfaced that the denial of protection for foreign nationals, in the long run, exhibited a deterrent to foreign trade, hence, injured domestic industries and the access of domestic public to foreign products and innovations.[87] When the situation is read backwards, this has also enfolded that the prevalent practice of denying the protection for aliens resulted for the countries in inability to protect the intellectual property interest of its citizens abroad.[88]

It was initially through the bilateral efforts that such downsides to intellectual property territoriality were addressed. The followed modalities usually concerned according extraterritorial effect to national intellectual property rights with a view to protect the citizens'

[85] LUNDSTEDT, *supra* note 75 at 84; KUR & DREIER, *supra* note 75, at 13
[86] Id. at 84
[87] Id. at 85
[88] Id.

intellectual property interests outside the national territories and, in return, recognition and enforcement of foreign rights would be ensured to the similar extent. In other words, reciprocity has been the common thread of the bilateral arrangements.[89] At the end however, not only did the aforesaid method soon engender a complicated web of bilateral IP arrangements on the interstate level,[90] but it also, to the extent that it structurally concerned only two states milieu, could not effectively correspond to multinational pattern of trading activities.[91]

It may be well argued that the most tangible benefit of the bilateral arrangements of 19th Century is having revealed the necessity of a more comprehensive and inclusive IP framework on the international scale. Towards the end of the 19th Century, such realization yielded the two major pillars of international intellectual property law: 1883 *Paris Convention* for the protection of industrial property rights and 1886 *Berne Convention* for the protection of literary and artistic works.

The bilateral arrangements that preceded the Conventions were, usually, constructed upon a strong requirement of reciprocity[92] with a likely aim of achieving national treatment.[93] The Conventions, so to say, jump-started this ideal and have taken the national treatment principle as one of their pillars from the outset. National treatment clauses contained in the Conventions, in essence, implicitly strengthened the territoriality principle; as such, for the foreign nationals to be treated equally as the nationals required: (i) the national IP laws to set the standards in the respective territories; (ii) the foreign nationals within the respective member country's territories to be treated in the equal manner as the domestic nationals. So did the principle of minimum standards. In that, the Conventions, though with some limited exceptions in the Berne Convention, ruled out material reciprocity and, instead, required the states to provide for the minimum standards as per the Conventions.[94] That is to say, through

[89] PILA & TORREMANS, *supra* note 84, at 30
[90] For an overview of bilateral copyright arrangements, see: Samuel Ricketson, *The Birth of the Berne Union*, 11 COLUM.-VLA J.L. & ARTS 9 (1986); in respect to industrial property rights see: LADAS, *supra* note 68 at 43.
[91] PILA & TORREMANS, *supra* note 84, at 31
[92] William R. Cornish, *The International Relations of Intellectual Property*, 52 Cambridge LJ 46, 48 (1993)
[93] SAM RICKETSON, THE PARIS CONVENTION FOR THE PROTECTION OF INDUSTRIAL PROPERTY: A COMMENTARY 26 (Oxford University Press 2015); Drahos states that the bilateral arrangements operated on the basis of national treatment principle which in itself was an outcome of (formal) reciprocal adjustments; see: Peter Drahos, Intellectual Property and Human Rights, 3 I.P.Q. 349, 351 (1999). It should however be noted that while formal reciprocity concerns the existence of the rights of foreign nationals (who, then, may be treated as nationals) on bilateral basis, material reciprocity determines the extent of the rights accorded to foreigners on reciprocal basis. On the nuances between formal and material reciprocity and national treatment, see: Silke von Lewinski, *Intellectual Property, Nationality and Non-Discrimination* (In INTELLECTUAL PROPERTY AND HUMAN RIGHTS: A PANEL DISCUSSION TO COMMEMORATE THE 50TH ANNIVERSARY OF THE UNIVERSAL DECLARATION OF HUMAN RIGHTS, GENEVA, NOVEMBER 9, 1998 175 (World Intellectual Property Organization 1999)
[94] LUNDSTEDT, *supra* note 75 at 87

the Conventions the signatories perpetuate the liberty to design the national intellectual property law and policy, so long as the minimum standards in safeguarding the rights are met, thus, independent from the other contracting states beyond the minimum standards.

On the other hand, the approach taken in the Conventions -the approach that added up to territoriality- is largely due to the inherent difficulty of providing further approximation of intellectual property legislation on a global level. Indeed, among the other alternative approaches, the ideal of a unitary law was spoken out throughout the preparation phases of both Conventions without, however, leading to much arguments supporting its possibility.[95] Clearly, a unified setting of global intellectual property regime, in which an immense number of states are involved, tends to overlook the vast gap of socio-economic and industrial diversities between those states; and by mandating a single regime for all, it unduly equates all the participating states. Secondly, even in the far assumption that a creation of the unitary regime, at the cost of ignoring the intrinsic diversities of the countries, has been agreed upon, then the question as to the level and standards of protection will persist being insoluble. As we pointed out above, socio-economic welfare and the industrial development level is the utmost determinant of whether a high or a moderate level of IP protection is more favorable in respect to interest of each individual country. Depending on these motives the diverse interests therein are liable to contradict, hence rendering almost impossible the attainment of a standard of protection that pleases all the members.

Accordingly, what clearly surfaces is that the ideal and -more importantly- functional supranational regime is to consist of the compound of national treatment and minimum standards of protection. The former predicates on the national legislations to be in place and subsequently to expand to the foreigners in its territory; and the latter, minimum standards having been met, leaves the room to the national legislature to shape up the laws in the direction of the country's interest. Both elements in themselves signify, and in fact, strengthen the principle of territoriality of IP rights. In the same vein, and more recently, TRIPs agreement, drawing on the policy tool function of intellectual property regulations, confirms the territorial nature of intellectual property rights. In that, it maintains that the member states, as long as consistent with the Agreement, may formulate their laws and regulations and amend them, likewise adopt certain measures in order to protect public health and nutrition, and to promote

[95] For a chronology and overview of the discussion on alternative approaches see: MIREILLE VAN EECHOUD, CHOICE OF LAW IN COPYRIGHT AND RELATED RIGHTS: ALTERNATIVES TO THE LEX PROTECTIONIS 58-68 (Kluwer Law International 2003) in respect to Berne Convention; see LADAS, *supra* note 75 at 61-63 in respect to Paris Convention.

the public interest in sectors of vital importance in consideration of their socio-economic and technological development.[96]

It should, however, be noted that it is fairly misleading to confine the still-existing IP territoriality to a mere desire of individual countries to perpetuate the policy instrument function of intellectual property laws. Although this desire is inarguably true and it persists being a prevalent motive, the existence of IP territoriality principle is also owed to the improbability of a unified global legislative framework. The two motives, thus, factored in the retainment of the principle of territoriality up to the day.

In the end, notwithstanding whatever motive has been most influential over the ever-persistence of territoriality, the latter has been, beyond argument, a defining character of intellectual property rights. Despite the incremental supranational legislative progress in the realm of intellectual property, the territorial quiddity, along with its consequences, made their way to the present times. The said consequences saturate to a great area which tends to include pure legal and procedural issues such as the emergence of rights, jurisdictional matters and the questions pertaining to enforceability of the rights, as well as those which relate to rather practical dimensions, cross border commercial activities in general and trade in goods in particular. In the outlines however, as we discussed above and Pila & Torremans likewise illustrated, the connotations of territoriality are susceptible to be subsumed under three headers. Firstly, the rights are principally conferred by the national laws of each individual state, therefore stemming from territoriality, the rights are national in nature. Subsequently and by extension, the legal effects of the rights conferred are delineated by the territorial reach of the conferring state. Lastly, from a procedural view point, the rights are enforced by the national courts of the conferring state through application of domestic laws, rulings of which likewise, in effect, are bound to remain territorial.[97]

### 3. Exclusionary/Monopolistic Character of IP Rights

The defining characteristic of intellectual property rights is the conferral of certain exclusivities to their holders. Such characteristic typically entails two pillars: (i) the warrant (or power) of the right holders to exploit the invention or the work in respect to which intellectual property rights granted; (ii) to exclude the others from availing themselves of IP

[96] Article 8 TRIPS Agreement
[97] PILA & TORREMANS, *supra* note 84, at 28.

protected invention or work, hence creating a set of exclusionary and monopolistic nature of rights in favor of the right holder. Nonetheless the first element is mostly rhetorical; the creator of the intellectual property does not actually need an authorization to exploit it. The merit of the IP rights therefore resides at the exclusionary character. It is also this exclusionary character that helps the lawmaker attain its goals that it intended by granting the rights. Though philosophical background and objectives underlying the grant of rights differ, their realization depends on constant and enhancing intellectual creativity.

On the end of those who create, without exclusivity afforded by the IP laws, creativity would be a burden rather than a trait or an advantage. This is because it would allow the others, which are likely to be with competing interest within the same sector, to free ride the creative outcome, with no self intellectual endeavor and developing costs attached, hence taking up or removing the profits of the original inventor/creator who actually is intellectually and materially invested in the work. Said exclusivity directs to the right holder any value embedded in what is protected. Secondly. It confers, from an economic view point, the authority of determining that value when the rights -as property objects- or the goods incorporating the intellectual property are to be commercialized.

Intellectual property rights do not give the recoup itself; but they prepare the ground of financial retribution. Though leaving the rest to the actual market worth of the invention or the work as well as marketing abilities of the right holder. In short, the ground prepared by the intellectual property laws - amounts to the exclusivity (or monopoly) of the rights and safeguarding thereof. That is to say the value of what is protected by IP rights is as dependent on the exclusivity as it is on the actual intellect (knowledge) embedded in the work/invention.

Beyond this abstract background, though exclusivities fluctuate from one genre of intellectual property to another, the general outlines remain alike: they give the creator (or the right holder)[98] of the works or inventions the exclusive right to use it. Hence, the terminology of ‘use’ depicts a generously large area and this is what actually differs from one type of intellectual property to the other. As far as patents are concerned, exclusivities pertain to the commercial manufacturing, exploitation, sale, distribution, import and export of the protected invention, meaning that the right holder retains the exclusive warrant in engaging in these activities as well as in authorizing or excluding the others to do so. Copyright and related rights,

[98] Noteworthy however, the creator and the right holder may not always coincide on the same body, for example some employee inventions belong to the employer even though the creator of the work in real terms is the employee. Therefore, it befits using the term ‘right holder’ instead of that of creator.

on the other hand allow the creators of the literary artistic works the exclusive right to engage in and exclude the others from producing copies of the work, performing and displaying it, communicating it to public, and distributing the produced copies of the work. Furthermore, certain non-economic interests are also to avail of copyright protection.[99] Trademark protection likewise confers on the right holder the exclusive power to commercially exploit the mark, which foremost covers the manufacturing of the goods bearing that mark and the initial sales of them as well as offering services under that mark. In the same vein, the right holder retains the authority of permitting – and certainly that of prohibiting- the use of the mark by the others. Such a permit typically emanates as licensing agreements.

The fabric of intellectual property rights is identified by territoriality and exclusionary impact that they naturally and functionally institute. The reality remains, however, that intellectual property rights, thus the consequences of the aforesaid qualities thereof, are inextricably entangled with the tangibles in which they are embodied. A major portion of such tangibles that, in one way or another, interface with intellectual property rights amount to 'goods' for the purposes trade. In other words, nearly all goods and services that are subject to commerce -particularly to trade- has at least one or more intellectual property attached to them: a patented technology, a trademark, a copyright protected content or an industrial design. Further, this is the case for pretty much any good conceivable, from a simple loaf of bread which bore a brand on it to a smart phone, a cluster of dozens of patented components, designs, copyrighted apps etc. The rights emerging from the latter, namely the exclusivities, could -by the reason of territoriality as we referred above- principally be granted, safeguarded and enforced by the national laws and finally the reverberations of these would be restricted to the territory of the state whose national laws applied. Conversely, the subjects of IP protection seem to have severed all ties with the national territorial lines, with the help of ever-expanding cross border trade activities as well as that of the major advancements in digital and communicational technologies that facilitated the formation of a supranational market place above the national ones. Furthermore, certain contemporary forms of IP subject matter undeniably, either resulted from the said advancements in various digital technologies or -at least- communication of them along with many sorts of intellectual property thus became effortless. Therefore, such IP subject matters, being mostly but not exclusively copyrighted

[99] Article 6bis of the Berne Convention recognizes the moral rights as follows: "Independently of the author's economic rights, and even after the transfer of the said rights, the author shall have the right to claim authorship of the work and to object to any distortion, mutilation or other modification of, or other derogatory action in relation to, the said work, which would be prejudicial to his honor or reputation."

content, structurally remain free from physical territories. One could infer therefore that the intellectual property subject matter is less and less territorial, while the intellectual property rights still are.

### 4. Market Segregating Effect of National Intellectual Property Rights

Following from the territoriality principle, the same intellectual property -be subject of a trademark, patent, design, copyright etc.- separately and independently forms as many national rights as the number of countries where it is protected; further, none would normally entail an extraterritorial effect. This implies, for instance, that a trademark is held by someone in the country A meanwhile the same mark is held by someone else in the other country, B. Likewise the patent to one invention is registered by the inventor in A, naturally granting the right holder the exclusivities within its territory. Correspondingly, anybody may freely use the invention in another country where the protection is absent.

The exclusivity entails *inter alia* the right to use the intellectual property and that of importing the goods and services bearing them into the country of protection. Therefore, as far as the first example goes, by invoking its trademark rights in country A, the right holder may prevent the importation into country A of goods that have been legally produced by a third person in country B. Similarly, on the basis of the second example, the patent holder in the country A may invoke its rights to exclude the importation of the invention in question into A from the other countries where it may or may not be protected by another patent. In either case, such exercise of intellectual property rights serves to insulate the market of the country of protection from the imported goods, hence vesting the right holder with a rigid monopoly with respect to that particular market. This insulation, thus the monopoly, represents the very instrument, in favor of the right holder, to territorially control the level of prices and the volume of supplies insofar as outsourcing from foreign markets becomes impossible without the right holder`s consent. This is the result foreseen, and partially aimed, by intellectual property laws. While the latter represents the inherent function of national intellectual property rights, what appears problematic is that the same result (i.e. segregating national markets) could normally be achieved even if different rights protecting the same subject matter are held by the same or economically tied person(s) in different territories.[100] Quite evidently the latter case is the utmost reality: Different national rights, that is to say parallel rights, are readily held by the

[100] Norbert Koch & Franz Froschmaier, *The Doctrine of Territoriality in Patent Law and the European Common Market*, 9 PAT. TRADEMARK & COPY. J. Res. & ED. 343, 345 (1965)

same bodies in respect to products and services that are commercially available worldwide. Intellectual property rights, having allowed the monopoly on imports along the national lines, are often used by the right holders solely with a view to deploying such national barriers, hence ruling out the inter-brand competition between the initial supplies and parallel imported ones.

***The example of parallel trade***

Parallel trade activities, amid the contention of the territorial exclusivities and cross-border trade, lucidly exhibit the market partitioning effect when intellectual property exclusivities approximate national monopolies over the commerce of the related goods and services. Parallel trade eventuates when the parallel importer (the term connoting any party other than manufacturer of goods) transfers the goods to a second country which was not initially designated by the manufacturer for that particular consignment of goods.[101] Such acts typically transpire when the manufacturer sells the goods in question in both country of origin (for that consignment of goods) and that of destination (where the parallel trader imports the goods into), therefore, what the parallel trader commences is to open a stream that is parallel to the manufacturer's intended distribution structure in regard to the destination country.[102] In a way, the parallel importer functions as an unauthorized distributor of the goods in the second country. Needles to reiterate that the goods that subject to parallel trade are authentic ones and were initially introduced to the market by the legitimate manufacturer Frankly, on the other hand, the motive behind the parallel trade is to benefit from the price level differentials between the origin and destination markets -the control of which otherwise rested with the manufacturer- thus making profit. It is therefore emblematic that the prices level in the origin country is lower than that of the destination country. However, capitalizing the price differences is not only spur to ignite parallel trade moves. Alternatively, the reason why an outsider imports the goods into a non-designated country may be motivated by the lack of that particular good in the destination market. Manufacturers, by choice or by the force of circumstances (e.g. due to low demand, or a strategical refrainment from the market), might have refused placing the goods in the second country. In that case, the parallel importer avails himself of the exclusion of the destination market, thus seizing upon the benefit thereof the manufacturer neglected or refrained from picking up.

[101] CHRISTOPHER STOTHERS, PARALLEL TRADE IN EUROPE: INTELLECTUAL PROPERTY, COMPETITION AND REGULATORY LAW (Bloomsbury Publishing 2007)
[102] Id.

From the outset, such alternative trading activities virtually amount to an interference with the manufacturer`s intended distribution chain, stripping the manufacturer entirely or partially of its command on (and the privilege of) market designation. This is, in itself, susceptible to create notable adverse effects on the economic performance as well as on the envisaged business model of the manufacturer. Further, certain ramifications of parallel import are apt to evolve the image of the product, hence that of the brand and the manufacturer, for the worse. The first conceivable scenario in that is the potential disorganized and off-the-grid marketing conditions in the destination market in a way as to undermine the brand image. Given that in most cases the commercialization of the goods in the designated markets is carried out through standardized visual and operational schemes -that combined encapsulate the brand image-, many components, in case of parallel trade in the realm of which the manufacturer does not retain control over such elements, may fail to meet the standards. Inherently such connotes a large realm, ranging from the supply channels to the end buyers and to wholesalers, all to way to the quality of the advertisements introducing the goods and their presentation by the parallel trader. This particularly, however not exclusively, becomes an issue when the goods in question cater to high-end needs and characteristically retain a notable 'allure, prestigious image and aura of luxury'.[103] Also, a constant travel of the goods from the origin market towards the alternative ones wherein parallel importers hope making profit tends to impede the balance and capacity of supply, purging the origin country of the goods and potentially creating product shortages there.[104]

In either case instabilities in the origin market, say, supply shortages and subsequent rise in the prices, as well as those in the destination market such as marketing conditions beneath the habitual quality of that of manufacturer or capacity problems as to further supplies and post-sales services are likely to be perceived, by the customers -especially by consumers-, as to cause from the manufacturer. Thus, one may say, the sequences of parallel trade are not quite favorable on the account of the manufacturer in majority of the cases. Nevertheless, insofar as the goods in question are authentic ones and as they have been first put in the market by the manufacturer, parallel trade activities neither identified completely illegal nor have they been deemed fully legal by a uniform perception; hence notoriously addressed as 'gray market'.

[103] This definition has been articulated by the European Court of Justice in the case (C-337/95) Parfums Christian Dior SA and Parfums Christian Dior BV v Evora BV in respect to use of the trademark of a top-notch perfume by a parallel importer in advertising.
[104] STOTHERS, *supra* note 101, at 22.

Adjusting the above explained scheme into the context of intellectual property, all the cross-border trade that is carried out by those other than the IP right holder in the destination country itself or those authorized by the latter amount to parallel trade. This is exactly where intellectual property rights come into play so as to keep the others from engaging in trade activities as such, the kind that tends to take away -or free ride on- certain exclusivities of, and that could potentially be harmful to, the right holder. The absolute territorial protection conferred by a national intellectual property right converts to the effect of partitioning the market on national lines, therefore insulating each national market from parallel imports.[105] Hence, intellectual property rights, being territorial exclusivities as discussed at length above, represent the ultimate response of the national right holder to the trade activities of this kind. In the simplest equation, the grand total of exclusivity and territoriality, more precisely the territorial exercise of the exclusivities, equals to secluding the national markets from one another in respect to IP protected goods; the impact which retains an extremely vital importance in the realm of European Internal Market as shall be depicted below.

**5. Interim Conclusion**

From the historical perspective, ever since the earliest antecedents of intellectual property rights made an appearance, the idea is to privilege the creators and/or introducers of new arts and technologies with a view to reward, promote etc. their knowledge, intellect or ingenuity. Although, the way as well as the philosophical bearings for doing so have remarkably varied throughout the history up to the present day, the core of said phenomena remained as giving out to those, at first, certain privileges; and later exclusive rights over their works. As far as the radix of such exclusivities is concerned, though the underlying philosophy as to the origin of rights has also materially evolved over time, they are at first granted by the head of the state, then evolved to personal rights that are safeguarded and granted by the law. In both ways, the mandate of exclusivities was bound to remain territorial, since the contrary would amount to encroaching upon the other monarchs` or states` area of sovereignty. Fast forward to the end of 19th century, inevitable necessity of a multilateral intellectual property framework came to fruition. Only plausible way in constructing a global framework, however, appeared to be that of abiding by the national laws of sovereign states, albeit aligning and enhancing them as to provide certain minimum standards. Hence, territoriality being preserved

[105] CATHERINE BARNARD, THE SUBSTANTIVE LAW OF THE EU: THE FOUR FREEDOMS 157 (1st ed. Oxford University Press 2004)

up to the day. In summary, for demonstrative purposes, it may be plausible to lay the elemental quiddity of intellectual property as follows:

> *Exclusivity*, defining element of contextual nature of intellectual property rights; *Territoriality,* defining element of rise of the rights and the protection accorded thereto.

The two defining elements, territorially exercised exclusivities, together, boil down, albeit usually for a limited time[106], to the monopoly of the national right holder. However, the monopolist practices as such, and as illustrated above, are objectively not a dark side of intellectual property rights (quite the contrary in fact, they are the very purpose and the essence thereof), the subsequent impact remains: market partitioning. Unless such a use is restrained by law -the case which is exceptional as we shall see- intellectual property rights are keen to insulate the markets from imports (also from the exports as the counter part of imports), regardless whether the rights in different territories are held and exercised by the same body (or the agents of the same body) or by entirely different bodies.[107]

On a final note, it is necessary to stress that the ramifications of the territoriality and exclusivity are not only apparent in the parallel import cases, latter connoting the goods movement, but they are also as topical in relation to cross-border supply of services that entail intellectual property. Intellectual property rights can (and they have) also come into conflict with the freedom to provide services.[108]

## 6. Particular challenge for the European Internal Market

### *A brief look into the Internal Market: Free movement and undistorted competition as the constituent of the Internal Market*

The Community tasked itself primarily with establishing a common market,[109] as it was further detailed in the Article 3 of the Rome Treaty, that would be characterized *inter alia* by (i) the elimination of customs duties and of quantitative restrictions on the import and export of goods, and of all other measures having equivalent effect between the Member States; (ii) the establishment of a common customs tariff and of a common commercial policy in respect to third countries; (iii) the abolition of obstacles to freedom of movement for persons, services

[106] With the exception of trademark.
[107] This very scenario has been in the center of the ECJ`s early doctrine of 'Common Origin', to which we will turn in the ensuing parts of the study.
[108] KEELING, *supra* note 9 at 22
[109] Article 2 Treaty of Rome

and capital; (iv) the institution of a system ensuring that competition in the common market is not distorted.[110] The envisaged integration into the Common Market, shall be initially based on a customs union[111] that covers all goods in trade, in that, Member States are obliged to refrain from introducing new customs duties on imports or exports or any charges having equivalent effect, and from increasing those which they already apply in their trade with each other.[112] Moreover, existing custom duties between the Member States are to be progressively eliminated.[113]

An updated terminology[114] of the envisaged market model and a first-hand definition thereof has been introduced into the founding Treaty by the Single European Act and remained intact ever since. Accordingly, as now contained in Art. 26(2) of the Treaty on the Functioning of the European Union (TFEU) '*The internal market shall comprise an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of the Treaties*'.[115] The fundamental freedoms thus identify the most prominent characteristics of the Internal Market. Moreover, these characteristics are not complementary but constitutive in nature. In other words, free movement is not a result of an internal European market but, rather, the existence of such a market is hinged on the achievement of these freedoms. To this end, free movement principle is the foremost integrating factor and an ongoing task.

The second pillar of the internal market is constructed by the principle of undistorted competition. Although the above-referred internal market description of the TFEU does not per se address the constructive role of competition rules, it was concretized by a multitude of provisions in the founding treaties and confirmed by the European jurisprudence as well as other auxiliary sources. To start with, the Treaty of the European Union (TEU) characterizes the internal market as '*a highly competitive social market economy*'[116] and that market is to include a system ensuring that competition is not distorted.[117] This connotes a constitutional aim of the Union. Secondly, substantive competition rules encapsulated in the TFEU (Art. 101

[110] Respectively, Article 3(a), 3(b), 3(c) and 3 (f) Treaty of Rome
[111] Article 9 Rome
[112] Article 12 Rome
[113] Article 13(1) Rome
[114] However, acknowledging the nuances between these two notions, in order not to exceed our purposes, we shall not delve into such an analysis. For a comprehension on that issue, see: Lawrence W. Gormley, *Competition and Free Movement: Is the Internal Market the Same as a Common Market*, 13 Eur. Bus. L. Rev. 517 (2002)
[115] Treaty on the Functioning of the European Union, Article 26(2)
[116] Article 3(3) TEU
[117] Protocol No 27 on the internal market and competition, annexed to the Treaty of Lisbon (OJ 2010 C 83, at 309)

and 102) regards the anti-competitive behavior[118] described in those articles as '*incompatible with the internal market'* and prohibit them for that reason. Therefore the *raison d'etre* of the competition rules is the internal market itself. Particularly in both provisions, such behavior is prohibited to the extent that their object or effect is the prevention, restriction or distortion of competition within the internal market[119]; or that may affect the trade between the Member States.[120] To that end, undistorted competition and the rules ensuring thereof retain a constitutive value in the market integration. Moreover, it must be borne in mind that free movement provisions, in general, remove the legal obstacles to trade between the Member States; commercial behavior of the market participants does not directly fall into this ambit. Competition rules prevent the practical reconstruction -by private undertakings- of barriers to trade between the Member States, which were otherwise eliminated by free movement provision.

***The Conflict in Nature***

Creating a realm of monopoly within the national frontiers, therefore capturing a financial value, that is -depending on the theory and policy objectives of the respective law- attributable to the purposes of compensating, rewarding or incentivizing the intellectual effort, and to recoup the resources invested;[121] and in addition, on the business level, converting the

[118] Behavior is construed broadly such as to cover agreements, decisions as well as concerted or unilateral practices.

[119] Art. 101(1) TFEU

[120] Art. 102 TFEU

[121] It should however be noted that, when defining the functions and objectives of intellectual property laws, an all-pervasive language scarcely falls appropriate. The above-referred ones, at best, portray an abstract panorama of such functions and objectives. Not only such drives, underlying the grant of intellectual property rights, differ in accordance with the theory and policy behind the laws of the granting jurisdiction, but they also, inevitably, vary from one type of intellectual property right to another [For an overview of different arguments for patent protection see: FRITZ MACHLUP, AN ECONOMIC REVIEW OF THE PATENT SYSTEM 21 (US Government Printing Office 1958); Fritz Machlup & Edith Penrose, *The patent controversy in the nineteenth century*, 10(1) The Journal of Economic History 1 (1950); for a wider undertaking on various justification of intellectual property rights and accompanying functions and objectives, see: PETER DRAHOS, A PHILOSOPHY OF INTELLECTUAL PROPERTY (Routledge 2016) and ROBERT P. MERGES, JUSTIFYING INTELLECTUAL PROPERTY (Harvard University Press 2011). Moreover, just as different objectives and proprietary theories might accumulate in the backdrop of the grant of rights, some national laws may lack a clearly discernable pattern for that matter. In the same direction, Ricketson notes that *"Each of these arguments has respectable philosophical and/or economic or social theories underpinning it, with variants of each as well as hybrid justifications that have run several together. Indeed, protagonists on both sides have not hesitated to use whichever argument or arguments suited their purpose at a particular time."* See: RICKETSON, *supra* note 93 at 11.
Indeed, the diversity of theoretical and teleological backgrounds of different laws was the merit of the criticism levelled against the specific subject matter doctrine of the European Court of Justice (discussed in Chapter 3 of this study) to the effect that it often spoke of 'rewarding' the creative effort (See, for instance, the rulings in C-241-242/91: *RTE and ITP v. Commission (Magill)* in respect to copyright and in C-15/74: *Centrafarm v. Sterling Drug* in respect to patents) without basing this belief on a substantive analysis of the national law(s) in question (To that effect, see: KEELING, *supra* note 9 at 68; Francis G. Jacobs, *Industrial Property and the EEC Treaty: A Reply*, 24 Int'l & Comp. LQ 643, 657 (1975)). As noted by Korah, the reward function is not the only influential

exclusive privileges over intellectual creations and commercial reputation into a competitive strength; all these represent the right holders` principal interest in and expectancy from intellectual property rights. Relying on that very ground, the right-holders retain the exclusivity to manage, and by extension cut off, the importation of the incorporating goods, as well as cross boarder supply of services. It is a matter of fact that any impediment on imports would also mean cancelling out its counterpart: exports. Therefore, no good -that incorporates an intellectual property right- could possibly be subject of free trade unless the holder of the right allows.

At the macro level, intellectual property, more particularly the national level of regulatory sovereignty, is notably potent to reflect and promulgate the preferred economic policies insofar as it enables an ample maneuvering room in realization of such policies. The countries are likely to address their own unique economic, industrial and even social needs in their intellectual property laws, in the balance of which the level of development plays a key role. In line with the profile of the country, the fundamental fine-tuning that IP laws are concerned with being that of whether to prioritize the protection (hence the exclusivity) or the availability new technologies and arts to public so as to facilitate the industrial and cultural progress. Conceivably well-developed ones tend to prioritize the exclusive interest whereas the others are concerned with adding up more to the public domain, hence the interest of access. Such distinct needs eventually give rise to distinct intellectual property laws; while difference as such is susceptible to create yet another obstacle to free trade, and correspondingly, competitive environment between domestic and foreign products.

The set of problems that intellectual property and free trade equilibrium inevitably faces is both a result of and caused by IP territoriality. Free trade is the system that tends to erase the obstacles to good movements starting with territorial restrictions and continuing with removal of regulatory restrictions. Intellectual property rights on the other hand sharply deploy the territorial restrictions so as specifically to stop what free trade does, further, it relies on a proprietary right in doing so. The persisting territorial trait, whether as appears in exercise of territorial exclusivities or in form of domesticity of IP laws and divergences thereof, leaves the markets vulnerable to get sharply divided by the national borderlines as regards the commercial

motive prevailing in the continent [See: Valentine Korah, *National Patents and the Free Movement of Goods within the Common Market*, 38(3) Mod. L. Rev. 333, 336 (1975)].

activities involving the goods and services embodying the intellectual property rights; or, at best, otherwise inhibits the commercial activities as such.

From the outset, the founding pillar of the European Union resides at the aim of establishment and proper functioning of a Single European Market. The latter connotes an area where the internal borders are eliminated, so that goods, services, persons and capital move freely. Principally, once goods are lawfully marketed in one Member State, they may freely be transferred to any other Member State; they may be bought, sold, used there. The ultimate aim being to unify the national markets of the Member States into one Single Market, (i) custom duties and charges having an equivalent effect; (ii) discriminatory and protectionist tax provisions; (iii) quantitative restrictions on imports and exports and measures having equivalent effect are strictly prohibited. Further any restrictions, regardless whether direct or somehow disguised, to these movements are shown, if at all, very little tolerance. Nevertheless, the sub-elements of the conceived Single Market are the sovereign Member States whose national legal systems, thus intellectual property laws, are necessarily territorial.[122] Therefore at default, the exercise of intellectual property rights quite feasibly evolve to trade barriers between the Member States. Intellectual property rights functionally represent a tough challenge to creation of the envisaged Single Market.[123] On that note, the reason why the territorial quiddity of intellectual property poses an extreme challenge to the EU is rather explicit.[124] There is an inevitable conflict between the free movement principle and the protection of exclusive rights which are limited to the territory of a Member State.[125] Hence, the goal to ensure free movement of goods over national borders within the Single Market is liable to clash with the principle of territoriality governing intellectual property law.[126]

It may well be asserted that the prerequisite to a due apprehension of the European Intellectual property law in general and of any specific matter branching out from the latter, is the acknowledgement of two contrasting concepts on its very canvas. That is the sharp dichotomy of territorial rights versus free movement of goods. Each one of the contrasting concepts are of existential importance respectively to very concept of intellectual property and to the institution of the European Union. From many aspects the two are seemingly in an absolute hostility that makes it impossible for them to coexist. Say, A is a patented

[122] CATHERINE SEVILLE, EU INTELLECTUAL PROPERTY LAW AND POLICY 311 (Edward Elgar Publishing 2016)
[123] BARNARD, *supra* note 105, at 156.
[124] KEELING, *supra* note 9, at 22.
[125] Id.
[126] KUR & DREIER, *supra* note 35 at 45.

pharmaceutical in France, but the patent protection has not been obtained, for some reason (that may be due to unavailability of patent for pharmaceuticals in the domestic law, or entirely preferential), in Italy. Another manufacturer in Italy embarks on producing the same pharmaceutical as A`s patent incorporates and sells it to the domestic market. Naturally, anyone may obtain the generic pharmaceutical from the Italian market with a view to exporting them to other Member States, and free movement principle perfectly allows that. What would be the situation if France, where the pharmaceutical is protected by a patent, was one of the targeted exports markets? Is a trader allowed to import them to France, despite the patent; or could the holder of French patent stop this importation by invoking his/her patent (or bring an infringement action if import is already occurred)? Aforesaid depicts a typical parallel import case, and not surprisingly the first appearance of intellectual property rights in the horizon of the European Union law was in the context of parallel import cases.[127] For another example, take a literary work that is automatically protected by copyright. International conventions set out a minimum term protection of 50 years in addition to the lifespan of the author,[128] therefore, Member States, in principle, are free to accord a longer term of protection than the minimum requirement. On that note, say, a book the author of which passed away 60 years ago has already fallen in public domain in one Member State, insofar as it offers copyright protection for author`s life + 50 years; meanwhile it is still protectable for 10 more years in another since the latter offers 70 years of protection *post mortem auctoris*. What if the work in question is published freely in the first Member State and someone wants to import it to the second Member State where the protection is still intact? Are the successors of the author able to bar the importation relying on the copyright, or the importation is allowed pursuant to free movement provisions?[129] However, the collection of the examples can be enriched towards other types of intellectual property rights, this far sufficiently demonstrates the inevitable tension that initially existed between the free movement principle and intellectual property protection.

At this point it is worth pausing to recall two different, albeit logically interconnected, outlooks of territoriality. First, territoriality connotes the independency and individuality of IP laws of each Member State, in a way to correspond to its idiosyncratic industrial, economic

[127] Id.
[128] Article 7 of Berne Convention for the Protection of Literary and Artistic Works as amended on September 28, 1979.
[129] A question of this manner had presented itself in the dispute underlying EMI v. Patricia judgement of the ECJ (Case C-341/87: EMI Electrola GmbH v Patricia Im- und Export and others) discussed in Chapter 4.

and social circumstances; the flexibility, as an outcome of sovereignty, to craft the IP laws as those circumstances necessitate or otherwise desired. Albeit, international framework set the lower bars in some respects, said flexibility may quite liberally extend beyond those minimum standards. This being the case, the end result is ample discrepancies between national laws. These discrepancies coincide certain substantive provisions of different national laws such as duration of protection, requirements for the grant of rights, covered subject matters by each type of intellectual property right etc. Such provisions may lead to situations, as demonstrated above, in which a product that is lawful in one Member State would virtually become an infringing product when marketed in another Member State.[130] Second connotation, on the other hand, is the limitedness of national IP laws, hence that of the rights granted by them, in their effect, to territories of those countries, regardless of whatever manner they are crafted in.

The problems created by the first implication of territoriality, that are the ones stemming from the discrepancies between the national laws of Member States, have their built-in formula: leveling out the different substantive provisions of national laws wherefrom the impediments originate. Said approach, that is of removing the problematic discrepancies, hence, aligning the national laws, is notoriously known as harmonization. Once the laws defining the scope of protection were harmonized among all Member States, problems that the first connotation entails are less likely to occur. This formula has been utilized, for example, in circumventing the aforesaid issue arising from -initially- divergent terms of copyright protection. In that, the duration of the protection afforded to copyright and related rights has been harmonized by the Term Directive[131] as 70 years *post mortem auctoris* and 50 years respectively.[132] Therefore the adverse effect of the inharmonious national copyright terms on the commercialization of copyright protected goods or services in the Internal Market has been eliminated for the most part.[133]

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[130] KEELING, *supra* note 9 at 25

[131] Directive 93/98/EEC of 29 October 1993 harmonizing the term of protection of copyright and certain related rights (subsequently replaced by "Directive 2006/116/EC of the European Parliament and of the Council of 12 December 2006 on the term of protection of copyright and certain related rights" and amended to its present form by "Directive 2011/77/EU of the European Parliament and of the Council of 27 September 2011 amending Directive 2006/116/EC on the term of protection of copyright and certain related rights.")

[132] The central rule of the Term Directive is a 70-year copyright protection term. Around this main rule, the Directive specifies the situation for joint authorship, anonymous or pseudonymous works, collective works, legal person vis-à-vis the moment when the specified period starts running. As regards related rights, the fixed period of 50 years starts running from the date of performance (performers rights), fixation (rights of producers of phonograms and of film producers), and first transmission (rights of broadcasters). Though the said term is liable to run from a later date depending on the date these are published, communicated to the public or broadcast.

[133]In the face of certain scholarly observations regarding the actual serviceability of the term harmonization, it is worthwhile underlining the expression "for the most part". It is emphasized that the Term Directive and the

Nevertheless, as Keeling points out, harmonization of laws may tackle some of the problems in this area, however it cannot solve all of them. As a matter of fact, it cannot address the most difficult ones, because they are due, not to discrepancies in national law, but to the territoriality of intellectual property rights.[134] Accordingly, the second connotation still prevails notwithstanding how comprehensively the diverse laws have been harmonized. Quite the opposite in fact, even in a utopian prospect that the laws governing intellectual property in each Member State have been crafted in an absolute identical manner; the effect of the identical laws, that is to say protection accorded to intellectual property and their enforceability, will take effect only in their respective national territory. Therefore, this ramification of territoriality, regardless of what manner of rules the other Member States impose, persists representing a fundamental impediment to free movement. Harmonization keeps intact the different laws, as many as the number of Member States and, potentially, as many parallel IP rights. Therefore, it is structurally incapable of getting to the bottom of the problems -the most difficult ones- created by intellectual property territoriality. This, so-called, *de jure* territoriality is precisely how territorially independent parallel rights get in the way of parallel trade and, therefore, that of realization of the free movement principle.[135]

On that account, one might *a contrario* suggest that the way to redress these is to wreck down the territorial quiddity attached to intellectual property rights all together.[136] Removal of national territoriality infers creating one whole territory, the borderlines of which obviously coincide to that of envisaged Single Market, and applying one whole set of intellectual property law homogenously across that realm. In other words, the whole idea depicts a unitary European intellectual property law. Although its attainment has seemed incrementally persuasive in

harmonized term of protection intended therein could be effective only to the extent that the terminology and definitions employed in that Directive are understood and applied in a unified manner across the Member States. Despite the fixed period of protection (70 years for copyright and 50 years for related rights), the moment this period starts running depends heavily on (and differs on the basis of) the classification of the work (i.e. joint work, collective work or adaptation) and the identification of the author(s). As the Directive has no undertaking as regards the definition and interpretation of the terminology (nor does any other source in the legal order of the Union), the applied term of protection is liable to vary due to diverse meanings and interpretations ascribed by the national laws to these concepts and the terminology. See: Christina Angelopoulos, *The Myth of European Term Harmonisation: 27 Public Domains for the 27 Member States*, 43(5) IIC 567 (2012); MIREILLE VAN EECHOUD, ET AL., HARMONIZING EUROPEAN COPYRIGHT LAW: THE CHALLENGES OF BETTER LAWMAKING (Kluwer Law International 2009)

[134] Keeling, *supra* note 16 at 133

[135] See the general consideration of parallel imports above.

[136] In a valuable contribution in 1965, Koch and Froschmaier -even before any actual dispute occurred- had quite thoroughly foreseen the potential conflict between the national intellectual property protection and the rules of the Treaty aimed at the Common Market, to the effect that the parallel rights could be used for preventing the inter-state circulation of goods. In that regard, they confronted the relevance of national exhaustion rights, thus arguing for a Community-wide exhaustion model, more than two decades before the same idea is hinted by the European jurisprudence. See: Koch & Froschmaier, *supra* note 100.

recent times having in mind the Community Design, European Trademark (Community Trademark) and Unitary Patent which is at standstill by the moment, the unification of laws is far from complete. Further, given the divergent political choices a complete uniformity has been often perceived to be a utopian goal to attain.[137] This is visibly so when the certitude is taken into account that a unitary intellectual property regime encompasses a more elaborate groundwork than mere unification of statutory laws.[138]

Moving back to the foundational dichotomy, in the end, the two interests; that of the IP right holder on one hand, and the interest of free movement and subsequent market integrity on the other hand, are not susceptible to be simultaneously protected. This follow that one side of the conflicting concepts should necessarily be prioritized, albeit at the cost of compromising the other. Should the exercise of intellectual property right be permitted at the cost of make concessions to free movement principle; or alternatively free movement principle -thus the integrity of the Single Market- has to be held in a higher esteem and it should prevail over intellectual property rights? What brings further complication into the equation is when the choice among the two is made in favor of the free movement principle, it amounts to encroaching upon and undermining proprietary right of the right holder. This is particularly problematic insofar as the right to intellectual property from the perspective of property ownership (i.e. right to property) has often not been differentiated from the general concept that originally pertained to tangible property; therefore, on the international level, right to intellectual property is also endorsed as a fundamental right,[139] which inherently cannot be extinguished in the wake of free movement. Further, the Union law, as will be cited below, firmly abides by the principle of non-interference with the property ownership, instead and quite the contrary, leaving this genre entirely to the national laws of the Member States.

On this archaic clash, the primary legal source, which is conceivably tasked to make the selection amongst the two conflicting interests, that is primary law of the Union, at the first

[137] Keeling, *supra* note 16 at 134

[138] Having implied unification as the making of law, Ladas draws attention to four elements of law: (i) legislative texts and regulations containing the substantive rules and procedures for application of the latter; (ii) judicial and administrative decisions interpreting and applying these texts; (iii) traditional methods of handling legal materials; (iv) philosophical, political and ethical ideas and ideals that shape these texts, decisions and techniques. He maintains that, when the matter of uniformity of laws on international level is spoken of, many tends to take into consideration only the first element of law, however he adds, the other three elements are of decisive importance. See: LADAS, *supra* note 75

[139] Article 17 on right to property of the European Charter of Fundamental Rights reads: "…Intellectual property shall be protected."

glance, sheds very little light on the issue. In that, it tends to cover intellectual property and free movement interface in a few provisions:

-Article 34 & 35 TFEU:

"Quantitative restrictions on imports (Art. 34) / exports (Art. 35) and all measures having equivalent effect (hereinafter MEQR) shall be prohibited between Member States."

-Article 36 TFEU:

"The provisions of Articles 34 and 35 shall not preclude prohibitions or restrictions on imports, exports or goods in transit justified on grounds of public morality, public policy or public security; the protection of health and life of humans, animals or plants; the protection of national treasures possessing artistic, historic or archaeological value; or the protection of *industrial and commercial property*. Such prohibitions or restrictions shall not, however, constitute a means of arbitrary discrimination or a disguised restriction on trade between Member States."[140]

In addition, and as we insinuate above, property ownership, more particularly its independence from the realm of Union law has been safeguarded as follows:

-Article 345 TFEU:

"The Treaties shall in no way prejudice the rules in Member States governing the system of property ownership."

On this note it is relevant to break up the general provisions of the Treaty into three fragments.

(1) First of all, Article 34 and 35 TFEU play the safeguard role as regards free movement of goods; and these are at the outset aimed to catch any disguised impediment to free movements as such. It naturally follows from this logic that, once the intellectual property rights are invoked in such a way as to curtail free movement of goods -which is very function of IP rights-, this would amount to a measure with equivalent effect to quantitative restriction, thus it is susceptible to get caught by the prohibition in Article 34.

(2) The second fragment, that is the first postulate of the Article 36 TFEU exhaustively sets forth specific grounds on which MEQR would be permissible, that is to say the

[140] Emphasis added.

exceptions/restrictions to free movement principle. The latter, *inter alia,* contains the protection of industrial and commercial property, the area in which intellectual property is immanent.

It is so indicated up until this stage that Article 36 TFEU acknowledged the existence of a conflict between intellectual property rights and the free movement of goods.[141] Subsequently in the following provision, this conflict seems to have been extinguished by determining industrial and intellectual property as a justifiable ground for derogation from free movement. Therefore, the choice among the conflicting interest, that we earlier referred to, has seemingly been made in favor of protection of intellectual property, leaving the principle of free movement, as it were, with a big hole in it.[142]

(3) Nevertheless, the third fragment, that is the second clause of Article 36, sharply and immensely narrows down the scope of the justifiable restrictions to free movement that are listed in the preceding postulate. In that it provides "Such prohibitions or restrictions shall not, however, constitute a means of *arbitrary discrimination* or a *disguised restriction* on trade between Member States."[143] In the final instance, this follows that intellectual property rights may … only to the extent that they do not constitute an arbitrary discrimination or a disguised restriction to intra-Union trade.

In addition to these postulates, necessary to remember, the principle yet remains that property ownership shall, by no means, be prejudiced. All read together, the Treaty provisions virtually, albeit with little nuances, seems to have cyclically led back to the original dichotomy: the competing interests of intellectual property on one hand and that of free movement on the other hand. Moreover, this handful of instruction is all to what can be found in the primary law of the Union; that is to say, no further substantive legal source providing guidance in striking this balance or that prescribes what should arbitrary discrimination or disguised restriction entail. However, the Treaty provisions addressed the intellectual property and free movement contrast modestly compact, what flows from the wording of it opens up a greatly abstract area of interpretation. The actual scenery, therefore, is far from being simple. So much so that it would not be absolutely mistaken to suggest that the EU intellectual property law and to a certain degree the competition law, have largely emerged from the sensitive balance between the exercise of intellectual property rights -with their exclusionary, monopolistic or divisive

[141] KEELING, *supra* note 9 at 28
[142] GARETH DAVIES, EUROPEAN UNION INTERNAL MARKET LAW 187 (Routledge Cavendish, 2003)
[143] Emphasis added.

impacts- and sustainment of the free movement of goods and services as well as that of fair competition environment.

The task of interpreting and applying these provisions, and correspondingly that of instituting a proper balance between the two competing interests of free movement of goods and protection of intellectual property has been largely placed on to the European Court of Justice.[144] Reconciling the two interests into a sustainable balance, in our view, is the identifying feature of the intellectual property law in the European Internal market; in a way, said balance and its construction represent the 'Europeanization' element of intellectual property. European intellectual property law and its cumulative substantive foundations up to present, i.e. secondary law of the Union, have been largely laid and, all along shaped, by the European Court of Justice; the starting point being this very clash of IP rights and free movement. And come-into-scene of this clash was on the occasion of parallel imports, the phenomena of which has been the central to European intellectual property law ever since. Therefore, the continuum of striking and sustaining this balance – which is as old to the Union as intellectual property itself is- also determine the meaning of intellectual property commercialization in the European Internal Market. Reconciliation of the two is what makes intellectual property commercialization, i.e. commerce of goods and services that incorporate intellectual property rights, possible in the European Internal Market.

[144] Keeling, *supra* note 16 at 129

# CHAPTER 3

# RECONCILING THE CONFLICT IN NATURE; EARLY DOCTRINES

We had previously noted that the balance had to be struck between the intellectual property protection and the free movement principle. Moreover, the two concepts being in an existential contradiction, redressing such a balance, in principle, necessitates preferring one of the competing interests to the other. Should the choice be made in the favor of free movement principle (the choice which comes intrinsically insofar as the free movement principle pinpoints the very essence of the Internal Market) yet another major issue surfaces: limitation to proprietary right. Art. 345 TFEU (ex. 295 TEC, previously 222 TEEC) specifically provides that the Treaty provisions shall by no means prejudice the rules of the Member States governing property ownership. Thus, the provision of the Treaty, judging by the general outlines, make up an obstacle to straightforward selecting the interest of free movement over that of intellectual property.

## 1. Existence and Exercise of Rights

The earliest method the ECJ jurisprudence developed so as to flee from this dilemma concerned circumventing the effects of exercise of intellectual property rights, yet meanwhile - at least virtually - preserving nationally granted intellectual property rights so that property ownership would not have been interfered by the Union law. The foundational premises of the principle that the Court envisaged are based upon the presumption that the objective existence of the nationally granted rights on one hand and their existence on the other hand are different matters. Further, the two aspects of the rights are separable from one another, thus a dividing line can be - and as far as the free movement principle is at stake[145], it must be - set between the existence and exercise of rights. Accordingly, the Treaty provision on the non-interference of the Union law with the property ownership, the regime of which falls straightforward within the ambit of Member State`s discretion, solely guarantees the existence of the rights. The exercise, which is of another aspect, may nevertheless be limited by the prohibitions laid down in the Treaty.

[145] It is necessary to note that the distinction between the existence and exercise of rights has been originally envisaged in the context of competition law.

However, the known terminology, i.e. the doctrine of existence and exercise of rights, was initially articulated in *Parke, Davis*; the actual underlying idea was invoked by the Court much earlier in *Consten Grundig*[146] where the competition rules of the Treaty were of central concern.

Grundig, a German company and manufacturer of consumer electronics, granted Consten, a French company, the exclusive right to distribute its products and spare part thereof in France. Consten was also authorized to register, in its own name, in France the international trademark (GINT) of Grundig. Meanwhile, German resellers were contractually prohibited from delivering the product to France. Nevertheless, UNEF, another French company managed to parallel import the goods from Germany into France. Subsequently, Consten brought infringement proceedings against UNEF before French court, in response to which UNEF notified the European Commission. The Commission found that the sole agency agreement between Grundig and Consten infringed the competition rules laid down in Art. 101 TFEU (Art. 85 EEC Treaty at the time). On that account, it concluded that Consten and Grundig have to refrain from taking measures which are aimed at keeping the others from acquiring the respective products with a view to sell them in France. Grundig and Consten went on to challenge the Commission`s ruling before the ECJ. On their end, they purported that the ruling in question effectively prejudiced their intellectual property right protection of which has been enshrined by Art. 36 and 345 of TFEU (ex. Art. 36 and 222 TEEC).[147] From their perspective "GINT" trademark registered in France by Consten is the intellectual property of the latter, hence, it shall not be undermined by the Treaty provisions, including those governing competition, insofar as Treaty as such assures non-interference with the national system of property ownership.

The Court however, rather sensationally, took a different opinion. Accordingly, the Commission`s order prohibiting the use of national trademark rights such as to set an obstacle to parallel imports *does not affect the grant of those rights but only limits their exercise* to the extent necessary to give effect to the prohibition under Art. 85(1).[148] Therefore, the Court for the first time resorted to setting a dividing line, arguably a superficial one, between the objective existence of intellectual property rights and their exercise. This contemplation was followed by its observation that what was guaranteed by the combination of Art. 36 and 222

[146] Joined cases C-56/64 and C-58/64, Consten & Grundig v. Commission, 1966
[147] Respectively setting out (i) the 'protection of industrial and commercial property' as a derogation from the prohibition of quantitative measures and measures having equivalent effect; (ii) that the Treaty shall in no way prejudice the system existing in Member States in respect of property.
[148] Joined cases C-56/64 and C-58/64, Consten & Grundig v. Commission, 1966, 345. (Emphasis added)

TEEC is the mere existence of the rights; their exercise, in consequence, may be limited to the extent that the prohibitions in the context of competition rules of the Treaty necessitate.

The birth and the early examples of the existence / exercise distinction, as mentioned, transpired on the axis of competition rules of the Treaty. This is understandably so when the historical sequence is followed, Treaty articles on quantitative restrictions on imports and measures having equivalent effect did not come into force until 1968 and 1970 respectively.[149] Subsequently, the Court extended the application of this dichotomy to the cases involving free movement of goods.[150]

In *Deutsche Grammophon v. Metro*[151] case, Deutsche Grammophon (hereinafter DG), a sound recording manufacturer in Germany, normally distributes its recordings in Germany through retailers and certain wholesale booksellers which contractually agreed on marketing the recordings at DG`s preset retail price. Metro, owner of a hypermarkets chain in Germany, offered for sale in its stores the recordings produced by DG. Incidentally however, Metro was not bound by said price-fixing agreement, therefore it was able to undercut the retail prices of the recordings. Having discovered the lack of a price-fixing agreement, DG approached Metro in order to bring the latter in line with its preset pricing. Metro however refused doing so, in response to which DG resorted to cutting off the supply of its products to Metro`s stores. Metro, nevertheless, through its French subsidiary, acquired the recordings that DG marketed in France and re-imported them into Germany and placed on the market, again, below the preset retail price. Relying on its exclusive distribution right under the copyright, DG obtained from the German court an injunction ordering Metro to cease to import and market the recordings in question. Moreover, the major disagreement between the parties pertained to whether, in recognition of German copyright law, exclusive distributions rights of DG over the recordings at hand exhausted. DG maintained that its rights was not exhausted given that the initial marketing of the Art. took place in France, therefore its distribution rights in respect to Germany remained unaffected.[152] Metro on the other hand, argued that it is not the country of initial marketing that is the determining factor of exhaustion; but it is the right holder`s consent to distribution that triggers the exhaustion of rights.[153] Eventually the dispute reached up to the Higher Regional Court of Hamburg, by which two questions were referred to the ECJ for a

[149] Christopher Stothers, *Article 36 TFEU: intellectual property* 315 (In PETER OLIVER ED., OLIVER ON FREE MOVEMENT OF GOODS, 313-369, Hart Publishing 2010)
[150] KEELING, *supra* note 9 at 53; BARNARD, *supra* note 105 at 158
[151] Case C-78/70: Deutsche Grammophon v Metro-SB-Großmärkte
[152] Id. a. 490
[153] Id. at 493

preliminary ruling. The questions, in essence, concerned (i) whether it is contrary to the competition rules of the Treaty to rely on copyright and related rights so as to prohibit the parallel imports of incorporating goods which were marketed in another Member State; (ii) whether it amounts to abuse of dominant position to implement a price control over the retails.

The Court, in response, reiterated its holding in *Parke Davis* with regard to application criteria of the rules of competition. Firstly, in the context of Art.85(1) TEEC it has to be tested, in each instance, whether the exercise of the exclusive rights manifests itself as the subject, the means or the result of an agreement which, having prevented imports from other Member States of products lawfully distributed there, has as its effect the partitioning of the market.[154] Secondly, as far as the prohibition of dominant position enshrined in Art. 86 TEEC is concerned, it once again accentuated that mere exercise, by the manufacturer of sound recordings, of exclusive right to distribute the protected Art. does not necessarily amount to occupying dominant position within the meaning of the prohibitions in said provision.[155] In order for such an exercise to be caught by Art. 86 (now Art. 102 TFEU), a dominant position must be abused; further such an abuse is not solely disclosed by the differential between the controlled price and price of reimported product, however, depending on the circumstances, price differential as such may factor into determination of the abuse.[156]

Crucially however, the Court further held, if the practice in question does not exhibit the elements of those prescribed in Art. 85(1) TEEC, it is necessary to further scrutinize whether the it is compatible with the other provisions of the Treaty, particularly those relating to the free movement of goods.[157] On that note, and drawing upon the previous formula of existence and exercise distinction, it held, although the Treaty does not affect the existence of rights recognized by the legislation of a Member State with regard to industrial and commercial property, the exercise of such rights may nevertheless fall within the prohibitions laid down by the Treaty.'[158] Admittedly Art. 36 TEEC on derogations from free movement of goods nominally addresses *inter alia* protection of industrial and commercial property, nevertheless such a justification, the Court emphasizes, is permitted only to the extent that it safeguards the specific subject matter[159] of such property.[160] The Court further justified this stance by

[154] Id. para 6
[155] Id. para 16.
[156] Id. para 19.
[157] Id. para 7.
[158] Id. para 11.
[159] Specific subject matter of intellectual property rights shall be discussed in the ensuing sub-chapter.
[160] *Supra* note 158

depicting the reverberations of the contrary situation. Accordingly, if a right related to copyright is relied upon to prevent the marketing in a Member State of products distributed by the holder of the right or with his consent on the territory of another Member State on the sole ground that such distribution did not take place on the national territory, such a prohibition, which would legitimize the isolation of national markets, would be repugnant to the essential purpose of the Treaty, which is to unite national markets into a single market.[161]

Besides extending the application of the existence and exercise distinction to free movement provisions, the ruling of the Court also entailed other significant reverberations. The foremost significance of the judgement is that it planted the seeds of a unique form of regional exhaustion regime for intellectual property rights across the Community.[162] What is formulated in the aforesaid paragraph as 'products distributed by the holder of the right or with his consent on the territory of another Member State'[163] in fact precisely defines the breadth of the exhaustion of rights in respect to both covered Art. and peripheral limits. Accordingly, the intellectual property right holder cannot invoke his rights to object to further marketing of the goods within the Community once those particular goods are put on the market in any Member State by the right holder or in line with his consent. What is also of a notable importance, though to a lesser extent, is that the judgement implicitly responded, in affirmative, to the potential question of whether the rights related to copyright fall within ambit of industrial and commercial property for the purposes of Art. 36 TEEC (now Art. 36 TFEU).

***Significance of the Doctrine***

The judicial solution that the Court generated has been in the center of criticism, on various points. The most notable one however revolved around the question of how could the rights practically exist when their exercise ceases to be permitted. It was rightly uttered that the existence of rights is undetachable from their exercise; they can hardly be deemed to exist when they cannot be exercised.[164] Moreover, absent the definition of a legitimate exercise, any exercise of the rights in the context of intra-Community trade almost intrinsically contradicts what the Treaty stands for on the account of free movement principle. The extent to which the

[161] Id. para 12
[162] KUR & DREIER, *supra* note 35 at 47; KEELING, *supra* note 9 at 51
[163] *Supra* note 161
[164] Stothers, *supra* note 149, at 315; DAVIES *supra* note 142 at 187; KEELING, *supra* note 9, at 55; KATARZYNA CZAPRACKA, INTELLECTUAL PROPERTY AND THE LIMITS OF ANTITRUST: A COMPARATIVE STUDY OF US AND EU APPROACHES 96 (Edward Elgar Publishing 2010); STOTHERS, *supra* note 101 at 28-30. Although the latter commentator reaches to a different conclusion, he nevertheless emphasizes that '… there would appear to be little practical significance that a right exists if it cannot be exercised.' and '... this effectively prohibits very existence of these sub-rights.'

exercise of rights, for the purposes of free movement and competition rules, could be cropped out had no apparent limits. The only indicator, (i.e. to the extent necessary to give effect to Community rules) does not offer an objective limit, therefore it is not particularly helpful. Without further clarification, it may, at one extreme, imply that the exercise, if necessary, may be purged out completely by the Treaty prohibitions, leaving the plain ownership behind, much like an illusion of ownership, solely to go around Art. 222 TEEC (Art. 345 TFEU now). Furthermore, the contemplation of a specific subject matter of rights, connoting an untouchable area of exercise of the rights which incidentally was envisaged five years after the first emergence of the existence - exercise distinction, was not of substantial help to further clarify this problematic. This was the case at least at the early stages including the time when *Deutsche Grammophon* was decided, insofar as the Court made no attempt to define the what should 'specific subject matter' of the intellectual property entail.[165] This, besides putting the intellectual property rights under an existential threat, expressly results in a lack of legal certainty. To that end it is rather manifestly observed that the doctrine is flawed in merits. Not surprisingly, the Court`s invention has been almost uniformly criticized by commentators and this concerned both legal-theoretical and practical points.[166]

Among the critiques, Korah suggests that, except for the extremes, to draw a line between the existence of the rights and their exercise is impossible from a legal theoretical perspective.[167] This is because what the existence entails is comprised of all the ways in which that right can be exercised.[168] One would be tempted to confront this proposition with the 'bundle' argument, according to which, intellectual property rights (much like other proprietary rights) are represented by a bundle of rights and the sticks comprising the bundle are not necessarily existentially dependent to each other. Therefore, limitation to one would not necessarily affect the bundle, at least to an existential level. This confrontation could, moreover, be supplemented by the possible divisibility of existence and exercise on a theoretical plane.[169] However this is true from a theoretical perspective (for instance, the

[165] KEELING, *supra* note 9, at 62
[166] SEVILLE, *supra* note 122, at 322 "artificial, baseless, inconsistent"; DAVIES, *supra* note 142, at 187 "an empty distinction" KEELING, *supra* note 9 at 54 "vague, artificial, unhelpful, unworkable"; IRINA HARACOGLOU, COMPETITION LAW AND PATENTS: A FOLLOW-ON INNOVATION PERSPECTIVE IN THE BIOPHARMACEUTICAL INDUSTRY 104 (Edward Elagar 2008) "incoherent, unnecessary"
[167] KORAH, *supra* note 20 at 3; See also Schovsbo who raises the question whether a right may exist if it cannot be exercised, and answers to this question in negative. Jens Schovsbo*, Free Movement of Goods and Exhaustion* (In COMMON PRINCIPLES OF EUROPEAN INTELLECTUAL PROPERTY LAW, ASGHAR OHLY ED. 169 MOHR SIEBECK 2012)
[168] Id, Korah.
[169] To that effect, see: Georges Friden, *Recent Developments in EEC Intellectual Property Law: The Distinction Between Existence and Exercise Revisited*, 26 Common Market L. Rev 193, 193.

possession of a patent and relying on that patent in order to prevent parallel imports are different matters), the fact should nevertheless not be overlooked that, given the lack of physical substance, property-like rights on intangibles are only as meaningful as the possibility of their exercise.[170] Further, from a proprietary right perspective, it is submitted that the limitations to the exercise of any right in the bundle will diminish the property to the same extent.[171] Question thus boils down to following "To what extent the exercise can be curtailed before it encroaches upon their existence which is rooted in the national law?" If 'existence' is confined to the formal presence of the right under the national law (or 'grant' as was originally conceived), then the limitations to exercise introduced by the Community law might escape the intervention of Art. 345. Would, however, the preservation of plain ownership fulfil the protection accorded to industrial and commercial property by Article 36? It is without doubt that the plain ownership of the rights would be of no benefit if they were unconditionally held inferior to the free movement principle. Although the common-sense dictates that 'the limitations that are necessary to give effect to Community law' are not always likely to purge the existence of the rights, from this doctrine alone, the extent of such limitations does not objectively confinable. Seemingly, the latter was the actual problem with the distinction the Court drew.

Though it`s dubious whether above considerations have been fully dwelled upon by the Court in creating this distinction, it is speculated, at very least, that it was intended by the Court as a way of iterating and effectuating the supremacy of the Community law.[172] The latter principle, on the other hand, co-exists with the principle that national laws govern the fields which have not yet been regulated by the Community law; in this case intellectual property law. With the distinction between the existence and exercise of the rights, the European jurisprudence thus took a stance that the objectives of the Treaty must be respected (regardless of the fact that the provision of the Treaty substantiating those objectives do not offer a clear-

[170] For the contrary view see: David Gladwell, *The Exhaustion of Intellectual Property Rights*, 8(12) EIPR 366, 370 (1986). The latter author takes the view that '[I]t is not sufficient merely to say that the existence of a right is manifested by its exercise.'. In doing so the author brings examples from the UK Patents and Designs Act 1907 and the Patents Act 1977 in respect to the nullity of certain clauses in patent licensing and sales agreements concerning patented articles (such as prohibitions on purchasers or licensors right to use the goods supplied by other suppliers -i.e. tie-up clauses- and further purchase obligations), in turn reaching the conclusion that "the subsistence of the patent is not affected but merely a term as to its exercise is made void." However this view reflects an obvious merit on the axis of the said example, we believe, it is not directly comparable with the Court`s doctrine of existence and exercise. This is because, in the aforementioned example, the limitation to the exercise of (patent) rights is objectively confinable, however the existence and exercise doctrine -in itself- is devoid of such an objective demarcation; and this is the actual problem with that doctrine, rather that merit of a distinction between the existence and exercise on a theoretical plane.

[171] ALAN DASHWOOD, ET AL., WYATT AND DASHWOOD'S EUROPEAN UNION LAW 2595 (Bloomsbury Publishing 2011), also quoted by KEELING, *supra* note 9, at 55

[172] Roberto Casati, *The Exhaustion of Industrial Property Rights in the EEC: Exclusive Manufacturing and Sales Provisions in Patent and Know-How Licensing Agreements*, 17 Colum. J. Transnat'l L. 313, 323 (1978)

cut norm) as far as the claims arising from the national law contradict those objectives. Therefore, not only did the supremacy of the Treaty has left a residual scope to the exercise of the national intellectual property rights, but also the jurisprudence, by not defining the extent of intervention, enabled itself a free discretion[173] thus a disquietingly large area of play in achieving the policy objectives underlying the Treaty. This flexibility clearly comes at the cost of legal predictability.

On the flip side, a relatively unpopular opinion suggests that the Court`s doctrine does not deserve much of the criticism that was levelled against it.[174] In fact, this proposition has a great share of truth when the doctrine is put in the correct analytic perspective. That is, the doctrine was never actually intended as a conclusive solution to the problem at hand; if anything, it amounted to the realization of the problem and to the initial step taken on that axis.[175] In a rational assessment of the principle, one should necessarily observe that the main objective in that very likely be that of responding as quickly and effectively as possible to the inherent conflict between territorial rights and the principle of free movement, in which balance the latter has been consistently favored by the Court`s jurisprudence as well as the Union law. On that note, having acknowledged the vagueness and perhaps affectedness of such a divide, especially when the subject matter of the rights as such are intangible in nature thus their existence is substantially intertwined with the ability of being exercised, its practical significance should nevertheless be recognized. Approvingly it is noted that the actual utility of the doctrine resides at its promptness, with reference to the considerably tedious procedure of addressing the problem by political means.[176] Notwithstanding how flawed it is in theoretical terms, practically it falls consistent with the propensity of holding the internal market -and correspondingly free movement principle- in a higher esteem than the intellectual property protection. From that view point the stance taken by the Court in contemplating this doctrine is a purposive approach and it is of very little dispute that it has been majorly helpful in practical sense.[177]

Finally, further attention should be paid to the fact that this judicial solution is likely to have been contemplated as a momentary relief by the Court. The hostility between intellectual property protection - which initially did not have a unitary regime across the Community to

[173] Valentine Korah, *Dividing the Common Market through National Industrial Property Rights*, 35(6) Mod. L. Rev 634, 636 (1972)
[174] Casati, *supra* note 172 at 321; KEELING, *supra* note 16 at 61
[175] Id.
[176] SEVILLE, *supra* note 122, at 322
[177] DAVIES, *supra* note 142, at 187

any extent- on the one hand, Community rules on free movement and competition on the other hand eventually required sophisticated and comprehensive reconciliation. This necessity was acknowledged in *Parke Davis* judgement of the Court, and the long-term solution is indicated to be a unitary legislation across the Community.[178] However an instant response, particularly with regards to parallel import activities, was more urgently necessary. The distinction between existence and exercise is said to be the foremost reaction to the latter - and practical - necessity. Seville approvingly highlights that this approach was only of transitional importance.[179] This argument has been notably corroborated by the Court`s gradual abandonment of reliance on the existence and exercise distinction, which all together was abandoned as from the *Coditel v. Cine-Vog* judgement in 1982.[180] It would nevertheless be naïve to conclude that the theoretical background set by this doctrine has become completely obsolete in the Union`s law and jurisprudence, particularly regarding the interface of intellectual property rights and the competition rules.[181]

**2. Specific Subject Matter of Rights**

The Court in *Deutsce Grammophon* had acknowledged the necessity of an additional criterion and signified its new concept that intended to set a limitation to the restrictions to the exercise of rights. In that, it pronounced an area what it addressed as 'specific subject-matter' of industrial and commercial property,[182] a safe zone within the vast area of 'exercise of rights' which is immune to the limitations flowing from the Treaty provisions on competition and free movement. The said concept was to address the foremost criticism that the existence/exercise separation itself has faced on the grounds of artificiality and vagueness. Accordingly:

"Although it permits prohibitions or restrictions on the free movement of products, which are justified for the purpose of protecting industrial and commercial property, Art. 36 only admits derogations from that freedom to the extent to which they are justified for the

[178] Case 24/67: Parke, Davis and Co. v Probel, Reese, Beintema-Interpharm and Centrafarm, pp. 71
'…In the absence of such unification, the national character of the protection of industrial property and the variations between the different legislative systems on this subject are capable of creating obstacles both to the free movement of the patented products and to competition within the Common Market.' 1
[179] SEVILLE, *supra* note 122, at 322
[180] KEELING, *supra* note 9, at 55
[181] The reaction of the competition rules of the Union against the intellectual property rights is essentially premised upon this distinction. See Chapter 8 of this study.
[182] Deutsche Grammophon, para. 11

purpose of safeguarding *rights which constitute the specific subject-matter of such property*."[183]

Nevertheless, no further demarcation of what specific subject-matter should entail nor any further reference to the term itself was made. Instead, this passage was instantly followed by the reverberations for the single market of the scenario in which preventing the subsequent marketing of the goods, relying on the distribution right which is conferred by copyright and related rights, was permitted. The said scenario, the Court maintained, *would legitimize the isolation of national markets and that would be repugnant to the essential purpose of the Treaty, which is to unite national markets into a single market*.[184]

The implication of the Court was that, albeit the specific subject matter area was not (yet) definite, that area did not coincide the exclusive distribution after the initial sales in the Union. Correspondingly, after the first sale of the goods in any Member State the exercise of a national exclusive distribution right can be prohibited so long as it is necessary for the functioning of free movement provisions. The latter observation insinuates an extra-national IPR exhaustion regime and the Court, therefore, reached its view not particularly through an examination of the specific subject matter of the right at hand but through an exclusionary listing. Not surprisingly, the decision in *Deutsche Grammophon* is taken to be the origin of Community exhaustion regime. Nevertheless, this imperative is only deduced from the Court`s holding and the outcome only practically amounted to exhaustion of the rights. Yet, what transpired in that case was only one form of exercise of the national rights; there are more layers to the tension between free movement and territorial rights. Clearly, therefore, specific subject matter doctrine is a greater -practical- tool which judicially yielded the precursors to exhaustion doctrine. Limit of exhaustion was to be determined by the specific subject matter of the rights. With that, the Court had seemingly set about waiting for the right occasions to clarify the specific subject-matter of each type of intellectual property right as far as they fall relevant.

***Patents and Trademarks***

The initial positive definition of specific subject-matter was offered by the Court in the context of a dispute that concerned the parallel trade of pharmaceutical products from the United Kingdom into the Netherlands. Sterling Drugs, an American pharmaceutical company,

[183] Id. (emphasis added)
[184] Id. para. 12

placed on the market in both countries, through its subsidies and under registered trademarks, the drugs for which it has patents. In the United Kingdom the price level of the drug has been controlled by the governmental regulations, whereas in the Netherlands this was not the case; hence sales prices varied in the two countries. Centrafarm the parallel importer, having been tempted by the remarkable price differential, imported into the Netherlands the drugs which obtained from the UK and Germany on lower prices. Following this, Sterling Drugs and its Dutch subsidiary, Winthrop, sought judicial remedy, including an injunction, before the Dutch Court. In that, Sterling and Winthrop brought two separate actions whereby Sterling invoked its Dutch patent for the drugs and Winthrop relied on the registered trademark used in their marketing. The cases ended up before the Dutch Supreme Court by which they were referred to the ECJ for a preliminary ruling in respect to the compatibility of such an exercise of patents and trademarks with the Treaty. On the basis of the same dispute and through two separate cases resulting therefrom, namely *Centrafarm v. Sterling* and *Centrafarm v. Winthrop*, the ECJ has found a dual opportunity in to define what specific subject-matter connotes for patents and trademarks respectively.

In *Centrafarm v. Sterling*, the Court started off with reiterating the abstract contemplation of 'specific subject-matter' that it initially introduced in *Deutsche Grammophon,* in essence, confining the derogations from free movement principle set out in Art. 36 TEEC to the specific subject-matter of the intellectual property right in question.[185] It, afterwards, went on to provide a positive definition of specific subject-matter as far as it concerns patent rights:

*In relation to patents, the specific subject-matter … is the guarantee that the patentee, to reward the creative effort of the inventor, has the exclusive right to use an invention with a view to manufacturing industrial products and putting them into circulation for the first time, either directly or by the grant of licenses to third parties, as well as the right to oppose infringements.*[186]

*In relation to trade marks, the specific subject-matter … is the guarantee that the owner of the trade mark has the exclusive right to use that trade mark, for the purpose of putting products protected by the trade mark into circulation for the first time, and is therefore*

[185] Case C-15/74: Centrafarm v. Sterling, para 8.
[186] Id. para. 9

*intended to protect him against competitors wishing to take advantage of the status and reputation of the trade mark by selling products illegally bearing that trade mark.*[187]

Subsequently in *Hoffmann-La Roche* essential function of trademarks have been further defined from a consumer perspective. Accordingly:

*[E]ssential function of the trade-mark (...) is to guarantee the identity of the origin of the trade-marked product to the consumer or ultimate user, by enabling him without any possibility of confusion to distinguish that product from products which have another origin.*[188]

***Copyright and Related Rights***

As a preliminary issue, it was uncertain whether copyright protected substance will qualify as industrial and commercial property within the meaning of Art. 36 TEEC. As a result, copyright and related rights have proven the most controversial type of rights when it comes to delineating the specific subject-matter. However in *Deutsche Grammaphon* the Court dropped some affirmative hints as to the relevance of copyright and related rights to the notion of industrial and commercial property -and decided on the assumption that they do fall within that notion-[189], it was in *Musik-Vertrieb Membran v. GEMA* that the question has been actually pondered upon.[190] In response to the argument of the French Government that copyright is not comparable to other industrial and commercial property rights[191], the Court of Justice established that so far as the economic aspects of copyright is concerned, in the application of Art. 36 of the Treaty there is no reason to make a distinction between copyright and other industrial and commercial property rights.[192] It therefore offered a definitive answer to the question of the relevance of copyright to the concept of industrial and commercial property and the precept of case law is applicable in the context of copyright: it cannot be relied on so as to restrict parallel imports once incorporating goods are legally put into circulation in one Member State.

[187] Case C-16/74: Centrafarm v. Winthrop, para 8.
[188] Case C-102/77: Hoffmann-La Roche v. Centrafarm, para. 7.
[189] Deutsche Grammophon, para.11
[190] Joined Cases 55 and 57/80 Musik-Vertrieb Membran v. GEMA
[191] French Government in the proceedings argued, in a nutshell, that the case law on exercise of the rights -that had patent and trademark at its center- should not be applicable to copyright since the latter is not made up only of economic rights it but also entails moral rights such as such the right of attribution to the work; that of objecting to any alteration, distortion or mutilation etc.
[192] Musik-Vertrieb Membran v. GEMA para 12.

It was on the occasion of *Coditel I* judgement that the Court, for the first time though rather unglamorously, made a reference to what is relatable to specific subject-matter of copyright. Although the terminology employed by the Court was 'essential function' of the rights, in the essence it seemed to indicate, instead, to the specific subject-matter of copyright; the difference we will discuss further below. In that, it said 'the right of a copyright owner and his assigns to require fees for any showing of a film is part of the essential function of copyright in this type of literary and artistic work.'[193] In the subsequent case of *Warner Brothers v. Christiansen*, the Court built upon the ontological definition of specific subject-matter, that is to say an area where the exercise of the rights is immune to the Treaty`s intervention, so as to define what it connoted as far as copyright is concerned. The Court was able to pin down two prerogatives being fall within specific subject-matter area, although again the allusion was made through a moderately altered terminology: essential rights. Accordingly, it held that 'The two essential rights of the author, namely the exclusive right of performance and the exclusive right of reproduction, are not called in question by the rules of the Treaty.'[194]

The European Court of First Instance (CFI, now General Court), subsequently in a competition case, namely *Magill*, retrieved the concept of 'essential function' preceded by the definition laid out in *Warner Brothers v. Christiansen*. Having referred to the aforesaid definition, i.e. exclusive right of reproduction and of performance, it maintained that "… its essential function, within the meaning of Art. 36 of the Treaty, […] is to protect the moral rights in the work and ensure a reward for the creative effort, while respecting the aims of, in particular, Art. 86."[195] On the appeal round, the ECJ cited the essential function definition of the Court of First Instance, from the fact of which the ECJ approval to such definition can be deduced.[196] What appears to be contentious, or under-elaborated, in the given notion of essential function is that it was based on an assumption of unified policy purpose that lie behind the grant of intellectual property rights by all Member States: rewarding the author. Nevertheless, as we will discuss below in the context of different meanings attributable to the term of 'specific subject-matter', this is not the first time the Court based its definition upon an assumption. Furthermore, intertwined with the varied intellectual property theories from one Member State to another, it is apparent that moral rights are not of equal importance in every Member State, in which the major contrast appears between the countries that follow common

[193] Coditel I, para. 14
[194] Warner Bros v. Christiansen, para 13
[195] Case T-69/89: RTE v. Commission; Case T-76/89: ITP v. Commission
[196] KEELING, *supra* note 9, at 268

law and those that follow civil law tradition. Therefore, the emphasis put on the moral rights in *Magill* decision of the CFI would not be universally accepted in all Member States.[197]

It is difficult to disregard the apparent eccentricity that, although the original terminology for this concept emerged in the context of copyright, the Court either purposefully - due to distinct nature of rights copyright entails - or incidentally avoided putting forward a sharp definition of what 'specific subject-matter' of copyright is. On different occasions as of *Deutsche Grammophon*, as we pointed out above, various meanings and contents were - although the terminology used appeared to be quite non-linear- ascribed to specific subject-matter of copyright. It took over two decades after *Deutsche Grammophon* for the Court to set about producing a more complete definition by using the original terminology of 'specific subject-matter' in relation to copyright. Accordingly, in *Phil Collins v. Imrat* it articulated with a reference to *MusikVertrieb membran v GEMA* that:

*"The specific subject-matter of those rights, as governed by national legislation, is to ensure the protection of the moral and economic rights of their holders. The protection of moral rights enables authors and performers, in particular, to object to any distortion, mutilation or other modification of a work which would be prejudicial to their honor or reputation. Copyright and related rights are also economic in nature, in that they confer the right to exploit commercially the marketing of the protected work, particularly in the form of licenses granted in return for payment of royalties."*[198]

***Design Rights***

From the first appearance of a design-related dispute before the Court of Justice, an initial doubt, similar to that existed in the context of copyright, as to whether design rights exhibit a sort of industrial and commercial property within the meaning of Art. 36 TEEC was topical. The Court on that occasion, namely *Keurkoop BV v Nancy Kean Gifts*, answered the question in affirmative.[199] Beyond that however, the Court neither defined nor did it have a recourse to specific subject-matter. After a decade-long silence, the Court of Justice, on the same day but in the context of two different judgements, came up with two fairly similar definitions. In *CICRA v. Renault* it held that:

[197] SEVILLE, *supra* note 122, at 324
[198] Joined Cases C-92/92 and C-326/92: Phil Collins v Imtrat, para. 20; Joined Cases 55/80 and 57/80 MusikVertrieb membran v GEMA, para. 12
[199] Case 144/81: Keurkoop BV v Nancy Kean Gifts BV, para. 20

*"[T]he authority of a proprietor of a protective right in respect of an ornamental model to oppose the manufacture by third parties, for the purposes of sale on the internal market or export, of products incorporating the design or to prevent the import of such products manufactured without its consent in other Member States constitutes the substance of his exclusive right."*[200]

In a similar vein but more compactly in *Volvo v. Veng* it stated:

*"the right of the proprietor of a protected design to prevent third parties from manufacturing and selling or importing, without its consent, products incorporating the design constitutes the very subject-matter of his exclusive right"*[201]

### 3. Polysemy of 'Specific Subject Matter' and Fluxional Definitions

The common watermark in the series of attempts devoted to defining the specific subject-matter is the fluxional contextual purviews ascribed to it by the Court. Likewise, the terminology used on different occasions to connote the notion of specific subject-matter appears to have amply varied. Essential function, essential rights, substance of right and the very subject-matter were only some of the enunciations the Court employed.[202] Although arguably these are aimed at indicating the same notion, some scholarly opinion, credibly, contends different layers are involved. Accordingly, all of the terms used in this context is perceived to have boiled down to two potential meanings. Roughly speaking one meaning infers the catalogue of the rights protected under a particular intellectual property right; i.e. what a copyright, patent, trademark or a design confers on its right holder. Second meaning on the other hand relates to the philosophical background of (the objective behind) the grant of the right, which presumably varies from one type to another.[203]

With the lack of consistent reference to both layers on several occasions, it is not fully discernable from the above-referred jurisprudence whether the intent of the Court was to

[200] Case 53/87: CICRA v. Renault, para. 11
[201] Case 238/87: Volvo v. Erik Veng, para. 8
[202] For a reference to the respective judgements revisit the preceding paragraphs where we mentioned the definitions of the notion for different intellectual property rights.
[203] Korah, in this regard, maintains that "[it] refers both to the nature of the right and the reason for conferring it." See. Valentine Korah, *The Limitation of Copyright and Patents by the Rules for the Free Movement of Goods in the European Common Market*, 14 Case W. Res. J. Int'l L. 7, 18 (1982); Keeling, in a similar vein, articulates that "it has a purely descriptive meaning: it describes the core of essential rights granted to the proprietor of a patent, trade mark or some other form of intellectual property… it [also] refers to the policy aims pursued by the legislation which created the intellectual property right." See. KEELING, *supra* note 9, at 633

embrace the both meanings or either one of them.[204] What brings further complexity into the test of specific subject-matter is that neither the collection of prerogatives that intellectual property rights confer on the right holder, nor the policy reasons in granting are identical among the Member States.[205] If the basis in determining specific subject-matter is the catalogue of essential prerogatives of intellectual property rights, what should be the reference point in adjusting that catalogue? If the intent was to provide a minimum common of the laws of the Member States then the protection accorded to that right by the law of that Member State that is more advanced than the minimum threshold would factually be inapplicable. If, on the other hand, the catalogue of rights that remain in specific subject-matter, i.e. an immune area, is to be determined with a reference to the substantive description laid out in the law of granting Member State then there would occur disparities between specific subject-matter of the rights granted by one Member State and the other; which is, in effect, not quite different than Member States having distinct laws inciting the market partitioning. Yet, in the case the Court is to set out minimum standards as to the core prerogatives of the rights, this would be akin to harmonizing the substantive intellectual property rights of the Member States for which the Court does not have authority, nor is there relevant basis in the Community law.[206] Alternatively, should the basis in organizing the specific subject-matter be the reason for grant, i.e. policy objectives therein, it is again incapable of offering a general criterion since on theoretical basis intellectual property rights are motivated by somewhat different objectives in different Member States. Secondly, regardless of what function (or objective) a particular Member State places in the background - be it incentivizing inventorship, rewarding creative effort or facilitating industrial and artistic progress - the minimum amount of protection that is required to actualize that purpose - and that protection also coincides the immune area - still remains ambiguous.

The Court, although not with utmost consistency, referred to the both meanings.[207] It is probable that its intent was to avail itself of the both connotations flowing from the term 'specific subject-matter' which clearly enables a greater room for maneuver. This very point also represents the merit of the criticism against the specific subject-matter test which was not

[204] It is noteworthy though, with a more systematic and linear apprehension of the doctrine, Torremans suggests that the essential function is an integral part of the specific subject matter, which stresses the fact that the specific subject matter is defined in such a way that the essential function will be fulfilled. TORREMANS *supra* note 1 at 129.
[205] See footnote 121 above.
[206] KEELING, *supra* note 9, at 68, with reference to Friedrich K. Beier, I*ndustrial Property and the Free Movement of Goods,* 21 IIC 131, 148 (1990)
[207] Korah *supra* note 121 at 335

considered to be able to shed further light into the imprecise outlines of the existence/exercise distinction. It is, therefore, only a statement of obvious, as follows from the cases above, that the ECJ tuned the definitions of specific subject-matter purposively and on each occasion, it ascribed them the meanings that would justify the Court`s preset view.[208] Undeniable however, these were aimed at offering case-specific and prompt solutions in the lack of Community-wide laws on intellectual property. Solutions of that sort are conceivably what the Court needed in early stages even at the cost of sacrifices from legal certainty so as to keep the free movements functioning against intellectual property rights.

It could be seen that the intent behind the Court`s enthusiasm to define specific subject matter was not the desire of approximating the intellectual property theories of the Member States or extracting a Union-wide applicable list of essential prerogatives. No would doing so fall into the competence area of the judiciary.[209] The said intent, on the contrary, more likely to be that of distinguishing the area of legitimate and illegitimate exercise of the national rights on the face of Community rules[210]; relying on the supremacy of the latter. Correspondingly, the specific subject matter was not judged by the catalogue of rights granted by national laws -which differs among the Member States-, but rather by the extent to which free movement provisions could tolerate the exercise of these rights. Nor did the Court fully regard the different objectives of individual national rights in granting those rights. Instead, it confined itself to taking an unelaborated look at generally discernable outlines of IP theory. Indeed, the contrary would render contrasting specific subject matter (hence immunity) areas depending on the *raison d'être* of the national law at issue.[211] Therefore the doctrine of the Court seems to have proceeded on a policy-oriented and intuitive line than a strictly doctrinal one. Consequently, occasion-based interpretation of specific subject matter makes, at least, practical sense and definitely serves the purposes of that doctrine. However it is equally clear that this ample functionality comes at the cost of legal predictability.

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[208] KEELING, *supra* note 9, at 65; STOTHERS, *supra* note 142, at 31; Korah, *supra* note 203 at 43

[209] Beier, *supra* note 206

[210] Maria José Schmidt-Kessen, *The Future of IP-competition Conflicts in EU Law*, Copenhagen Business School, 24 CBS LAW Research Paper 5 (2019). This idea has been reflected by the Court in its *Keurkoop v. Nancy Kean Gifts* judgement with the dichotomy of 'legitimate' versus 'improper' exercise; see: Case C-144/81: Keurkoop BV v. Nancy Kean Gifts BV, para. 24. It goes without saying, nevertheless, neither does such a dichotomy offer an objective criterion in determining the limits of exercise of national rights.

[211] On different implications of various IP theories in the context of exhaustion of rights, see: Michael Waelbroeck, *The Effect of the Rome Treaty on the Exercise of National Industrial Property Rights*, 21 Antitrust BULL. 99, 105-110 (1976)

The actual value of the specific subject-matter doctrine, besides the practical usefulness arising from its flexibility, is that it paved the way to the doctrine of Community exhaustion which since then proved to be the key instrument of reconciling intellectual property rights and free movement. Amidst the scattered definitions, holdings of the Court underline that the specific subject matter of a right does not encompass the right to erect barriers to free trade by preventing parallel imports of the goods, as long as they have been marketed by the right holder or with the right holder's consent.[212] Thus, although different types of rights connote their own specific subject matters, the common thread, or minimum exclusivity that constitute the core, is the authority to put (or authorize another person to do so) into market for the first time the goods on which the rights are incorporated.[213] The latter in effect corresponds to the merits of Community exhaustion, i.e. the rights are principally exhausted after the first sale.

[212] SEVILLE, *supra* note 122, at 327
[213] BARNARD, *supra* note 105 at 159

# CHAPTER 4

# EXHAUSTION OF RIGHTS

## 1. General Concept of Exhaustion and the its Function

Proprietary rights essentially vest the right holder with a set of absolutory prerogatives with respect to the subject matter of the ownership, i.e. the object on which proprietary right exists. This contains *inter alia* the right to use, sell, destroy or otherwise dispose of the subject on which proprietary right is established. Such fundamental construct of property ownership has, in the rudimentary sense, very little to do with whether the goods at the center of ownership incorporate intellectual property rights. In fact, it is hard to envisage, especially in contemporary times, any product that does not embody at least one intellectual property right. The simple logic of property ownership dictates that once the goods bearing intellectual property rights, be that patent, trademark or copyright, are lawfully acquired, the owners of goods should not face further interference of the intellectual property right holder in respect to subsequent use, sales or otherwise disposing of those goods.

Exhaustion doctrine actualizes the said logic by enjoining the intellectual property right holder`s exclusive prerogatives to market (that entails distribution right and the right to import) those goods after the first (initial) marketing thereof by the right-holder *per se* or the other agents who act upon the right-holder`s consent. Without exhaustion the intellectual property right holder would retain the ownership not only over the IP rights, but also retain control over the goods bearing the rights, even after the initial marketing of them. In other words, if it wasn't for the exhaustion of rights, intellectual property right holders would be permitted to exercise a perpetual control over the use, sale and import of the respective goods, leaving a strong adverse effect on commerce.[214] Also, it can be said that the exhaustion principle, obliquely, highlights the autonomy (or independence) of the IP right ownership from that of the physical goods that incorporate the latter.

The term of 'exhaustion', which is now uniformly employed to address the notion that demarcates the destiny of the goods from that of intellectual property rights therein as referred

[214] Enrico Bonadio, *Parallel imports in a global market: Should a generalised international exhaustion be the next step?* 33(3) EIPR 153, 153 (2011)

above, is said to have been devised by German *Reichsgericht* in the context of patents in 1902 judgement.[215] The German Court`s passage read as follows[216]:

> *"The effect of a patent (for a process) is that no-one, except the proprietor (or the persons whom he has authorized) may manufacture a product by the said process and put it on the domestic market. By this act, however, the effect of the protection conferred by the patent is exhausted. The proprietor who has manufactured the product and has put it on the market under this protection which excludes competition from other parties, has enjoyed advantages which the patent confers upon him and has thus exhausted his right."*

In an earlier stage, the same principle was practiced, albeit under a different name, by the US Courts: the first sale doctrine.[217] However differently the principle was addressed by the jurisprudence of the two different legal traditions, there is no significant guideline as to distinguish the doctrine of exhaustion from that of first sale; in practice these terms are used interchangeably up to this day. Exhaustion in this sense does not vest the right holder with an autonomous discretion *vis-à-vis* exclusive distribution right being extinguished; it rather intrinsically occurs upon a consensual marketing of the corporeal goods. A similar function to that of exhaustion, albeit more penetrable, has been ascribed to the implied license theory by the United Kingdom Law (likewise by the majority of the Common Law Tradition pursuers including Australia, Canada and New Zealand)[218] whereby in principle the possessor of the corporeal goods had to obtain the right holder`s authorization, i.e. license, so as to use, resell and distribute these goods. However the situation in the absence of such a license amounted to an absolute control of the IPR holder over the goods even after the transfer of the tittle, the proprietary interest of the purchaser and the interest of free trade was ensured by a default presumption of such a license. Accordingly, an implied license is presumed unless an express restriction on the type of use, sales and distribution is imposed by the right holder. This logic was articulated as follows *"When a man has purchased an article he expects to have the control of it, and there must be some clear and explicit agreement to the contrary to justify the vendor in saying that he has not given the purchaser his license to sell the article, or to use it wherever*

[215] Guajakol-Karbonat RGZ 51, 139 (26.03.1902)
[216] The relevant passage of the judgement was cited in English in Records of the Luxembourg Conference on the Community patent 1975, pp. 40
[217] In relation to patents, see: Adams v Burke 84 US (17 Wall) 453 (Sup Ct, 1873); in the context of trademark, see: Appolinaris v Scherer 27 F 18 (CC SDNY, 1886)
[218] Yusuf & von Hase, *supra* note 21 at 117

*he pleases as against himself*. "[219] By the same token however, the right holder has the liberty to impose such restrictions in the sales contract, thus retaining privilege to effectively derogate from the exhaustion. It is due to such privilege that, under the regime of implied license, the freedom to resell, and by extension freedom to import, were entirely vulnerable to the principle of freedom of contract.[220] It is noted that the European jurisprudence opted for the principle of exhaustion and not implied license theory very early on, due to this inherent risk.[221]

There are two crucial points in relation to the subject of exhaustion, i.e. incorporeal goods, that need to be highlighted. Firstly, the goods in question are genuine goods that were initially put in the market by the right holder or with its consent. The contrary scenario would constitute non-genuine goods that, at one extreme, would also cover counterfeit or piracy depending on the type of intellectual property right thus breached. This is also the case when similar rights held by economically and legally independent bodies in different states; even though both rights are recognized by the law in their respective state, the products incorporating those rights would amount to infringing goods in the other state given that the national rights in that state are held by economically and legally independent bodies. The products of this sort would obviously not trigger the exhaustion because they had not originated from the right holder. Therefore, the national right holder can oppose to the importation into the country of protection of the goods that were manufactured by a third party. Even if that third-party manufacturer holds the intellectual property rights in the country of export, his products infringe the national rights in the country of import; hence the right holder in the importing state could stop such importations relying on his/her intellectual property rights. In the end there is no room for ambiguity that infringing products do not constitute a basis for exhaustion.

Secondly, the subject of exhaustion must be definite. Exhaustion occurs in respect to each particular good - that may be a single product or a multiple number of products that were in one consignment - that were lawfully marketed; not to the particular type of product. Accordingly, merely because the right holder previously marketed the goods of that type, he cannot be deemed to have consented on marketing, in the future, of the similar articles: the consent, hence the exhaustion, in principle concerns each specific consignment (or batch) of goods. For example, trademark holder might have previously marketed soap bars bearing his trademark, however the said marketing does not exhaust his rights in respect to those articles

[219] Betts v Willmott (1871) LC 6 Ch App 239, 245
[220] DAVID I. BAINBRIDGE, INTELLECTUAL PROPERTY 828 (Pearson Education 7th ed. 2009)
[221] Schovsbo, *supra* note 167 at 175.

which were leaked, stolen or otherwise extracted from his storage unit and marketed without his consent.

The actual functioning of the exhaustion doctrine as well as its reverberations on trade are to be found in respect to genuine products that have been marketed by or with consent of the intellectual property right holder. The extent to which the exhaustion principle enjoins the right holder from intervening the subsequent sales of the products that were initially marketed by him or his consent is strictly dependent on the territorial scope of exhaustion that is determined by the law of the country of protection. Following the territorial pattern that is historically as well as -to a significant extent- contemporarily prevalent in intellectual property law, national exhaustion of rights is regarded as an essential minimum.[222] Typically in most jurisdiction, the intellectual property rights are exhausted in respect to the country of protection once the products are put on the domestic market, hence subsequent commercialization of the relevant products in the respective national territory cannot be prevented by the right holder; this represents the basic form of exhaustion. Indeed, reducing the scope of exhaustion within the national boundaries would result in fragmentation of the domestic market, thus it has no relevance or benefit.[223] This follows that intellectual property rights, in essence, are not keen to present an obstacle to trade, as long as the said trade is domestic in the country of protection: rights exhausted upon the initial marketing. However once international trade, as in the example of the EU, is at hand, the exhaustion regime is the determinant of whether or not the intellectual property rights would serve for partitioning of domestic markets. This intrinsically brings into question of parallel imports, the notion of which can simply be recollected as the importation by others into the country of protection of the genuine goods that were put on the market abroad by the right holder or with his consent.[224] In that case it will depend on the exhaustion regime that is adopted by the importing country where the intellectual property rights are protected whether parallel imports are permitted. On that note it is relevant to take brief glance at different exhaustion regimes.

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[222] KEELING, *supra* note 9 at 78

[223] It has to be noted that a regime stricter than the exhaustion modality had existed in French, Belgian and Luxembourgian laws under the name of 'right of destination' which, in essence, allowed the right holder to interfere with the flow of products until it reached the end-user by invoking his trademark or copyright. However as a result of Community rules, it is now of historical interest. See. Stothers, *supra* note 149, at 335; STOTHERS, *supra* note 101 at 41; MEZEI, *supra* note 1 at 30. Gotzen also emphasizes the difference between the exhaustion principle and the right of destination to the effect that the latter appears far more incisive and restrictive. In that, the notes that the right of destination amounts to rejection of exhaustion principle all together since it continues to apply to subsequent use or dealing with copies of the work, even after the stage of first marketing has been passed. Frank Gotzen, *Distribution and Exhaustion in the EC*, 12(8) EIPR 299, 301 (1990)

[224] CAHIT SULUK *et al.*, FIKRI MÜLKIYET HUKUKU 13 (2 ed. Seçkin 2018)

**-** *National:* In the jurisdictions which apply national exhaustion, the national rights are not exhausted on the basis of the sales abroad of the IP protected products. Therefore, the right holder retains the prerogative to stop importation into the said jurisdiction of the goods that he/she initially marketed abroad. In other words, the right holder could thus block the parallel imports.

- *International:* Intellectual property rights in the jurisdictions which adopted international exhaustion regime shall exhaust upon the first sale of the protected articles regardless of where the said sale took place. Accordingly, once the incorporating products are marketed abroad, the right holder can no longer oppose to parallel imports of those into the country of protection.

- *Regional:* A middle way to exhaustion is offered by a regional model. It embodies certain features of both national and international pattern. Resemblance to the national model is that the designated region acts, in respect to exhaustion of rights, as if it is one country; that means the parallel imports from outside the region can be blocked by the right holder(s) in the said region. However, the designated region in itself resembles, as it were, a limited model of international exhaustion due to multinational structure therein. This follows that the rights will be exhausted in respect to the entire region, i.e. all the countries thereof, once the product was put on the market anywhere within that region. The Community exhaustion is the most emblematic example of this modality.

Without calling into question the requirement of will or consent of the right holder to marketing, it is clear that, depending on the selected exhaustion regime, the place of first marketing thus will be the prime consideration in determining whether the exhaustion occurred. Although that is not necessarily the case for the jurisdictions applying international exhaustion, much will depend on territory of first sale when the country of protection follows the national or regional exhaustion model.

Certain arguments in favor of each type of exhaustion as well as critical stances have been expressed. Not surprisingly the same considerations identically apply *vis-à-vis* whether parallel trade should be permitted. Much of these tends transpire on the axis of the pro-free-trade arguments, preserving and incentivizing the domestic industries, consumer benefit and the potential risk of counterfeiting and piracy. Although putting forward a comparative empirical analysis of the commercial reverberations of different exhaustion regimes exceed the purposes of this study, it is clear from the variety of arguments in this regard that the selection

of regimes of exhaustion is interrelated with the market model and the policy goals envisaged for that particular jurisdiction. Accordingly, the easier and territorially broader the rights exhaust, the more liberal international trade gets. By the same token, the narrower the territorial scope of exhaustion, the stronger intellectual property protection thus the incentive for further innovate gets.[225] The market isolation would have been prevented to the geographical extent to which the rights are exhausted following the first sale. If such a partitioning is desired to be prevented within a certain region, then the solution comes as no surprise: regional exhaustion. If, however, the intent is to open the market to international competition with a probable view to advancing the customer welfare and to stimulating the competitive strength in the relevant market towards the level of international competition, then the chosen exhaustion regime would potentially be the international one. National exhaustion modality and that of international exhaustion represent the two opposite ends of that scale. National exhaustion in that would serve as a major tool of market partitioning given that in such modality the right-holder retains the privilege to block import of the genuine goods, i.e. parallel imports.

Consequently, the destiny of parallel trade activities strictly depends on the exhaustion regime applicable, particularly that of the importing state where the rights are protected. Here at this point it may be relevant to highlight the importance of parallel import activities for the European internal market. Activities of that kind are akin to and reflective of the characteristics of the Internal Market insofar as (i) they allow the third-party traders to compete with the intellectual property right holder (i.e. intra-brand competition) in the importing country; (ii) they require and rely on free movement of goods without being interrupted by intellectual property prerogatives on imports.

Due regard being had to the fundamental premises of the Single Market: i.e. free movement principle and that of undistorted competition, as enshrined by the Treaty, the inherent reverberations of national exhaustion appear to be intolerable. This follows that in order for the free movement principle to function, the realm of exhaustion of rights should coincide - at least - the territorial area where the free movement principle is intended to cover: that is the European Community and later the European Economic Area. It is important to realize that while the regime of national exhaustion is susceptible to impede free movement of goods thus it is off the question for the internal European market, international exhaustion is

[225] For an account of comparative advantages and disadvantages of national and international exhaustion modalities; See. Carsten Fink, *Entering the Jungle of Intellectual Property Rights Exhaustion and Parallel Importation* (In CARSTEN FINK & KEITH E. MASKUS EDS., INTELLECTUAL PROPERTY AND DEVELOPMENT: LESSONS FROM RECENT ECONOMIC RESEARCH 171-187, World Bank & Oxford University Press 2005)

not liable to create such an effect. On that note, until recently, the question of whether the regional exhaustion is the only modality or the Member States have the liberty for opting for international exhaustion was still topical; furthermore, international exhaustion has been enthusiastically advocated by a number of Member States up to the present. We shall focus on the territorial realm of exhaustion in the ensuing parts of the study.

**2. The Community Exhaustion (Formulation)**

The reconciliation of the conflicting aims of Articles 34, 36 and 345 of the TFEU, is achieved by the doctrine of Community (Union-wide) exhaustion[226] and the ECJ reasoned his way to the Community exhaustion by the medium of its earlier doctrines, that being the existence/exercise distinction and the doctrine of specific subject matter.[227] This, although introduced to be a general test, entails a rather case specific appraisal of the intellectual property prerogatives against the essential function thereof; only those which are within the realm of the essential function are to be protected in spite of free movement rules.

As far as patents are concerned, the essential function is to give out the patentee the exclusive possibility, in respect to each good incorporating that patent, to derive monopoly profit through the first sale thereof thus rewarding the creative effort of the inventor. Essential function ascribed to trademarks is to protect the mark holder against the competitors who desire to free ride on the reputation and goodwill embodied in the trademark; and to guarantee the origin of the products thus preventing consumer confusion and assuring the quality of products. Obviously in either case the right holder`s exclusivity to manufacture the products is not called into question; the contrary would result in counterfeit or pirated products.

With these essential functions in mind, and in line with the aims of the Treaty in respect to the Single Market, it appears to have no justification to prevent further distribution - including the distribution by way of imports in general and parallel imports in particular - of the products that were initially put on the market (put into circulation) by the right-holder or with his/her consent. Indeed, once the right holder had the privilege to select the place of initial marketing, and insofar as the right holder and those who are acting upon the latter`s consent retain the exclusive authority to make the initial sales in that selected market, the essential function can be said to have been fulfilled. In the same vein, the exclusive prerogative to initial

[226] JOSEF DREXL ed., RESEARCH HANDBOOK ON INTELLECTUAL PROPERTY AND COMPETITION LAW 412 (Edward Elgar Publishing 2010)
[227] KEELING, *supra* note 9 at 72

marketing of the products connotes that the genuine products incorporating trademarks can only be put in the market by the right holder or with his/her consent. Thus, once the genuine products are marketed by the right holder, further commercializing of those by the others would not undermine the commercial goodwill and reputation of the right holder as those products initially originated from the right holder. Nor would the functions of preventing consumer confusion and that of guarantee of origin be impeded, products being originated from the right holder who is the origin and the assurer of the estimated level of quality. The same is the case for other forms of intellectual property rights, not least for copyright, the essential function of which is to protect the moral rights in the work and to ensure a reward for the creative effort.[228] Therefore it follows that the right to interfere with the subsequent commercialization of incorporating products by relying on the right to distribution and to import, that are principally and typically among the intellectual property prerogatives, do not constitute the specific subject matter of rights: they are not susceptible to the immunity from free movement principle on the grounds of 'protection of industrial and commercial property'. They exhaust in the EEA after the initial sale by the right holder or with the latter`s consent so that the products can circulate freely.

Emerging through this logical sequence, the original prescription of the Community exhaustion, as constructed in *Deutsche Grammophon*, was rather compact. Accordingly, it would be repugnant to the *raison d'être* of the Treaty to allow the intellectual property right owners to rely on their rights to prevent the marketing in a Member State of the products that which were marketed in another Member State by the right holder per se or with the latter`s consent.[229] Although the right may constitute industrial or commercial property within the meaning of Article 36 TFEU, such exercise of that right would constitute 'a means of arbitrary discrimination or a disguised restriction on trade between Member States', thus prohibited, as prescribed in the same provision.[230] Quite evidently this passage puts in perspective the very essence of the issue between the free movement principle and the protection accorded to intellectual property rights. However the selection that the ECJ jurisprudence is keen to make among the said two competing interests is - and has been - foregone, the aforementioned passage prescribes a well-founded way and a proper medium of putting this selection into practice. That medium is, as we referred above, the Community-wide exhaustion of rights.

[228] Case C-241/91: RTE and ITP v Commission, para. 28
[229] Case C-78/70: Deutsche Grammophon v. Metro, para. 12
[230] STOTHERS, *supra* note 101 at 43

According to that prescription, the exhaustion is set into motion when two conditions are collectively fulfilled: (i) The products being put on the market in one Member State; (ii) that marketing being done by the rights holder or with his consent.

***Codification of the Exhaustion Doctrine in Community Law***

It is needless to state that, although exhaustion was thus conceptualized in a dispute that was centered around copyright and related rights, the same concept applied to different types of intellectual property rights including trademark[231], patents[232] and design rights.[233] This is of little surprise once it is realized that intellectual property rights of every type share the common thread of distribution right, that is susceptible to erect a barrier to intra-Union trade, if not exhausted. Furthermore, although it was the consideration of the primary law of the Union, particularly of articles 34 and 36 TFEU, that prepared the ground for such an exhaustion formula, it has also been codified, thus given a legislative form, by the subsequent secondary law of the Community harmonizing intellectual property legislations as well as those creating unitary European intellectual property.[234] In that, the first Trademark Directive on approximation of national trademark laws[235], as well as the Trademark Regulation on creating Community trademark of unitary character[236]; the copyright Directives on legal protection of computer programs[237], on rental right and lending right and on certain rights related to copyright[238], on legal protection of databases[239], harmonization of certain aspects of copyright

[231] Case C-16/74 - Centrafarm v. Winthrop
[232] Case C-15/74 - Centrafarm v. Sterling Drug
[233] Case C-144/81 - Keurkoop v. Nancy Kean Gifts
[234] Stothers, *supra* note 149, at 336
[235] Directive 89/104 (The First Trademark Directive), Article 7(1) reads: The trade mark shall not entitle the proprietor to prohibit its use in relation to goods which have been put on the market in the Community under that trade mark by the proprietor or with his consent.
[236] Regulation 40/94 on the Community trade mark, on its Article 13(1) provides for an identical provision to that of aforesaid directive; only difference is the expression of 'Community trademark'.
[237] Directive 91/250 on the legal protection of computer programs (replaced by Directive 2009/24), Article 4(c) reads: The first sale in the Community of a copy of a program by the right holder or with his consent shall exhaust the distribution right within the Community of that copy, with the exception of the right to control further rental of the program or a copy thereof.
[238] Directive 92/100 on rental right and lending right and on certain rights related to copyright in the field of intellectual property (replaced by Directive 2006/115), Article 9(2) reads: The distribution right shall not be exhausted within the … except where the first sale in the Community of that object is made by the right holder or with his consent.
[239] Directive 96/9 on the legal protection of databases, Article 5(c) reads: … The first sale in the Community of a copy of the database by the right holder or with his consent shall exhaust the right to control resale of that copy within the Community.

and related rights in the information society[240]; the Design Directive[241] and Regulation[242] uniformly adopted the exhaustion formula that referred to placement on the market in the Community of goods by or with the consent of the right holder. The rights on plant varieties which has been unified across the Community since 1994 also follow alike formulation on the exhaustion thereof.[243] Although the formulation of the exhaustion in the latter implicates 'disposing of to others' instead of 'putting on the market' of the protected material[244], relatively recent evidence over the case law of the European Court of Justice clarifies that the concept of 'disposing of to others' corresponds to the traditional notion of 'putting on the market'.[245]

Moreover, as far as patents are concerned, a great deal of empirical evidence on the face of the long history of failed patent unification attempts suggest that an identical formulation was likewise intended to be taken in respect to patent exhaustion.[246] At the outset, the First[247] and Second[248] Community Patent Conventions (CPC), which have never come into force, provided for the exhaustion to occur in respect both to the envisaged unitary patent and national ones when the incorporating goods are put on the market by the patent proprietor or with latter`s express consent.[249] Although as was previously emphasized the said regulations never came into force, hence they are now of historical interest, similar formulations have been employed in the subsequent attempts of creating a Community-wide patent system.[250] The final attention in this regard needs to be paid at the most recent attempt on constructing a European

[240] Directive 2001/29 on the harmonisation of certain aspects of copyright and related rights in the information society (Also known as the InfoSoc Directive), Article 4(2) reads: The distribution right shall not be exhausted within the Community in respect of the original or copies of the work, except where the first sale or other transfer of ownership in the Community of that object is made by the right holder or with his consent.
[241] Directive 98/71 on the legal protection of designs, Article 15 reads: The rights conferred by a design right upon registration shall not extend to acts relating to a [corporeal] product ... when the product has been put on the market in the Community by the holder of the design right or with his consent.
[242] Regulation 6/2002 on Community designs; Article 21 used a wording identical to that of Design Directive above, albeit having referred to 'Community design'.
[243] Regulation 2100/94 of 27 July 1994 on Community plant variety rights.
[244] Id. Article 16
[245] In the case C-140/10 Greenstar-Kanzi Europe NV v Jean Hustin and Jo Goossens, the ECJ, having pointed out that the scope of the principle of exhaustion had not yet been interpreted, has used the term of 'placing of the goods on the market' interchangeably with that of 'disposing of to others' as stated in the Plant Variety Regulation. See. para. 36 and 41 of the judgement.
[246] For the chronology and a detailed analysis of patent unification attempts in the EU, See: Aurora Plomer, *A unitary patent for a (Dis) United Europe: the long shadow of history* 46(4) IIC 508-533 (2015)
[247] 1976 CONVENTION FOR THE EUROPEAN PATENT FOR THE COMMON MARKET (Community Patent Convention) (76/76/EEC)
[248] 1989 AGREEMENT RELATING TO COMMUNITY PATENTS Done at Luxembourg on 15 December 1989 (89/695/EEC)
[249] Articles 32 and 81 of 1976 CPC; Articles 28 and 76 of 1989 CPC
[250] Proposal for a Council Regulation on the Community patent, Article 10; the expression used 'his consent' instead of 'his express consent'.

Patent With Unitary Effect and a Unified Patent Court (UPC), the regulatory framework of which was adopted but has yet to come into application. The start of application of the Regulations establishing the Unitary Patent system[251] is conditioned, by means of a self-contained provision, to the entry into force of the Agreement on a Unified Patent Court (UPC) which is to constitute the judicial pillar of the system.[252] The latter`s entry into force, on the other hand, requires the ratification thereof by at least thirteen Member States the cluster which has to include those three Member States with the highest number of European Patents effective.[253] As of yet, amid constitutional coherence debates, the actual holdup on the way of bringing the system into function seems to be the requirement of ratification by the top-three Member States.[254] Aside from the archaic encumbrances in adopting a unitary patent system that have been prevalent up to this day, the envisaged exhaustion modality thereof, nevertheless, remained loyal to the two factors established in *Deutsche Grammophon*.[255]

As compact as these two factors in pinpointing where the exhaustion starts, an ample array of modalities as to marketing and consenting to such marketing tends to branch out from the main concept. The complex quiddity of commercial relations and networks tends to make

[251] Regulation 1257/2012 implementing enhanced cooperation in the area of the creation of unitary patent protection; Regulation 1260/2012 implementing enhanced cooperation in the area of the creation of unitary patent protection with regard to the applicable translation arrangements

[252] Article 18(2) of the Regulation 1257/2012 states "It shall apply from 1 January 2014 or the date of entry into force of the Agreement on a Unified Patent Court (the 'Agreement'), whichever is the later."

[253] Agreement on a Unified Patent Court (2013/C 175/01), Article 89(1) reads "This Agreement shall enter into force on 1 January 2014 or on the first day of the fourth month after the deposit of the thirteenth instrument of ratification or accession … including the three Member States in which the highest number of European patents had effect in the year preceding the year in which the signature of the Agreement takes place..., whichever is the latest."

[254] By the time this study was being conducted, Germany being one of those three Member States with the highest number of European Patents, the most recent obstacle before the entry into force of the UPC Agreement was the decision of the German Constitutional Court (2 BvR 739/17) upon a plea of unconstitutionality in relation to the German Parliamentary Act of Approval to the Agreement on a Unified Patent Court. The complaint regarded, *inter alia,* the failure in following the procedural requirements in transferring the sovereign powers as enshrined by the Article 23(1) of German Basic Law, in conjunction with the Article 79 of the same law. In that, the German Federal Constitutional Court found that the Approval Act is deemed void for it lacked the constitutionally mandated voting majority.
For the said decision: https://www.bundesverfassungsgericht.de/SharedDocs/Downloads/DE/2020/02/rs20200213_2bvr073917.pdf?__blob=publicationFile&v=1 (Available in German);
For the press release of the German Federal Constitutional on the judgement in English language: https://www.bundesverfassungsgericht.de/SharedDocs/Pressemitteilungen/EN/2020/bvg20-020.html
For the text of German Basic Law in English: https://www.gesetze-im-internet.de/englisch_gg/englisch_gg.html#p0127

[255] Article 6 of the Regulation 1257/2012 reads "The rights conferred by a European patent with unitary effect shall not extend to acts concerning a product covered by that patent which are carried out within the participating Member States in which that patent has unitary effect after that product has been placed on the market in the Union by, or with the consent of, the patent proprietor, unless there are legitimate grounds for the patent proprietor to oppose further commercialisation of the product."

it more difficult than it sounds to pin down whether the conditions of exhaustion matured in each specific case. Indeed, the commercial activities do not usually transpire on end-to-end basis[256]; frequently multiple number of agents and entities, such as sub-companies, subsidiaries, licensees, assignees or distributors get involved in the commercial continuum. It is therefore not clear from the outset whether the consent of the right holder should be extracted from the practices of the said agents and entities which may or may not be strongly linked to the right holder. Insofar as the different scenarios therein tend to yield distinct reverberations on the account of exhaustion, we shall examine these scenarios in turn.

### 3. The Concept of Putting on The Market

The original language of *Deutsche Grammophon* regarded the exhaustion to be effected when the protected articles are placed on the market' by the right holder or with his/her consent. Subsequent case law (for example *Centrafarm v. Sterling*; *Centrafarm v. Withrop*; *Pharmon v. Hoechst*) referred to the same notion as 'marketed'; put into circulation (*Musik-Vertrieb membrane v. GEMA*; *Keurkoop v Nancy Kean Gifts; IHT v Ideal-Standard*); put on the market (*BMS v. Paranova*; *Eurim pharm v. Beiersdorf*). Occasionally a multitude of various terms were used within the same judgement (See. *Merck v. Stephar*). Furthermore, the codification of the exhaustion rule into the secondary law of the Union did not seem to unify the terminology used.[257] Nevertheless, it is apparent from the context that the whole range of different terminology connoted the act that effectuated the exhaustion, that is the initial marketing of the corporeal products.

However, as we pointed out above, the string of distribution following the production process is often complicated and involves a multitude of sub-steps of distribution. Some those steps are effectuated by the right-holder within its own operation, i.e. among vertically integrated entities of the same economic group. It is perfectly possible that all of the agents involved in the distribution process is the part of the same economic group; or it is just as possible that all the entities from the manufacturer to wholesaler, from the wholesaler to retailer, and finally from the retailer to the actual consumer are not economically or legally linked. Often in this chain there involved a combination of economically or legally linked entities and independent intermediaries. The actual hardship among this extensive chain of

[256] By end-to-end we mean the setting in which the products incorporating the intellectual property rights is supplied directly to the end user, or consumer by the right holder who is assumed to be the manufacturer.
[257] For instance, Trademark Directive and Community Design Directive speak of 'put on the market', whereas Unitary Patent Regulation refers to 'placed on the market'.

distribution is to pinpoint the moment at which the exhaustion should be deemed to have occurred.

***Peak Holding v. Axolin-Elinor***

In *Peak Holding*[258], the Court of Justice, having pointed out the decisive role of being 'put on the market' in the extinction of rights, acknowledged that this notion should be interpreted in a consistent manner within the Community legal order.[259] The factual background centered around a consignment of 25000 garments bearing the trademark (PEAK PERFORMANCE) that belonged to Peak Holding, a clothing company which sells its products under the said mark in Sweden and other countries. The articles in question had been manufactured outside the EEA on behalf of Peak Holding and imported by the latter into the EEA with a view to being sold there. The garments were first offered for sale through the sister store of Peak Holding in Denmark, however some of them remained unsold. The remainder was then brought back to the warehouse of Peak Holding, from where, it was subsequently sold to COPAD, a French company, with an alleged contractual restriction of resale in Europe, only 5% of the consignment could be resold in France. A Swedish company called Factory Outlet (Axolin-Elinor) acquired the said consignment of garments and having placed advertisements in the press offered those for sale at half price. This event was followed by the Peak Holding`s trademark infringement action that it brought against Axolin-Elinor. The latter asserted that the claim of Peak Holding must be dismissed insofar as the goods in question are put on the market in the EEA by itself thus exhausting its right in respect to further sales thereof. It went on to put forward four alternative events which, according to Axolin-Elinor, entailed 'putting on the market' of the goods so that exhaustion must have occurred[260]: (i) the importation of the goods into the EEA and the custom clearance having been completed by Peak Holding with the intention of selling them in the Community; (ii) the supply of those to individual reseller which in turn offered them for sale (although Peak Holding asserts that it never supplied the goods to the independent resellers outside of its own group); (iii) them being offered for sale through the sister company of Peak Holding; (iv) them being sold to COPAD, regardless of contractual restriction. According to Peak Holding, on the other hand, even if the putting on the market is found to have occurred by virtue of offering the articles for sale through its sister store, by its own act of re-sending those to the warehouse the exhaustion must have been reversed

[258] Case C-16/03: Peak Holding v. Axolin-Elinor
[259] Id. para. 31, 32
[260] Id. para. 17

(interrupted) and trademark rights have been restored. On account of the sale to COPAD, it claimed that the consent to putting on market is not present having in mind, in particular, the contractual restriction of resale in Europe that it imposed to COPAD.[261] The referring Court, on that note, called on the ECJ to interpret the expression of 'put on the market' provided by Article 7(1) of the Trademark Directive in relation to exhaustion. In that referring Court asked the following questions:[262]

1) Are goods to be regarded as having been put on the market by virtue of the fact that the proprietor of the trade mark: (i) has imported them into the common market and paid import duty on them, with the intention that they be sold there? (ii) has offered them for sale in the trade mark proprietor's own shops or those of a related company within the common market but a sale of the goods has not taken place?

2) If goods are regarded to have been put on the market in one of the above events, thus effectuating exhaustion, can a trade mark proprietor interrupt exhaustion by returning the goods to a warehouse?

3) Are goods to be regarded as having been put on the market by virtue of the fact that they have been sold by the right holder to another company which is contractually bound to not sell the goods in the common market?

4) Is the answer to question 3 affected if the trade mark proprietor, upon selling the consignment to which the goods belonged, gave the buyer permission to resell a small part of the goods (5% in this case) in the common market but did not specify the individual goods to which that permission applied?'

In response to the first question the Court started off with stating that under the present circumstances it is undisputed that, where he sells goods bearing his trade mark to a third party in the EEA, [that is the sale of goods to COPAD] the right holder puts those goods on the market within the meaning of Article 7(1) of the Directive.[263] The reason behind, to which the Court subsequently referred, seemed to bear the traces of essential function doctrine as established in the early case law. In that regard, the Court indicated that a sale which allows the proprietor to realize the economic value of his trade mark exhausts the exclusive rights in

[261] Id. para 48
[262] Id. para 21
[263] Id. para. 19

respect to prohibit the [subsequent] sales by the third parties.[264] It went on to state that mere importation of goods onto the EEC by the right holder to be sold in the Community does not exhaust his rights insofar as such importation itself does not allow the right holder to realize the economic value of trademark. This is so because such acts do not transfer to third parties the right to dispose of the goods bearing the trade mark. In the same vein, the Court ruled, offering these goods for sale in the right holder`s own shops or those of an associated company, without actually selling them does not constitute 'putting on the market'.[265]

Having thus rendered the second question irrelevant, the Court approached the matter exhaustion in case of sales in breach of a contractual restriction. It held that the exhaustion occurs solely by virtue of the putting on the market in the EEA by the right holder, not making the exhaustion itself a subject of an additional consent (or discretion) of him. Any stipulation, in the act of sale effecting the first putting on the market in the EEA, of territorial restrictions on the right to resell the goods concerns only the relations between the parties to that act.[266] Therefore, such a contractual restriction cannot be relied on in order to prevent the exhaustion.

***Peek & Cloppenburg v. Cassina***

In the InfoSoc Directive (Directive 2001/29 on the harmonisation of certain aspects of copyright and related rights in the information society) the exclusive right to initial marketing, which corresponds to the putting on the market for the purposes of exhaustion, of the products protected by copyright has been conceptualized as 'any form of distribution to the public by sale or otherwise'.[267] An interpretation of the latter was sought in *Peek & Cloppenburg v. Cassina*.[268] In the main proceedings, Cassina the furniture maker concluded a licensing agreement under which it manufactures and sells in Germany the furniture made from Le Corbusier designs, in particular armchairs, which are protected by copyright. Peek & Cloppenburg, which operates clothes stores in Germany, acquired the same design of chairs from another Italian undertaking that manufactured those without Cassina's consent. However, such furniture was not protected at the time by copyright in the Member State in which it was manufactured (Italy). Peek & Cloppenburg fitted that furniture in a customer rest area in one of its stores and in the display of one of its outlet stores. Cassina brought an infringement case

[264] Id. para. 40
[265] Id. para, 41 - 44
[266] Id. para, 52 - 54
[267] Article 4(1) of Directive 2001/29 on the harmonisation of certain aspects of copyright and related rights in the information society.
[268] Case C-456/06 Peek & Cloppenburg v. Cassina

against the Peek & Cloppenburg, asserting that the latter infringed its distribution rights. The referring court, on that note raised the question whether the concept of distribution to the public otherwise than through the sale of the original of a work or a copy thereof, must be interpreted as to include (i) granting to the public the right to use reproductions of a work protected by copyright without that grant of use entailing a transfer of ownership; (ii) exhibiting those reproductions to the public without actually granting a right to use them.

The ECJ found, with a reference to the similar concept provided for by the WIPO Copyright Treaty that the concept of distribution to the public, otherwise than through sale, of the original of a work or a copy thereof, for the purpose of Article 4(1) of the InfoSoc Directive, applies only where there is a transfer of the ownership of that object. In the absence of such a transfer in the present case, neither granting to the public the right to use reproductions of a work protected by copyright nor exhibiting to the public those reproductions without actually granting a right to use them can constitute such a form of distribution.

An issue similar to that of Peek & Cloppenburg v. Cassina is subsequently brought before Austrian Supreme Court.[269] On that occasion armchairs that presented similarities to Le Corbusier designs was placed by a designer commissioned by the lessor into the lobby of the hotel that is operated by the plaintiff. Reportedly those articles were in possession of the lessor; the defendant had not purchased them or arranged their placement in the lobby. According to the plaintiff, this practice infringed his rights in respect to Section 16 of the national copyright act, which in essence corresponds to 'distribution to public' set out in the Article 4(1) of the Directive. The Austrian Court emphasized that the features of the case at hand does not differ from that of Peek & Cloppenburg v. Cassina on which the ECJ already delivered a ruling. In both cases the articles were neither sold nor was the ownership transferred by other means. The legal basis of the case was Section 16 of Austrian Copyright Act which, as we pointed out above, corresponded to Article 4(1) of the Directive, particularly to the distribution to public thereof. The Austrian Court thus maintained that the requirement of interpreting the national law in accordance with the Directive was a sufficient ground for itself to not evaluate the matter at hand (which was almost identical to ECJ`s ruling) separately; and the notion of distribution to public was readily clarified in the judgement of the ECJ. Therefore, the Austrian Court found that distribution within the meaning of the Directive did not occur.

[269] *Le Corbusier*, 49(1) IIC 106, 112 (2017) https://link.springer.com/content/pdf/10.1007/s40319-017-0657-z.pdf

As we demonstrated so far, there are two sides to the coin of 'putting on the market' (or as is described in the context of copyright protected physical goods distribution to public), that are (i) the act commenced in by the right holder thus exhausting his rights; (ii) the act commenced by the third parties, which, if the transfer of the ownership is involved, constitutes an infringement of the distribution right.

However, over the last decade, on the point of finding the infringements, the ECJ seemed to have no longer sought the criterion of transfer of ownership. Quite conversely in *Donner*[270] and *Blomqvist*[271] it resorted to observe that the distribution to the public is characterized by a series of acts going, at the very least, from the conclusion of a contract of sale to the performance thereof by delivery to a member of the public.[272] Accordingly, those acts that precede the actual conclusion of a contract, such as advertising to the public of that member state where the work is protected under copyright; making available to the said public by setting up a specific delivery system and payment method, may constitute distribution to public, thus infringing the proprietor`s right in that state.[273]

The Court, in *Dimensione v Knoll*[274], ascribed the rationale of this new position to the objectives of the Directive in providing a high-level copyright protection which, according to the Court, must be rigorous and effective. It went on to articulate this new position more compactly and concluded that it is irrelevant for a finding of an infringement of the distribution right, that such advertising is not followed by the transfer of ownership of the protected work or a copy thereof to the purchaser in so far as it invites consumers of the Member State in which that work is protected to purchase it.[275] The Court importantly noted that, although this outcome might seem to imply a departure from what it established in Peek & Cloppenburg v. Cassina (where it established that the actual transfer of ownership is sought in order there to be an infringement of distribution right), the difference in the factual background (i.e. displaying with no intention to sell in Peek & Cloppenburg v. Cassina versus clear intention to market the reproduction in Knoll) necessitate this conclusion.

[270] Case C-5/11: Titus Alexander Jochen Donner
[271] Case C-98/13: Martin Blomqvist v Rolex
[272] Donner, para. 26; Blomqvist, para. 28
[273] Donner, para. 30
[274] Case C-516/13: Dimensione Direct Sales srl and Michele Labianca v Knoll
[275] Id. para. 35

Subsequently in *Syed*[276] the question referred to the ECJ by the Swedish Supreme Court was whether (infringing) goods bearing a protected motif which are kept, by a person, in storage facilities can be regarded as being offered for sale (thus being distributed for the purposes of Article 4(1) of the Directive) when that person offers identical goods for sale in a retail shop run by him. The ECJ reiterated the criterion: whether such storage of goods as in this case constitutes an infringing act prior to sale depends on the existence of an actual intent to sell those stored articles to the public without the right holder's authorization. Further, identical goods being stored and actually sold by the defendant might be the indicator of such an intent.[277] In that regard, it concluded, the storage by a retailer of goods bearing a motif protected by copyright on the territory of the Member State where the goods are stored may constitute an infringement of the exclusive distribution right when that retailer offers for sale, without the authorization of the copyright holder, goods identical to those which he is storing, provided that the stored goods are actually intended for sale on the territory of the Member State in which that motif is protected. It is finally for the national court to adduce this intent from the available evidence.[278]

More recently *Coty v. Amazon*[279] allowed the ECJ evince its opinion on the storage, on behalf of a third party, of some infringing goods in the context of online market place. The online market place scheme maintained by the respondent (Amazon) enabled the third-party sellers to place offers for sale in respect of their goods. The actual sales contract in the event of a purchase is concluded between the seller and the purchaser; Amazon the service provider is not a party to that contract. What Amazon provided, however, is a fulfillment scheme for the contracting parties that provided for the storage of those goods and handing over to the external dispatchers for delivery. Coty, who retains a license to the European Trademark of 'Davidoff' detected the perfumes that are infringing its trademark being offered and actually sold over Amazon market place and brought an action against Amazon. The case eventually was brought before the German Federal Court, which sought guidance as to whether the case at hand is relevant to 'offering the goods, putting them on the market or stocking them for those purposes' within the meaning of Article 9(3) EUTM Regulation on the end of Amazon. The referring case thus asked if a person who, on behalf of a third party, stores goods which infringe trade mark rights, without having knowledge of that infringement, stock those goods for the purpose

[276] Case C-572/17 - Criminal proceedings against Imran Syed
[277] Id. para 31
[278] Id. para 40
[279] Case C-567/18: Coty Germany v. Amazon Services Europe

of offering them or putting them on the market, if it is not that person himself but rather the third party alone which intends to offer the goods or put them on the market.

The ECJ, once again, emphasized the decisive role of underlaying intention to offer the goods or put them on the market. It further highlighted that Amazon merely stored the goods concerned, without themselves offering them for sale or putting them on the market nor it had the intention to do so.[280] This was evidenced by the fact that, within the systematic of the market place in question, the offers for sale are made by the sellers who are customers of the operator of that marketplace and not by that operator itself.[281] On that note it was concluded that such an act would not constitute stocking of those goods in order to offer them or put them on the market for the purposes of those provisions.

***Conclusion***

It is seen that the act of putting on the market can be done rightfully by the proprietor of the IP right, and this makes up the type of putting on the market for the purposes of exhaustion. On the other hand, the products may be put on the market by the third parties, that are the ones besides the right holder and those acting upon the right holder`s consent. This manner of putting on the market, depending on whether or not the rights of the proprietor have previously exhausted on those articles, may either be addressed as further commercialization or an intellectual property right infringement vis a vis right to first sale or distribution.

Over a series of case law that we indicated above the ECJ seemed to have interpreted the notion of 'putting on the market' such as to retain/preserve the rights of the proprietor until the ownership of the corporeal goods are transferred to a third party. In that neither the mere importation of goods into the EEA with a view to selling them in the Community, nor offering them for sale in the right holder`s own stores (that include those of economically and legally linked entities) would exhaust the rights. Nevertheless, the same logic dictates that once the tittle of the goods transferred to a third party in the EEA, a contractual stipulation on the latter not to sell them in the Community would not preclude the exhaustion.

As far as infringement of exclusive distribution right is at focus, the ECJ recently seems to have broadened its understanding of 'distribution to public' in favor of the copyright holders. The common subtext of the rulings of the Court from Donner up until now is that when there

[280] Id. para 34
[281] Id. para 40

is reasonable and solid evidence to the intent of the third parties to sell the products that are protected by copyright, it amounts to distribution to public, regardless of whether the third party actually marketed those products, thus infringing the exclusive distribution right of the proprietor. The solid evidence in that regard is the series of acts that, according to the Court, characterize and inextricably linked to actual distribution.

Nevertheless, it is doubted whether this new stance the Court seems to have taken should imply that the actual transfer of ownership will cease to be relevant when determining the distribution to public by the right holder (or with his consent), thus exhausting his exclusive rights. The reasoning in Peak Holding, i.e. the right holder has benefit in retaining its rights as long as the ownership of products are transferred to a third party, connotes that when determining the exhaustion disposal of the goods by the right holder in a way to transfer the tittle to a third part is necessarily sought[282]; offer for sale in itself and 'the series of acts' prior to actual transfer of ownership therefore, in our opinion, would not suffice for the purposes of exhaustion.

**4. Marketing by or with the Consent of the Right Holder**

For the purposes of exhaustion, the act of putting on the market necessarily to be carried out by the right holder or with the latter`s consent. Once such an act, as we discussed above, takes places the result of exhaustion depends on the identity of the party who effectuated such an act. The identity in this context is determinant to whether the intellectual property right is used in an authorized manner, thus exhausting the right of initial marketing; or in an unwarranted way such as to constitute an infringement of the rights in question. In line with Community exhaustion, should the putting on the market of the goods be affected by the right holder or with his consent, the right exhausts in respect to all Member States hence the parallel rights therein.

However, ascertaining this identity can scarcely be easy. Given the expansive vertical and horizontal integration of the undertakings engaged in commercialization of goods incorporating intellectual property rights, not only the consensual sales thereof by the others but also the sales by the right holder itself through its integrated members or related undertakings might likely be compelling. Especially when the EU is taken as the domain it

[282] This imperative was also confirmed in Coty v. Simex (Case C-127/09) where the samples of perfume (tester) that were made available by the trademark holder to the resellers without transferring their ownership and that bore phrases ‘Demonstration’ and ‘Not for sale’ regarded as not having been put on the market.

becomes clear that similar intellectual property rights held in different member states (i.e. parallel rights), although belonged to the same commercial origin, are often assigned to related national organizations such as subsidiaries, distributors etc. or licensed thereto. Thus, the scenery is of course further complicated by the fact that the intellectual property right holder is not necessarily the one that carries out the manufacturing of goods; but rather the latter is organized on the basis of intellectual property licensing and assignment.

From a semantic stand-point, it follows that the act of initial marketing that will effectuate the exhaustion of rights, may either be done by the right holder or by the others who act upon the right holder`s consent. Of all scenarios, it is perhaps easiest to pinpoint the exhaustion when the right holder itself puts the incorporeal goods on the market whereas consensual marketing by the others may be embedded in other legal or economical relationships that are present those two parties. As of the early cases various relations have been assessed for the purpose of exhaustion vis-a-vis what proximity entails consent, thus whose act results in the exhaustion of rights.

### 4.1. Putting on the Market by a Distributor

In *Consten Grundig*[283] the underlying relationship between the holder of trademark and the undertaking which put the corporeal goods on the market appeared to be (exclusive) territorial distributorship. Under the framework of the distributorship agreement the German manufacturer (Grundig) permitted the distributor (Consten) to register in France the trademark (GINT) that is used by the manufacturer. Later the distributor, relied on that trademark to prevent parallel imports from Germany into France. Although at the time of the dispute neither free movement provisions nor the Community exhaustion was in place, thus it was dealt with in the light of competition provisions of the Treaty, the outcome was that such a practice amounted to partitioning of national markets and was incompatible with the principles of the Common Market. The Commission emphasized that, although distributorship agreements in principle presupposes the involvement independent parties, once the agreement has been concluded it leads to interdependence or even to mutual dependence of the parties.[284] And it is undoubtedly so, when the agreement in question is made for a long period of time such as in the present case. This links in fact forms around the dispersal of the goods to the end users or

[283] Joined Cases C-56 and 58/64: Établissements Consten S.à.R.L. and Grundig-Verkaufs-GmbH v Commission of the European Economic Community
[284] Id. at 309

to other vendors, hence it typically entails the right holder`s consent to put them on the market. It is also rightly noted that if the said case had arisen after the insertion of Community exhaustion, it would have been resolved with the exact same result under the exhaustion principle, instead of competition rules.[285]

### 4.2. Putting on the Market by a Commercial Agent

Although from a purposive view point the act of an agent and that of distributor appear to be alike, a nuance that is vital for the purposes of exhaustion is nevertheless contained in the characteristics of the underlying contracts. Under a distributorship relation the right holder -that is presumed to be the manufacturer- sells the goods to the distributor which, in turn, resells them on its own account.[286] The activity of an agent on the other hand entails inter alia entering into sales contract on behalf of the right holder. In the light of this link, marketing of the corporeal goods by the commercial agents of the right holder is considered as a form of putting on the market by the right holder itself.[287] It is also apparent from the specific character of this relationship that there exist no sales between the agent and the right holder, thus exhaustion shall not take place on the axis of this relationship. Obviously, however, as soon as the agent concludes the sales agreement on behalf of the right holder, exhaustion occurs.

### 4.3. Putting on the Market by the Undertakings that Belong to the Same Economic Group

The bodies that are not organically belong to the right holder, such as distributors, insofar as they are acting upon the consent of the right holder, effectuate the exhaustion by their sales of respective goods. The reason why the link between these and the right holder is rather synthetic than organic lays at the fact that they gather around a contract for performing the sales. In other words, they do not essentially belong to -or form an organ of- one another. In fact, when distributorship in particular is taken into account, even the sales by the right holder to the distributor per se triggers the exhaustion insofar as the latter, typically, is a third party outside the body of the right holder, purchases the goods and resells them on his own account.[288]. Since the practice of the said independent parties form the sufficient link to the

[285] KEELING, *supra* note 9, at 84
[286] REBECCA ATTREE. A SPECIALLY COMMISSIONED REPORT; INTERNATIONAL COMMERCIAL AGREEMENTS 153 (Thorogood 2002)
[287] LAZAROS G. GRIGORIADIS, TRADE MARKS AND FREE TRADE: A GLOBAL ANALYSIS 282 (Springer 2014)
[288] The sale to the to a third party undertaking (COPAD) with a view that the latter would distribute the goods under the agreed terms has, thus, been considered to have exhausted the rights in *Peak Holding* (C-16/03) above. See para. 12 of the case C-16/03: Peak Holding AB v Axolin-Elinor AB.

right holder and the acts they carry out on behalf of the latter typically contain the right holder`s consent, it comes as no surprise that the sales of corporeal goods by the member of the same economic group, i.e. organically linked undertakings, will, *a fortiori*, result in exhaustion of rights.

Even if it is true that the actual member of the group who holds the intellectual property rights may be distinct from that who commenced in putting on the market, given the strength of commercial ties, i.e. organic, hence they present unity, the result of exhaustion cannot be avoided. Background motive is not to leave the exhaustion -which tends to be *erga omnes* guarantee of free trade- vulnerable to internal measures of the undertakings such as to strategically allocate intellectual property rights among the different members thereof. This result is of particular significance when the holders of parallel rights in different member states are various undertakings of the same economic group. If it was not for such assumption of unity, the right holder would have been able to partition the national markets of the Member States by different configurations of assignment of its intellectual property rights to different undertakings that are subordinate to itself. Hence it would be able to hinder the subsequent commercialization, and of course parallel trade, of corporeal goods between the Member States having relied on the national rights which, virtually and formally, belonged to different undertakings, although latter functioned in a unity.

For the undertakings to present such a unity, the link among them does not necessarily have to be legal. In fact, as far as the possession of parallel rights is concerned, it is typical that the national rights in different Member States held by the subsidiaries of the right holder in the respective Member State, incorporated under the law of the latter. Naturally, if the link sought for tracing such a unity was exclusively a legal one, it would often fail because they have been established under different laws. Economic and operational links are, therefore, a clearer indicator of that unity. In that regard, it is rightly noted that the concept of unity emerges from the general principles of competition law of the Community which regarded subsidiaries that has no freedom to determine their own course of action as constituting a single entity with the parent company.[289] Furthermore, this is not affected by whether the members had separate legal personality.[290] Similarly it is logical to conceive that the undertakings falling into this concept

[289] KEELING, *supra* note 9, at 83

[290] To that effect the ECJ ascertained well in advance that "The fact that a subsidiary has separate legal personality is not sufficient to exclude the possibility of imputing its conduct to the parent company." and "In the circumstances the formal separation between these companies, resulting from their separate legal personality, cannot outweigh the unity of their conduct on the market for the purposes of applying the rules on competition."

do not only involve the parent company and subsidiaries thereof (vertical integration) but also sister companies (horizontal integration) belonging to same economic group[291], insofar as allocation of tasks and intellectual property rights could take any possible shape. In either case, the outcome is straightforward: exhaustion applies to the goods that are put on the market by undertakings belonging to the same economic group as the right holder. This has been confirmed in the context of different types of intellectual property rights.

The referring court in *Deutsche Grammophon* blatantly asked the question whether the sound recordings manufactured by the right holder in Germany and put on the market in France through its French subsidiary can be prevented from being marketed in Germany in reliance upon the distribution right within the meaning of copyright and related rights. It was highlighted by that court that the recordings in question were supplied by the right holder itself to the French subsidiary and that, although the latter is independent in legal terms, it was commercially subordinate to the right holder.[292] The sequel of the case is notorious insofar as the ECJ laid the formula of exhaustion for the first time: such marketing exhausts the rights.

The identical conclusion has subsequently been reached by the ECJ in respect to patents and trademark. In *Centrafarm v Winthrop* and *Centrafarm v Sterling*, the undertaking that held intellectual property rights over medicinal products and processes invoked, respectively, patent and trademark so as to prevent the marketing of incorporating drugs in the Netherlands. The drugs brought into the Netherlands by a parallel trader undertaking were in fact put on the market in England and Germany by the subsidiaries of the parent company. In the light of the foregoing, the Court ruled that the marketing by the subsidiaries in other Member States exhausted the patent and trademark rights. National legislation under which those rights are granted, cannot prohibit the sale in that Member State of the goods that have been put on the market in another Member State by the right holder or with his consent; the contrary would fall foul of the free movement provisions of the Treaty.[293]

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See. the Case 48/69: Imperial Chemical Industries Ltd v Commission of the European Communities, paras. 132 and 140

[291] ALBERTINA ALBORS-LLORENS, EC COMPETITION LAW AND POLICY 12 (Taylor & Francis 2002)

[292] Case C-78/70: Deutsche Grammophon v Metro, para. 2

[293] For the consideration of trademarks, see: Case C-16-74: Centrafarm v Winthrop, para 12; for that of patent, see: Case C-15-74: Centrafarm v Sterling Drug, para 15.

### 4.4. Putting on the Market by the Licensees

Intellectual property rights are most typically commercialized by means of licensing agreements. Although a licensing agreement, in terms of contract law, usually needs to entail certain elements so as to be perceived as an agreement (such as term, consideration, scope of use and territorial limits etc.), from a broader perspective the term 'license' (or licensing) refers to authorizing someone to act in a certain way. Applying the latter onto the theme of intellectual property, it connotes the authorization to make, to sell and to use products, processes and services, embodying the intellectual property right in question.[294]. This also follows that not only the authorization granted to someone on the basis of a setting that includes the typical elements of an intellectual property licensing agreement; but also otherwise permitting *ex parte* the exploitation of an intellectual property right essentially fits in this concept.

A clear insinuation as to the sequel of exhaustion in the context of licensing agreements, therefore, resides at the etymology of 'license'. Authorization exhibited by the right holder (licensor) as regards the rights being exploited by a third party (licensee), thus, typically connote the consent. For this reason, it is noted that licensing is the most manifest expression of the consent.[295] Frankly therefore, the right holder`s rights in respect to the goods put on the market by the licensee will exhaust; the right holder cannot oppose to further commercialization thereof between the Member States. It is necessary, however, note that the result of exhaustion is less straightforward when the sale by the licensee has been done in infringement of certain provision of licensing agreement, such as the material or territorial scope of license and quality standard etc.; or when in case of compulsory licensing. Such cases shall be examined separately below, albeit, the general principle must be noted that the sales by the licensee exhausts the right holder`s right to initial marketing.

***A Summary of Different Scenarios:*** *IHT v Ideal Standard*

The considerations above have been compactly articulated by the ECJ in *IHT v Ideal Standard* judgement.[296] Although the actual significance of the judgement rested at the clarification offered therein in respect to the exhaustion in the case of trademark assignment -

[294] CHARLES D. DESFORGES, THE COMMERCIAL EXPLOITATION OF INTELLECTUAL PROPERTY RIGHTS BY LICENSING 2 (Thorogood 2001)
[295] KEELING, *supra* note 9, at 84
[296] Case C-9/93 - IHT Internationale Heiztechnik v Ideal-Standard

on the point of which we shall examine the judgement in the following sections-, it is vitally important on the general matter of exhaustion, at least, to three ends:

i) It has summarized the rationale of the Community exhaustion that is attributable to different kinds of intellectual property rights, albeit the wording had its reference to trademark rights. In that the Court stated: "application of a national law which would give the trade-mark owner in the importing State the right to oppose the marketing of products which have been put into circulation in the exporting State by him or with his consent is precluded as contrary to Articles 30 and 36 (Articles 34 and 36 TFEU).

ii) The link sought between the right holder and the marketing undertaking: The proximity, to the right holder, of the body which effectuated the putting on the market is the determinant in ascertaining the existence of the consent which in turn is the essential to exhaustion. As we highlighted earlier, the link may be legal and/or economical nature. One needs to observe, in that regard, that the domain represented by economically linked undertakings is necessarily wider than that of legally linked enterprises given that legal links, especially in multinational organizations, may not be as explicit as the economical ones. On that note the Court concluded that: "This principle, known as the exhaustion of rights, applies where the owner of the trade mark in the importing State and the owner of the trade mark in the exporting State are the same or where, even if they are separate persons, they are *economically linked*."[297]

iii) Having established the criterion as the economic link, the Court went on to enumerate certain situations, as we individually discussed above, where this link typically exists. In that the Court maintained: "A number of situations are covered: products put into circulation by the same undertaking, by a licensee, by a parent company, by a subsidiary of the same group, or by an exclusive distributor."[298] It is nevertheless worth pausing to note that, on the face of this wording and having considered the general clause of 'economical link' established in the preceding statement, this catalogue of situations should not be considered as an exhaustive list.

### 4.5. Putting on the Market by the Right Holder

Of all the possibilities, it is perhaps the most effortless for identification of exhaustion when the goods are put on the market by the right holder itself. It is well obvious that the right holder may be an undertaking as well as a real person. Nevertheless, aforesaid teaching of the

[297] Id. para 34 (Emphasis added)
[298] Id.

competition jurisprudence suggests that undertaking for that purposes is construed broadly; it can also be comprised of real persons, or a combination of real person and commercial entities as well as of a cluster of commercial entities. Although it is not of particular importance, as regards the exhaustion of rights, whether goods were put on the market by the right holder *per se* or by those who act on its consent, it might nevertheless be accurate to differentiate what qualifies -or must be regarded as- putting on the market by the right holder. These cases include i) Putting on the right holder who is a real person; ii) Agent which by definition acts as a part of the right holder, as mentioned above; iii) Domestic organizations of the right holder undertaking.

In *Merck v Stephar*[299], where the goods were put on the market by the right holder undertaking, it was established that the exhaustion of patent rights in respect to the Community does not depend on the existence or availability of a similar protection in the Member State of first marketing.

Dispute in the main proceedings revolved around patents for drugs and for manufacturing process thereof belonged to Merck in majority of Member States, albeit with few exceptions.[300] Italy was among those exceptions as its patent law at the time did not permit patenting of pharmaceuticals and their manufacturing processes, naturally therefore Merck was not able to obtain parallel patents there, despite having been marketing the relevant products in Italy. In the present case there was no dispute as to the fact that the products were put on the market in Italy by Merck itself.[301] Nevertheless, in the lack of patent protection in Italy, as it typically is, the price level of the drugs was lower than those in the other Member States where they were patented. Stephar, who was tempted by such price differential, engaged in purchasing the drugs in Italy at lower prices and reselling them in the Netherlands -where Merck held the patent rights- in profit, though still undercutting the Merck`s asking price.

Merck in invoking its patent rights against Stephar argued that the impossibility of obtaining patent under Italian law, if the goods are allowed being imported back in the Netherlands, undermines its Dutch patents by curtailing a return to the inventor to compensate for the costs of research. So much so that such a result encroaches upon the essential function

[299] Case C-187/80: Merck & Co. Inc. v. Stephar BV and Petrus Stephanus Exler
[300] Merck held patents for the drug in question in all the Member States except Luxembourg and Italy and for its manufacturing process in all the Member States except Luxembourg, Italy, Denmark and the Federal Republic of Germany.
[301] Merck v. Stephar, para. 6.

of its Dutch patents in the light of pervious case law of the Court prescribing the essential function of patents.[302] It further adds that the exhaustion of patent rights must be considered to have occurred only in those cases where parallel rights exist both in the importing and the exporting Member State. Since in the present case not only did the parallel rights not exist but they were also legally impossible to obtain in the exporting state, hence, Merck argued, its rights did not exhaust and it should be able to rely on the Treaty provisions on the 'protection of industrial and commercial property'.

The Court of Justice, rather unsurprisingly, reflected its unwavering advocacy of the free movement principle. Quite skillfully, it corresponded to the argument of 'essential function' by distinguishing the objective rationale of the latter and the de facto results thereof. Accordingly, the essential function of patent, and the corresponding right of initial marketing, enables the inventor to obtain the reward for his creative effort, by allowing him a monopoly in exploiting his product. This, however, does not mean guaranteeing that he will obtain such a reward in all circumstances.[303] The same logic dictates that the right holder, retaining the discretion to determine the place of initial marketing, was in command of whether to avoid or to afford the risk that is entailed in asymmetrical [legal and economic] circumstances prevalent in different Member States. To that effect the Court ruled, it is a commercial decision that falls to the right holder whether, in the light of all the circumstances, to market the products in a Member State where the law does not provide patent protection. If he decides to do so he must then accept the consequences of his choice as regards the free movement of the product within the Common Market, which is a fundamental principle forming part of the legal and economic circumstances which must be taken into account by the proprietor of the patent in determining the manner in which his exclusive right will be exercised.

What becomes clear from the events above is that the commercial decision on marketing, in its results, may impede the opportunity of first marketing under an absolute monopoly, hence that of full reward for the creative effort which is the essential function of patents. This impediment was the reliance of the plaintiff in arguing that exhaustion did not

[302] Essential function of patents, as laid out in Case 15/74: Centrafarm v Sterling Drug, is the guarantee that the patentee, to reward the creative effort of the inventor, has the exclusive right to use an invention with a view to manufacturing industrial products and putting them into circulation for the first time. (para. 9); Similarly, the French Government, in support of Merck`s argument, expressed more compactly that "if products put into circulation in Italy in such conditions of competition were to find their way into the territory of States in which the company has obtained patents it would lose the reward for its creative effort in those countries too. Such a result would therefore not be compatible with the 'essential function' of the patent right."
[303] Merck v. Stephar, para. 10.

occur. The Court of Justice, nevertheless, insinuated that the right holder perfectly had the option to not market the goods in that Member State so as to avoid what we described in the second scenario above. And it was this 'right of choice' that is safeguarded by the specific subject matter of the right, not the obtainment of desired reward on each occasion. Having put the goods on the market under these circumstances and on his free will - hence the consent - right holder exhausted its rights; in which context the existence of a parallel right is not relevant.

## 5. Marketing by Third Parties

(i) What is the situation of the goods, that were manufactured in the lack of intellectual property rights, *vis a vis* circulation thereof in the Union, especially their import to those Member States where incorporated intellectual property rights are protected. (ii) What is the situation regarding the circulation of the goods that were manufactured in other Member States by legally and economically independent third parties to which the related intellectual property rights belonged in that Member State. The latter is typically the case when intellectual property rights are assigned.

### 5.1. Marketing by Third Parties without Intellectual Property Rights

***Implication**: Parke Davies v. Probel*

It is undoubted that the sequel of *Merck v. Stephar* would be the exact opposite if the goods were not put on the market by the right holder or with his consent in the Member State of no protection.[304] Such a scenario was in fact touched upon well in advance by the Advocate General and some Member States opining on *Parke Davies v Probel* case.[305] In that case, Parke Davies, the holder of Dutch patent for certain medicaments and manufacturing processes opposed the importation into the Netherlands of pharmaceuticals made in Italy - in line with that patented invention - by Probel and the others. Such manufacturing and marketing were legal in Italy given that the patenting of pharmaceutical was not legally possible.

As regards the exercise of patent rights against other Community Goods that were manufactured (albeit legally due to the lack of patent protection in the exporting state), without the patent holder`s consent, the Advocate General, concluded that [if the patent holder is

[304] Stothers, *supra* note 149 at 313-369
[305] Case C-24/67: Parke, Davis and Co. v. Probel, Reese, Beintema-Interpharm and Centrafarm

deprived of the opportunity of exercising his rights against those goods] persons other than the patent holder could easily supply the whole of the Common Market from a country where patents do not exist. And permitting so would preclude the 'substance and the essence' of national patent law, i.e. the legal monopoly to exploit an invention, which is intended to guarantee the chance of a reasonable return for the inventor.[306] It is for these considerations that it 'cannot be said that patent rights cease to be protected in a country because the products protected by them have been placed on the market without the consent of the holder of the patent in a country where the product is not patentable'.[307] Similar considerations were also expressed by the Member States delivering their opinion in the proceedings before the Court of Justice. However, acknowledging that manufacturing and marketing of those goods in respect to Italy - where protection was not available - was not illegal, they argued that if the character of 'non-illegality' were to be extended to the whole territory of the Community, including those Member States where the inventor is in possession of patents, the fundamental principle of patent law would be affected, and be drained of its substance.[308]

Crucial however, by the time of the judgement, neither Community exhaustion doctrine nor that of specific subject matter was in place, therefore the main evaluand before the Court of Justice was whether such invocation of patent rights conformed with the competition rules, in particular whether it constituted an abuse of dominant position. The ECJ, albeit having answered the latter in negative, did not base its decision on (nor made an express reference to) the fact that the goods were manufactured and marketed by the third parties, albeit legally, in the absence of the right holder`s consent. In other words, the same result was reached without entering in the latter discussion. At any rate however, given the express utterance of that view in the following judgements and the insertion of the doctrine of specific subject matter, it seems to have implicitly endorsed those views expressed by the AG and those Member States. It was, concordantly, noted that the sequel of the judgment, at the time, had been widely interpreted as to mean that the use of a patent to block imports from a country where a patent could not be obtained is entirely legal.[309] This interpretation of absolute freedom nevertheless was rejected in *Merck v. Stephar* referred above. Finally, it is of little doubt, if the similar facts arose after

[306] This definition seems to have indicated to the forthcoming doctrine of specific subject matter which was not in place at the time of the decision.
[307] Opinion of Mr. Advocate-General Roemer Delivered On 7 February 1968, at 77-78
[308] Parke Davies v. Probel. at 67-68
[309] Korah, *supra* note 203 at 15

the adoption of the specific subject matter doctrine and of Community exhaustion, the decision of the Court would have been based on these imperatives.

***Affirmation:*** *Centrafarm v. Sterling Drug*

The postulate that was implicit in *Parke Davies* was tidily articulated in *Centrafarm v Sterling Drug*.[310] This time, putting the matter on the axis of free movement provisions, the Court of Justice established:

*"[A]n obstacle to the free movement of goods of this kind may be justified on the ground of protection of industrial property where such protection is invoked against a product coming from a Member State where it is not patentable and has been manufactured by third parties without the consent of the patentee and in cases where there exist patents, the original proprietors of which are legally and economically independent"*[311]

It was thus affirmed that the manufacturing and marketing of corporeal goods by unlinked third parties, in the lack of intellectual property protection in one Member State, although it is legal there, does not entail the consent of the right holder in the importing Member State. Hence the latter should be able to invoke his intellectual property rights against importation of these goods.

***Re-affirmation:*** *EMI Electrola v. Patricia*

In *EMI Electrola v. Patricia*[312], it was confirmed that the same applied to the goods protected under copyright and related rights. Distinctly however, in that case the legitimacy of the production by the third parties was not based on the objective unavailability of intellectual property protection in the exporting Member State but rather on the lack of harmonization, between the Member States, of the laws governing the duration of copyright protection.[313]

EMI Electrola. the German subsidiary of the British company EMI Records, owned the reproduction and distribution rights of musical works of Cliff Richard in respect to the territory of Germany. Meanwhile, another company Patricia, marketed in Denmark the recordings entailing the same musical works. This marketing was legal to the effect that the copyright for the said musical works had already expired in Denmark. It was when Patricia exported and sold

[310] Case C-15/74: Centrafarm v. Sterling Drug
[311] Id. para. 11
[312] Case C-341/87: EMI Electrola GmbH v Patricia Im- und Export and others
[313] Id. para 10; it was noted that, although the term of protection was alike, the date that the period started running was regulated differently by the national laws of Germany and Denmark.

these recordings to Germany that EMI Electrola invoked its German rights against such importation and distribution. The referring Court asked whether it is compatible with the free movement provisions for a manufacturer of sound recordings in Germany to exercise his exclusive rights for reproduction and sale of these musical works in a manner as to prohibit the sale in the German territory of sound recordings of the same musical work manufactured and sold in Denmark, in which territory it had previously enjoyed copyright protection for the musical work, albeit, the copyright period has already expired.[314]

The Court of Justice emphasized that the lawfulness of the marketing in Denmark was due not to a consensual sale by the German right holder, but to the expiry of protection in Denmark under its national law.[315] Accordingly, the goods produced and marketed by an unrelated third party in the lack of protection following the expiry of copyrights, although such acts are legal in the exporting Member State, do not entail the consent of the right holder in the importing Member State; to that end the situation in this case is akin to that in *Parke Davies*. Not surprisingly, the ECJ concluded that in the absence of the right holder`s consent, the exercise of the rights against such goods do not present arbitrary discrimination or a disguised measure to restrict the Intra-Union trade; quite the contrary it was inseparably linked to the existence of rights.[316] Consequently, exercise by EMI Electrola of its rights to exclude the recordings was justifiable under free movement provisions.

It is finally crucial to note, by analogy to *Merck v Stephar,* that, if, the recordings were marketed by EMI or with consent in Denmark, even after the expiry of its rights therein, the right of initial marketing on the face of the German copyright would have exhausted. Hence importation thereof into Germany would not have been blocked.

### 5.2. Marketing by Third Parties with Related Intellectual Property Rights and IP Assignment

The discussion above concerned the free circulation and importation of the goods into the Member State of protection of the goods that were manufactured and put on the market by unrelated third parties in another Member State by taking advantage of either the lacking or expired intellectual property protection in that state. At any rate manufacturing and marketing in that Member State was of lawful character since no IP rights therein were infringed.

[314] Id. para. 5
[315] Id. para. 10
[316] Id. para. 12, 13

However, as the above-mentioned case law confirmed, the importation thereof into the Member States, where intellectual property protection existed, could be legitimately prevented by the right holder. This imperative comes naturally on two ends. Firstly, because allowing the free circulation of such goods throughout the entire Union would render the right holder`s exclusivity to initial marketing completely nugatory, thus, depriving him of essential function of intellectual property right. Right to initial marketing uniformly constitutes the specific subject matter of intellectual property rights of all type.[317] Secondly because the right holder`s consent is objectively impossible in respect to the goods that were produced and marketed by the irrelevant third parties, meaning that the exhaustion of his rights does not occur.

The situation might be - and historically was - less straightforward when the goods were manufactured and put on the market under parallel rights held by legally and economically unrelated undertakings. The latter landscape is of central importance in the context of intellectual property right assignments, particularly that of trademarks. To that end, we shall first discuss the early doctrine of the ECJ in treating such cases, which, eagerly prioritized the free movement principle and subsequent abandonment of this extremist position. We shall then revisit, in brief, the nature of intellectual property assignment to the effect that it may subdivide and rupture the intellectual property rights that were once under a unitary control and reverberations of the latter on exhaustion of rights. Finally, we shall discuss the further development in the ECJ jurisprudence in that context.

***The Doctrine of Common Origin:*** *HAG I*

As regards the apparent tension between the free movement and intellectual property protection, it is needless to reiterate that, the view taken by the European Commission and the judiciary has been in constant favor of the former. It would perhaps be true to suggest that the doctrine of common origin - on which basis the interest of free movement principle further and aggressively dominated the intellectual property protection - best reflects this view. The impetus in that could be seen as to rid the Internal Market of intellectual property subdivision[318], which, by default, is seen as a threat to the market integrity. The said doctrine has its roots in notorious judgement of *Van Zuylen Frères v. HAG AG*[319] (hereinafter *HAG I*).

[317] See the Chapter 3 above for the definitions of specific subject matter in relation to different intellectual property rights.
[318] Irene Calboli, *Trademark Exhaustion in the European Union: Community-Wide or International -The Saga Continues,* 6 Marq. Intell. Prop. L. Rev. 47, 55 (2002)
[319] Case C-192/73: Van Zuylen v. Hag AG

However admittedly the factual subdivision of trademarks underlaid in the dispute was rather unusual, the imperative laid down by the judgement was, at the time, susceptible to expand beyond that eccentric factual background at issue.

HAG AG a German undertaking, which is the manufactured and marketed decaffeinated coffee under the trademark 'Hag' in Germany, Belgium and Luxembourg. In 1927 HAG AG set up a subsidiary in Belgium and assigned its Belgian and Luxembourgian trademarks to this subsidiary (HAG Belgium). Towards the end of the WW2, HAG Belgium was subjected by the Belgian government to a sequestration as enemy property, including trademarks held by it in Belgium and Luxembourg. This sequestration was followed by the sales of HAG Belgium to another independent company (Van Zuylen Freres, hereinafter VZF), the result being an involuntary split of the trademark, whereby 'Hag' trademark is held in Germany by HAG AG while the identical marks in Belgium and Luxembourg are held by an unrelated third party: VZF.

*The Facts*

The dispute in main proceedings arose when the German undertaking commenced in marketing its products under 'Hag' trademark in Luxembourg and the right holder in the latter opposed to such marketing. The referring court sought a preliminary ruling on whether such exercise was justifiable in the light of free movement provisions. The Court of Justice, quite sensationally established that prohibiting the marketing in a Member State of a product legally bearing a trademark in another Member State, merely because an identical trade mark having the same origin exists in the first state, would fall foul of free movement provisions.[320] Having disregarded the lack of legal or economic links between the two undertaking at the material time, the Court of Justice ascribed this result to the historical -albeit no longer present- common origin that the two marks emerged from. Concluding otherwise, according to the Court, would contribute to the partitioning of the national markets.[321]

*The Analysis of HAG I*

The synopsis of the doctrine developed over HAG I judgement is as follows "when marks at issue were sharing the same origin, it was incompatible with Art. 34 and 36 of TFEU to prohibit the trading of the trademarked product in a Member State that was lawfully

[320] Id. para. 15
[321] Id. para. 11

registered in another Member State because an identical trademark registration already existed in the first state.[322]

The problem in this position is inherent: how is this consistent with the specific subject matter? The conclusion the Court arrived at in the said judgement tends to defeat the purpose, that is the essential function, of trademark. It is particularly so once the very nature of trademark assignments in respect to parallel marks is taken into consideration. The said nature principally entails the enjoinment of the assignor`s legal and commercial attribution from the mark in question in countenance of the assignee. The only legal and economical link between the assignor and the assignee, as Keeling articulates, is the assignment contract between the parties.[323] This normally follows that the mark parted from the assignor`s realm of control; thus, in the case of parallel marks, the same marks in different countries – both of which belonged to the assignor prior to the assignment- will go on to belong to legally and economically independent entities.

However in HAG I the grounds of separation was not an assignment -at least not a voluntary one-, the end result was similar to that of an assignment: the same mark in different Member States belonging to different, i.e. legally and economically independent, entities. Having been branched out of the same origin, the Court believed in a far-fetched manner, was sufficient to consummate the legal and economic link for the purposes of exhaustion; thus, importation of the similar goods bearing similar marks cannot be prevented relying on protection of industrial and commercial property.

Interestingly however, assignment of parallel trademarks of every sort would essentially infer a common origin; and if, just as Court established in HAG I, this common origin was to be considered as a legal and economic link, it would render the result of coexistence of the same mark in one Member State, which were in fact held by unrelated entities. Specific subject matter of trademark, more particularly the essential function thereof, as established in *Centrafarm v. Winthrop* is to protect him against competitors wishing to take advantage of the status and reputation of the trade mark by selling products illegally bearing that trade mark. Such a view could potentially render meaningless parallel trademark assignment between the Member States; furthermore, it would, in a bigger perspective, deprive trademarks of transactional value of intellectual property rights. To that end, the Court of

[322] Calboli, *supra* note 318
[323] KEELING, *supra* note 9, at 88

Justice on that occasion seems to have fanatically defended free movement of goods, beyond reason, having misappropriated the consent which conventionally has been at the center of exhaustion.

***Terrapin v. Terranova***

In the subsequent case *Terrapin v. Terranova*[324], the issue had not originated from a subdivision of marks, hence there was no common origin at stake; it rather concerned confusingly similar marks that existed in separate Member States. The issue centered around the query whether it is compatible with the free movement provisions of the Treaty when the right holder in Member State A, in reliance on the trademark rights existing there, prevent the importation of similar goods which were marketed by another (unrelated) undertaking, under a confusingly similar trademark in Member State B, where that mark is lawfully registered by the latter.[325] In that case the undertakings were not legally or economically linked nor did they have a common origin.

The Court of Justice, having approached the matter from the viewpoint of specific subject matter of the rights, took the view that such exercise of the rights as in the present case is justified under the 'protection of industrial and commercial property'. Therefore, the right holder in Member State A could legitimately oppose to the importation of the goods that were put on the market in Member State B, under a confusingly similar trademark which, in the latter state, belonged to a legally and economically unlinked undertaking. The contrary view as to prioritize the free movement would, under these circumstances, undermine the specific objective of industrial and commercial property rights.[326].

Nevertheless, this conclusion applied insofar as there is no common origin. In the same vein, the implication being that the doctrine of common origin as devised in *HAG I* applied only to those cases where a subdivision occurred. Crucially however, the ECJ refrained from mitigating the fallacy of common origin doctrine. Quite the contrary, it seemed to have further affirmed its position as regards the latter. In that, it established that, it was irrelevant whether subdivision was due to a voluntary act or compelled by public constrains.[327] This was of no relief in respect to the assignment of national trademarks, which may take the form of voluntary subdivision. This view, according to the Court, was justified by the presumption that the

[324] Case 119/75: Terrapin (Overseas) Ltd. v. Terranova
[325] Id. para. 1
[326] Id. para. 7
[327] Id. para. 6

subdivision of a trademark, either voluntarily or involuntarily, would have already undermined the function of the guarantee of origin, thus there would factually no longer be an objective to protect against the free movement provisions.

***The Common Origin Doctrine Reversed:*** *HAG II*

The facts to *HAG II* case were identical to those of previous *HAG I* case, except, this time it was the German HAG that invoked its trademark rights to oppose the importation into Germany of the goods that were manufactured under the identical Belgian trademark which was possessed by HAG Belgium which is legally and economically unconnected to the former. In many senses the action underlying the dispute was to counter attack or take a revenge of the sequel of *HAG I* judgement[328], however the greater motive, in the legal interest and in the presence of a perfect opportunity, was to invite the ECJ to reconsider the absurdity created by the common origin doctrine. The latter motive was comprehensively expressed by AG Jacobs who addressed the said doctrine simply as a mistake.[329] In pointing out that mistake, he rightfully drew on the very function of trademarks and suggested that a trade mark can only fulfil that role if it is exclusive.[330] Such exclusivity is clearly undermined when, even for the sake of free movement, the rights are exploited by two distinct undertakings. He further concluded that, unlike the other notions that the Court developed in the same direction[331], the said doctrine was devoid of any legal basis in respect especially to the primary law of the Community.

In the light of the foregoing, the Court admitted the necessity of reconsidering the validity of the common origin doctrine. The cornerstone of that reconsideration, as expressed by the Court, was the essential functions of the trademarks 'which is to guarantee the identity of the origin of the marked product to the consumer or ultimate user by enabling him without any possibility of confusion to distinguish that product from products which have another origin.'[332] The latter is precisely what has been modified since *HAG I* judgement where the Court initially believed the subdivision *per se* undermined this function hence it is not worth defending at the cost of free movement principle. However, in *HAG II,* it concluded in parallel of the AG Jacobs` view that trademarks could fulfil their function only when the goods bearing

[328] SEVILLE, *supra* note 122 at 414
[329] Opinion of AG Jacobs on Case C-10/89: SA CNL-SUCAL NV v. HAG GF AG. (HAG II), pp 3730
[330] Id. pp. 3733
[331] These being the doctrine of existence / exercise of rights, that of specific subject matter and Community exhaustion. See OP pp. 3729
[332] HAG II para 14

them have been produced under the control of a single undertaking which is accountable for their quality.[333] This function could be fulfilled insofar only as the right holder can oppose to the importation of the goods that were marketed, under a similar mark, by an unrelated undertaking. In the evaluation of the latter, it is irrelevant whether those two similar national trademarks once belonged to a single undertaking, given that as of expropriation each of the marks independently fulfilled its function, within its own territorial field of application.[334] Consequently, such an exercise of the rights was compatible with the free movement provisions, thus having effectively reversed the common origin doctrine.

***Voluntary assignment of trademarks***

*The essence of the problem*

The subtext as regards the exhaustion of rights in *HAG I* on one hand and in *HAG II* on the other appeared differently, hence rendering distinct outcomes.[335] In the former, the consent was perceived to have been substituted by the existence of a historical common origin of the mark, as a result, it was irrelevant whether the change of ownership was consensual or legally compelled. In the latter, however, the central role of consent has been reinstated, therefore, in cases where the change in ownership of the marks is involuntary, it was admitted that the consent or a legal or economical link that entails the consent lacked. The result being that the exhaustion did not occur. However, the latter judgement clearly appears correct in the light of the concept of consent and of specific subject matter of the rights, the lack of consent was nevertheless ascertained on the basis that the subdivision of marks was legally compelled.

The sequel *of HAG II,* although thus removed the unjust consequences of the common origin doctrine on the trademark holder, the question persisted as regards the voluntary assignments. Furthermore, the enthusiastic stance the Commission and the ECJ have historically taken such as to favor the free movement principle against territorial intellectual property protection puts in doubt the destiny of assignments which transpired on voluntary basis. Neither of *HAG* judgements responded to this question. The most prominent risk in that

[333] Id. para. 13
[334] Id. paras. 17, 18
[335] P. Oliver asserts a strict distinguish between the common origin doctrine and exhaustion to the effect that the latter is based on consent while the former is not. Peter Oliver, *Of Split Trade Marks and Common Markets*, 54(4) Mod. L. Rev 587, 588 (1991). Though this is true from a formal view point, the point should, nevertheless, not missed that the common origin doctrine implicitly presumes the consent be present (or inherent) in the historical economic links between the parallel marks. Therefore, while the two doctrines are not alternative to each other or otherwise comparable, the fact remains that the common origin doctrine substitutes the 'consent' element which, in turn, is determining factor of exhaustion.

regard is whether the voluntary assignments -which are of contractual nature thus a consensual transaction between the assignor and assignee- should be perceived as to intrinsically involve the 'consent' for the purposes of exhaustion. If such a view is adopted the result appears that the assignor will amount to have consented to marketing by the assignee of the goods that bear the trademark in question, regardless whether the assignee is legally/economically linked to the former or an unrelated undertaking. Obviously when the assignee is legally or economically linked, marketing by the latter will inevitably exhaust the parallel rights of the assignor in the Community and this is completely clear from the flow of the case law we discussed above. When, however, the assignee is an unrelated undertaking the presumption of a built-in consent in the assignment agreement tends to be immensely problematic.

Before delving into exposing this problem, the background should be briefly revisited that intellectual property rights are principally granted, protected and enforced by the jurisdiction of a particular territory, that is referred as *de jure* territoriality.[336] Flowing from the territoriality principle, each national trademark forms a separate intellectual property; this aspect has also been referred to by the ECJ as 'independence of national trademark rights'[337]. Therefore, national trademarks in different Member States, even if they connote the same commercial origin; belong to the same undertaking and be comprised of the identical signs, could independently be subject to legal transactions. The latter include *inter alia* intellectual property licensing and assignment as the prominent forms of commercialization.[338] With that background in mind the following demonstration may explain this problem.

The company Z is the holder of a trademark in Member States A, B, C where it markets the products under the said trademark. For, say, financial reasons, it assigns its trademark in Member State C to another undertaking (Y) to which it is legally and economically unrelated. The end result being that the same trademark belongs to (Z) in the territories A and B; and to (Y) in the territory of C. Normally an assignment of this sort conclusively cuts the assignor`s links to the national trademark which was the subject of the assignment agreement, depriving him of any command or control over that mark. If the consent - of any parties to the marketing of corporeal goods by the other party - is perceived to be embedded in an assignment agreement, neither the assignor nor the assignee could be permitted to invoke its rights against

[336] Robert S. Smith, *The Unresolved Tension Between Trademark Protection and Free Movement of Goods in the European Community*, 3 Duke J. Comp. & Int'l L. 89, 95 (1992); Also see the previous chapter on intellectual property territoriality.
[337] Case C-9/93: Ideal Standard, para. 24,25
[338] See the chapter above on the concept of intellectual property commercialization.

the goods of one another, simply because they are deemed to have preemptively consented, by means of the assignment agreement, to the sales by each other. In the foregoing demonstration, this would mean that (Z) shall be able to market its products in Member State C and (Y) will be able to do the same in respect to the Member States A and B. All three markets, therefore, will -on the coat tails of the free movement principle- have been supplied by the goods that bear the trademark in question, although those goods originate from completely different undertakings which has no common other than the trademark and the type of goods in question.

It is clear in the light of foregoing that if the consent for the purposes of exhaustion is to be confined to the 'mutual will' underlying the assignment agreement, neither parties` trademark could possibly fulfill its function (i) creating a goodwill and reputation around the trademark over which you do not retain exclusive control is impossible; (ii) hence would not be able to protect the right holder against competitors wishing to take advantage of the status and reputation (iii) it is no longer a reliable indicator of a commercial origin, thus cannot convey to the customer a reliable information in that regard.

*Ideal Standard*

Above-described scenario came under scrutiny in *IHT v Ideal-Standard*.[339] In that case the trademark 'Ideal Standard' was originally held by American Standard group in Germany and France, through its subsidies in those Member States. Over time, unprofitable turn of business events and the following financial difficulty drove the French subdivision to insolvency. Subsequently the French trademark, alongside the corresponding business, was assigned to an undertaking of IHT group, to which American Standard group has no link. At the meantime American Standard, through its subsidiary, retained the German operation of the business and German trademark. The dispute arose when IHT group commenced in marketing in Germany the goods it manufactured in France, bearing 'Ideal Standard' mark. The German subsidiary of American Standard (Ideal Standard GmbH) having brought infringement proceedings against IHT, sought an injunction for the latter to desist marketing those goods. In a query as to the compatibility of such exercise of trademark rights by the German right holder, the Court of Justice, in substance, was called on to clarify whether the sequel of *HAG II* was also applicable in respect to voluntary assignments.

[339] Case C-9/93: IHT Internationale Heiztechnik v. Ideal-Standard

According to AG Gulmann, the outcome of *HAG II* was not applicable under the circumstances of the present case insofar as the latter involved a voluntary subdivision of trademark. The subtext being that, where there is no legal dictate -within the meaning of the facts prevailed in *HAG II*- to assign the trademark, the proprietor might just as well omit assigning the marks; hence the assignment appears to be a solely commercial decision. Rather fortunately on the end of trademark holders the Court of Justice took a different view. According to the Court, the transactional function of trademarks and the independency of national trademarks which pioneered this function was not trivial. This was based on the Paris Union Convention for the Protection of Industrial Property which ensured that 'A mark duly registered in a country of the Union shall be regarded as independent of marks registered in other countries of the Union ...'[340] Accordingly, a trademark might be assigned for one country without at the same time being assigned by its owner in other countries.[341]

As regards the substance of the dispute, it went on to reiterate the line of argument it adopted in *HAG II* and highlighted that for a trademark to be able to fulfil its role, it must offer a guarantee that all goods bearing it have been produced under the control of a single undertaking which is accountable for their quality.[342] This was clearly not the case after the conclusion of the assignment in the present dispute. The result was rather that the identical marks in two Member States belonged to completely unrelated entities, that is to mean a unitary structure nether legally nor economically existed. Clearly, the fact that the subdivision of the mark such as to remove the unitary control was due to a voluntary agreement does not change the end result that such a unitary power has diminished. Indeed, after such a conclusive assignment, the assignor is not objectively capable of retaining any control over the assigned mark, which has now become exclusive property of the assignee in the respective national territory. This also follows that whether the assignment was legally compelled or voluntary is not a criterion to ascertain the exhaustion. What was relevant in that regard is the existence, after the assignment, of legal or economic links that would enable the any one of the parties to exercise control over the quality of the goods produced by the other party. In the absence of such a link, the consent -or more particularly the mutual will- implicit in the assignment agreement, the Court established, was not the consent that is required for the application of the

[340] Article 6(3) of the Paris Union Convention for the Protection of Industrial Property of 20 March 1883, as last revised at Stockholm on 14 July 1967; reference made to the latter in para. 25 IHT v Ideal Standard
[341] Id. para 26
[342] Para. 13 HAG II; para. 37 IHT v. Ideal Standard

doctrine of exhaustion of rights.[343] For that type of consent to be present the owner of the right in the importing State must, directly or indirectly, be able to determine the products to which the trademark may be affixed in the exporting State and to control their quality.[344] This ability to control would obviously form an economic link for the purposes of exhaustion.

Consequently, in the light of the foregoing, it held that "*There is no unlawful restriction on trade between Member States within the meaning of Articles 30 and 36* [now Art. 34 and 36 TFEU]. With that, the Court, rightly, rid the trademark assignments of the unconditional prevalence of free movement provisions. Although it is not absolutely certain why the Court put the emphasis, almost solely, on the possibility[345] of quality assurance from the view point of legal and economic links while such links could appear in various other manners, the conclusion it arrived at nevertheless seems to be persuasive on the end of both specific function and of transactional function of trademarks.

*Schweppes v Red Paralela*[346]

In the same direction, the ECJ more recently concluded that the holder of a national trademark is precluded from objecting to the imports of identical goods bearing the same mark originating in another Member State where the mark initially belonged to that the right holder, but then acquired through an assignment by a third party in following scenarios: (i) where the right holder, either unilaterally or in coordination with that new acquirer, has actively and deliberately continued to promote the appearance or image of a single global trade mark, thus causing unclarity as to the commercial origin of corporeal goods, or (ii) where found economic links between the right holder and the new acquirer, such as to align their commercial policies or to reach an agreement in order to exercise joint control over the use of the trade mark, thus it is possible for them to determine, directly or indirectly, the goods to which the trade mark is affixed and to control the quality of those goods.[347] It follows from the holding of the Court, economic link for the purposes of exhaustion is not necessarily a superior-subordinate relationship; moreover, such link may be exhibited either consensually or behaviorally.

***Analysis (a general framework for the assignment)***

[343] Ideal Standard para. 43
[344] Id.
[345] "Possibility" in that regard needs to be highlighted insofar as the ECJ emphasized that the actual exercise of such a quality control is not sought; instead, possibility of such control suffices. See: para. 38 of the judgement.
[346] Case C-291/16: Schweppes v. Red Paralela C-291/16
[347] Id. para. 55

In the said judgement the ECJ considered the reverberations of voluntary assignment under the header of '*The situation where unitary control of the trade mark has been severed following assignment for one or several Member States only*'[348]. In that regard, assignment agreements in classical sense were distinguished from those cases where the products come from a licensee or a subsidiary to which ownership of the trademark right has been assigned in the exporting State.[349] In the latter cases the existence of a unitary structure is of no question and the assignor retains the control over the manufacturing; to that end, assignments of this nature resemble licensing. This follows that the arrangements which are formally assignment but actually confers on the assignor certain controlling mechanisms over the assigned rights should not be regarded as to have altered the commercial origin of the goods to be manufactured by the assignee. Retainment of such an economic link would entail the consent.[350] Naturally therefore parallel rights of the assignor in other Member States would exhaust in respect to the goods sold by the assignee.[351] The latter is justified by the specific function of trademarks, that is to say, when there remains a trace of a unitary control after the assignment, especially as regards the specification of goods to be produced thereunder, the reputation and goodwill centered around the mark as well as the commercial origin information to be conveyed to consumers are not likely be eroded; hence there exists no legitimate interest, within the specific subject matter are of the trademark, to be protect against free movement principle.

Assignment in classical sense however conclusively disconnects the assignor`s affiliation from the intellectual property right in question, which in this case is trademark, thus normally leaving no continuing control or influence over the activities to be carried out by the assignee in the use of the mark.[352] This was the case for the assignment between American Standard and IHT. The Court of Justice coherently delivered the imperative that neither the core objective nor the transactional function of trademark rights can be sacrificed for the sake of free movement principle. The contrary scenario, (i.e. where the consent – or the contractual will- implicit in the assignment agreement is deemed to be a *preemptive* consent for the purposes of exhaustion) would simply render ineffective the remainder of national rights in other Member States which are in possession of the assignor. The Court seems to have formed its line of decision in a proper consideration of transactional function of intellectual property

[348] IHT v. Ideal Standard, para. 40
[349] Id. para. 41
[350] Stothers, *supra* note 149 at 344
[351] KEELING, *supra* note 9 at 88; Rene Joliet & David T. Keeling, *Trade Mark Law and the Free Movement of Goods: The Overruling of the Judgement in Hag I*, 22 I.I.C. 303, 304 (1991)
[352] Smith, *supra* note 336 at 115 with a reference to Joliet & Keeling, *supra* note 351 at 317

rights as enshrined by the Paris Convention and Madrid Agreement. On the other hand, the said transactional function follows from the proprietary aspect of intellectual property rights. Should the Court have decided otherwise in *Ideal Standard*, it could have brought along a grave impediment to the transactional function and the value of trademark rights, which in turn puts in danger the proprietary aspect of the rights. In that landscape, one could be led to question the compatibility of the latter with the Article 245 TFEU which enshrined the principle that the Union law is not to encroach on the proprietary rights in Member States.

In the aftermath of *HAG II* and *Ideal Standard* it becomes clear that exhaustion results from the right holder`s consent to the first marketing in the Union or from the existence of legal and economic links, in that unitary commercial control, between the right holder and the undertaking that commenced in marketing.[353] More importantly the links required in that regard are not historical ones (as proposed through the common origin doctrine), but rather present ones.[354] Trademark assignments, in the absence of such links, do not intrinsically involve this consent, regardless of whether it was consensual or legally compelled. Finally, it is necessary to highlight that even if the assignment between legally and economically unconnected undertakings steer clear the exhaustion of rights, it may nevertheless bring into play the prohibition of market sharing agreements within the meaning of Article 101 TFEU regarding competition rules.[355]

### 5.3. Marketing Under Compulsory Licenses

The type of sales that effectuate the exhaustion is the consensual ones, this depicts the central role of the right holder`s consent to the initial marketing in determining the freedom in further commercialization of the goods. Compulsory licensing arrangements, as the name signifies, are characteristically devoid of such consent and they typically relate to patents.[356] These allow the governments to grant patent licenses, without seeking the patent holder`s permission, in those cases where a dependent patent is being blocked, where a patent is not

[353] Calboli, *supra* note 318 at 57
[354] This point was well articulated by the AG Jacobs in his opinion on HAG II case: "…the word 'origin' in this context does not refer to the historical origin of the trade mark; it refers to the commercial origin of the goods. The consumer is not, I think, interested in the genealogy of trademarks; he is interested in knowing who made the goods that he purchases.". See OPINION OF MR JACOBS —CASE C-10/89, I - 3735
[355] Stothers, *supra* note 149, at 344
[356] TRIPs Agreement expressly excludes the compulsory licensing arrangements in relation to trademarks. In that, Article 21 of the Agreement reads: "Members may determine conditions on the licensing and assignment of trademarks, it being understood that the compulsory licensing of trademarks shall not be permitted…"

being worked or where an invention relates to food or medicine.[357] The actual function is to avail the public of the invention at the cost of proprietary right of the patent holder when the greater public interest requires so[358], for example when the right to access to medicinal products for life-threatening diseases is at stake.[359] Although compulsory licensing arrangements may entitle the patent holder a governmentally determined remuneration, the result is often a sharp decrease in prices[360]; the fact, therefore, remains that the patent holder is essentially deprived of (i) the freedom of whether or not to grant the license (ii) the possibility of marketing in monopolistic conditions.

Having the consent excluded from the equilibrium, the question pertains to whether the sales under compulsory licenses exhaust the patent holder`s rights, and correspondingly to whether or not the patent holder can oppose further commercialization within the Union of the goods manufactured and marketed under compulsory licensing arrangements. This very question was at the center of the preliminary ruling procedure in *Pharmon v. Hoechst.*[361]

Hoechst held the patents, in Germany as well as in the Netherlands and the United Kingdom, for a certain manufacturing process of medicinal products. In the United Kingdom, a local company (DDSA), in reliance on the Patent Act of the UK, obtained a compulsory license to exploit the patented invention of Hoechst in relation to manufacturing and supplying the relevant medicines within the territories of the United Kingdom of Great Britain and Northern Ireland and the Isle of Man. Despite the export prohibition contained in the licensing arrangement, DDSA sold to a Dutch company, Pharmon, a large consignment of medicines which it had produced based on Hoechst`s invention; and Pharmon intended to market these in the Netherlands.[362] To prevent such marketing, Hoechst invoked its Dutch patent; in response to which, Pharmon claimed that marketing in the Netherlands cannot be excluded since the articles were lawfully put on the market in the UK. It argued that the patent holder`s rights were exhausted not because the latter consented to the first marketing but rather because the

[357] Gianna Julian-Arnold, *International compulsory licensing: the rationales and the reality*, 33 Idea 349, 350 (1992)
[358] Joseph A. Yosick, *Compulsory Patent Licensing for Efficient Use of Inventions*, 2001 U. ILL. L. REV. 1275, 1275 (2001)
[359] Sara M. Ford, *Compulsory Licensing Provisions under the TRIPs Agreement: Balancing Pills and Patents*, 15 AM. U. INT'l L. REV. 941, 946 (2000)
[360] Id.
[361] Case C-19/84: Pharmon BV v. Hoechst AG
[362] Id. para. 7, 8.

requirement of consent was substituted by the decision of the national authorities on the grant of a compulsory license.[363]

The Court of Justice, agreed with the Dutch courts which had, in several instances, took the view that Hoechst should be able to invoke its rights to prevent the marketing in Netherlands of the goods that were manufactured under a compulsory license in the United Kingdom; such exercise of parallel patent rights was compatible with the Article 30 and 36 of the EEC Treaty (Art. 34 and 36 TFEU). The Court of Justice simply based this view on the apparent actuality that the patent holder cannot have consented to the grant of license to a third party when such grant is made by the national authority on its own motion, hence the patent holder as such had no involvement whatsoever. This clearly deprives the patent holder of his right to determine freely the conditions under which he markets his products; in short, this deprives him of specific subject-matter of his patent.

However compact the Court`s holding was, the observations submitted by the Commission and the Member States, whereby the distinction between consensual and compulsory licenses was illustrated, seems to offer a better reified background to this view. Accordingly, compulsory licensing arrangements, unlike consensual (or contractual) licensing, are in the nature of administrative measures firstly because there is no actual negotiation between the patent holder and the licensee; secondly because neither of those sign the document.[364] Another distinction appears as regards the objectives of licensing: while consensual licensing is a way through which the patent holder generates the reward as conceptualized by the specific function of the patent protection, compulsory licensing is aimed at fulfilling the specific need of that Member State for the underlying invention.[365] Furthermore, it was emphasized that the aforesaid premises are a clear indicator of lack of consent, which, having connoted the free and voluntary marketing, represents the precursor of the whole theory of exhaustion. Should that fundamental premise have lacked, exhaustion falls out of question.[366]

Another important point that the Court went on to clarify, as requested by the referring court, was whether this finding is affected when the patent holder is entitled to royalties under the licensing arrangement. The ECJ answered the latter in negative. In that, it held "it makes

[363] Id. para. 16.
[364] Id. para. 18
[365] Id. para. 19
[366] Id. para. 20

no difference to the reply [to the question of exhaustion] ... whether that license fixes royalties payable to the patentee or whether the patentee has accepted or refused such royalties."[367] This conclusion, once more, plainly reveals the key role in ascertaining the exhaustion is played by the right holder`s consent. Once the right to consent is debarred -which is quintessentially the case in compulsory licensing agreement- exhaustion does not occur even if there is a certain royalty available.

Finally, in consideration of the general patterns of the exhaustion doctrine, it is relevant to conclude that in the existence, within a compulsory licensing arrangement, of legal and economic bonds between the patent holder and the licensee, exhaustion should nevertheless occur. Clearly in those cases, the identity of patent holder and that of licensee effectively overlap within two bodies which are in fact a single undertaking. The consent to marketing, likewise, practically remain with the said undertaking, through the 'licensee' identity. It is therefore pointed out that should the links of that sort exist, exhaustion cannot be avoided simply because the licensing arrangement was, from a formal point of view, compulsory.[368]

***Possibility of Subjective Compulsion: Ethical Obligation to Market***

As it will be recalled, the ruling of the Court in *Merck v. Stephar,* had put utmost emphasis on the element of consent to the first marketing in the context of exhaustion of rights; and this was regardless of the fact that a patent protection was not available in the Member State of first marketing. The Court simply told the right holder to bear the consequences of commercial choice s/he made at the risk of not being able to make as high profits in that state as it possible in the presence of patent protection. This was because s/he also had the luxury of not making that commercial choice, and not taking that risk, in the first place.[369] As explained above, the same luxury, that is the discretion of whether or not to consent, was obviously not present in the case of compulsory licenses. This is the very reason why the sales effectuated by

[367] Id. para. 30
[368] KEELING, *supra* note 9, at 86
[369] Important, however, to note that this view raised serious theoretical concerns and inconsistency as regards the specific subject matter doctrine which the Court utilized as a reference point in defining the scope of exhaustion. That is, the reward function the court spelled out in the context of patents could not be possibly achieved when low price levels are inherently dictated due to the lack of availability of patent protection in some Member States. [(To that effect, see: Opinion of AG Fennelly on Joined Cases C-267/95 AND C-268/95, at I-6330,34; KEELING, *supra* note 9 at 113; for an analysis of different views on this, see: Paul Torremans & Irini A. Stamatoudi: *Merck v Stephar Survives the Test*, 22 Eur. Law Rev. 248 (1997)]. However the Court seems to have tackled this question preemptively by stating that This, however, does not mean guaranteeing that he will obtain such a reward in all circumstances; see: *supra* note 303

a compulsory licensee did not exhaust the patent holder`s parallel rights in other Member States.

Subsequently the in *Merck v. Primecrown*[370], the relevance of the ruling in *Merck v. Stephar* as well as the threshold of admissible 'compulsion' in order to avoid the exhaustion of patent rights have been tested. The question put to the Court in the latter case concerned, *inter alia,* whether a moral / ethical obligation to continue supplying the pharmaceutical in the market of a Member State where patent protection is not available constitutes a compulsion on the end of the patent holder for the purposes of exhaustion, thus avoiding the parallel imports of those product to the other Member States where patent protection exists. Put differently, the Court was invited to establish whether ethical obligation to market in that state connotes a compulsion akin to those under compulsory licenses.

In responding to this, the view of the Court was fairly clear: the compulsion such as to deprive the right holder of the authority to freely decide how the products shall be marketed occurs only when there is a genuine, existing legal obligation.[371] The Court regarded such a subjective element way too hazy to be of any use in identifying the cases where the right holder is deprived of this authority. Moreover, it implied that arguments of this fashion would easily be blended with economic considerations[372] and misappropriated with the aim of partitioning the national markets. In sum, the right holder cannot seek refuge to mere ethical obligations to market in order to prevent the parallel imports of the products put on the market.

### 6. Marketing in Breach of Licensing Agreement

A great deal of importance is attached to the question whether the breach of a contractual stipulation would *per se* deemed to have extinguished the underlying consent of the right holder to the marketing. In other words, it remains to be a matter of question whether the consent should be considered to be diminished when the licensee commenced in marketing of the corporeal goods in a way distinct than what is agreed upon in contractual terms. Should the answer to the latter be affirmative, then the follow-up question would be whether every minor contractual non-observance is liable to cancel out the consent or a particular degree of graveness is required for such a result. If the consent is thus precluded, this naturally connotes that the rights have not been exhausted, hence the right holder shall be entitled to preclude

[370] Joined cases C-267/95 and C-268/95: Merck v. Primecrown and Beecham / Europharm
[371] Id. para. 51
[372] Id. para. 53

further commercialization of the goods marketed in breach of the contractual stipulation. That is to say, the right to consensual first sale, forming a part of specific subject matter of the right, should be prevailed over free movement principle. It is obviously the specific subject matter of the rights that the derogatory provisions (Art. 36 TFEU) aimed at safeguarding.

As a preliminary point, it needs to be noted that the breach of a contractual provision, -albeit may coincide with an infringement at the same time- does not necessarily constitute the infringement of the subjecting intellectual property right. At this point it is obvious that there are two types of non-observances, i.e. i) breach of a contractual provision; ii) infringement of the subjecting right, which may or not accumulate on the same occasion. The former relates to the contractual relations between the parties and the remedies thereto should principally be sought under contract law. The latter on the other hand relates to the *erga omnes* proprietary aspect of intellectual property rights, violation of which exhibits the infringement of intellectual property right.

The actual nuance therefore, resides at the different portfolios upon which the effect is created by contractual relations one hand and by exhaustion on the other hand. Needless to reiterate the principle of privity, the archaic cornerstone of contract law, principally excludes a third-party effect being created by the contract; it is rather binding for the contracting parties. Likewise, a potential non-compliance has its impacts only on the contracting parties. In that regard, from a contractual view point, when the licensee conducts the acts in breach of the underlying licensing agreement, the claims that the licensor is entitled emerge from the contract and these can solely be brought up against the licensee. However the landscape may appear differently from the view point of substantive intellectual property provisions, the latter having included the proprietary interest into the equation. Unlike the rights and obligations stemming contractual relations, proprietary rights are of absolutory nature and binding for the third parties as well. Accordingly, if exhaustion has not occurred due to the lack of proper consent, the right holder -who accounts for the 'licensor' on the basis of the licensing agreement- retains its 'right of distribution' which can be invoked not only against the licensee but also against third parties who acquired the corporeal goods.[373] This follows that if the proper consent fails ripening, the right holder can preclude the subsequent commercialization of the goods, even if those were initially marketed by someone who is formally the licensee of the right holder.

[373] Jens Schovsbo & Thomas Riis, *Concurrent Liability in Contract and Intellectual Property Law: Licensing Agreements in Light of Case C-666/18 IT Development SAS*, 69(10) GRUR International 989-997 (2020)

The provisions that enable the derogations from the free movement principle, allowed doing so insofar as such derogation pertains to protecting industrial and commercial property. It is equally crucial to remember that the derogatory provisions are aimed at safeguarding intellectual property rights *per se* against free movement provisions where the latter tends to undermine the very essence of these rights. *The same derogatory provisions are, however, not aimed at policing the compliance of the parties to intellectual-property-based agreement, which typically is a license.* In that regard, it is noted that the breach of a contractual stipulation should imply that no consent, for the purposes of exhaustion, exists if that breach is, at the same time, infringement of the subjecting intellectual property right.[374] In other words, the consent must be deemed nullified when the contractual violation in question relates to right which could be invoked by the right holder *erga omnes,* not solely by the reason of the fact that it was committed by the licensee.[375]

This is of particular interest in the realm of trademarks insofar as the implications of the aforesaid view were reflected in the trademark legislation of the Union vis-à-vis trademark licensing. With identical wordings, both the Trademark Directive of the Union (TMD) in its Article 25(2) [Former Art 8(2) of Directive 89/104] and the Regulation on the EU Trade Mark (EUTMR) in its Article 25(2) [ Former Art. 22(2) of Regulation 207/2009] envisaged specific non-observance situations where the holder of the trademark could invoke its rights against the licensee, as follows:[376]

> *Article 25*
>
> 2. The proprietor of a trade mark may invoke the rights conferred by that trade mark against a licensee who contravenes any provision in his licensing contract with regard to:
>
> (a) its duration;
>
> (b) the form covered by the registration in which the trade mark may be used;
>
> (c) the scope of the goods or services for which the licence is granted;
>
> (d) the territory in which the trade mark may be affixed; or
>
> (e) the quality of the goods manufactured or of the services provided by the licensee.

Above provision delineates the intersection set of contractual contraventions which at the same time constitute the infringement of the trademark, despite the authorization contractually granted to the licensee to exploit thereof. In that sense it exhibits the specific

[374] GRIGORIADIS, *supra* note 287 at 297
[375] Id.
[376] Article 25(2) of Directive 2015/2436; Article 25(2) of the Regulation 2017/1001 [former Article 8(2) of Directive 89/104 and Article 22(2) of Regulation 207/2009 respectively]

appearances of infringement on the medium of licensing relation. It follows that, should the licensee breach the contractual stipulations on the aforesaid, there emerges two options ahead of the right holder: (i) resorting to the remedies on the grounds of contractual violation; (ii) infringement of the rights. Although it is true, from a general view point, that the provisions were aimed, *prima facie*, at regulating the relationship between the right holder and the licensee,[377] having not explicitly approached to the reverberation of such situations on the exhaustion of rights, albeit it was the ruling of the ECJ in *Copad* that signified the consent shall be impaired in the occurrence of contractual contravention as regards the above matters.

***Copad v. Christian Dior[378]***

The dispute in the main proceedings centered around the trademark licensing concluded between Dior and SIL in respect to manufacturing and distribution of high-end fashion products reflecting the luxurious image of Dior. To that end, the latter had stipulated in the underlying agreement that SIL would refrain, in order to retain the repute and prestige of that trademark, from selling the products to wholesalers, buyers' collectives, discount stores, mail order companies, door-to-door sales companies and the like. Nevertheless, in breach of its contractual obligation, SIL sold the products bearing 'Christian Dior' mark to Copad which operates discount stores. Quite evidently Dior brought infringement proceedings against SIL and Copad whereupon the latter claimed that Dior`s right had exhausted. While the court of first instance took the view that the sales in contravention to the agreement did not infringe the trademark rights but it merely gave rise to contractual liability. Subsequently, the Paris Court of Appeal, albeit not finding infringement, considered that the sales did not imply exhaustion of Dior`s rights. Finally, the Court of Cassation disagreed with the latter`s view on the point of exhaustion and held, in turn, that the marketing by SIL exhausted Dior`s rights. Following the opposition from Dior, by way of cross-appeal, that court referred the question to the ECJ, requesting clarification on whether the rights against the licensee as granted in Article 8(2) of the Directive [now Art. 25(2)] can be invoked on grounds of contravention to a provision of the agreement as regards the mark`s prestige and sales to discount stores and whether the sales in breach of such contractual provisions must be regarded as having been made without the right holder`s consent;

[377] Schovsbo & Riis, *supra* note 373, at 994
[378] Case C-59/08: Copad SA v Christian Dior couture SA

The Court of Justice initially delved into a grammatical interpretation of the provision of the Directive whereupon it concluded that the list offered in Article 8(2) [now Art. 25(2)] had exhaustively laid down the cases where the rights can be invoked against the licensee.[379]

As regards the main question, it sided with the AG who proposed that the quality of luxury goods is not a mere result of their material characteristics, but also of the allure and prestigious image which provide them with an aura of luxury.[380] Correspondingly, an impairment to that aura of luxury is likely to affect the actual quality of those goods.[381] With that background in mind, the Court suggested, the possibility exists for the right holder to invoke his rights, under Article 8(2) of the Directive, against the licensee given that the practice in contravention of the contract has actually damaged the allure and prestigious image.

The Court subsequently set about responding to the question whether the contravention as regards these specific provisions of the agreement shall be construed as to avert the consent for the purposes of exhaustion. Having reiterated, in the light of the settled case law, that the consent as such shall either be an express statement or alternatively be deduced from legal and economic links between the right holder and the person who effectuate the marketing. Licensing arrangement typically engenders such links, thus normally bringing exhaustion in play. However, the Court continued, license agreements do not imply an absolute and unconditional consent of the right holder in respect to the act of the licensee.[382] In line with this very postulate, Article 8(2) [now Art. 25(2)] of the Directive, sets out -in a limited manner- the contractual elements whose breach exceeds beyond the limits of the consent embedded in that legal and economic links. *Consequently, the licensee's contravention to one of those exhaustively listed clauses precludes exhaustion of the trademark holder`s rights.*[383]

***Overall Remarks and Particular Situation of Marketing of Inferior Quality Goods***

Should the licensing agreement be violated in respect to (i) its duration; (ii) the form covered by the registration in which the trade mark may be used; (iii) the scope of the goods or services for which the license is granted; (iv) the territory in which the trade mark may be affixed; (v) the quality of the goods manufactured or of the services provided by the licensee, trademark holder`s right to interfere with the further commercialization is deemed to have not

[379] Id. para. 20
[380] Id. para. 24
[381] Id. para. 26
[382] Id. para. 47
[383] Id. para. 50

exhausted. As a result of the absence of exhaustion, the rights may be invoked not only against the licensee who violated the contract but also against subsequent buyers.[384] Crucially, however, the possibility of precluding the exhaustion is strictly limited to those specific cases. All other claims arising from contractual contraventions are to be pursued within the realm of contract law, albeit with the express proviso that the contractual stipulation in question is compatible with the competition rules of the Union (Art. 101 and 102 TFEU); or else they would be automatically void.[385] By the same token, breach of contractual stipulations other than those listed would not suffice to eliminate the consent, therefore exhaustion could not be precluded. Indeed, the latter imperative was already affirmed in the above-discussed *Peak Holding* judgement, on the basis of a distribution agreement. The Court in that ruled, the right holder, having sold the product to a distributor within the EEA, has exhausted its rights. This was unaffected from the fact that the distributor had contractually committed not to sell those articles in the EEA.[386] Territorial restrictions on the right to resell the goods concerns only the relations between the parties to that act[387], thus, the remedies to that breach was to be sought under the purview of contract law. Consequently, in the event that the licensee contravenes to contractual stipulations in relation to those subject *numerus clausus* listed in Article 25(2), the right holder shall retain two options ahead: either to raise a claim on the basis of contractual violation or to claim infringement of the rights. Yet, quite intrinsically, the latter appears more advantageous on the end of the right holder given that it precludes the exhaustion hence enabling the claim in respect also to downstream sales of goods.[388]

It is of a little surprise that the specific types of contractual breaches, as listed in Art 25(2) of Directive, constituting an infringement of the trademark were found to nullify the consent underlaid in the licensing arrangement. What is surprising however is the extraordinary flexibility that the Court exhibited in relating the 'aura of luxury' to the quality standards. Conversely however, the Court had expressed in *Ideal Standard*, so as to exhibit the rationale of legal and economic links, that the decisive factor was the possibility of control over the quality of goods; not the actual exercise thereof.[389] It is this possibility that represents the legal and economic links where the consent is inferred from; exhaustion thus occurs in the presence

[384] Schovsbo & Riis, *supra* note 373, at 5
[385] To that effect, see Article 101(2) TFEU; See, also KEELING, *supra* note 9, at 90-92.
[386] Case C-16/03: Peak Holding AB v Axolin-Elinor AB, para. 56
[387] Id. para. 54
[388] KUR, ET AL., *supra* note 14 at 307
[389] Case C-9/93: IHT v. Ideal-Standard, para. 38

of these links. Such links undeniably exists in licensing agreements; indeed, this was articulated in the aforesaid judgement.[390] This follows that, where such a possibility of control exists, regardless of the formal character of the relation between the right holder and the marketing body, exhaustion cannot be avoided on the grounds of poor quality. Yet again, such possibility intrinsically exists in license agreements.

In the light of foregoing one feels compelled to find an inconsistency between the two judgements of the Court: on one hand poor quality was considered not to be the sufficient grounds to exclude the exhaustion in the presence of the possibility of quality control (Ideal Standard); on the other hand, relatively abstract concept of 'aura of luxury' was construed as a dimension of the quality of goods, accordingly, breach of contractual provision in a way to impede that 'aura' was deemed to preclude the consent. The potential answer, in our opinion, resides at the expression of 'possibility' and whether or not that possibility has been properly implemented. When the contractual inclusion of the quality assurance mechanism has been omitted, it should imply that that the right holder had but denied this 'possibility'. Furthermore, one could infer from the wording of Article 25(2) of the Directive that it opens up the possibility of invoking the rights against the licensee exclusively when the following conditions are cumulatively met: (i) the *numerus clausus* subjects are ascertained by the provisions of the licensing agreement (ii) those provision are violated by the licensee. Inherently, in the lack of such stipulations in the contract, exhaustion cannot be avoided. Likewise, when the licensing agreement includes the relevant quality assurance and monitoring provisions but the right holder nevertheless tends to not deploy them, or uses them in an ineffective manner, it should be deemed to have tolerated the marketing of inferior quality goods. It is noted that the imperative follows from *Ideal Standard* ruling is that the licensor`s failure to take the necessary steps to enforce contractual stipulations as to quality amounts to acquiescing in the licensee's breach, thus exhaustion applies.[391] In both cases exhaustion must have occurred. As a matter of course, these are valid insofar as exhaustion of distribution right is at stake; that is to say, contractual remedies could still be sought in that regard.

The significance of the specific infringement cases set out in Article 25(2) of the Directive, thus, hence the possibility of precluding the exhaustion, comes into play when the marketing, by the licensee, of inferior quality of goods takes place despite the possibility of quality assurance was contractually ascertained and was dully practiced by the licensor. This

[390] To that effect, see. Id. para. 34
[391] KEELING, *supra* note 9, at 92

approach also seems to have found a good deal of favor from legal scholars. Keeling, to that end, had noted, even before the judgement in *Copad*, that there are circumstances in which the holder of trademark must be allowed to oppose further commercialization, hence the parallel import, of a licensee's 'shoddy' goods, given that the licensor took all the possible steps and implemented all the precautions to ensure the licensee`s compliance with quality standards.[392] In that, he drew a particular attention to the product liability sanctions which may fall on the trademark holder, when inferior quality of goods are allowed being further commercialized.[393] He added, however, that the wording of the Article 25(2) [at the time, Art. 8(2) of Dir. 89/104/EEC] on the rights can be invoked against the licensee was not absolutely clear in the matter of exhaustion.[394] That clarity, as we referred above, was provided by the Court`s interpretation in *Copad*.

The same approach has been more systematically articulated by Grigoriadis, who suggested that the breach of quality standards -as the grounds of invoking the rights against the licensee- set out in Article 25(2)(e) of the Directive cannot be relied on so as to preclude the exhaustion when one of the following is met: (i) the right holder did not include in the licensing contract clauses enabling him to check the quality of goods manufactured by the licensee; (ii) the right holder, albeit having formally included such clauses, *de facto* tolerated the manufacture of poor quality goods by the licensee, or, in all cases, the right holder did not exercise an actual control over the quality of the goods manufactured by the licensee.[395] In the meantime, he incisively suggests, the said provision of the Directive could be relied on when the following conditions are cumulatively met: (i) the right holder included in the license agreement clauses enabling him to monitor the quality compliance of the licensee; (ii) the right holder actually conducted, in line with those clauses, surveillance over the quality of goods of the licensee; (iii) the right holder tried to prevent the licensee from manufacturing and putting on the market poor quality goods by seeking prohibitory and/or eliminatory injunctions before the court of jurisdiction; (iv) despite all these measures having been taken by the right holder, the licensee nevertheless put the inferior quality of goods on the market.[396] In addition to this thorough analysis, it is also necessary to state that the quality differences arising from the customization the goods in accordance with the consumer profile of the target Member State,

[392] Id.
[393] Id.
[394] Id.
[395] GRIGORIADIS, *supra* note 287, at 302
[396] Id.

quite obviously, would not constitute a legitimate ground to oppose to the parallel import of lower quality of legitimately marketed goods into the other Member State where higher quality of goods are originally marketed. Such quality difference can be said to clearly and consensually emanate from the marketing strategy of the right holder; as long as the goods are legitimately marketed in the EEA, regardless of their targeted national consumer profile, the rights exhaust.

*Application to licensing arrangements in respect to other intellectual property rights*

A point which should not be omitted, however, is that the limited types of contractual violations by the licensee that were listed in Article 25(2) of the Trademark Directive, and were subsequently found, in *Copad,* to nullify the exhaustion are applicable, from a formal view point, only to trademark licensing. This leaves unanswered the question of exhaustion in cases of contractual violation when the subjecting intellectual property right is something other than a trademark. Certain guidelines are, nevertheless, present in respect to design rights and plant variety rights on the face of similar provisions (to those in Art. 25(2) of the Trademark Directive) existing in the Union law.

Remarkably, the Design Regulation[397] accommodates provisions similar to that of the Trademark Directive setting out certain contractual violations that allow the holder of the design rights to invoke his rights against the licensee. Although the list of specific types of breach is, for the most part, identically inferred from the Trademark Directive, the Design Regulation excluded the 'territory of affixing' as a ground of infringement. Accordingly, the relevant provision of the Design Regulation, spelling out four specific cases whereunder the rights can be invoked against the licensee, reads:

> *"…[T]he holder may invoke the rights conferred by the Community design against a licensee who contravenes any provision in his licensing contract with regard to its duration, the form in which the design may be used, the range of products for which the license is granted and the quality of products manufactured by the licensee."* [398]

As will be recalled, the ECJ had strictly established in *Copad* that the list in Trademark Directive was exhaustive and this postulate follows primarily from the wording of the said

[397] Regulation 6/2002 on Community designs
[398] Id. Article 32(2)

provision. The reason dictates, given the identical wordings, add to the jurisprudence of the Court in the aforesaid judgement, that the list accommodated in the Design Regulation must, likewise, be construed as exhaustively laid. This should also imply that the fifth element which was excluded from the scope of design law provision (i.e. territory of affixing) cannot be applied, by analogy, to design right licenses. Consequently, should the licensee contravene the licensing agreement on one of those four points, exhaustion must be able to be precluded by the right holder.

On the other hand, the language employed in the Plant Variety Regulation[399] remarkably differs from the aforesaid. The framework of licensing arrangements concerning plant variety right are considered by the Regulation under the header of "contractual exploitation rights". Accordingly, Article 27(2) establishes that:

> "*The holder may invoke the rights conferred by the Community plant variety right against a person enjoying "the right of exploitation who contravenes any of the conditions or limitations attached to his exploitation right…"*[400]

Plain reading of the provision seems not to reveal a specific list, nor does it imply any differentiation between the types of breaches. One might, therefore, be tempted to deduce from the wording of the article that contractual contraventions of any type would entail the possibility for the right holder to raise an infringement claim against the beneficiary of the contract, that is the licensee. Furthermore, taking the infringement to be the antecedent to the preclusion of exhaustion, it is equally tempting to reach the conclusion that any contractual contravention by the licensee would impede the consent, hence preventing the exhaustion. Such an outcome would clearly entail harsh implications on the end of further commercialization of 'material of the protected variety'[401] with effect to third parties, and be impolitic to very rationale of the exhaustion of the rights over this material. This potentially over-reaching implication has been moderated by the ECJ in *Greenstar-Kanzi Europe*.[402] Although, as might be expected, the Court did not set about specifying the contractual breaches, it envisaged the concept of 'essential features of right', whose assessment was to be made by the national courts. In that regard, the ECJ established that *"If the referring court were to establish that the*

[399] Regulation 2100/94 on Community plant variety rights
[400] Id. Article 27(2)
[401] The phrase 'material of the protected variety' is employed by the Regulation to refer to the goods protected under plant variety rights. See. Id. para. 16.
[402] Case C-140/10: Greenstar-Kanzi Europe NV v Jean Hustin and Jo Goossens

*protected material was disposed of by the person enjoying the right of exploitation in breach of a condition or limitation in the licensing contract relating directly to the essential features of the Community plant variety right, it would have to be concluded that that disposal of the material, by the person enjoying the right of exploitation to a third party, was effected without the holder's consent, so that the latter's right is not exhausted."*[403]

Differentiation, therefore, must be made not between the specific emergences of a breach, but rather between simple contractual breach and those with direct impact on the protected right.[404] Nevertheless, this nuance was to be ascertained by the national court of the Member State. It is finally presumable, and *a contrario* inferable from the Court`s line of judgement, that non-essential breaches, albeit cannot eliminate the exhaustion, may be pursued within the framework of contract law.

As far as copyright and patents are concerned, it is noted that - unlike trademarks, Community designs and plant variety rights - there is no apparent legal basis in the Union law under which the right holder is enabled to raise an infringement claim against the licensee.[405] Given the graveness of exhaustion within the context of free movement principle, and the concordant restrictive interpretation of the Court as to the cases whereunder exhaustion can be precluded due to a contractual contravention, applying the provisions of trademark, design or plant variety rights by analogy to patents and copyrights would likely be devoid of proper legal basis. In the absence of such provision in Union law, proper legal basis for asserting infringement against the licensee is to be sought in the national law, albeit with the express proviso that this basis shall not constitute arbitrary discrimination or a disguised restriction within the meaning of Article 36 of TFEU. Furthermore, in certain cases the absence - or extinction - of consent might flow from plain logic. For instance, it comes quite intrinsic that, the breach of licensing agreement on point of 'duration' forms not only a breach of contract, but it also - insofar as it exceeds the temporal scope of agreement - constitutes the unauthorized use of underlying intellectual property right, hence infringement. This has very little to do with the type of the underlying intellectual property right. Consequently, we tend to believe, such self-evident cases, notwithstanding the absence of legal basis in the Union law, should be deemed, at least by the national courts, to preclude the consent for the purposes of exhaustion.

[403] Id. para. 43
[404] Gert Würtenberger, *Plant variety rights and breach of licence*, 7(3) J. Intell. Prop. L. 161, 164 (2012)
[405] Schovsbo & Riis, *supra* note 373, at 997

## 7. The Geographical Scope of Exhaustion

The first two constituents of the exhaustion are defined by the goods being 'put on the market' which is done 'by the right holder or with his consent'. The third and the most definitive element of the Community exhaustion is its territorial scope. The initial marketing of corporeal goods, in line with the first two elements, exhausts the rights in respect to the Union only when it takes places within the Union. By the same token, when the goods are initially marketed outside this territorial scope, the right holder could still oppose to parallel imports into the Union.

Certain premises, we had already discussed in relation to territoriality principle, need to be recalled. It is the choice of exhaustion regime that predestine the further commercialization of the goods in international trade. The territorial scope of exhaustion delineates the area within which the goods are tradable without the interruption of the intellectual property right holder. This scope traditionally appears to be a national one or international one. The peculiarity of the exhaustion regime of the Union, that classifies as a regional exhaustion model, arises from the fact that it is placed between these two extremes. It is frankly coherent with the rationale that the free movement -without the interruption of intellectual property territoriality- is intended between the Member States whose territory collectively demarcate the territorial scope of exhaustion. This result would not have been achieved if national exhaustion was, at any level, permitted. Quite the contrary national exhaustion model, as we discussed at length above, would add up to partitioning of national markets, thus remaining to be a natural hostile of the free movement principle. From a purposive view point, it is clear that the Community exhaustion has been devised with a view to setting aside the adverse impact of national exhaustion on trade between the Member States; and it has done so by eliminating the national exhaustion possibility all together. Under the imperative of the Community exhaustion there is no doubt as to what is prohibited, i.e. national exhaustion of rights. The early judicial formulation[406] and the subsequent codification (that is by the first Trademark Directive)[407] of the Community exhaustion were influenced by this exclusionary understanding.

[406] Case C-78/70: Deutsche Grammophon v. Metro-SB-Großmärkte, para. 12,13
[407] See Article 7 of the first trademark directive (Directive 89/104/EEC of 21 December 1988 to approximate the laws of the Member States relating to trade marks) on the exhaustion of rights.

### 7.1. Less is Prohibited; What About More?

It has not been equally clear, however, whether the other extreme, i.e. international exhaustion, was permissible. As the geographical scope of exhaustion defines the destiny of -what is referred to as- 'further commercialization' of the incorporeal goods, the latter question retains important subtexts as to the level of trade liberty the EU is willing to afford. By the same token, it indicates at least two different camps the Member States are divided into as regards such level of liberty. On one hand, a protectionist understanding echoed that the regional exhaustion model must be perceived to be limited to the free movement principle so as merely to safeguard the integrity of the internal market; on the other hand, from a more liberal view point, it is construed as a minimum standard, leaving room for adoption of the international model.

In the sequel of eliminating the national exhaustion of the rights and establishing the Community-wide exhaustion, a subsequent question however arose: Not having explicitly precluded the international exhaustion, did the Trademark Directive intend to leave the room to the Member States whether to adopt international exhaustion? In other words, the question was whether community-wide exhaustion is the only option or rather a minimum standard beyond which the Member States may go on to adopt international exhaustion. The ECJ set about clarifying this in *Silhouette*[408]. Accordingly, the Court articulated that the primary purpose of the Directive in approximating the national trademark laws of the Member States is to remove the disparities that may impede the free movement of goods and services, thus ensuring the functioning of internal market. The setting where some Member States provide for international exhaustion while others provide for Community exhaustion would give rise to barriers to the free movement of goods and the freedom to provide services.[409] In this connection, the Court ruled that the Directive cannot be interpreted as to leave it to the Member States' discretion to provide in their domestic law for international exhaustion of the rights.[410] Such a preclusion takes vital effect as regards parallel import from outside of the European Economic Area [EEA]. Accordingly, when the goods are first marketed on the outside of the EEA, the proprietor of the trademark would not exhaust its rights in respect to the EEA, therefore, the subsequent sales of the goods in question into the EEA require the proprietor's

[408] Case C-355/96 - Silhouette International Schmied v Hartlauer Handelsgesellschaft
[409] Id. para. 27
[410] Id. para. 26

consent. Having stated later, in *Sebago*[411], that the provision of Directive does not leave it open Member States whether to provide for international exhaustion, the Court of Justice reaffirmed its position. It further established that consent within the meaning of the provision must be that which relates to each item of product of the consignment over which exhaustion pleaded.

Finally in *Laserdisken II*[412], law of the Union the settled jurisprudence prohibiting the adoption of international exhaustion was -rather unavailingly- challenged; though this time with respect to distribution of copyright protected works. In the underlying dispute, the claimant, whose business is confined to importing the copies of cinematographic works from outside the EEA and selling them internal market, asserted the invalidity of the provision InfoSoc Directive on exhaustion. In doing so it claims that the prohibition of international exhaustion regime[413] falls contrary to the international obligations of the Union aimed at facilitating international trade.[414] The Court, in response, held not only was such a provision immensely vague to be a basis of a normative obligation, but also it did not, by any means, intend to regulate the issue of exhaustion.[415] Eventually, through a analysis of the legal basis of the Directive and the teleology of the exhaustion rule therein, the Court concluded in essence that the Community exhaustion was exclusive standard.[416] It is without doubt that this teleology is the very integration and the functioning of the internal market; and the hypothetical *'situation in which some Member States will be able to provide for international exhaustion of distribution rights whilst others will provide only for Community-wide exhaustion of those rights will inevitably give rise to barriers to the free movement of goods and the freedom to provide services.'* [417] Important to observe that the universal language the Court employed in the quoted reasoning clearly reflects the redundancy of raising the identical question (i.e. the possibility of an international exhaustion regime) as regards different intellectual property rights on different occasions. It is beyond doubt that the answer will not change regardless the goods in question incorporate a patent, a trademark, copyright or a design: the exclusive scope of exhaustion is the regional one.

[411] Case C-173/98 - Sebago v. GB-Unic SA.
[412] Case C-479/04: Laserdisken ApS v. Kulturministeriet (Laserdisken II)
[413] See Article 4(2) of the InfoSoc Directive in conjunction with the 28th recital of the said Directive
[414] That are some non-normative provisions of the OECD Convention (Convention on the Organisation for Economic Co-operation and Development, 1960) that the aims of the conventions.
[415] Laserdisken II, para. 37,38
[416] Id. para. 24
[417] Id. para. 26 (Emphasis added)

### 7.2. A Push Towards International Exhaustion: Implied Consent and Consent Defined

On the other hand, the positioning of the Court in *Silhouette* and *Sebago* has not found equal favor from the Member States but remained rather contentious as regards the preclusion of international exhaustion. More particularly, England and Sweden reacted to such a prohibition and advocated for international exhaustion, whereas the Member States such as France and Italy that associate with the industry of high-margin goods -which in most instances the fashion goods- sided with the views of the ECJ. Said convergence has, eventually, been reflected in *Zino Davidoff*[418] in the main proceedings of which the High Court of Justice of England Wales (the Chancery Court) challenged the positioning of the ECJ by putting forward the concept of implied consent according to which, it stated, there is no presumption that the proprietor of the trademark should be deemed to object importation into the EEA of goods that were marketed outside of Community. It argued that, as much as the recent case law of the Court favored the proprietor`s ability to prevent such importations, proprietor, however, also has the right to consent to such importation. The plaintiff in the present case was free to place the goods on the market outside the EEA with an effective restrain on their further sale, but failed doing so, thus, it implied its consent to further sales. Therefore, the buyers in the distribution chain should be free to sell the products further wherever they wish to, including EEA.[419]

Afore mentioned decision of the Chancery Court was referred to the Advocate General (the AG). However, the AG mostly disagreed, having described the nature of consent,[420] she suggested that implied consent should be permissible under exceptional circumstances. Nevertheless, she emphasized that the Member States could not establish a presumption of waiver of exclusive rights within the EEA based merely on the put on the market of the goods outside of the community, waiver has to be, therefore, judged in connection with the circumstances of each specific case.[421]

The Court of Justice, however, presented an inclination towards adhering rather to the express consent model that it had formerly followed. Nevertheless, it went on to admit the

[418] Joined Cases C-414/99; C-415/99; C-416/99 - Zino Davidoff SA v A & G Imports Ltd and Levi Strauss & Co. and Others v Tesco Stores Ltd and Others

[419] CATHERINE SEVILLE, EU INTELLECTUAL PROPERTY LAW AND POLICY 363 (1 ed. Edward Elgar Publishing 2009)

[420] In the case of parallel imports from non-member countries, the trade mark proprietor's consent to placing the products in question on the market in the EEA therefore consists of the waiver of his exclusive right to control distribution within the EEA. See. Opinion of Mrs. Stix-Hackl — Joined Cases C-414/99, C-41J/99 and C-416/99, para. 99.

[421] Opinion of Advocate General Mrs. Stix-Hackl — Joined Cases C-414/99, C-41J/99 and C-416/99, para. 123(3)

inevitableness, in some cases, of the consent being inferred from the facts and circumstances prior to, simultaneous with or following the placing of the goods on the market outside the EEA.[422] It went on to state that, even in the said circumstances, for implied consent to be permissible, it has to demonstrate "unequivocally" that the proprietor has renounced his right to oppose subsequent marketing of the good in the Community.[423] Accordingly, implied consent cannot be inferred from[424]:

- The fact that the right-holder failed to communicate to all subsequent buyers its opposition regarding the importations of the goods into the EEA;
- The fact that the goods bore no warning note stating such opposition;
- The fact that the proprietor has not stipulated any contractual provision to contain this manner or restriction;
- The importer being unaware of the proprietors` objection.
- The fact that authorized resellers failed to stipulate in their contracts such a reservation.

Reading all together, the Court has adopted a strictly narrow concept of implied consent and confirmed its views to retaining Community exhaustion principle.[425]

***Summary***

Clear from the foregoing, the Community exhaustion is not a minimum standard but it was rather the exclusive standard.[426] As far as the exhaustion of the rights is at the stake, the consensual first marketing necessarily to be made within the Union. Neither national intellectual property rights nor those with unitary effect across Europe shall be exhausted in respect to the goods that were initially sold outside the Union. This follows that importation of these goods, by the third-party traders,[427] into the Union would amount to 'putting on the market in the Union for the first time'; it is, therefore, subject to the right holder`s consent.

[422] Joined Cases C-414/99; C-415/99; C-416/99 - Zino Davidoff SA v A & G Imports Ltd and Levi Strauss & Co. and Others v Tesco Stores Ltd and Others, para. 46.
[423] Id.
[424] Id. Article 2 of the holding.
[425] Elizabeth Brasser, *Sharing the Burden of Proof in Parallel Importation Cases: A Proposal for a Synthesis of United States and European Union Trademark Law*, 1 J. High Tech. L. 119, 130 (2002)
[426] Irene Calboli, *Reviewing the (shrinking) principle of trademark exhaustion in the European Union (ten years later)*, 16 Marq. Intell. Prop. L. Rev. 257, 259 (2012)
[427] It should be remembered at this point that the mere importation of the trademarked goods into the EEA by the right holder with a view to selling them on the internal market would not exhaust his/her rights until there is an actual sale. To that effect see: Case C-16/03: Peak Holding v. Axolin-Elinor discussed above.

### 7.3. The Earlier Practice on Allocating the Burden of Proof and the Core of the Issue

Although the Court Justice in *Silhouette* and *Sebago* decisions put an emphasis on the central role of consent in parallel import cases and further delineated its scope, it has not made a conclusive statement regarding the allocation of the burden of proof. In the main proceedings of *Zino Davidoff,* however, the Chancery Court expressed that the evidentiary burden laid with the defendant regardless of who bears the burden of proving where the goods come from.[428] Having presented parallel patterns to this in *Zino Davidoff*, the Court of Justice -in addition to comprehending the fashion of consent at length- has also undertaken the mission to make an implication as regards the evidentiary burden. In doing so, the ECJ built upon its brand-new and fairly rigid notion of implied consent, namely the "unequivocal demonstration of waiver". Accordingly, for the proprietor`s conducts to be construed as implied consent they must very clearly and inarguably demonstrate the waiver, so much so that, it logically falls to the importer alleging consent to prove it and not for the trade mark proprietor to demonstrate its absence.[429] In this manner, the Court of Justice has deemed the evidentiary burden to be on the importer as a logical sequence of its views as regards implied consent.

The Court of Justice, at that stage, deduced an evidential burden pattern what seems to be echoing the simple civil procedural logic,[430] such a model can be said to subsume certain perils, characteristically in parallel import disputes in connection with intellectual property rights. Particularly when the full burden of proof is imposed on the importer, it would very likely require the importer to disclose the entire supply chain to enable the tracing of prior purchases all the way to the first sale by the proprietor so as to establish the existence of consent. Moreover, it is apparent that the importer`s ability to procure the information pertaining the sources of all prior purchases is not unlimited. Thus, even though parallel importers are normally expected to show the preceding source that they acquired the goods from, they will often not be able to push their supplier to reveal the rest of the distribution chain.[431] Leaving no choice to the importer but revealing the supply chain, on the other hand, would pretty much mean handing to the proprietor -on a silver platter- the opportunity to "plug

[428] Davidoff SA v. A&G Imports, Ltd. [1999] 3 All ER 711; See. Thomas Hays, An Application of the European Rules on Trademark Exhaustion to Extra-Market Goods, 91 Trademark Rep. 675 (2001), pp.713; See. The Opinion referred above, pp. 127
[429] Joined Cases C-414/99 to C-416/99: Zino Davidoff, para. 54.
[430] General rule in regard to the burden of proof in civil procedure may perhaps be summarized thusly: Evidentiary burden lies with the party which is to derive a legal result in his favor from the proving of that respective claim.
[431] SEVILLE, *supra* note 419, at 368

the holes"[432] in its distribution channel. Inevitably, the said scenario also involves the risk that trademark proprietors could initiate court proceedings for mere purpose of finding out the leaks in their distribution system.[433] Most of all, *de facto* restriction of parallel imports by means of this scheme could clearly serve for market partitioning, thus, seriously endangering the free movement of goods.

### 7.4. Shift of Evidentiary Burden: *Van Doren* Case

The aforementioned concerns were addressed in the preliminary ruling request of German court[434], and largely scrutinized by the ECJ in *Van Doren* Case.[435] The dispute in the main proceedings concerned 'Stüssy', a registered mark of an American company[436], in respect of clothing and articles bearing this trade mark are marketed worldwide. However, the items lacked any particular sign to indicate where they have been and can be marketed. *Van Doren* is exclusive distributor of Stüssy clothing in Germany and it is bound not to sell the goods to intermediaries for resale outside his contractual territory. However, another company, namely *Lifestyle,* turned out to market in Germany 'Stüssy' articles which it has not acquired from *Van Doren*. Having been informed of the sales, *Van Doren* brought proceedings against *Lifestyle* alleging that the products which had originally been put on the market outside the EEA, in the United States. Meanwhile the defendants in the main proceedings contend that they were initially placed on the market within the EEA by the proprietor or with its consent, so that the exclusive right of the trade mark proprietor is exhausted. The defendant also went on to argue that it was not required to name the suppliers before *Van Doren* proved the imperviousness of its distribution system.[437]

The referring court raised its concerns that if the evidentiary burden is placed on the plaintiff i.e. dealers, there occurs a serious risk that those who are not connected to the proprietor would be precluded from marketing products bearing that mark even, where the products have been put on the market in the EEA with the consent of the proprietor. In general, a dealer will be able to show from whom he has purchased goods but he will not be able to

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[432] Thomas Musmann, *No Mercy: Exhaustion of patent rights and burden of proof*, KLUWER PATENT BLOG, (2014) <http://patentblog.kluweriplaw.com/2014/03/14/no-mercy-exhaustion-of-patent-rights-and-burden-of-proof/>
[433] SEVILLE, *supra* note 419, at 368
[434] German Federal Court of Justice *(Bundesgerichtshof)*
[435] Case C-244/00 - Van Doren + Q. GmbH v Lifestyle sports + sportswear Handelsgesellschaft mbH and Michael Orth.
[436] Stussy Inc., headquarter in Irvine, California, United States
[437] C-244/00 - van Doren + Q, para. 13.

make his suppliers reveal the previous supplier or demonstrate other links in the distribution channels. Moreover, even if he were able to trace the distribution channel back to the trade mark proprietor and to show that the goods were put on the market in the EEA with the consent of that proprietor, his supply source would be liable to dry up immediately.[438] It went on to suggest that under the given circumstances it is very likely that the trademark holder would invoke his rights for market partitioning. Taking all into account, the referring court asked whether the appropriate solutions to tackle these perils would be to impose the burden on the importer only if the manufacturer has affixed reasonable signs to distinguish the goods which have been put on the market in the EEA by him or with his consent from goods which have been put on the market outside the EEA.[439]

The Court of Justice acknowledged the significance of the issue uttered by the German court. The ECJ primarily reaffirmed that the rule of evidence (i.e. obliging the importer to prove) was consistent with Article 5 and 7 of the Directive[440] as well as with its views established in *Davidoff*. It subsequently went on to admit that this rule of evidence might need to be reviewed to the extent that ensuring the free movement of goods enshrined in the establishing treaties of the Community is the matter of first priority. In doing so, the ECJ adopted quite a distinct approach from the suggested solution of the referring court, although it did not correspond specifically to this suggestion. Accordingly, where a third party succeeds in establishing that there is a real risk of partitioning of national markets if he himself bears that burden of proof, particularly where the trade mark proprietor markets his products in the European Economic Area using an exclusive distribution system, it is for the proprietor of the trade mark to establish that the products were initially placed on the market outside the European Economic Area by him or with his consent. If such evidence is adduced, it is for the third party to prove the consent of the trade mark proprietor to subsequent marketing of the products in the European Economic Area.[441]

[438] Id. para. 21.
[439] Id. para. 23.
[440] Article 5 and 7 of "First Council Directive 89/104/EEC of 21 December 1988 to approximate the laws of the Member States relating to trade marks" concerning respectively "Rights conferred by a trade mark" and "Exhaustion of the rights conferred by a trade mark"
[441] Last para. – Case C-244/00 - van Doren + Q

# CHAPTER 5

# INEXHAUSTIBLE RIGHTS: SPECIFIC CONSIDERATIONS FOR COPYRIGHT

The *raison d'etre* of the exhaustion doctrine is to set free movement of goods in motion against the trap of territorial intellectual property rights, exclusive distribution right in particular. In doing so it enjoins the right holder from interfering with the further commercialization by way of subsequent trade of the corporeal goods. Subsequent trade, therefore, corresponds to further 'distribution' of such goods; and the exhaustion doctrine relates principally to distribution right. With that being said, important to reiterate, exclusive distribution right, albeit a central one, is only one of the prerogatives conferred to the holder of a particular intellectual property right; in other words, it is only one element in the cluster of rights. It is only the exclusive distribution rights of corporeal goods that are considered exhausted after the first distribution made or consented to by the right holder.[442]

As far, especially, as copyright protected substance is concerned, the use of protected subject matter can take other forms besides initial and subsequent sales. This sequel is partly owed to the wide - and ever expanding - scale of creations that fit into the definition of 'work' for the purposes of copyright. Correspondingly, even if the tangibles embodying the copyright protected work were consensually marketed (in which case the distribution right is obviously exhausted), their subsequent use may take other forms than the resale of these goods. Certain other rights among this cluster corresponding to these distinct forms of exploitation, by their very nature, are not (legitimately) affected from the initial marketing. This follows that the right holder may rely on his intellectual property rights of this sort so as to restrict other uses of such a product regardless of having put them on the market.[443]

## 1. Rental and Lending Rights

In a relatively early stage, the Court of Justice came to conclude that the exhaustion, following the initial marketing, does not necessarily extend to rental and lending rights. In *Warner Brothers v. Christiansen*[444] the dispute concerned the importation of the video cassette

[442] Yusuf & von Hase, *supra* note 21 at 117.
[443] STOTHERS, *supra* note 101 at 126
[444] Case C-158/86: Warner Brothers v. Christiansen

of a film from the United Kingdom into Denmark by the owner of a Danish video shop with a view to renting it out in the latter country. Under Danish law, notwithstanding whether the copy of the work is of national origin or it is imported, the rental of such copies, in this case a video cassette, was subject to consent of the copyright holder. However, no similar provision existed under the legislation of the UK, results being that the rental of the work, in that jurisdiction, cannot be controlled by the right holder after the initial marketing. Upon the proceedings brought by the holder of Danish copyright to the film, in reliance to the exclusive rental right under Danish law, the ECJ was called on to answer whether this provision of Danish law was in conformity with the free movement provision.

The ECJ having noted that the rental of such recordings of cinematographic works is an emerging market and caters to a greater audience than that is accessed by means of the sales of recordings, thus offering an appreciable source of revenue for the producers.[445] Logically, should the rental rights be exhausted upon the first sales of recordings, the right holders would only be entitled to derive remuneration from those sales, the market of which loses ground to that of rental. Along the same lines, the greater and expanding potential in the market of hiring-out would be endorsed to the others on the sole ground that they possess an original copy of the work.

The view of the Court appeared to have recognized this potential fallacy. It held that "*by authorizing the collection of royalties only on sales to private individuals and to persons hiring out video-cassettes, it is impossible to guarantee to makers of films a remuneration which reflects the number of occasions on which the video-cassettes are actually hired out and which secures for them a satisfactory share of the rental market*."[446] Accordingly, Danish law setting out the exclusive rental right is justified within the meaning of the protection of industrial and commercial property that enables the derogations from free movement provisions.

The outgrowth of the above ruling shaped up the direction of harmonization in the field of rental rights, resulting in the Rental and Lending Rights Directive.[447] Accordingly, Member States are obliged to provide for the right to authorize or prohibit the rental and lending of

[445] Id. para. 14
[446] Id. para. 15
[447] Directive 2006/115/EC of the European Parliament and of the Council of 12 December 2006 on rental right and lending right and on certain rights related to copyright in the field of intellectual property. (Formerly, Directive 92/100/EEC)

originals and copies of copyright works, and other subject matter; and the latter right shall not be exhausted by any sale or other act of distribution thereof.[448]

Further effort was, however, put so as to bring the exclusive rental right within the ambit of exhaustion. Immunity of such rights to initial sale or other acts of distribution, however was made clear by the provision of the Directive, in *Laserdisken I*,[449] exhaustion thereof has been tested in respect to initial hiring out. The Court, consistent with its earlier view, held that it follows from the very nature of the exclusive right to hire out the recordings of the work that they can be exploited by repeated and potentially unlimited transactions, each of which involves the right to remuneration.[450] The specific right to authorize or prohibit rental would be rendered meaningless if it were considered to be exhausted as soon as the object was first offered for rental.[451]

**2. Rights in Performances & Communication to the Public**

Besides the exploitation of the copyrighted work by incorporating them into goods and commercializing them, many other possible forms of exploitation do not necessarily depend on a physical medium. In that, first examples to spring to mind is when protected material is broadcast on television, or when the work is disseminated on the internet in a way that public can have access thereto, also when a piece of musical work is played in public domain, say in a café, or when a cinematographic work is put on display in movie theatres. Evidently, in these cases the work is exploited, not by distribution of its physical counterpart, but rather by way of communication or performances. In the lack of physical attribution, these acts of exploitation are mostly regarded as services, as a result of which, they fall out of the scope of Article 34 and 36 of TFEU. Along the same lines, the archaic teaching[452] has been that copyright exhaustion applies so far only as physical counterpart of the works are concerned; the right holder however retains the exclusive right to exploit -and prevent the others from doing so- the protected work in the form of services.[453] The nature of the rights in performances and right to

[448] Id. Article 1(1) and 1(2)
[449] Case C-61/97: Foreningen af danske Videogramdistributører v. Laserdisken
[450] Id. para. 15
[451] Id.
[452] This archaic teaching is liable to be altered by the ruling in UsedSoft, as we shall mention below.
[453] Peter Mezei, *Digital first sale doctrine ante portas: Exhaustion in the online environment*, 6 J. Intell. Prop. Info. Tech. & Elec. Com. L. 23, 28 (2015)

communicate the work to the public was found to require the same treatment as rental rights in respect to exhaustion: none applies.

A multitude of sources in the Union law provided for exclusion of such rights from the scope of exhaustion.[454] The InfoSoc Directive, being the centerpiece of harmonization of copyright laws, in its Article 3, defined the scope of such rights and ascertained that any prior act of communication is not feasible to exhaust the rights. It is relevant to reproduce the full text of the article which reads as follows[455]:

> *Article 3*
>
> 1. Member States shall provide authors with the exclusive right to authorise or prohibit any communication to the public of their works, by wire or wireless means, including the making available to the public of their works in such a way that members of the public may access them from a place and at a time individually chosen by them.
>
> 2. Member States shall provide for the exclusive right to authorise or prohibit the making available to the public, by wire or wireless means, in such a way that members of the public may access them from a place and at a time individually chosen by them:
>
> (a) for performers, of fixations of their performances;
>
> (b) for phonogram producers, of their phonograms;
>
> (c) for the producers of the first fixations of films, of the original and copies of their films;
>
> (d) for broadcasting organisations, of fixations of their broadcasts, whether these broadcasts are transmitted by wire or over the air, including by cable or satellite.
>
> 3. The rights referred to in paragraphs 1 and 2 shall not be exhausted by any act of communication to the public or making available to the public as set out in this Article.

The imperative of the provision in respect to the exhaustion, more particularly to the exemption of this right from the scope of exhaustion, can rationally be traced back to *Coditel I*[456] judgement of the ECJ. In the underlying dispute, Cine-Vog acquired from the producer company the exclusive broadcast right in respect to Belgium of the film *Le Boucher*. The same right in respect to Germany was assigned to a German television whose broadcast could incidentally be picked from the territory of Belgium. Another Belgian cable television provider, Coditel, availing himself of the latter event, picked up the German broadcast and conveyed the film by cable to its subscribers in Belgium. Cine-Vog invoked its exclusive rights against

[454] See: Art. 3(3) of Directive 2001/29 on the harmonisation of certain aspects of copyright and related rights in the information society [InfoSoc Directive]; Art. 4(1) of Directive 2019/789 laying down rules on the exercise of copyright and related rights applicable to certain online transmissions of broadcasting organisations and retransmissions of television and radio programme; Recital (43) of Directive 96/9 on the legal protection of databases.

[455] Article 3 of Directive 2001/29/EC of the European Parliament and of the Council of 22 May 2001 on the harmonisation of certain aspects of copyright and related rights in the information society

[456] Case C-62/79: SA Compagnie générale pour la diffusion de la télévision, Coditel, and others v. Ciné Vog Films and others.

Coditel which in return argued that such exercise of rights infringed the freedom to provide services.

The Court of Justice having recognized the peculiarity of this type exploitation of copyrighted works, distinguished the latter from the distribution of tangible objects entailing the work. It held that films are made available to the public by performances which may be infinitely repeated; this is dissimilar to the case of books or records which are placed at the disposal of the public through the circulation of material form of the works.[457] According to the Court, this very nature enables the right holder to require fees for any showing of a film and this prerogative is a part of the essential function of copyright in this type of literary and artistic work.[458] Moreover, it concluded in regards the freedom to provide services enshrined in the Article 59 of the Treaty (now Art. 56 TFEU) that the merely because the geographical limits of assignment of the exclusive rights coincide the national frontiers does not necessarily infer that such exercise of rights constitute a means of arbitrary discrimination or disguised restriction. In fact, given the reality that televisions are organized on the basis of national legal broadcasting monopolies, any other pattern of assignment than national frontiers would be impracticable.[459]

Subsequently in *Basset v. SACEM*[460] the Court distinguished between the distribution right on the physical copy of a musical work and the right to communicate to the public of the work in that very copy. The question in the underlying dispute was whether it is permissible under free movement provisions the charging of an additional royalty (i.e. supplementary mechanical reproduction fee), by the French copyright collecting society as opposed to single royalty payable (regardless of whether public use or private use) in the Member State where the recordings were put into circulation. It was noted that under French copyright law such dual royalty was authorized insofar as the first one, by default, concerned the private use and the 'supplemental mechanical production fee' was due in relation only to public use.

The ECJ was convinced that the supplementary royalty was not charged on the basis of importation of the recordings from another Member State, but it was rather by the reason of their public use.[461] This view was supported, first, by the very fact that the latter charge applied

[457] Id. para. 12
[458] Id. para. 14
[459] Id. para. 15, 16
[460] Case C-402/85: G. Basset v. Société des auteurs, compositeurs et éditeurs de musique (SACEM)
[461] Id. para. 12

to the recordings of French origin and the imported ones equally[462]; and secondly by the basis of calculation thereof which strictly depends on the turnover of the public place where it is to be played.[463] Although the point of exhaustion is not explicitly spelled out in the judgement, the connotation is clear: the rights on performance of the work is not exhausted by the initial sale of the recordings in the Union. The right to require royalties on the basis of public performance of the work, such as in this case, thus falls within the ambit of normal exploitation of copyright and it does not amount to an arbitrary discrimination or a disguised restriction on trade between Member States.

Finally, in *Ministère public v. Tournier*[464] in a concurrent analysis of free movement of goods and the freedom of providing services, the Court reaffirmed that making the work available to the public through performances gives rise to distinct problems [as regards the further commercialization] than those arisen by the act of making a work available to the public that inseparably entails the circulation of that work in physical medium. Accordingly, it held, the requirements of (i) free movement of goods, (ii) freedom to provide services and (iii) copyright must be reconciled in a way that the copyright owners may invoke their exclusive rights in order to require the payment of royalties for music played in public by means of a sound-recording, even though the marketing of that recording cannot give rise to the charging of any royalty in the country where the music is played in public.[465] The reconciliation the Court offered clearly implies the exclusion of performance and public communication rights from the scope of exhaustion. It moreover implies that such rights are segregated from the exhaustion of distribution right. Accordingly, even though, the exhaustion of distribution right applies to the physical recordings to the effect that they are goods for the purposes of the Treaty, the copyright holder`s right to authorize the performances and communication to the public of the underlying work and right to require fee for these acts remain unaffected.

Moving back to the aforementioned provision, it is obvious that, with a subtle terminological nuance, two different concepts were introduced: 'communication' and 'making available' to the public. The Court of Justice clarified in a recent that the notion of 'making available to the public' forms part -and a subset- of the wider concept of 'communication to the public'.[466] The difference noted to be that the right of making available is a separate right

[462] Id. para. 14
[463] Id. para. 15
[464] Case C-395/87: Ministère public v. Jean-Louis Tournier
[465] Id. para. 13
[466] Case C-279/13: More Entertainment AB v. Linus Sandberg, para 24.

only for holders of neighboring rights that do not enjoy a general right of communication to the public, such as those listed in the second paragraph of the provision.[467] A great variety of specific acts are plausible to subsume under the range of activities indicated by the said provision; the latter corollary flows especially from the expression 'by wire or wireless means' and from ever expanding concept of communication *per se*.[468]

It should, also, be pointed out that a comprehensive set of case law, in addition to the above referred essential jurisprudence, came to define -and occasionally complicate- the concepts within the meaning of the public communication and performance rights. This complication may potentially be ascribed to the ample variety of forms in which communication to public can take place; in the lack of material substance, to the abstract and technically complicated nature of these forms; and partly to the eccentric construction, and the resultant interrelation, of secondary law of the Union on copyright law. Nevertheless, sticking with our purposes, it is sufficient to highlight the subtext in foregoing that the rights over performances and that of communicating of works to public to public do not come under the scope of exhaustion.

### 3. An Overview on digital 'further commercialization' and exhaustion

Over a decade ago, it was noted, in relation to the exploitation of copyright in immaterial form, that the question of a second-hand market in that regard was not in issue.[469] This observation appeared relevant by the time because the jurisprudence of the Court had distinguished between the exploitation of copyrighted material in form of circulation of physical corporeal goods on one hand and dissemination of work by immaterial means such as making it available to the public by performances. Moreover, this division was reflected in the InfoSoc Directive which stated "[c]opyright protection under this Directive includes the exclusive right to control distribution of the work incorporated in a tangible article.[470]

With the internet taken over the dominance as regards the dissemination of both commercial and non-commercial dissemination of protectable subject matter, the above

[467] P. Bernt Hugenholtz & Sam C. van Velze, *Communication to a New Public? Three Reasons Why EU Copyright Law Can Do Without a "New Public"*, 47(7) IIC, 797, 810 (2016)
[468] JUSTIN KOO, THE RIGHT OF COMMUNICATION TO THE PUBLIC IN EU COPYRIGHT LAW 53 (Bloomsbury Publishing 2019)
[469] Stothers, *supra* note 149 at 356
[470] Recital (28) of Directive 2001/29/EC of the European Parliament and of the Council of 22 May 2001 on the harmonisation of certain aspects of copyright and related rights in the information society

observation is susceptible to fall behind the time. Moreover, in digital world, online remit became the main medium of dissemination for some copy right protected works which were traditionally embodied in physical form, changing the nature of the latter gradually and for once and all from tangible to intangible (such as from books to e-books; from phonograms to digital music platforms). Inevitably, the type of online use, within the meaning of copyright prerogatives, is not always clearly identifiable. The contention arising from this haziness prevails over the issue of online exhaustion of copyright protected works *vis-à-vis* whether all acts of dissemination on the online realm should be regarded as communication, performance or rental of the work; or it is possible to recognize a digitalized concept of distribution for the purposes of exhaustion. Also, to the layman`s experience it is admittedly of a little significance under what form the digital content is put at their disposal. On the end of legal interest, however, the formal modality under which they access to digital content is of vital importance to the effect that this form is determinant on the end of exhaustion. Several dichotomies are to be regarded.[471]

First of all, a distinction is to be made between the transactions that shifts the tittle on the protected subject matter and the licensing thereof. As it is known from the context of tangibles, exhaustion is triggered by the transfer of ownership whereunder sales *a fortiori* subsumed.[472] The said transfer of ownership on the other hand is not at issue under licensing; instead the licensee is authorized to use the protected works for an agreed term. In the lack of an actual transfer of ownership in the latter case, there is no way applying exhaustion doctrine.[473] The second distinction is to be drawn between the acts entailing distribution and those entailing communication or making available to the public. As already pointed out earlier, distribution right traditionally relates to the physical copy of the protected work. The second one, according to the wording of the provision above, is done by wire or wireless means; and according to the case law, is done by performances. Adaptation of this mold to the digital exploitation, in the lack of physical medium, is particularly problematic. Helpful, however, the latter was also characterized in that provision as being accessed on demand[474]. If the concept of distribution is to be possibly perceived digitally, it is suggested that, the difference between these two acts would be whether the work is accessed on demand or a permanent digital copy

[471] For an illustration of the dichotomies see: Caterina Sganga, *A plea for digital exhaustion in EU copyright law*, 9 J. Intell. Prop. Info. Tech. & Elec. Com. L. 217, 217-222 (2018); Mezei, *supra* note 453 at 40-43
[472] See to that effect: Article 4(2) of InfoSoc Directive; C-16/03 Peak Holding, para. 29; Peek & Cloppenburg
[473] Mezei, *supra* note 453 at 40
[474] That is to say, in such a way that members of the public may access them from a place and at a time individually chosen by them.

thereof has been conveyed to the user.[475] The dichotomy of goods and services is, on the other hand, based primarily on the tangibility criterion which also lays the background to the nuance between the aforementioned distribution and communication rights. It is noted, in this regard that the goods are defined by tangibility and capacity of being subject to commercial transactions; leaving the services as a residual category that is devoid of tangibility as such.[476]

Frankly, the above referred characterizations cannot be perfectly isolated on a vertical level. Yet, equally clear, two camps seem emerge from this cluster, [i.e. (i) sale, distribution and goods on one hand; (ii) licensing, making available and services on the other hand] of which, the first one connotes premises the exhaustion and intrinsically falls relevant to exploitation of copyrighted subject on physical medium. The second camp, in turn, infers the immaterial exploitation of protected work, including that in digital realm, to which exhaustion is not a natural fit.

Yet another, equally grave, issue in that regard emanates from the ease of multiplication of the work in digital realm. Admittedly, the exhaustion of distribution right was mainly based on the premises of the goods: the owner, by selling the good, is deprived of that. In other words, subsequent distribution of a particular tangible does not involve the risk of that subject being duplicated. On the contrary the digital realm is highly potent to duplication and reproduction of the copyrighted subject matter, either deliberately by its user or incidentally as a part of functioning of the hardware or software through which the access is provided. Setting aside some exceptions provided for by the law[477], such multiplication of the protected content amounts to a new copy, thus infringing the exclusive reproduction right. Applying the fundamental premises of the distribution right to the digital realm, the erasure of the content from the access of the first user - either simultaneously with or immediately after the acquisition thereof by the new user - appears necessary for a potential digital exhaustion. It is furthermore noted that there have been, so far, no technologies available that provides an absolute control the use of protected subject matter in digital realm.[478]

However acknowledging that the matter of online exhaustion in itself is a vast area of scrutiny which should be, and was, the subject of an exclusive interest, it is nevertheless of a

[475] Sganga, *supra* note 471, at 219
[476] Id. at 220
[477] See to that effect: Article 5 of InfoSoc Directive; Article 5(1) and (2) of the Directive 2009/24 (the Software Directive)
[478] Péter Mezei, *The Doctrine of Exhaustion in Limbo-Critical Remarks on the CJEU's Tom Kabinet Ruling*, 10, Available at SSRN (2020)

great relevance to mention the most contemporary examples thereof that have been laid through *UsedSoft* -being the landmark case in the context of digital exhaustion of rights- in relation to computer software and *Tom Kabinet* case whereby the same question directed to subsequent trade of e-books.

### *UsedSoft v. Oracle* judgement

In the notorious *UsedSoft* ruling of the Court, the idea of enabling a second-hand market for computer software has been staggeringly advocated. This outcome has also brought to the forefront the question whether the same approach could be followed as regards the other digital subject matter, thus paving the way to a general digital exhaustion jurisprudence. Background to the dispute is summarized as follows: Oracle develops and markets computer software, among which there are programs for business use. The principle of operation is that the customers download, from Oracle`s website, a copy of the software which is then operated with the user right granted by a license agreement (EULA). Those licenses are offered for a minimum number of 25 users and for an unlimited period of time; also accompanied with the term that the license includes the right to store a copy of the program permanently on a server and to allow a certain number of users to access it by downloading it to the main memory of their work-station computers.[479] The business definition of UsedSoft is to market second hand software licenses, including that of Oracle, which it obtains from the first acquirers in respect either to entire user licenses or, in case the original license relate to a greater number of users than needed by the first acquirer, to parts of them.[480] Customers of UsedSoft. Having downloaded the software from Oracle`s website, use it with the second-hand licenses that they purchase from the former. Oracle brought an action against UsedSoft so as to enjoin the latter from offering its software licenses on second hand market. The referring court put the following question to the ECJ:

> 1) Is the person who can rely on exhaustion of the right to distribute a copy of a computer program a "lawful acquirer" within the meaning of Article 5(1) of the Software Directive?[481]

[479] Case C-128/11: UsedSoft GmbH v Oracle International Corp., para. 21,22,23
[480] Id. para. 24
[481] Article 5(1) of the Directive 2009/24 reads:
"In the absence of specific contractual provisions, the acts referred to in points (a) and (b) of Article 4(1) [the acts of permanent or temporary reproduction] shall not require authorisation by the rightholder where they are necessary for the use of the computer program by the lawful acquirer in accordance with its intended purpose, including for error correction."

2) Is the right to distribute a copy of a computer program exhausted in accordance with the first half-sentence of Article 4(2)[482] of the Software Directive when the acquirer has made the copy with the right holder's consent by downloading the program from the internet onto a data carrier?

3) [C]an a person who has acquired a "used" software license for generating a program copy as "lawful acquirer" under above referred provisions of the Software Directive also rely on exhaustion of the right to distribute the copy of the computer program made by the first acquirer with the right holder's consent by downloading the program from the internet onto a data carrier if the first acquirer has erased his program copy or no longer uses it?[483]

The ECJ started off with answering to the second question, having indicated that the answer would necessarily depend on whether the relationship between the right holder and the acquirer, on which basis the downloading of the copy of the software took place, entails a [first] sale.[484] It went on to delineate the latter as an agreement by which a person transfers to another person his rights of ownership in an item of tangible or intangible property belonging to him, in return for payment; as such, it is necessary to determine if the transfer of ownership of the computer program in the present case has occurred. Oracle, on its end, deduces from this definition that sales did not happen not least because the copies of the software made available for download free of charge but also because the user licenses required to use the latter were non-transferrable.[485] Such a reasoning, the Court implied, was unconvincing insofar as the downloaded copy *per se* was useless in the absence of an user license and vice versa. To that end the Court observed that the downloading of a copy and the conclusion of a user license agreement must be regarded as an indivisible whole which should also be the basis for the classification of the relationship between the acquirer and the right holder from a legal view point.[486] That classification, under the prevalent circumstances -i.e. making the downloaded copy usable to the customer permanently in return for a payment which in turn enables the

[482] Id. Article 4(2) reads:
"The first sale in the Community of a copy of a program by the rightholder or with his consent shall exhaust the distribution right within the Community of that copy…"
[483] UsedSoft, para. 34
[484] Id. para. 38
[485] Id. para. 43
[486] Id. para. 44

copyright holder to retrieve the economic value of that copy- must be 'transfer of ownership', thus constituting a first sale of the work.[487]

Question of exhaustion is thus narrowed down to that of whether distribution right relates exclusively to the tangibles incorporating the software. The Court, exhibited a surprising effort to insert a broader understanding, such as to cover immaterial marketing as well, and in doing so it availed itself of the lack of an explicit preclusion of intangibles from the scope of distribution. It is clear from the wording of InfoSoc Directive that conveyance of the protected work in an intangible form is excluded from the scope of distribution.[488] However this explicit exemption did not exist in the wording of Software Directive; nor did it suggest a distinguish between a tangible and intangible copy.[489] It is this very nuance that the Court found both material and immaterial conveyances are to be covered under the Software Directive`s exhaustion regime.[490] In defense of that view, it went on to illustrate the contrary scenario whereby it concluded that, if such a broad interpretation is to be opted out the very essence of exhaustion principle would be undermined by the right holder by simply labeling the legal relationship as a 'license'.[491]

The argument posed by Oracle and the Commission asserted that the distribution right within the meaning of the InfoSoc Directive (and WIPO Copyright Treaty which is codified by the latter) related exclusively to tangible property and the type of conveyance of the protected software at issue was 'communication to public' within the meaning of the InfoSoc Directive, thus not subjecting to exhaustion. The Court responded to this assertion on the basis of the hierarchy of norms envisaged between the two Directives. Accordingly, Software Directive occupies a *lex specialis* position in front of InfoSoc Directive that is construed as the centerpiece of European copyright legislation.[492] A corroborant to that postulate is inferred from the provision of that Directive which ascertained that it would leave intact existing Community provision in relation *inter alia* to the legal protection of computer programs.[493]

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[487] Id. paras. 45-48
[488] Recital (28) of InfoSoc Directive reads "Copyright protection under this Directive includes the exclusive right to control distribution of the work incorporated in a tangible article";
Article 4(2) of InfoSoc Directive reads "The distribution right shall not be exhausted within the Community in respect of the original or copies of the work, except where the first sale or other transfer of ownership in the Community of that *object* is made by the rightholder or with his consent." (Emphasis added)
[489] Article 4(2) of Software Directive reads: "The first sale in the Community of a copy of a program by the rightholder or with his consent shall exhaust the distribution right within the Community of that copy...."
[490] UsedSoft, para. 55
[491] Id. para. 49
[492] Id. para. 56
[493] Article 1(2) InfoSoc Directive

Therefore, regard must be paid to the provision of Software Directive in line with its specific intentions and context the European legislator expressed therein. Part of that intentions, according to the Court, was to equate tangible and intangible copies of computer programs.[494] Consequently, exhaustion occurs when the copyright holder who has authorized the downloading of that copy from the internet onto a data carrier has also conferred a right to use that copy for an unlimited period in return for payment of a fee intended to enable him to obtain a remuneration corresponding to the economic value of the copy of the work.[495]

Crucially the Court also noted that, in case of a license for multiple number of users concerned such as the case in the present case, the first acquirer is not permitted, relying on the exhaustion, to divide the license and resell only the user rights that excess his need, while keeping a part of the user rights.[496] Connotation being that resell in the sequel of exhaustion of distribution right needs to be holistic. Finally, as regards the first and third question referred, the ECJ held that the subsequent purchasers of the user license (those who are buying thereof from the initial acquirer) are deemed 'lawful acquirer' hence authorized to rely on exhaustion of the distribution right and to reproduce the works insofar as necessary for its use. Important though, the first acquirer must make his copy downloaded onto his computer unusable at the time of its resale to another party.[497] The latter proviso also underlays the reason why the multiple user rights must, in case of resale, be transferred holistically (i.e. prohibition to divide the licenses). In fact, such a division, if allowed, would mean that a part of license is not made unusable, thus failing the erasure requirement.[498]

### *Tom Kabinet* judgement

The most recent *Tom Kabinet*[499] case has been the occasion on which the permissibility of a second market for e-book was tested. The main dispute centered around the virtual second-hand e-book market operated by the Dutch publisher Tom Kabinet whereby the latter allowed its users to purchase and sell lawfully acquired e-books, under a setting what it addresses as a book club. Digital books offered under that setting were either purchased by Tom Kabinet from the original publishers of acquired from individuals who had so purchased. In the case of acquisition from individuals, Tom Kabinet required from that individual a statement

[494] UsedSoft para. 58
[495] Id. para. 72
[496] Id. para. 69
[497] Id. para. 79
[498] SEVILLE, *supra* note 122 at 32
[499] Case C-263/18: Nederlands Uitgeversverbond and Groep Algemene Uitgevers v. Tom Kabinet Internet BV

confirming that they have not kept a copy of the book in question.[500] This business model faced a copyright infringement claim brought by two Dutch publishing associations, namely NUV and GAU. The referring court, unsure as to the permissibility of digital exhaustion in the sequel of UsedSoft jurisprudence, albeit in relation to subject matter other than software, directed several questions to the Court of Justice. These included, *inter alia*, whether the distribution right within the meaning of the InfoSoc Directive includes making available by downloading, for use for an unlimited period, of e-books at a price; and, if so, whether the described act exhaust the distribution right in respect to the Union.[501]

The ECJ, reducing these down to a single question, observed that the referring court, essentially intended to seek clarification on whether the supply by Tom Kabinet is covered by the concept of 'communication to public' or by that of 'distribution'; this formulation, the Court suggested, better reflected the crux of questions referred. In the construction of its reasoning, an immense amount loyalty -which apparently was missing in the UsedSoft judgement- was exhibited by the Court to the rationale of the WCT which was transposed into Community law by the InfoSoc Directive. It, then, continued with a teleological and historical interpretation of the said Directive with a great amount of reference to the preparatory stage thereof, in conjunction with the auxiliary guidelines involved in that stage, such as explanatory memorandum of the Commission.[502] Excessive teleological and historical reasoning was, first, instantiated and deviated into a verbal analysis by means of references to the recitals of the InfoSoc Directive which emphasized and laid the basis of tangible and intangible difference[503], then with a reference to the wording of the Directive which employed the term 'object'.[504] The conclusion intended was clearly a broad understanding of the concept of 'communication to public', forming a residual category in a way to cover all immaterial supply of the protected subject matter; and distribution must be regarded, in line with the archaic understanding, to relate solely to tangibles.

As regards the referring court`s doubt whether the same outcome as emerged in UsedSoft applies to the present case -the doubt which brought the case at hand into being-, the ECJ almost sarcastically stated 'an e-book is not a computer program'[505] Even in the event that

[500] Id. para. 24
[501] Id. para. 30
[502] See: Id. paras. 41-46
[503] Recital (28) of the InfoSoc Directive uses the term "tangible article"
[504] Id. Article 4(2)
[505] Tom Kabinet, para. 54

the e-book comprises a software, the latter character would be auxiliary to the works contained in that book, therefore InfoSoc Directive would still be the applicable legal framework.[506] That is to say any hesitation inspired by the outcome of UsedSoft judgement was irrelevant since the latter was dealt with under the specific law designed for that specific intellectual property, shortly conceptualized as a *lex specialis*. Along the same lines, the Court concluded, as it also did in UsedSoft, that assimilation of tangible and intangible copies was unique to the Software Directive, however that is not what the European legislator desired in respect to InfoSoc Directive to which e-books are subject.

The referring court was also not convinced with the qualification of the supply by Tom Kabinet as 'communication to public' to the effect that, according to the previous case law, the latter act must comply, cumulatively, with the requirements that (i) the existence of an act of communication of the work; (ii) that communication being made to public; moreover the public for that purposes must be a large number of people.[507] The Court of Justice, however, took the view that the both conditions were fulfilled in the present case. Particularly in recognition of the existence of a 'public' large enough to qualify with that requirement, the ECJ stated that any interested person can become a member of the reading club; furthermore in the absence of any technical measure to ensure (i) a one-copy-one-user modality; (ii) the erasure of the copy by the user who is disposing the copy of to another user, the number of persons who may have access, at the same time or in succession, to the same work via that platform is substantial, hence constituting the 'public' element.[508]

Consequently, the Court concluded the supply of the work, which is an e-book, to the public for permanent use is covered by the concept of 'communication to the public' within the meaning of InfoSoc Directive, under Article 3(1) thereof, to which exhaustion principle does not apply.[509]

### 4. The Aftermath of the Judgements and Remarks

The judgements we covered above, albeit relate only two specific types of copyright protected digital subject matter, this limited examination may nevertheless be somewhat sufficient to grasp the overall scenery in the Union law in relation to digital exhaustion of

[506] Id. para. 59
[507] Case C-610/15: Stichting Brein v. Ziggo BV, paras. 24,27
[508] Tom Kabinet, para. 69
[509] Id. para. 72

copyright. The classification of these two types of digital subject matter, in that their feasibility for the concept of distribution, and by extension, for the application of exhaustion doctrine, was made on the basis of the statute to which each one of them is subject. One thing that is inarguably apparent from the above judgements is that the general scenery is represented by the InfoSoc Directive whose subject matter -when it is immaterially disseminated- does not fall within the scope of 'distribution' but instead amounts to 'communication'; hence no exhaustion applies. Within that general scenery, however, a contained area of contrast is drawn by the Court in respect to computer software, albeit rather boldly.

It needs to be noted that the outcome of the UsedSoft case does not by any means open up the doors to a digital exhaustion model that is applicable to copyright protected works within the meaning of the InfoSoc Directive. Quite the contrary, this outcome, from a formal view point, was based on (i) the absence of any prohibitory wording regarding the form of distribution, which was construed by the Court as to cover (and permit) both material and immaterial distribution; (ii) the *lex specialis* nature of the Software Directive, which in turn, renders the InfoSoc Directive *lex generalis.* Interrelation of the norms as such, in fact, was reflected in the latter Directive by appointing a residual scope thereto; and accordingly, it would leave intact and shall not affect the existing provisions in the Union law in relation *inter alia* to the legal protection of computer software.[510] With that the Software Directive seems to have placed computer programs out of the reach not only of the InfoSoc Directive, but also that of the archaic classification 'literary work'[511] traditionally ascribed to computer programs.

Of particular significance, the Court approaching the matter from an economic perspective, in UsedSoft, devised that the online transmission method is the functional equivalent of the supply of a material medium.[512] On the basis of this approximation alone, one would certainly be tempted to adhibit the 'functional equivalence' theory to the other digital material that benefits from copyright protection.[513] There is in fact no [self]evident reason why musical work downloaded should not be the 'functional' equivalent of recordings or why should e-books not be the functional equivalent of a hard copy? However this kind of interpretation has been denied by the Court by the Court in the subsequent Tom Kabinet case,

[510] Article 1(2) of the Software Directive
[511] See, to that effect: Article 2 of Berne Convention for the Protection of Literary and Artistic Works; and Article 4 of WIPO Copyright Treaty.
[512] UsedSoft, para. 61.
[513] Before the delivery of Tom Kabinet decision, this possibility was rightly credited. To that effect see: Reto M. Hilty et al., *Software agreements: stocktaking and outlook–lessons from the UsedSoft v. Oracle case from a comparative law perspective*, 44(3) IIC 263, 284 (2013)

there hardly appears to be a convincing explanation either on what 'economic equivalence' should entail or on why in that case e-book is not connote that kind of equivalence to hard copies. The only, subtle, hint appears the physical explanation that e-books do not age with use and they are perfect substitute for the physical copies, hence threatening the market for physical copies. This postulate seems to suggest that what the Court might have actually intended with 'functional equivalence' is some sort of substitute that does not threaten the other forms of dissemination of the same work. One way or another, there seems to exist a terminological dilemma, resulting in an unconvincing line of argument which seemingly stands prejudicial against and immaterial distribution within the realm of InfoSoc Directive. Furthermore, with the digital books taking over the dominance in the entire market, the argument of 'rivalry' is extra unconvincing. The wording of 'functional equivalence' *per se* in our opinion, at very least, misleading. We equally believe that such wording perfectly justifies a potential extension of the exhaustion in respect to other types of works digitally disseminated.[514]

While summarizing Tom Kabinet case above, we had already stressed that the Court exhibited a remarkably consistent willingness to adhere to the obligations of the Union emanating from international law. Accordingly, it emphasized that the Union legislation must be interpreted in a manner that is consistent with international law, in particular where its provisions are intended specifically to give effect to an international agreement concluded by the European Union[515]; which is exactly the case for the InfoSoc Directive insofar as in transposed WCT into the Union law. As a result, Articles 3(1) and 4(1) of the Directive concerning, respectively, distribution right and right to communicate to the public must be interpreted in line with their counterpart in the WCT, namely Article 6 and 8 of the latter. Particularly, the Agreed Statement to Article 6 WCT, which stated that *"the expressions "copies" and "original and copies," being subject to the right of distribution [...] under the said Article, refer exclusively to fixed copies that can be put into circulation as tangible objects."*[516] was the very basis of tangible and intangible copy differentiation within the meaning of InfoSoc Directive, and the latter therefore should be interpreted in accordance with the former. And it was on this basis that the Court, in Tom Kabinet, arrived at the conclusion

[514] In the same direction see: Sven Schonhofen, *Usedsoft and Its Aftermath: The Resale of Digital Content in the European Union* 16 Wake Forest J. Bus. & Intell. Prop. L. 290 (2015)
[515] Tom Kabinet, para. 38
[516] Agreed statement concerning Articles 6 and 7 of the WIPO Copyright Treaty adopted by the Diplomatic Conference on December 20, 1996

that the distribution right -hence exhaustion- did not apply at that case in respect to e-book, that are being digital copies in nature.

Although there is nothing particularly wrong in that logic and accompanying interpretation (in fact quite the contrary it seems consistent with the obligations under international law and with the intendment of that law), what appears problematic is almost a complete omittance of a similar interpretation on the occasion of UsedSoft in relation to the Software Directive. Albeit it is true that the Software Directive is not *per se* intended to codify the WCT, the European legislator, when crafting that Directive, is nevertheless bound take into consideration the wording and intendment of the WCT. That consideration must particularly be compelled by two reasons: (i) firstly the WCT comprises an international law obligation with which the Union legislation is required to comply; (ii) secondly the WCT in itself did not differentiate between the computer programs and other protectable subject matter *vis-à-vis* distribution right and exhaustion. To that end, the European legislator is, from a formal view point, bound to comply with that Agreed Statement even when it is passing a directive which it regards as *lex specialis*. In the light of the foregoing, we agree with Mezei who rightly pointed out that any argument that excludes the application of the Agreed Statement to Article 6 of the WCT to the Software Directive is in fact misleading.[517]

Factually, however, it is clear from the wording of the Software Directive, the Agreed Statement (6 and 7) of the WCT was effectively disregarded when the European legislator drafted the said Directive. Although it is the subject of another discussion whether this omittance was a mistake by the European legislator or it was a result of the intention to create an inroad such as to apply the exhaustion principle in respect to computer programs,[518] the fact remains that there exists a discrepancy between the provisions regarding the form of distribution of the Software Directive on one hand, and that of the InfoSoc Directive and the WCT on the other hand. With that being the case, at very least, the judicial interpretation would be expected to patch up this discrepancy -or unclarity- by interpreting the Software Directive in line with the intendment of the WCT, in particular, with the said Agreed Statement thereof for aforesaid reasons. The necessity of such interpretation flows also from the settled principle of the Union`s legal order that requires coherent and unitary interpretation of terminology and concepts contained in the Union legislation*, a fortiori* including those within the same legal ambit, i.e. copyright. This postulate was also brought up by the Commission and Oracle in

[517] Mezei, *supra* note 478, at 12
[518] Id.

UsedSoft. Strikingly, however, the Court, refused doing so, by simply relying, again. on the envisaged *lex specialis* status which it used to fully isolate the Software Directive from the InfoSoc Directive and the WCT. It is rightly noted, as we also agree, that the resulting asymmetry as regards the online exhaustion in the aftermath of the two judgements is not a mistake caused by the Tom Kabinet decision, but it was rather the aforesaid doctrinal fallacies in the UsedSoft judgment that ultimately led the Court to a peculiar outcome.[519]

On a comparative reading, one could observe that the Court in UsedSoft exhibited an extraordinary willingness to apply digital exhaustion in the context of computer software; so much so that, it afforded the risk of wrecking down several significant doctrinal considerations for doing so. Although it is hard to strictly pinpoint the motivation behind that. On the contrary, the most recent judgement of the Court gives the impression that there appeared no desire (at least none as vigorous as was in UsedSoft) on the end of the ECJ to convert the sequel of the UsedSoft into a generally applicable digital exhaustion mold. However, that unwillingness might just as well be compelled by the explicit prohibitory language of the InfoSoc Directive, which almost left no room to circumvent the tangibility requirement in order for the act distribution to take place hence exhausting the rights. Furthermore, as we discussed above, there is a strong case to justify the postulate that the Software Directive, on the point of distribution right, should have likewise been interpreted within the borderlines of that prohibitory language and intendment. Outstandingly rapid digital growth and the persistence of - what we can call - 'digital ownership' therein might, from the end of the users, not be satisfied with the exclusion of digital exhaustion. Such a practical issue is certainly not trivial, however with the legislative and doctrinal material at hand for the time being, the judgement in Tom Kabinet -even though it may not necessarily come to the aid of that practical issue- seems formally accurate.

Still, however, from an extremely optimistic view point one might be tempted to read the lines between the criterion the Court laid in the para. 69 of Tom Kabinet judgement where the Court based the fulfillment of 'public' criteria on the fact that there is no apparent technical possibility in the present case to ensure (i) one-copy-one-use modality and (ii) the erasure of the copy upon a resale. This might, albeit with a devastating optimism as we stated, mean that if such technical means -such as a fool-proof forward-and-delete technology- are somehow provided, the possibility of excluding the qualification as 'communication to public' may

[519] Ansgar Kaiser, *Exhaustion, Distribution and Communication to the Public–The CJEU's Decision C-263/18–Tom Kabinet on E-Books and Beyond*, 69(5) GRUR International 489,495 (2020)

resurface. It is, still, necessary to admit, even in that extreme scenario, the mere exclusion of the latter classification does not necessarily mean that the supply of e-books will be regarded as distribution, especially in the existence of prohibitory language of InfoSoc Directive. On the other hand, if there actually was a desire on the end of European legislature to apply the exhaustion modality in respect to, say, e-books, the only alternative seems to be to create a *lex specialis* just like in the case of software, and ditch the tangibility presupposition in the context of distribution right. From a rational view point, however, for the time being the jurisprudence of the ECJ made it remarkably clear that the exhaustion principle is not to expand towards the other types of digital material.

# CHAPTER 6

# TRADEMARK SPECIFIC CONCERNS: REPACKAGING, REBRANDING and DEBRANDING

## 1. The Essence of Question

The default presumption in application of exhaustion doctrine envisages the goods being further commercialized in the original form and integrity in which they were initially put on the market by the right holder. Undoubtedly, exhaustion principle allows the further commercialization of the goods without being impeded by the intellectual property right holder. The reality, however, more often than not tends to differ from this presumption. As far as further commercialization within the Union is concerned, interference with the original form of the goods may be required by the legal mandates of the importing Member State. Parallel importers, in such cases, may find themselves in a position where they have to interfere with the original form or integrity of the goods in order solely to be able to resell them in the target Member State, even if they do not have any commercial benefit from doing such alterations. The prime example to these could be when the regulation of the importing Member State, for ensuring the consumer safety or public health, requires instructions or other informatory notes be attached to the product. Logically, for those attachments to objectively fulfill their function, they necessarily be in the language of the importing Member State. Albeit far fetchingly, but again rooted in the linguistic differences, the phrases originally attached to the goods either in the form of trademark or otherwise phrases may contradict public morality and the like in the importing Member State.

In addition to the general measures aimed at ensuring the consumer information, and in particularly respect to pharmaceutical products, rigid governmental surveillances might be imposed as to the size of the packaging, amount of pharmaceutical contained in each package and the like. In fact, reimbursement schemes for medical expenses often take the latter quantities as the basis; incompliance of the imported pharmaceuticals with the relevant quantity requirement could result in their exclusion from the scope of reimbursement.[520] The same governmental health measures may also be reflected as legally imposed price ceilings, motivated by the public policy concerns as to facilitating the access to medicine; meanwhile

[520] To that effect see: Case C-238/82: Duphar BV and others v The Netherlands State

no such measure exists in the other Member State. Price differentials resultant from the latter asymmetry, inherently, attracts the interest of parallel traders who desires exploiting the price differentials by purchasing the pharmaceuticals from the Member States where the prices are suppressed by governmental health measures and selling them in another Member States where higher level of prices apply. In addition to the potentially high profit margins, another enticement of parallel trading of pharmaceutical is the ease of transport,[521] which naturally enables the traders a great profit per transaction. Not surprisingly, as we have also empirically observed over the case law above, pharmaceuticals have been traditionally at the center of parallel import activities and, by extension, that of free movement vs. intellectual property clash.[522] Should such legal obligations exist, parallel traders are compelled to make alterations on the presentation of the goods in order to make them 'legally' suitable for the target market.

Secondly, even if there is no legal mandate that requires alterations in the presentation of the goods, parallel traders may find benefit in adjusting the goods to the particular market conditions and customer profile in the importing Member State. In these cases, there exists a desirable benefit for the right holder in interfering with the presentation of the goods in a way to blend them in with the similar goods that already exists in the market of importing state. Indeed, the possibility of approximating the presentation of imported products to that of local ones provides advantage to parallel importers to the effect that the local consumers may habitually approach the imported goods, say the goods with foreign language inscriptions on them, with a remarkable suspicion as regards *inter alia* to their origin and quality. Trademark holders, in practice, tend to exploit this particular consumer reaction so as to isolate pharmaceutical markets of Member States, by affixing different trademark to similar medicinal products in different Member States. However in this case, in the light of the exhaustion principle, there is no reason why parallel traders cannot sell the imported goods in that Member State where the same pharmaceutical is marked differently, the said consumer reaction (or the suspicion as to the origin of the goods due to different marks) is very likely to undermine the commercial performance of the imported goods. Clearly in that case, parallel importers have benefit in assimilating the presentation of the imported goods to that of domestic ones. It can be said that the alterations to the products, on this occasion, are driven by commercial concerns.

[521] SEVILLE, *supra* note 122 at 473

[522] Pharmaceuticals have been at issue on the basis of trademarks as well as trademarks. See, for instance: C-24/67: Parke, Davis v. Probel; C-187/80: Merck v. Stephar ; C-15/74: Centrafarm v. Sterling Drug; C-16/74: Centrafarm v. Winthrop

These interferences, be that legally compelled or driven by commercial concerns, typically affect the external aspects and presentation of the goods, while leaving the substance of the goods unaffected. The acts of interference, however, might potentially take various forms. Parallel importers may resort to replacing the packaging of the imported article with new ones that are similar to the packaging used in the importing Member State, thus assimilating their external aspects. In that case the act typically entails repackaging. However, repackaging may not always be limited to assimilation; with or without approximating the visuals, it may also be done for increasing or decreasing the quantity included in each package.[523] Moreover, replacement of the original packaging with a plain one, in a way to remove the original trademark; or replacement thereof with a new one which bears (in addition to the original manufacturer`s trademark) the parallel importer`s own mark also implies repackaging. In specific terms, the former may be addressed as de-branding and the latter connotes co-branding.[524] On the other hand, the original packaging might be combined with additional leaflets embodying relevant instruction and other notes in the language of the importing country; or the latter might be attached to the original packaging in form of labels.

Apparent from the nature of these particular acts of alteration, they are mostly likely to come to clash with the trademark rights in respect to the signs and packaging that were originally borne by those goods. The question thus presents itself: whether the trademark holder is allowed, on the basis of the alterations that have been done to his products in the course of further commercialization, to invoke his trademark rights against the parallel importer. This question *per se* presents perhaps one of the most significant encounters of the interest of free movement and intellectual property protection. As we have highlighted above, the principle of exhaustion, after the first consensual marketing, conclusively enjoins the trademark holder from opposing the further commercialization of the goods within the Union in their original form. If, however, the right holder is permitted to invoke his rights on the basis of such alterations to product, this might allow an inroad to market segregation, especially in those cases where such alterations are legally mandated prerequisites for marketing in the importing Member State.[525]

In answering to this question, instead of a categorical approach to each type of interference, the Court of Justice made available a sizable set of case law through which it

[523] STOTHERS, *supra* note 101 at 74
[524] Id. 75
[525] Id. 75

addressed different situations with a view to striking a balance between free movement principle and the protection of industrial and commercial property. Important to remember, this issue dates back to before there was any harmonization measure across the Community on trademarks. Initially, therefore, the only material to work on was free movement provisions of the Treaty.

## 2. Pre-Harmonization Jurisprudence

### *Hoffman-La Roche v. Centrafarm*

The Court of Justice, for the first time, found itself in a position to rule on the legitimacy of repackaging in *Hoffman-La Roche*.[526] In the main dispute, Centrafarm a parallel trader and manufacturer specializing in pharmaceuticals, imported from the UK into Germany, psychopharmacological drugs called "Valium" which were originally marketed in both of those states under the trademark of the original manufacturer Hoffman-La Roche. Obviously, prices charged by the that manufacturer were significantly higher in Germany than those in the UK; it was this price differential that motivated the parallel trader. Valium was made available in the UK, where Centrafarm acquired them, in packages containing maximum 500 tablets. However, in the course of parallel import, Centrafarm also made an alteration to the quantity of tablets included in each package by repackaging them into batches of 1000 tablets and it subsequently affixed the original manufacturer`s trademark on that new packages, having also inserted German translation of the original prospectus and disclosed its own business information as the marketer of the products.

The Court began with highlighting the essential function of trademarks which is to guarantee the identity of the origin of the product to the consumers and end-users. This guarantee, according to the Court, also conveys to the consumer and ultimate users that the goods bearing the mark have not faced, at a previous stage of marketing, to interference by a third person, without the authorization of the proprietor of the trade-mark, such as to affect the original condition of the product.[527] Therefore, from a formal viewpoint, the holder of the mark is entitled to prevent the importer, who repackaged the products, from affixing the trademark to the new packaging; such exercise of trademark normally falls within the specific subject

[526] Case C-102/77: Hoffman-La Roche v. Centrafarm
[527] Id. para. 7

matter of the right, thus availing of the protection afforded by the Treaty, in its article 36 (now Article 36 TFEU) to industrial and commercial property .[528]

Crucially, this exercise is, nevertheless, subject to the express proviso in the same article that it should not constitute a disguised restriction on trade between the Member States. In that regard the Court laid down the conditions, in the presence of which, the exercise of the rights against repackaged goods is construed as disguised restriction to intra-EU trade. Along the same lines, should these conditions exist, the right holder will not be able to rely on trademark so as to prevent marketing of the repackaged products. These conditions, also known as Hoffman-La Roche conditions,[529] are where:

— It is established that such exercise will contribute to the artificial partitioning of the markets between the Member States;
— It is exhibited that the repackaging cannot adversely affect the original condition of the products;
— The parallel trader has given a prior notice to the right holder on the marketing of repackaged products;
— It is stated on the new packaging by whom the product has been repackaged.[530]

***Centrafarm v. American Home Products***

The Court of Justice in a subsequent judgement[531] set about clarifying the permissibility of re-branding by a parallel trader. In the main dispute, American Home Products held the trademarks "Seresta" in the Benelux Countries and "Serenid D in the United Kingdom under which marks it marketed tranquilizers in the respective countries. Seresta and Seranid D tablets were, in essence, similar products in respect to their active ingredients and therapeutic effect; main difference on the end of the consumer was the flavor each tablet is enriched with. Centrafarm, the parallel trader, purchased Serenid D tablets in the United Kingdom and, having inserted them in a new packaging which replaced the latter mark with "Seresta" (in order to assimilate the imported products to those in the target market), subsequently marketed them in the Netherlands. On the query whether the right holder in the importing state could oppose to the importation of the goods on the grounds of unauthorized affixing of the mark to the

[528] Id. para. 8
[529] SEVILLE, *supra* note 122, at 475
[530] Hoffman-La Roche v. Centrafarm, para. 14
[531] Case C-3/78: Centrafarm BV v. American Home Products Corporation

imported products, the Court of Justice again drew upon two-step test flowing from Article 36 of the Treaty (now Art. 36 TFEU). Accordingly, the guarantee of origin implies that only the right holder can ascribe an identity to the product by affixing the mark; by the same token, the said guarantee of origin would be jeopardized if someone else was permitted to affix the mark to the product, even if the product may be original.[532] Therefore, the right to prohibit an unauthorized affixing of the mark to the product, having fallen within the specific subject matter of trademark rights, is justified under that article of the Treaty, even if the original product to which the mark is affixed was previously marketed in another Member State.[533] Secondly however, this *prima facie* justified exercise is required to be tested on the point whether it constitutes an arbitrary discrimination. To that end the Court emphasized that, albeit it is formally lawful for the manufacturer to use different marks for the same product in different Member States, if such a practice is driven by the aim of artificially partitioning the national markets, it will constitute a disguised restriction to the intra-EU trade; hence trademark rights cannot be relied on.[534] It is, however, for the national court to assess whether the use of different trademarks is motivated by the goal of market partitioning.[535]

***Pfizer v. Eurim-Pharm***

In a follow up judgement[536], in relation to the repacking of medicaments contained in blister strips into folding boxes, the ECJ held that the right holder cannot rely on his trademark to exclude the importation of repackaged pharmaceuticals where "the importer, in re-packaging the product, confined himself to replacing the external wrapping without touching the internal packaging and made the trade mark affixed by the manufacturer to the internal packaging visible through the new external wrapping at the same time clearly indicating on the external wrapping that the product was manufactured by the subsidiary of the proprietor and re-packaged by the importer"[537]; without, however, prejudice to the conditions established in Hoffman-La Roche.

[532] Id. para. 13, 14
[533] Id. para. 17, 18
[534] Id. para. 20-22
[535] Id. para. 23
[536] Case C-1/81: Pfizer Inc. v Eurim-Pharm GmbH
[537] Id. para. 13

### 3. Adoption of the First Trade Mark Directive

These early cases on repackaging issue had approach the matter on the basis of the provisions of the Treaty alone and gradually develop a set of jurisprudence therein.[538] It was only after those cases were decided that the adoption of the first harmonization measures in the field of trademarks took place. This particular issue was, however, not directly addressed in the Trade Mark Directive; neither a specific right to oppose repackaging was formally conferred on trademark holders, nor the conditions developed in the early case law *(Hoffman-La Roche)* were in any way codified.

However, the provision of the Directive on exhaustion of trademark rights, whereby that judicially developed doctrine is given a normative form,[539] has also laid out a derogatory provision to the exhaustion principle, which *a fortiori* pertains to repackaging. Accordingly, [exhaustion principle] shall not apply where there exist *legitimate reasons* for the proprietor to oppose further commercialization of the goods, especially where *the condition of the goods is changed or impaired after they have been put on the market*.[540]

#### *Bristol-Myers Squibb (BMS)*

In *Bristol-Myers Squibb*[541] the Court clarified, with the introduction of the aforesaid provision, neither the Treaty provisions nor the jurisprudence developed thereunder ceased to be the relevant basis in dealing with the legitimacy of repackaging. Quite the contrary, provisions of the Directive -and the national provision implementing the latter- and Article 36 of the Treaty (now Art. 36 TFEU) must be collectively taken into the account.[542]

The judgement in *Bristol-Myers Squibb,* insofar as it collectively regarded three individual cases referred to the ECJ, offered a generous array of repackaging scenarios, hence a remarkable opportunity to shed further light onto this particular issue. The parallel importer carried out various natures of repackaging which included *inter alia* changing their external packaging and reaffixing the mark, adjustment in the quantity of the batches, insertion of additional products into the packaging and the like. The conditions established earlier have

[538] SEVILLE, *supra* note 122, at 475
[539] Article 7(1) of Directive 89/104 [Now Article 15(1) of the Directive 2015/2436], formulating the exhaustion principle, read: "The trade mark shall not entitle the proprietor to prohibit its use in relation to goods which have been put on the market in the Community under that trade mark by the proprietor or with his consent."
[540] Id. Article 7(2) [Now Article 15(2) of the Directive 2015/2436]. Emphasis added.
[541] Case C-427/93: Bristol-Myers Squibb and Others v Paranova
[542] Id. para. 28

been taken couple of steps further as the Court set about clarifying these in details, which were to become notorious BMS Conditions.

Accordingly, the holder of the trademark could oppose to further commercialization of a pharmaceutical product where the importer has repackaged the product and reaffixed the trade mark unless:

— The reliance on the trademark as such would contribute to an artificial partitioning of the markets between the Member States. It would particularly amount to such contribution where the right holder has put identical products on the market in several Member States in various forms of packaging, and *the repackaging by the importer is necessary* in order to market the product in the Member State of importation.[543] Repackaging, in particular re-boxing, could be opposed to when marketability of the imported products could be achieved by less radical alterations, such as relabeling or insertion of additional instructions and notes.[544]
— It is exhibited that the manner in which the importer repackaged the products *cannot affect the original condition* thereof. Such a risk, the Court suggested, is not present as regards mere removal of the content from the original external packaging in order for them to be placed in a new one; or when new user instructions or information or an extra article inserted in the packaging however subject to the verification of the national court that inaccuracy in those instructions are not to indirectly affect the condition of the actual product.[545]
— *The new packaging clearly states (i) the undertaking which repackaged the product and (ii) the manufacturer*. The Court also noted that "clearly" means being perceivable by a person with normal eyesight, exercising a normal degree of attentiveness.[546]
— The presentation of the *new packaging is such as to be liable to damage the reputation of the mark*. Importantly, the latter criterion was introduced in addition to the those established in *Hoffman La-Roche*. The Court also exemplified the packaging such as to damage the reputation with those cases where the new packaging is defective, of poor quality or untidy.[547]

[543] Id. para. 56
[544] Id. para. 55
[545] Id. para. 61, 64, 65
[546] Id. para. 71
[547] Id. para. 76

— The *importer gives a prior notice to the holder of trademark* as regards the marketing of repackaged product. In addition, the Court ascertained that, should the holder of the mark demand, *the importer must supply the latter with a specimen of the repackaged product.*[548]

***The Aftermath of BMS***

The judgement in *Bristol-Myers Squibb* pinned down the list of fundamental prerequisites for the permissibility of repackaging. Setting the afore mentioned details aside, for the repackaged products to benefit from free movement the following conditions are to be met cumulatively:

**I.** Necessity for repackaging
**II.** Effect on the condition of the goods
**III.** Indication of the repackaging undertaking and the manufacturer
**IV.** Presentation that is not liable to damage the reputation of the mark
**V.** Prior Notice

These five conditions, set out in the sequel of the aforesaid judgement, constitute the base material, and in a way serve as a checklist, in determining the permissibility of repackaging. Numerous questions that were referred to the ECJ, however, helped deepening the details under each imperative as we shall discuss under corresponding numbers below.

**I.** As regards the first condition, the Court disclosed further clarification in *Upjohn v. Paranova*[549]*,* where it established that the necessity for repackaging must be objective. Accordingly, objective necessity, whose assessment falls to the national court in consideration of the specific circumstances of each case, is considered to exist if, without repackaging, the effective access to the markets of the importing Member State would have been hindered.[550] On the contrary, the element of objectivity is not fulfilled when the repackaging is solely attributable to the importer`s attempt to secure a commercial advantage. [551] This view was reiterated in *Boehringer I*[552]*;* in addition, the Court also suggested that -albeit the existence of a consumer resistance towards relabeled product do not always undermine effective market access- when this resistance is significantly strong, it might be regarded as a hinderance to

[548] Id. para. 78
[549] Case C-379/97: Upjohn v. Paranova
[550] Id. para. 43
[551] Id. para. 44
[552] Case C-143/00 - Boehringer Ingelheim and Others (*Boehringer I)*

effective market access.[553] This follows that, the national courts are required to take into account the magnitude of the consumer resistance in the importing state in order to determine whether repackaging is necessary or less interventionist way of alteration would suffice.[554] However once the objective necessity of repackaging is established, the importer is, in principle, under no obligation to proceed with a minimal alteration to the original packaging. That is to say, objective necessity is directed at the very act of repackaging and not at the manner and style of repackaging.[555] Frankly, however, the fourth BMS Condition (i.e. presentation in a way to not damage the reputation of the mark) is to be weighed against the importer`s choice of presentation and determine the limits thereof.[556]

**II.** It was made clear from the sequential rulings of the Court from *Hoffman-La Roche* all the way to *Bristol-Myers Squibb* that neither relabeling nor the change of the external packaging - without interfering with the actual substance- cannot affect the condition of the product. Such adverse effect is not created merely by removal of blister packs, flasks, phials, ampoules or inhalers from their original external packaging and their replacement in new external packaging, or by fixing of self-stick labels on the inner packaging of the product, the addition to the packaging of new user instructions or information and the like.[557] However, an indirect effect on the original condition of the product persists when the added instructions or information on composition, effect, use or storage of the product are inaccurate or when these are omitted at all.[558]

**III.** It was already established in *Bristol-Myers Squibb* that the indication pertaining to the repackaging undertaking must be printed in such a way as to be understood by a person with normal eyesight, exercising a normal degree of attentiveness. It was, however, not necessary to enunciate that repackaging was carried out without the authorization of the actual manufacturer.[559] Furthermore, if the parallel importer inserted in the packaging another article that does not necessarily originate from the trademark holder, the origin of that extra article must be indicated in a way to dissociate it from the holder of the mark.[560] More recently, the

[553] Id. para. 51, 52
[554] STOTHERS, *supra* note 101, at 91; See for the requirement of minimal intervention: Bristol-Myers Squibb v. Paranova, para. 55
[555] Case C-348/04: Boehringer Ingelheim and Others (*Boehringer II*), para. 39;
[556] Case C-276/05: The Wellcome Foundation Ltd v. Paranova Pharmazeutika Handels GmbH, para. 30
[557] Bristol-Myers Squibb, para.79
[558] Id. para. 65
[559] Id. para. 72
[560] Id. para. 73

Court emphasized that the repackager which is to be indicated on the product is not necessarily the one that has carried out physical act of repackaging; it is permissible to indicate the importer as such, on whose instructions the repackaging was carried out.[561]

**IV.** Defective, poor quality or untidy packaging by the importer would be liable to damage the reputation of the mark, the Court had held.[562] If repackaging was carried out in such manner, it would be liable to fail complying with the fourth BMS Condition. The subsequent case law made it clear that the aforementioned cases do not delineate an exhaustive list but they were only exemplary. [563] This follows that other manner of inappropriate presentation of the product could fall foul of this requirement. However, in assessing whether it is the case, the regard must also be had to the manner in which the product is offered to the patents; accordingly, when they are offered to the patients through hospitals and medical professionals, presentation is of little importance, when, however, they are sold to consumers through pharmacies, presentation is of a greater importance.[564]

**V.** Further details to the 'prior notice' was comprehended by the Court in *Boehringer I* where the referring court had taken the view that excluding the circulation of repackaged products merely due to lack of prior notice was disproportionate, especially when repackaging was not liable to encroach on the specific subject matter of trademarks.[565] The ECJ, in turn, stood firm on the necessity of prior notice. Accordingly, the parallel importer must, in any event, fulfil the requirement of prior notice so as to be entitled to repackage the product; the contrary would entitle the trademark holder to oppose the marketing of repackaged products.[566] Furthermore, the notice must be given by the parallel trader itself; in the failure of the latter, the condition is not fulfilled, even if the right holder is incidentally aware of that marketing by having been informed by the others.[567] From a teleological stand point, the Court also emphasized that not only a notice but rather a 'prior' notice was sought. This was evident from the purpose of notice which is to secure a reasonable time for the holder of the mark to react to the intended repackaging.[568] Albeit the exact timeframe for the notice had not previously been under

[561] Case C-400/09 - Orifarm and Others, para. 36
[562] Bristol-Myers Squibb, para. 76
[563] Boehringer I, para. 44
[564] Bristol-Myers Squibb, para. 77
[565] SEVILLE, *supra* note 122 at 480
[566] Boehringer I, para. 63
[567] Id. para. 64
[568] Id. para. 66

consideration, the Court found a period of 15 working days could likely be sufficient. Noteworthy however, this timeframe was purely indicative.[569]

***General Considerations***

The clarification brough about by the subsequent case law is not limited to the details of each individual condition. Following outcomes are extremely important to highlight.

*Repackaging as a broader term:* On the account of application of BMS Conditions, the Court made it clear that there is no difference between repackaging, i.e. the change in the external packaging (re-boxing) and re-bundling the content, and relabeling; in both cases BMS Conditions equally apply.[570] In fact, the Court pointed out that relabeling has been envisaged to be subsumed under the general concept of repackaging.[571]

*General assumption of infringement*: Quite crucially, it was emphasized that, regardless of whether it was a repackaging or a relabeling, the very act of the interference with the pharmaceutical products is prejudicial to the specific subject-matter of the mark and it is not necessary in that context to assess the actual effects of the activity performed by the parallel importer.[572] It is therefore the default presumption that the holder of the mark can oppose to the marketing of repackaged products. Similarly, the very act of repackaging constitutes, regardless of its type, legitimate reason to oppose further commercialization, within the meaning of the Directive,[573] thus derogating from the application of exhaustion principle. Derogation from the latter imperative is possible insofar only as the five conditions are cumulatively met.

*Recourse to the general legal basis in the context of re-branding*: From a technical perspective, peculiarity arises on those occasions where the repackaging also involves re-branding of the products, i.e. when the parallel importer replaces the original mark with the one that is used by the trademark holder in respect to the same product the importing state. The said peculiarity is rooted in the wording of Article 15(1) of the Directive [formerly Article 7(2)] which naturally admitted the trademark exhaustion 'in relation [only] to goods which have been put on the market in the Union under *that trade mark*'.[574]

[569] Id. para. 67
[570] Boehringer II, para. 31
[571] Id. 28
[572] Id. para 29, 30
[573] Article 15(2) of Directive 2015/2436. [formerly Article 7(2) of Directive 89/104]
[574] Id. Emphasis added

*Burden of proof:* In *Boehringer II,* a compact prescription has been drawn as regards the burden of proof: once the existence of repackaging is established it falls to the parallel importers to prove that the BMS Conditions are satisfied.[575] Rationally, certain lenience was afforded, by the Court, to the importer in relation to proving that the original condition of the product is unaffected. In an analytic sense, positive determination of an actual existence of such an effect to the original condition of the product might, in fact, be quite challenging. In recognition of this reality, the Court held that it suffices when the parallel importer furnishes evidence that leads to the reasonable presumption as to the fulfillment of that condition.[576] This follow, as the Court pointed out in *Upjohn v. Paranova,* that the said article applies where, after repackaging of the product, the original trade mark is reaffixed.[577] By the same logic, the same article ceased to be the relevant legal basis where the parallel importer replaces the original trade mark with a different one.[578] In the latter case a recourse to be made to the general legal basis, which is the Article 34 and 36 of TFEU.[579]

It, nevertheless, needs to be highlighted that substitution of the legal basis in the latter case is, for the most part, only formally driven. The Court suggested that there is no practical difference rendered by application of two different legal basis; those two provisions, which pursue the same result, must be interpreted in the same way.[580] This undoubtedly follows that the BMS Conditions are to be sought, with no difference, in the cases of re-branding.

**4. Threshold of Intervention Required for Repackaging; Junek Europ-Vertrieb[581]**

In a recent judgement, the Court enunciated that for the goods to be tested against BMS Conditions, the intervention made thereto after the initial marketing should qualify as 'repackaging'. This very postulate connotes that not every alteration that is made to the products necessarily infers repackaging in general; and relabeling in particular.

In that case, the parallel importer, while having importer the medical devices (i.e. medical dressing for wounds)[582] from Austria to Germany, had added a sticker on the packaging containing his business information as the importer of the products. The said sticker,

[575] Id. para. 52.
[576] Id. para. 53
[577] Case C-379/97: Upjohn v. Paranova, para. 28
[578] Id.
[579] This recourse is akin to situation in very early cases where only legal basis was the provisions of the Treaty.
[580] Upjohn v. Paranova, para. 30
[581] Case C-642/16: Junek Europ-Vertrieb GmbH v Lohmann & Rauscher International GmbH
[582] The subject matter of the case does not necessarily concern medication. To that end this case also can be suggested to be an example of application of repackaging principle to other products.

as reported and demonstrated by the Court, was neatly placed in a way to not conceal any original printing on the box.[583] Besides not curtailing any original printing, the size of the sticker covered only approximately 5 percent of one face of the packaging. The importer, however, omitted giving prior notice to the right holder; nor did it supply the latter with a sample.

The ECJ articulated that in order for the added label to be tested against the BMS Conditions, there must exist an intervention that qualifies as a repackaging, of which relabeling is a part.[584] Taking a practical approach, the Court distinguished the present case from the previous judgements to the effect that the intervention in all the present cases, at very least, included the opening of the original packaging in order to insert an information leaflet in a language different from that of the country of origin;[585] and this was not the case in the present dispute insofar as the countries used a common language. Furthermore, the additional label in the present case (i) was small in size; (ii) was affixed to the unprinted portion of the packaging thus not covering up any original printing and (iii) was solely limited to the information of the importer. In reliance to these facts the Court concluded that the attachment of such a label cannot affect the specific purpose of the mark, which is to guarantee the origin,[586] implication being that repackaging, for the purposes of opposing the further commercialization, has not occurred. Naturally therefore, the parallel importer does not bear the onus of complying with the BMS Conditions so as to market the products.

The Courts finding, in the light of the specific characteristics of the intervention at issue, seems relevant. In fact, it is of very little doubt that an artificial partitioning would likely occur if the right holder could oppose to further commercialization in reliance to the mere external affixation of a minimal size of label that does not curtail the original printing or offer any additional instruction as to the actual product. What is interesting, on the face of this judgment is that the Court seems to have, slightly, departed from the rigid understanding of repackaging, which, according to the earlier case law, regarded any act of repackaging, including relabeling as naturally prejudicial to the specific subject matter of trademarks, without delving into substantive effects created by that act of repackaging. In *Junek Europ* however, the very scrutiny of the existence of a repackaging in the present case, and correspondingly the

[583] Junek Europ-Vertrieb, para. 6
[584] Id. para. 29, 30
[585] Id. para. 33
[586] Id. para. 36

indication of an implied threshold of alteration so as for an act to connote 'repackaging' may lead one to thinking that the Court is now ready to embark on an analysis of actual effect of intervention.

## 5. Application of Repackaging Principles Beyond Pharmaceuticals

Although it is true that pharmaceuticals have been the primary concern of repackaging rules, the Court of Justice, in essence, has affirmed the application of the latter principles to other products as well. Particular nature of different product groups nevertheless compels a fine tuning of the original principles.

*Loendersloot v. Ballantine*[587]: Application of BMS Conditions in respect to alcoholic drinks was considered in *Loendersloot*, where the parallel importer (i) removed the identification numbers originally placed underneath the labels by the trademark holder and (ii) and removed the word 'pure' which was again so placed by the trademark holder.

As the first nuance the Court enunciated that, instead of objective necessity, what has to be brought under question in the present case was whether relabeling was necessary to protect the supply sources of the parallel trader,[588] which, if revealed, would be dried up by the trademark holder. The identification number applied, in practice, fulfilled a dual function. Firstly, it enabled the right holder to screen the delivery channels and pin down the supply sources of the parallel trader; then reconstruct this delivery chain so as to prevent the parallel trade as such. Based on this premise, the parallel trader rightfully argued that the removal of the identification number was necessary. However, the right holder held on to the second function of that number, which was to provide the compliance of the products with the legal obligations under the Community law, particularly concerning food safety and product liability, and secondly to make it possible to recall the products in case of any defect. The ECJ, in respect to the competing interests of the two parties on the axis of identification number, attached a particular importance to the second function. Accordingly, it held that the holder of the mark is permitted to prevent the third parties from removing and then reaffixing or replacing labels in order to eliminate identification numbers.[589] On the other hand, the Court went on to state that the concern of the parallel trader as regards the use of that number by the right holder in order to dry up parallel supply chains was also relatable. It concluded however, the parallel

[587] Case C-349/95: Loendersloot v Ballantine & Son and Others
[588] Id. para. 38
[589] Id. para. 42

trader, in the latter case should seek protection under the competition provisions of the Treaty.[590]

As regards the removal of the word 'pure' from the original label, the Court simply made reference to the rules of labeling in the targeted state. Accordingly, if the presence of that word is a legal obstacle to marketing in the destination Member State, the trademark holder cannot legitimately oppose to the marketing on the basis of its removal.[591]

As far as the application of BMS Conditions is concerned, the Court initially admitted that the said principles were originally envisaged in the context of pharmaceuticals. However, the conditions emanate from the very recognition of the rights which are normally reserved to the right holder himself.[592] That is to say, because the trademark rights are at the main focus, there is no reason for the conditions not being applied in respect to other trademark protected goods. Particular to these cases however, the requirement of 'identification of the repackager' is not necessarily sought because the notice given by the parallel trader to the right holder already gives sufficient weight to the interest of the right holder.

*L'Oréal v. eBay*[593]*:* Although it did not refer to BMS Conditions, in the absence of repackaging or relabeling but instead as regards unboxing, the Court of Justice arrived at a similar result through impediment to indication of origin. It recognized two different scenarios in which the holder of the mark may oppose to further commercialization of the goods whose packaging was removed by the reseller. The first scenario appears where removal of the packaging harms the image of the products thus undermining the reputation of the trademark they bear. In this case, trademark holder may oppose the sale of an unboxed product (in that case perfume and cosmetics) as long as he establishes that the removal of packaging has actually damaged the image of that product, hence the reputation of the mark.[594] Damage for that purpose is liable to occur when the packaging is as important as, or more important than, the bottle or the container in the presentation of the image.[595] Secondly, on the occasions where the removal of packaging resulted in the loss of essential information, such as information relating to the identity of the manufacturer or the person responsible for marketing, the trademark's function of indicating

[590] Id. para. 43
[591] Id. para. 45
[592] Id. para. 48
[593] Case C-324/09: L'Oréal SA and Others v eBay
[594] Id. para. 79
[595] Id.

origin is impaired.[596] Consequently, the right holder in the latter case may, likewise, oppose the marketing of those products.

[596] Id. para. 80

# CHAPTER 7

# USING OTHER`S TRADEMARK FOR ADVERTISING

From an economic perspective advertising function of trademarks is of undeniable importance. Arguably, the latter function is rooted in a more central one, i.e. guarantee of origin, to the effect the said origin is where goodwill and reputation is accumulated. Nevertheless, advertising function has significantly grown up to form another self-contained gravity center within the concept of trademark. As we contended in the initial chapter of study, the plain activity of trading is expanded toward "commerce" when it is combined with ancillary acts such as advertising. To that end, commercialization of trademarks, and naturally that of trademarked goods, indispensably implies the use of trademarks for advertising. Furthermore, this observation is true not only in respect to the initial marketing but also to further commercialization.

It is of very little trouble, it is as a matter of fact quite natural, when the holder of trademark uses that mark for advertising in respect to the corporeal goods while offering them on the market. The question arises when the subsequent third-party trader, who acquired the goods after those were put on the market by the right holder or with his consent, intends to use that mark for advertisement in order to attract attention to further commercialization thereof, in which he is engaged. This problem is rooted in two premises which are causally interrelated:(i) it is among the trademark holder's exclusive prerogatives to prevent any third party from using the mark for advertising;[597] (ii) insofar as the concept of exhaustion is principally confined to subsequent change of ownership -generally referred to as distribution-, other exclusive prerogatives conferred by trademarks, including the aforesaid right to use for advertising, do not intrinsically come under the scope of exhaustion. Question thus presents itself whether the subsequent traders are entitled to use the trademark for advertising in the course of further commercialization of the corporeal goods that were initially put on the market by the right holder. In other words, this is the question of whether exhaustion principle expands to exclusive right to use that mark for advertising, to which the Court proposed an express answer in *Dior v. Evora* below.

[597] Article 10(3) of the Trademark Directive (2015/2436) [formerly Article 5(3)(d) of Directive 89/104] delineating the rights conferred by a trademark, reads: "The following, in particular, may be prohibited […] (e) using the sign on business papers and in advertising"

## 1. Use in Relation to the Right Holder`s Goods*: Dior v. Evora*[598]

The dispute in *Dior v. Evora* resulted in a benchmark ruling wherein not only did the Court of Justice, having built on an economic consideration of the advertising function of trademarks, answered to the above question; but it also considered the said function, from a legal perspective, *vis-à-vis* the extent to which the protection of this function is provided. To put differently, what the Court brought to clarity were, first, whether the exhaustion applies to exclusive right to use the mark for advertising; secondly, if so, whether there are legitimate reasons that can exclude such exhaustion. We shall split our analysis into two parts in line with these two cruxes of the ruling. Primarily however it is relevant to summarize the facts to that dispute.

Dior produces luxury perfumery and cosmetics and distributes them to the end users through its exclusive representatives and selected retailers which are committed to never resell the products to other retailers. Dior held in various Member States trademarks consisting of the names of the perfumes as well as pictorial marks consisting of illustration of their packaging. On the flipside, Evora, the operator of a chain of drugs stores, acquired and embarked on selling Dior products despite not being a part of Dior`s distribution system. However the legality of retail of those products by Evora did not come under question, the practice challenged by Dior was when Evora depicted the packaging and bottles those products in its advertising leaflets during seasonal promotion.[599] This practice, according to Dior, was harmful to the luxurious and prestigious image of its mark; it was this argument that formed the basis of the infringement claim Dior brought.

### 1.1. Exhaustion of the right to use the mark for advertising

The question of exhaustion appeared to be a preliminary matter in *Dior v. Evora*. The referring Dutch court sought clarification on whether a reseller, besides being free to resell those goods, is also free to use the associated trademark to bring to the public's attention the further commercialization thereof. The Court of Justice corresponded to the later in affirmative through a functional and practical interpretation of the exhaustion principle on the face of the provisions of the Treaty (no artificial partitioning allowed), however not dwelling on a contextual analysis of exhaustion principle. § It simply observed that if the rights conferred to the holder of a trademark -as set out in article 5 of the Directive (now article 10 EUTMD- are

[598] Case C-337/95 - Parfums Christian Dior v Evora
[599] Id. para. 5,6

liable to exhaust after the initial consensual market, so must be the right to use the mark for advertising. *(Without distinguishing the between the exclusive rights under that article though is misleading in my opinion; it fallaciously conveys the postulate that all rights exhaust after the consensual marketing).* The justification of that imperative, according to the Court lies in the very purpose and function of exhaustion principle which, in a concurrent reading with the article 36 of the Treaty, is to prevent owners of trade marks from being allowed to partition national markets.[600] Accordingly, this principle would be effectively undermined if the right to make use of a trade mark in order to attract attention to further commercialization were not exhausted in the same way as the right of resale.[601]

### 1.2. Limitation to exhaustion

Having thus brought the right to use the mark for advertising into the scope of exhaustion, the Court went on to draw the limitations to such use. Subtext being that the advertising function was recognized not only as an economic phenomenon, but also as something worthy of legal protection.[602] In that, it tested the particular use of the trademark for advertising in the present case, in relation to "legitimate reasons" for the proprietor to oppose further commercialization. As we discussed within the context of right for repackaging, "legitimate reasons" for the purposes of the Directive particularly mature when an impairment to the condition of the goods is caused following the initial marketing. Obviously in that case, impairment was envisaged to relate to the physical integrity of the goods induced by repackaging or otherwise interference. Strikingly, in *Dior v. Evora* the impairment which could give a rise to the possibility of opposing further commercialization, was found not to be limited to the physical condition of the goods. The Court acknowledged the existence -and gravity- of a "mental condition" that comes intrinsic to certain group of products.

A balance had to be struck between the interest of the trader who engages in further commercialization of those products and that of the holder of trademark in preventing the subsequent traders from damaging the luxurious and prestigious aura of the mark. Accordingly, a reseller -albeit being free to use the trademark for advertising- he must nevertheless endeavor to prevent that advertising from affecting the value of the trade mark by detracting from the

[600] Id. para. 36
[601] Id. para. 37
[602] I. Simon Fhima, *The Court of Justice's Protection of the Advertising Function of Trade Marks: an (Almost) Sceptical Analysis*, 6 J. Intell. Prop. L. 325,328 (2011)

allure and prestigious image of the incorporeal goods and from their aura of luxury.[603] The reseller is therefore permitted to use the mark in advertising in a way that is customary in that sector; the mere fact that the reseller`s advertising does not correspond to the standard of advertising that the right holder carries out does not constitute a legitimate reason to oppose further commercialization. However legitimate reason for this purpose occurs when the reseller`s choice of advertising seriously damages the reputation of the trade mark, analysis of which is to be made in the light of specific circumstances of each case.[604]

One would be tempted to observe the very affirmation of the impairment to the 'mental condition' to considerably expand the concept of legitimate reason within the meaning of Article 15(2) of the Trademark Directive.[605] Though this observation is true, it is crucial to note that such a conclusion is reached on the basis of luxury products, which are distinguished by their top-notch aura of prestige hence the reputation; therefore the same sequel might not as easily applicable to the products which do not necessarily qualify as luxurious. It is also important to remember that, even in the context of luxurious goods, the existence of 'legitimate reason' depends on fulfilment of cumulative conditions. Not only should the way of advertising be inferior to the prestige of the mark but it should also necessarily damage the reputation thereof, or as referred to by the AG Jacobs it should 'positively degrade' its image[606]; and finally that damage must be 'serious'. That is to say only under strict conditions would the right holders be able to oppose the use of their trademark by the others in advertising, the conditions are seemingly hard ever to exist within the context of non-luxury products. The fact remains, though, that the advertising function of trademarks is thus recognized and found protection-worthy even after the first marketing of the goods bearing them.

**2. Referential Use of Other`s Trademark**

*Dior v. Evora* above centered around the use of trademark in the course of further commercialization, particularly in subsequent sales, of the goods which were initially put on the market by or with the consent of the trademark holder. Such a use was permitted on the basis of exhaustion principle. Practically speaking, the activities inferring commercialization cover more than mere subsequent trade of those goods. Trademarks belonging to someone may,

[603] Dior v. Evora, para. 45
[604] Id. para. 46
[605] Directive 2015/2436; [formerly Art. 7(2) of Directive 89/104]
[606] Opinion of AG Jacobs in Case C-337/95, I - 6030

in reality, be used in relation to the good and services provided by the others in order particularly to indicate the intended purpose of such goods or services. So much so that the latter provider cannot potentially convey to its customers the essential function of its goods or services without referring to the others` trademark. Primary example would be when a third party provides services, such as repair and maintenance, for the trademarked goods; or when the latter manufactures and markets his own goods whose intended purpose is linked to the goods of the trademark holder (such as accessories and spare parts)[607]. The use of trademarks under these circumstances is conceptualized as referential use of trademarks.[608]

There are obviously two opposite pathways concerning the treatment of these. The option one is to exclude the third parties, in providing their own goods or services, from the use of the trademark notwithstanding the fact that such a use is not intended to indicate any commercial link to the right holder, thus it is only informative or referential. The result being that no third party can speak of that trademark in a commercial context, unless they are sub-trading the goods of right holder. Rightly noted by Senftleben, should this path be followed, the commercial freedom of speech would be undermined and, metaphorically, trademarks would act like black holes that absorb all the communication surrounding them.[609] The second option is to enable those third parties to use that mark for informative and referential purposes which, in turn, brings the exclusivity of the marks under question. Naturally, the guarantee of origin function is liable to be affected insofar as the use of that trademark by the others may fallaciously give the impression that the latter is linked to the holder of the mark, thus allowing him derive an – undeserved - commercial advantage from the reputation and goodwill that the mark embodies.

In selecting the second option, however, exhaustion principle cannot lay the proper legal basis for liberating the referential use (unless the right holder`s goods are being further commercialized); and that is clearly because there is no good at issue that has been put on the market by the actual right holder. Instead of exhaustion principle, such use is permissible under the limitations to trademark rights set out in Article 14 of the Directive (formerly Article 6,

[607] Besides trademark considerations, the actual legitimacy of spare parts -particularly that in automotive sector- is discussed within the ambit of design law.
[608] Annette Kur, *Trademark Functions in European Union Law-Also Containing a Comment on CJEU case C-129/17, Mitsubishi v. Duma*, 19-06 Max Planck Institute for Innovation & Competition Research Paper, 6 (2019); Martin Senftleben, et al., *Recommendation on measures to safeguard freedom of expression and undistorted competition in EU trade mark law*, 37 (6) EIPR 337,338 (2015)
[609] Martin Senftleben, *Trade mark protection—a black hole in the intellectual property galaxy?*, 42(4) IIC 383,384 (2011)

Dir. 89/104) which prohibited the holder of the mark from exercising his right, *inter alia,* "where the use of the trade mark is *necessary* to indicate the intended purpose of a product or service, in particular as accessories or spare parts."[610] This limitation is bound to comply with the express proviso that "the use made by the third party is in accordance with honest practices in industrial or commercial matters."[611] These two legal bases were differentiated by the ECJ in *BMW v. Deenik*.

***BMW v. Deenik[612]***

The dispute concerned the use of BMW trademark in advertising by *Mr. Deenik* who specializes in dealing second hand BMW cars and in their repair and maintenance; however, his business was not a part of BMW`s dealer and service network. The Court of Justice in that case, having pointed out that the use of trademark by others in a way to inform the public as to the scope of its own business activities, in fact, qualifies as a use in the course of trade within the meaning of Article 14 of the Directive (formerly Art. 5 of Dir. 89/104), went on to comprehend under what circumstances such a use could be permitted. Important though, since the activities of the trader include both second hand dealing of the cars manufactured by BMW and their repair/maintenance, the Court was led to analyzing these separately.

*a) Second-hand dealing:* As regards the first constituent of Deenik's business operation, which is the sales of second-hand BMW cars, there evidently exists goods, i.e. automobiles that were put on the market in the Community by BMW, and a part of the advertising in the present case was aimed at bringing the public's attention to further commercialization thereof by way of second hand dealing. Much like the circumstances in *Dior v. Evora*, the advertising in this case is also to be regarded under the exhaustion principle. To that end, the Court held, the trader was permitted to use the mark belonging to BMW in the course of further commercialization of the automobiles that were initially put on the market by the latter[613]; because that first marketing exhausted, in respect to those cars, the exclusive right to use the mark. This however also follows that in the existence of legitimate reasons within the meaning of Article 15(2) of the Directive [then Art. 7(2) of Dir. 89/104], the holder of the mark is entitled to oppose the use of that mark for advertising. According to the Court`s view, it may particularly give a rise to such legitimate reasons when the advertising gives the impression that the business of the

[610] Article 14(1)(c) of Directive 2015/2436, emphasis added
[611] Id. Article 14(2)
[612] Case C-63/97: Bayerische Motorenwerke AG (BMW) and BMW Nederland BV v Ronald Karel Deenik
[613] Id. para. 50

trader is a part of, affiliated or otherwise economically linked to the right holder's business.[614] However the existence of such an impression -thus that of a legitimate reason- cannot be deduced from the mere fact that the reseller derives an advantage (including lending an aura of luxury) from using the mark in the advertisement for the sale of incorporeal goods as long as the advertising is honest and fair. What matter in that regard is the existence of a risk that the public might be led to perceive a commercial connection between the reseller and the holder of the mark[615]

*b) Repair and maintenance:* As regards the other leg of the other activities, i.e. maintenance and repair of BMW cars, other considerations should apply. These activities -likewise the advertising devoted to them- are habitually irrelevant to further commercialization, particularly the sales, of the trademark holder`s goods; correspondingly falling out of the ambit of exhaustion principle.[616] Their legitimacy is to be comprehended in the light of Article 6 (now Art. 14) of the Directive which as we highlighted above, imposes a limitation to the exercise of the rights against a third part who used the mark due to a necessity to indicate the intended purpose of a product or service. The "necessity" for the purposes of that provision was found to persist in the present case given that an independent trader carrying out the maintenance and repair of BMW cars and is a specialist in that field, cannot in practice communicate this information to his customers without using the BMW mark.[617]

The limitation applies only to the extent that the use by the third party is within the limits of honest practice. Although the legal bases thus differ, the Court approximated the interpretation of those two provisions to the purposive effect that they both are aimed at reconciling the interest of the right holder and free movement goods/freedom to provide services. Accordingly, the compliance of the advertising with honest practice should be interpreted much like the 'duty to act fairly' when determining the legitimate reasons to oppose further commercialization *vis-à-vis* exhaustion.[618] In other words, unless the mark is used in a way that implies a commercial connection between the other undertaking and the trademark holder, and in particular that the reseller's business is affiliated to the trade mark proprietor's distribution network or that there is a special relationship between the two undertakings, it must

[614] Id. para. 51
[615] Id. para. 53
[616] Id. para. 56, 57
[617] Id. para. 60
[618] Id. para. 61

be deemed to have been used in line with honest practice[619]; hence the right holder cannot exclude such a use.

Albeit the end result is the same (that is to say the trader is permitted in both cases to use the trademark for advertising) the judgement in *BMW* put forward a clear exhibition of the distinction fair use limitations to trademarks and their exhaustion. On one hand, the use of the mark in advertising was permitted on the basis of exhaustion principle to the extent that it is aimed at bringing public`s attention to further sales of the goods over which the trademark holders rights had exhausted. On the other hand, services provided by the third party in respect to those goods do not imply further sales thereof; naturally exhaustion principle falls irrelevant to justifying the use of the trademark in advertising those services. The proper legal basis for the latter use is found in the fair use limitations to trademark rights.

***Gillette v. LA-Laboratories[620]***

The limitation set out in the Article 14(1)(c) of the Directive stipulates the express proviso of 'necessity' to indicate the intended purpose of a product or service. In *BMW* the Court had confined itself to assessing the existence of such necessity in the dispute at hand, though not offering a general concept. Subsequently in *Gillette*, that concept was given further clarification. Differently from the preceding case, here the dispute originated from the -referential- use of the Gillette`s trademark by another undertaking which, just like the right holder, specialized in manufacturing and marketing of razor blades. The defendant`s use is particularly consisted of affixing labels on his own products which read "Gillette handles are compatible with this blade".

The Court initially clarified that it does not necessarily affect the application of that provision whether the products of the third party technically qualifies as an accessory or spare part to the trademark holder`s goods; these two types enlisted in the provision of the Directive were only exemplary.[621] Without clinging on to the qualification of the products as accessory or spare part, the Court seems to have implied that what matters is whether there is necessity to use the mark.

On the other hand, 'necessity' for the purposes of that provision was interpreted rather strictly. The Court concluded that it is deemed to exist only when there is no other means of

[619] Id. para. 64
[620] C-228/03: Gillette v. LA-Laboratories
[621] Id. para. 31,32

conveying the information (as to the intended purpose of those products) to the customers.[622] Should other means -such as technical standards or norms that are known by the public and used for that type of product- be available, there appears no necessity;[623] thus rendering the use of the mark illegitimate.

The Court also shed further light on the concept of 'honest practice' by way of negative sampling. The third party, in using the trademark, is deemed to have contravened honest practice where such use (i) arises the false impression that there is a commercial connection between that third party and the holder of the trademark; (ii) affects the value of the trademark by taking unfair advantage of its distinctive character or repute; (iii) discredits or denigrates the mark; (iv) is made in relation to the goods which were presented by that third party as an imitation or replica of the good that originally bear the mark.[624]

It is of little doubt that the list above is not exhaustive; compatibility of the use with honest practice, much like the criterion of objective necessity, is to be considered by the national courts with regard to the circumstances of each specific case.

***Portakabin v. Primakabin***

In *Portakabin v. Primakabin*[625] The Court once again considered concurrently the fair use limitations and the exhaustion principle, albeit this time in relation to online advertising by means of keyword use. The parties are competitors in the same sector and sell their products over their internet pages. Primakabin picked the word 'Portakabin', which belonged to its competitor, as a keyword so as for its website to appear in the search results. Consequently, the users typing the latter word in the search engine would come across the ad entitled "used portakabins" which linked the users to Primakabin's website.

The Court found that such a use (that, although not explicitly indicating a commercial link to the right holder, entails -to the experience of a normally informed and reasonably attentive user- vagueness as to whether the advertiser is so linked to the trademark holder or it's a third party)[626] of other's trademark, insofar as it relates to goods or services identical to those in respect of which the mark is registered, is objectionable under Article 10(1) [formerly Art. 5(1)] of the Directive. However it is for the national court to decide whether the use of the

[622] Id. para. 35
[623] Id. para. 36
[624] Id. para. 49
[625] C-558/08: Portakabin v. Primakabin
[626] Id. para. 35

mark by Primakabin is justifiable within the meaning of limitations set out in Article 14(1) [then Art. 6(1)] of the Directive, in particular referential use of marks, the Court of Justice took the view that the advertiser cannot, in general, rely on that provision. This is mainly because the vagueness created by that advertisement as to whether the advertiser is the holder of the trademark or a third party[627], in itself, is liable to fall foul of honest business practices which is a prerequisite for the application of that provision.[628]

The second question concerned whether the keyword advertising in the present case should be given countenance in the light of exhaustion principle, regard being had to the fact that it concerned, to a remarkable extent, the resale of second-hand products originally manufactured by Portakabin. The Court having stated that the latter typically connotes "further commercialization", reiterated its position in *Dior* and *BMW*: the right holder cannot oppose the use of trademark in the course of further commercialization of incorporeal goods unless there exists a legitimate reason. In the said judgements such a legitimate reason had been found *inter alia* where that use in advertising (i) seriously damages the reputation of the mark and (ii) gives the impression that there is a commercial link between the reseller (advertiser) and the right holders. Along the same lines, the ambiguity created by the advertising in the present case, to the effect that it does not perceivably rule out the impression of a commercial link, is likely constitute a legitimate reason.[629] It is however still for the national court to substantiate the existence of that kind of impression; or that the goods -other than that of the right holder-, by being resold alongside, seriously damage the image which the right holder has succeeded in creating for its mark.[630] For a bit of guidance, the Court emphasized, the impression of a commercial link cannot be deduced from the use of mark with additional wording "used" or "second hand". Also, unless the sales of other products, in the light of their volume, their presentation or their poor quality, is liable to seriously damage the image of mark, the use of the latter in advertising needs to be permitted, save the aforesaid legitimate reason vis-à-vis ambiguity as to commercial link.

***Note on other fair use limitations***

[627]Vagueness for that purpose infers where th[e] use [of trademark in advertising] does not enable normally informed and reasonably attentive internet users, or enables them only with difficulty, to ascertain whether the goods or services referred to by the ad originate from the trade mark proprietor or from an undertaking economically linked to it or, on the contrary, originate from a third party. See para. 68
[628]Portakabin v. Primakabin, para 69
[629] Id. para. 81
[630] Id. para. 91

Referential use is not the only limitation to trademark rights; the same provision of the Directive also recognizes fair use limitations (i) in respect to the name or address of the third party, where that third party is a natural person[631]; and (ii) that mark entails signs or indications which are not distinctive or which concern the kind, quality, quantity, intended purpose, value, geographical origin, the time of production of goods or of rendering of the service, or other characteristics of goods or services.[632] However as we approach the matter on the axis of exhaustion of rights, we shall confine our discussion to referential use of marks in advertising, which, as we illustrated above, may or may not come in the scope of exhaustion principle depending on whether there is subsequent sales of the right holder's goods at issue. It is nevertheless worth noting that each one of those limitations sets free the use of the mark by third parties only to the extent that such use is in accordance with honest business practices. To that end, it is fairly clear that the concept of honest practice resides at the center of application of limitations to trademark holders' exclusive rights. Not surprisingly a comprehensive set of case law came to further define the said concept.[633] However the primary concern of those limitations is not necessarily the emancipation of parallel trade between the Members States, the subtext apparent from the jurisprudence of the Court is that they also seek to reconcile the interest of free movement of goods and freedom to provide services, thus contributing to undistorted competition environment.[634]

### 3. Conclusions on Repackaging and Advertising

Exhaustion principle primarily concerns (and limited to) the exclusive right of distribution, which includes *inter alia,* offering the corporeal goods, importation and exportation thereof. Free movement of goods among the Member States characterized by that distribution; to that effect the principle of exhaustion is the major instrument of providing that freedom which, otherwise, is susceptible to be hampered by territoriality of intellectual property rights. It is equally clear, however, the mere freedom of further distributing the goods after their initial sale by the trademark holder appears to fall short of the envisaged trade liberty between the Member States. That freedom is complete in real sense only when the goods can, without facing a trademark-based resistance from the right holder, be adjusted to the regulatory

[631] Article 14(1)(a) of Directive 2015/2436 [formerly Art. 6(1)(a)]
[632] Id. Art. 14(1)(b) [formerly Art. 6(1)(b)]
[633] In addition to C-228/03: Gillette v. LA-Laboratories, see: C-100/02: Gerolsteiner Brunnen and Putsch, para. 24; C-245/02: Anheuser-Busch v. Budejovický Budvar, para. 83; C-17/06: Céline SARL v Céline SA, para. 34
[634] BMW v. Deenik, para. 62; Gillette, para. 29; Portakabin v. Primakabin, para. 57

climate of the Member State of destination which must be complied with in order for the goods to be marketed there. Also, that freedom cannot fully function where subsequent trader is prohibited from using the mark so as to bring the public`s attention to its activity of further resales. To that end exhaustion principle is extended such as to practically cover the right to affix the mark as well as the right to use the mark for advertising. In both cases however the fundamental pattern is to provide that freedom while not undermining the interest of the right holder as well as the essential function of trademarks.

As regards repackaging,[635] the main principle remains that any interruption with the presentation of goods - pharmaceuticals in particular - is liable to give a rise to the legitimate reason in reliance of which the holder of trademark can derogate from exhaustion. Nevertheless, for the interest of free movement, under certain conditions such alterations to the products cease to be a legitimate reason to oppose further commercialization. Accordingly, following conditions must be cumulatively met: (i) objective necessity; (ii) no effect on the original condition of products; (iii) indication of the repackager; (iv) presentation such as not to liable to damage the reputation of the mark; (v) prior notice to the right holder.[636]

Exhaustion principle covers to use the mark in advertising to the extent that the said use concerns further resales of the goods that were consensually marketed by the right holder; this proposition is the clear outcome of the judgement in *Dior v. Evora*. The same sequel applied in *BMW v. Deenik* in relation to sales of second-hand cars. Nevertheless, the freedom to use the mark is subject to a duty of acting fairly in relation to the legitimate interest of the right holder; in that effort must be put towards preventing that advertising from affecting the prestige and luxurious aura of the mark. The contrary, to the extent that it damages the reputation of the mark, will result in a legitimate reason to oppose further commercialization.

Frankly, from a formal view point, in order for the exhaustion principle to apply, there has to be goods at issue which were initially put on the market by or with the consent of the right holder. This follow that when the activity of the third-party trader is does not entail resale of the right holder`s goods, he cannot rely on exhaustion principle to use that mark in the course of trade. However, the activity of that party, be that providing services or marketing of other products, might necessitate a reference to other`s marks in order to define the intended purpose of those goods or services. On those occasions, such a use of the third party could fall on the

[635] Necessary to recall that repackaging is used as an umbrella term which covers a variety of alteration to the outer aspects of goods, including re-boxing, relabeling and the like.
[636] See 'The Aftermath of BMS' above

fair use provisions, which *inter alia* affords to third parties the right to use other`s trademark with the express stipulation that such use must be in line with honest business practices.[637] The Court made it clear, such referential uses need to be driven by an objective necessity to indicate the intended purposes of the products or services of a third party; such a necessity occurs when there is no other means to convey such information to customers. Even in the presence of that qualified necessity, the use needs to comply with honest business practices. The latter terminology is, arguably, intended as a catch-all phrase availing the judiciary of some room of maneuver in assessing the right holder`s interest. At very least however, an impression of (or even certain ambiguity as to) commercial link (to the right holder) that flows from the way the third party used the mark for advertising is liable to run afoul of honest practice.

It is true that different legal bases highlighted above apply to different subject matter; in particularly the exhaustion principle, in general terms, facilitates intra-brand competition, while the fair use limitations, to some level, factors into the competition between the brands and sub-sectors. The primary concern of those limitations is not necessarily the emancipation of parallel trade between the Members States. Nevertheless, the subtext apparent from the jurisprudence of the Court is that, much like the exhaustion principle, the fair use limitations also seek to reconcile the interest of free movement of goods and freedom to provide services, thus contributing to undistorted competition environment. From the widest perspective, the common motivation of the both sets of provisions appears to be to make the monopolistic nature of intellectual property right fit into the peculiar characteristics of the internal market. Based on this background, the Court seems to have equated both sets of provisions, albeit naturally in relation to different subject matter, and interpreted thereof along the same lines. Finally it is worth noting that the original language of the Trademark Directive, particularly the provision thereof on exhaustion, also conveys that the said approach is not instantly devised, but was also teleologically pertinent in the legislation. That is to say the term "commercialization" as we have purported at the outset, saturates to a greater area than mere trade. It should therefore presumably cover the act of advertising which is an ancillary to trade: the result which the Court attained in *Dior* and *BMW*.

[637] Article 14(1)(c) of Directive 2015/2436 [formerly Art. 6(1)(c)]

# CHAPTER 8

# COMPETITION LAW CONSIDERATIONS

## 1. Introduction

Intellectual property rights are of commercial nature; either potentially or kinetically retaining some value that is economically worthwhile. Contractual arrangements concerning the exercise of those exclusivities, we initially identified as legal instruments of intellectual property commercialization, as well as non-contractual practices, even pure commercial behaviors are highly potent to influence the competitive environment in the market for corporeal goods and services. These influences necessarily transpire from the earlier stages than the of distribution of what has been offered under that intellectual property right; they, for the most part, tend to practically determine who can compete in the same market with the intellectual property right holder by offering goods and services alike. The latter reverberation is beyond the reach of exhaustion principle. Competition laws function to ensure fair commercial behavior, without differentiating whether anti-competitive behavior is contractually contemplated among certain business actors or they are completely discretional or unilateral. In substance what it regards is whether commercial behavior is such as to distort the competition. The interface between the two bodies of law is incontrovertible and intellectual property commercialization cannot be properly conceptualized without comprehending this interface.

-We shall first briefly define this interplay along the general outlines and secondly, we shall outline the specific connotations of that interplay for Internal European market, which, at the periphery, is the bedrock of European integration, in consideration of its peculiar quiddity.

-How and to what extent the anti-competitive impacts of intellectual property rights are reconciled -if they are- in the Internal European market on the face of typical abusive exercise of intellectual property rights so as to complete the understanding of intellectual property commercialization.

### 1.1. Interface between two bodies of law: convergence and divergence

Among the other foundations, one positive rationale of intellectual property laws is to incentivize innovation and cultural progress by conferring exclusive rights over the use of protected subject matter. From a straightforward perspective, there would be very little

incentive, for instance, to (i) create literary and artistic works, (ii) devote immense resources and time in inventions, (iii) create quality and reliable products if the others were able to have a free ride on those thus providing commercial advantage without putting effort. In a perfectly healthy market environment, the response of the other market participants would be to further innovate and create so as not to fall behind the market and to get entitled to such exclusivities of their own. To that end, from a rather theoretical view point, intellectual property protection enhances the competition, hence pro-competitive.[638] Similarly, the idea of undistorted competition, and competition laws as their guarantor, tend to root, *inter alia,* for consumer welfare.[639] In doing so it seeks to avoid market barriers and benefit consumers by encouraging competition among a multiplicity of suppliers of goods, services and technologies.[640] Consumers, therefore, benefit from competition through lower prices, better quality and a wider choice of new or improved goods and services.[641] This side of the coin, therefore, implies a convergence of objectives between the two bodies of law, at least at the teleological level, albeit subject to a historically pertinent debate.[642]

However, from the outset, the tension between competition and intellectual property is rather apparent. Intellectual property rights, by definition, manifest an exclusionary character; that is the privilege to determine who has the access to protected information or technology both at consumer and competition level as well as to determine under which conditions that access will be provided. This, practically, well enables the holder of the rights to set barriers to the market entry of potential competitors, for instance, by refusing to license a core (basic) technology for the sector of which it is in possession; thus cutting the competition at the source. Subsequent impact of such a practice would clearly be detrimental to the advancement of

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[638] Nikolaos E. Zevgolis, *The Interaction Between Intellectual Property Law and Competition Law in the EU: Necessity of Convergent Interpretation with the Principles Established by the Relevant Case Law* 22 (In ASHISH BHARADWAJ ET AL. EDS., MULTI-DIMENSIONAL APPROACHES TOWARDS NEW TECHNOLOGY 21-42, Springer 2018)

[639] For an overview of various goals that competition laws seek to attain, see: ALISON JONES & BRENDA SUFRIN, EU COMPETITION LAW: TEXT, CASES, AND MATERIALS 26-29 (Oxford University Press 2016)

[640] Carlos Correa, *Intellectual property and competition law: exploration of some issues of relevance to developing countries*, 21 ICTSD IPRs and sustainable development programme issue paper, at 1 (2007)

[641] See. Communication from the Commission — Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty (now Art. 102 TFEU) to abusive exclusionary conduct by dominant undertakings (2009/C 45/02), para. 5

[642] More detailed account can be found in: E. Thomas Sullivan, *The Confluence of Antitrust and Intellectual Property at the New Century*, 1(1) Minn. Intell. Prop. Rev. iii (2000); Josef Drexl, *Is There a 'More Economic Approach' to Intellectual Property and Competition Law*? (In JOSEF, DREXL ED., RESEARCH HANDBOOK ON INTELLECTUAL PROPERTY AND COMPETITION LAW 27-53, Edward Elgar Publishing 2008); Olav Kolstad, *Competition law and intellectual property rights–outline of an economics-based approach* (In JOSEF, DREXL ED., RESEARCH HANDBOOK ON INTELLECTUAL PROPERTY AND COMPETITION LAW 27-26, Edward Elgar Publishing 2008)

innovation. Secondly, instead of engaging in arduous competitive process, the market actors might, in reliance to those exclusivities, collude to fix prices, share the markets or limit the production to the disadvantage of the consumer.[643] To that end intellectual property rights - particularly the exercise of the exclusivities thereunder - make up perfect instruments to leverage anticompetitive behavior and - if taken to be unrestrained - are likely to assimilate to monopolies. This also follows that "monopoly" for this purpose shall not be perceived only as doing of a single entity. It might entail, on the one hand, collective practices of a multitude of market participants, which could be commenced on contractual basis or in a purely behavioral manner, and unilateral actions of an undertaking which is significantly influential in its respective sector on the other hand. In the former case there exists traces of a *de facto* cartelizing (collusion) and, in the latter, abuse of a dominant position is observed, though the common thread remains that there is very little - if any - room left to competition, the cost thereof being impediment to innovation in relevant sectors and devastation of consumer welfare.

***Function of -balance intended by- competition rules***

However, from a formal stand point, IPRs are exclusive and naturally inferring a quasi-monopoly privilege, it is imperative from the perspective of competition law that IPRs are, while providing competitive advantage to their holder, not to create absolute monopolies. Therefore, statutory intellectual property exclusivities, although liable to affect competition climate as they should, competition laws set the hand to ensure that effect is not such as to practically distort the competition beyond their intended purpose.

### 1.2. Specific consideration for the Internal Market; peculiarity

Above considerations are of general relevance. What makes this concern of a distinct importance in a European context is the quiddity of market model (Common Market and subsequently Internal Market) around which the European integration has been envisaged. This model is characterized by two constituents that are (i) free movement (that of goods, persons, services and capital) and (i) undistorted (or free) competition. On the account of Internal Market, these two pillars are not complimentary or auxiliary but rather existential or constitutive. In other words, European integration in general and European internal market in particular are held together by the principle of undistorted competition as well as free

[643] JONES & SUFRIN, *supra* note 639

movement principle. To that end, albeit competition laws from a teleological perspective are motived to enhance consumer welfare, in specific context of European internal market an independent constitutional function is thus ascribed to competition. That being the case, at one extreme, it is suggested that competition enjoys protection for its own sake.[644] Along the same lines, the objective of competition in the European context is not necessarily confined to customer welfare; the envisaged integration, at the outset, also infers equal opportunities for undertakings thus putting the interest of market participants at the center of the objectives of competition.

In addition, the foremost peculiarity of competition in the context of the internal market arises from the fact that the envisaged undistorted competition environment is to be provided on a (formally) multinational realm that is delineated by the Member States. It is rather predictable that retaining a uniform competition standard in a domain where the market participants are of different nationalities tends to exhibit a unique difficulty. This very structure enables the territoriality principle to factor into the equilibrium of undistorted competition against anti-competitive impact of intellectual property rights. Therefore territoriality, in addition to exclusivity, further intensifies anti-competitive potential of intellectual property rights as it enables, *inter alia*, market sharing and otherwise territorially designated commercial barriers: an open threat for the integrity of the internal market.

Whatever deontology lays behind, a constant environment of undistorted competition is essential to the functioning of the internal market and, by extension, to the perpetuality of European integration. Intellectual property rights, notwithstanding the mutual aim that they share with competition policies, do not escape the adhibition of competition rules to the extent that their exercise in commercial sphere distorts the competition. In other words, intellectual property rights are not immune from the competition rules in mere recognition of the fact that the exclusivities ascribed to them have statutory basis. Naturally, intellectual property commercialization is demarcated by the application of competition rules. To that end we shall discuss the interface between competition rules of the Union and the exercise of intellectual property rights so as to complete the understanding of intellectual property commercialization in the internal market. Initially, however, we find great benefit in highlighting the nuance

[644]WALTER FRENZ, HANDBOOK OF EU COMPETITION LAW 6-11 (Springer 2016); For the contrary view, see: Kolstad, *supra* note 642, at 3

between the principle of free movement and competition rules *vis-à-vis* ensuring market integrity in front of intellectual property rights.

### 1.3. Nuance from free movement provisions: what is offered vs. what can be offered and more

The continuous dictate by the intellectual property right holder over the goods put on the market (i.e. what has been offered), *vis-à-vis* their further commercialization, has been circumvented by the exhaustion principle. This is a necessity compelled by the free movement provisions. In completion of the internal market, free movement envisages the elimination of explicit or implicit restrictions to trade between the Member States, providing for a unitary trade area devoid of physical and regulatory borders which would otherwise be undermined by the territorial quiddity of intellectual property rights.

The exhaustion principle, by its very definition, applies in respect only to what the right holder offered on his own discretion; the prerequisite is for the goods to have been put on the market by or with the consent of the right holder. Exclusive distribution right is thus broken down in respect to further commercialization of those goods by way of import, export and resale; also extending to certain auxiliary activities such as use of the trademark for advertising and repackaging of those goods, albeit subject to strict conditions.[645] In brief, the principle of exhaustion safeguards free movement of goods, and in turn the integrity of the internal market, against the threat posed by territorial exclusivity, albeit as far as what has been offered is concerned.

Nevertheless the said exclusivity, aggravated by territoriality, tends to create quasi-monopoly (and even actual monopoly) states and these are not necessarily confined to further commercialization of what has been offered. It equally poses limitation to 'what can be offered', that is to say what can be initially commercialized, by the present and potential competitors in the same sector. The consequences of the latter on the competition environment are straightforward.

If the monopoly is absolutory, the development in the particular subject matter that is protected by intellectual property rights will, as it were, at the mercy of the right holder. Innovation is perhaps simply defined by the act of carrying that particular realm a step beyond the present state of art. This also implies that is not completely divergent from the current; but

[645] See: Dior v. Evora; Bristol Myers Squibb

it is rather built upon the accumulated knowledge, with added novelty. Consequently, a fragment of that knowledge that is essential to (or basic for) that sector, if monopolistically belonged to one [as in the example of standard essential patents (SEP) we shall see below], is liable to bring innovation and competition to a standstill. And the principle of exhaustion *per se* has very little remedy to this. Furthermore, the principle of exhaustion has shortcoming even in respect to further commercialization of 'what has been offered'; its perfect functioning cannot be provided especially in those cases where the right holder retains an exclusive distribution channel from the manufacture till the end user. Although the exclusive right of distribution is exhausted, the goods are not practically accessible to the third-party traders, at least not so on reasonable terms. Noteworthy however, exclusive distribution systems as such are not anti-competitive from the outset, certain contractual restrictions, as we shall examine below, may nevertheless offend against the competition rules. In the light of foregoing, it comes clear that the principle of exhaustion in itself is insufficient to complete and retain the market integrity, hence it is solely incapable of covering the concept of intellectual property commercialization in the European Internal market.

### 1.4. Statutory Bases of Competition Rules

#### 1.4.1. Central Provisions: TFEU

Competition rules of the Union are set out in Articles 101-109 of the TFEU, though the nuclei of these rules are contained in Articles 101 and 102 which, in substance, concerned prohibition on cartels and prohibition on the abuse of a dominant position respectively. It is beneficial to remind beforehand the rather obvious fact that the scope of competition rules - much like that of free movement provisions - is not confined to intellectual-property-based conducts. However, as we stated above, intellectual property rights, in particular the exercise thereof, remain to be a major instrument in execution of the prohibited acts under those provisions. As a reference point for the discussion on compatibility of specific contractual arrangements and other practices with competition rules, we shall reproduce the full text of Articles 101 and 102 below[646]:

[646] Treaty on the Functioning of the European Union, Article 101 (emphasis added); Treaty on the Functioning of the European Union, Article 102.

*Article 101 (ex. Art. 81):*

1. The following shall be prohibited as incompatible with the internal market: all agreements between undertakings, decisions by associations of undertakings and concerted practices **which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the internal market,** and in particular those which:

(a) directly or indirectly fix purchase or selling prices or any other trading conditions;

(b) limit or control production, markets, technical development, or investment;

(c) share markets or sources of supply;

(d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

(e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

2. Any agreements or decisions prohibited pursuant to this Article shall be automatically void.

3. The provisions of paragraph 1 may, however, be declared inapplicable in the case of:

- any agreement or category of agreements between undertakings,
- any decision or category of decisions by associations of undertakings,
- any concerted practice or category of concerted practices,

which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not:

(a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives;

(b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

*Article 102 (ex. Art. 82):*

Any abuse by one or more undertakings of a dominant position within the internal market or in a substantial part of it shall be prohibited as incompatible with the internal market in so far as it may affect trade between Member States. Such abuse may, in particular, consist in:

(a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions;

(b) limiting production, markets or technical development to the prejudice of consumers;

(c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

(d) making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

### *The Balance Reflected*

An important implication as to the balance of positive (pro-competitive) and negative (anti-competitive) effects of intellectual property rights flows from the structure of Article 101 above. When the pro-competitive effects of contractual arrangements and/or concerted practices between undertakings outweigh anti-competitive effects thereof, they are regarded as pro-competitive, thus, compatible with the objectives of the Union competition rules.[647] In recognition of such net positive impact, Article 101(3) set forth certain exemptions to the application of prohibitions set out in that article. However, in line with the teleology of the

[647] Communication from the Commission — Notice — Guidelines on the application of Article 81(3) [now 101(3)] of the Treaty, para. 33

exemptions, application thereof is subject to following criteria: the contractual arrangement or practice in question should (i) contribute to improving the production or distribution of goods or to promoting technical or economic progress; (ii) allow consumers a fair share of the resulting benefit; (iii) be indispensable to the attainment of the aforesaid objectives; and it must enable the parties to eliminate competition in respect of a substantial part of the products in question.[648] Albeit, as we already stated, the concern of competition rules is not necessarily confined to intellectual-property-based arrangements and practices, an undeniable relevance to intellectual property is embedded in the substance of the said criteria. The exemptions, by putting at the center *inter alia* improving production and promoting technical and economic development, almost spot-on addressed the domain of intellectual property and the transactions commenced therein, by acknowledging that a limited degree of monopolization is an essential necessity for the intellectual property rights to function.

Moreover the structure consisting of prohibition and subsequent exemption ventures an answer to the question whether all the restrictive practices in reliance of IPRs are to be caught by the competition rules. As it was seen, at the outset, the question was answered in negative. And that answer is justified on the basis of the general rationale of competition rules; because in those cases which fall under the exemption set out in that provision, restrictive agreements are likely to generate greater economic benefits to consumers, by leading the undertakings involved to offering cheaper of better products.[649] The provision, thus, also has an implicit reference to (corroborates to) the shared rationale of intellectual property rights and competition rules, that are promoting innovation and advancing consumer welfare.

### 1.4.2. Procedural guidance on the application of the provisions: Regulation 1/2003[650]

The power to enforce the competition, to a great extent, rests with the Commission.[651] The way in which these powers are to be implemented is concretized by the Regulation 1/2003. Although we refrain from descending to particulars, a few ground rules are worth recalling.

Of great importance to the enforcement of the competition rules, with this Regulation 'guilty until proven innocent' approach has been abandoned as regards the agreements and practices falling within the scope of Article 101(3). Therefore, the general prohibition of conduct is

[648] Article 101(3) TFEU
[649] Id. para. 34
[650] Council Regulation (EC) No 1/2003 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty
[651] The legal basis for that power stems from Article 103(2)(d) TFEU

replaced by the principle of general permission, unless expressly prohibited.[652] Powers that are put at the disposal of the Commission in that context includes investigation, inspection and imposition of penalties, in form of fines and periodic penalty payments, on the undertakings which were found in non-observance of the competition rules.[653] Jurisdiction over the judicial review of the decisions taken by the Commission is shared by the European General Court (EGC) and the European Court of Justice in a vertical alignment. Accordingly, the former court retains the first instance jurisdiction and the latter court hears the appeals on point of law.[654] Besides this general modality of judicial review, an express jurisdiction is reserved to the Court of Justice in relation to the decisions of the Commission whereby it imposed penalties on the undertakings.[655]

Prohibitions of Art. 101(1) and the exemptions in the light of 101(3) stems directly from the objective of competition rules, that is the balance such as to apprehend the net competitive impact of agreements. That outstanding pro-competitive effect is judged by whether it '*contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit'*.[656] Normally, it is rational to survey the net outcome of the agreement or collective practice in question on a case-by-case basis. Nevertheless, certain type of agreements and concerted practices, due to their very nature and objective, are likely to render comparatively pro-competitive outcomes, despite there exists certain restrictive, thus-anticompetitive effect involved. To that end, such agreements and practices are typified and exempted, as a particular category, from the application of the prohibitions set out in Art. 101(1) under so-called block exemptions (BER). That is to say, the type of agreements and practices that *prima facie* benefits from the exemption envisaged by the Art. 101(3) are systematically regulated in several block exemption regulations.[657] Accordingly, when an agreement fulfils the conditions set out in a block exemption regulation, the agreement is automatically valid and enforceable. This modality is also in harmony with the principle of general freedom to conduct unless expressly

[652] KUR & DREIER *supra* note 35 at 381
[653] Articles 17-26 of Regulation 1/2003
[654] Articles 263 and 256(1) TFEU
[655] Article 31 of Regulation 1/2003
[656] As worded in Article 101(3)
[657] The burden of proving the infringement, by an agreement or concerted practice, of the prohibitions set out in Art. 101(1) rests with the party or the authority that contends the infringement. It, on the other hand, falls to the parties to the conduct or agreement seeking to benefit the exemption under Art. 101(3) to prove that the conditions in that provision are fulfilled. See: Art. 2 of Regulation 1/2003.

prohibited that has been adopted by the Reg. 1/2003.[658] Some of the BERs are of particular significance in the context of intellectual property commercialization and licensing agreements in particular.

### 1.4.3. Vertical Restraints Block Exemption Regulation (VBER)[659]

Exclusivity or selectiveness in distribution systems for the goods are liable to affect the trade between the Member States as well as intra-brand price competition. Nevertheless, as regards certain group of products, competition enhancing impact created by qualitative distribution systems is also recognized. To that end selective distribution agreements, are also subject to a net competitive impact test in order for their position under Art. 101(1) of the Treaty to be identified. Subject to the conditions set out in the VBER and in the case law of the ECJ, selective distribution systems may be permissible under Art. 101(1) or be exempted from the application of that article. Selective distribution agreements from the view point of competition rules and the context of VBER are analyzed in the ensuing section.

### 1.4.4. Technology Transfer Block Exemption Regulation (TTBER)[660]

Of particular importance in the context of intellectual property transactions, technology transfer agreements are covered by a specific block exemption within the meaning of Art. 101(3). Technology transfer is defined as the process of conveying results stemming from scientific and technological research to the market place and to wider society[661]; that is nearly synonym for intellectual property commercialization of which licensing agreements are the foremost instrument. Along the same lines the subject matter of technology transfer agreements coincides the licensing of technology rights. Such agreements are presumed to be pro-competitive and economically efficient at the outset, as they can reduce duplication of research and development,[662] as well as the costs incurred; in a way, preventing the scarce resources to be invested in re-inventing the existing technologies. And this pro-competitive characteristic is regarded to have outweighed any anti-competitive effect resultant from the restrictive nature

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[658] Art. 1(2) states "Agreements, decisions and concerted practices [...] which satisfy the conditions of Article [101(3)] of the Treaty shall not be prohibited, no prior decision to that effect being required. Thus, categorical conceptualization, under BERs, of what shall *prima facie* fulfill the said conditions complements the application of the general conduct of freedom as such.

[659] Regulation 330/2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices

[660] Regulation 316/2014 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of technology transfer agreements (TTBER)

[661] *What is technology transfer?*, EUROPEAN COMMISSION (26 Jan. 2021) https://knowledge4policy.ec.europa.eu/technology-transfer/what-technology-transfer_en

[662] TTBER, Recital (4)

of licensing agreements *vis-à-vis* the competitors. To that end agreements falling in the scope of TTBER are treated with a default presumption that they have complied with the general criteria of exemption set out in Art. 101(3), as long as the criteria set out in TTBER is complied with. The latter criteria include *inter alia* the observance of 'hardcore restrictions' and of the market share thresholds expressed in that Regulation. Finally, it is worth noting that the exceeding share does not necessarily mean that the agreement is straight forward caught by the prohibitions of Art 101(1); in that case a market effect analysis is needed.

For an initial consideration, the terminology employed in the Regulation proves significance in delineating its scope of application. Accordingly, 'technology rights' connotes know-how and (i)patents, (ii)utility models, (iii)design rights, (iv)topographies of semiconductor products, (v)supplementary protection certificates for medicinal products or other products for which such supplementary protection certificates may be obtained, (vi)plant breeder's certificates, (vii)software copyrights or a combination thereof.[663] On the contrary, the exemption does not apply to other intellectual property rights, say trademarks and copyrights (besides software) unless they are directly related to the production or sale of the goods that are actual subject matter of the agreement.[664] The concept of 'agreement', rather widely, covers the agreements in a statutory sense, decisions of an association of undertakings as well as concerted practices.[665] Finally 'technology transfer agreements' imply licensing agreements and assignments in relation to those technology rights, for the purpose of production of contract goods.[666] At any rate however, the parties are comprised of the licensor and the licensee (or assignor and assignee) and the sub-contractors of the latter. That is to say multilateral agreements and practices are off the scope of this particular exemption, thus they to be judged by the general prohibitions and exemption under Art. 101, in the light of individual nature of the agreement.

As for the substantive requirements of exemption, a dual approach has been adopted. Accordingly, if the parties to the agreement are competitors on the relevant technology and product market, the combined market share thereof cannot exceed 20% of that market; if, however, the contracting undertakings are non-competitors, the share of each undertaking cannot exceed 30% on its respective market.[667] Secondly, certain no-no clauses, i.e. hardcore

[663] TTBER, Art. 1(1)(b)
[664] Id. Art. 2(3)
[665] Id. Art. 1(1)(a)
[666] Id. Art. 1(1)(c)
[667] Id. Art. 3

restrictions, if contained, would push the agreement in question out of the application of the exemption. In the case of competing undertakings, restrictions on the ability of a party to determine its prices in relation to the sales of goods to third parties and those on the ability of using its own technology rights; limitation to output besides contract goods; certain types of market and customer allocation fall under hardcore restrictions.[668] Similar considerations, albeit more leniently, apply to non-competing undertakings. Accordingly, although the restriction on the ability of determining its own price - in the form of price fixing - is still among the hardcore restrictions, imposing a maximum sale price or recommending a sale price would not necessarily offend against that that hardcore restriction. Certain configurations of territorial restrictions in relation to the licensee`s sales of contract goods are also to be caught by the hardcore restrictions.[669] Furthermore, under the 'excluded restrictions' of the Regulation, any exclusive grant-back or assign-back dictate[670] on the licensee; or any obligation on a party not to challenge the validity of intellectual property rights which the other party holds in the Union, i.e. no-challenge clause, is also excluded from the scope of exemption.[671] In the latter case however, specific to exclusive licensing arrangements, the licensor can retain - or impose - the right to terminate the technology transfer agreement in the event that the licensee challenges the validity of the subjecting intellectual property right.

It is crucial to note that the agreements falling in the scope of the TTBER enjoy a default presumption of compatibility with the exemption criterion set out in Art. 101(3), hence steer clear the risk of being declared void as per Art. 101(1). This does not necessarily imply that the agreements outside the scope of the TTBER - such as those conceptually akin to the scope of the latter but, for instance, exceeding the market threshold - are straight forward caught by the competition rules. In such cases, first, the actual breach of competition rules and, second, the possibility of benefiting from general provision of exemption need to be ascertained on the basis of a market analysis as regards the effects of the agreement.

### 1.5. Ground Rule: IPRs are not anticompetitive *per se*

The action radius of competition rules is not necessarily confined to a typified activity or behavior. Simply put, they concern present and potential effect on intra-Union trade created

[668] Id. Art. 4(1)
[669] Id. Art. 4(2)
[670] Provisions which put the licensee under the obligation of granting an exclusive license or assigning to the licensor, partly or wholly, the improvements that he made to the technology that is subject of the initial license.
[671] TTBER, Art. 5

by dual or unilateral behavior, without focusing on the instrument thereof. In the same vein, it was made clear in an early stage that the competition rules of the Union do not attack intellectual property rights from the point of being 'territorial exclusivities'; nor do they take intellectual property law as an exclusive realm. They rather put IP rights on the target to the extent that they are instrument to anticompetitive collusions or behaviors that are liable to affect the trade between the Member States. From a purely formal viewpoint, the fact that IP rights are perhaps the most potent instruments for such purposes is a different issue.

To that end IP rights are not *per se* anticompetitive; the way in which they are used, however, may be so beyond the tolerance of competition rules.[672] This prospect was reflected by the early jurisprudence of the ECJ. As regards Art. 101, which concerns agreements and concerted practices, the Court in *Consten Grundig* considered a trademark transaction which was an auxiliary to a distribution agreement in order to control parallel imports as a *method* of eliminating any possible competition at the wholesale level.[673] On the account Art. 102 prohibiting the abuse of a dominant position, it was held in *Parke Davis* that for the application of that provision "three elements shall be present together: the existence of a dominant position, the abuse of this position and the possibility that trade between Member States may be affected thereby. *Although a patent confers on its holder a special protection at national level, it does not follow that the exercise of the rights thus conferred implies the presence together of all three elements in question.*"[674]

This follows that IPRs are not anticompetitive at the outset against the Art. 101 and 102 of the Treaty. In order to conclude the contrary, as Seville puts, "an extra element" revolving around the IP rights is needed.[675] That element is an agreement or a concerted practice liable to affect trade between the Member States by preventing, restricting or distorting the competition; or a dominant position which is abused such as to affect the trade between the Member States.

***Conclusions***

[672] This very cognition is the basis of existence/exercise dichotomy initially exhibited by the ECJ jurisprudence to reconcile internal market -representing the integration- and intellectual property rights -representing territoriality-.
[673] Joined Cases 56-58/64: Établissements Consten S.à.R.L. and Grundig-Verkaufs-GmbH v Commission, pp. 343,45 [Emphasis added]
[674] Case 24/67: Parke, Davis and Co. v Probel, pp. 72 [Emphasis added]; See also: C-40/70: Sirena S.r.l. v Eda S.r.l. and others, para. 16
[675] SEVILLE, *supra* note 122 at 510

Common objectives shared by the two bodies of law is of very little reconciliation when it comes to the practical anti-competitive potential of intellectual property laws. Originating from -or motivated by- these objectives, the two bodies of law are bound do diverge *vis-à-vis* the method each one follows. Competition laws are not concerned with creating a positive incentive for competition enhancing conduct by granting rewards or legal recognition (identity);[676] they instead react, in a prohibitory way, to anticompetitive conduct that are detrimental to consumer welfare. This is not the method intellectual property laws follow; it rather reacts positively. In that, as Pate articulated, it imparts affirmative rewards for an important type of pro-competitive behavior— innovation with the hope that such innovations will lead to increased competition and increased consumer welfare in the long run.[677] However, it is beyond doubt that the two bodies of law, on aforementioned accounts, neither fully complementary to one another nor fully hostile. On that note, the interrelation, could, more lucidly be expressed as teleologically harmonious but practically contradictable.

The interest of the intellectual property right holder, the subjective interest, quite explicitly faces objective or more general interests. As we summarized the first one was the interest of free movement; and secondly the interest of undistorted competition. It is not difficult to perceive in either of those occasions that the competing interests are reconciled in a manner in which the sacrifice is made from the monopolistic -bookish- prerogatives that are conferred by IPRs, for the interest of access / competition, which evidently is a greater interest in the particular realm of the European Internal market. However superfluous the doctrine of existence-and-exercise seemed at the outset, one could still be tempted to trace the pattern of that doctrine in the functioning of intellectual property rights in the internal market, in relation particularly to competition rules.

**2. Selective Distribution Systems**

Selective distribution systems (hereinafter SDS) enable the manufacturers to perpetuate a control over the supply chain of the goods, often, from the production all the way to end user. Systems as such are widely conceptualized as a structure *where the supplier undertakes to sell the contract goods or services, either directly or indirectly, only to distributors selected on the*

[676] R. Hewitt Pate*, Competition and Intellectual Property in the US: Licensing Freedom and the Limits of Antitrust* 50 (In CLAUS-DIETER EHLERMANN & ISABELA ATANASIU EDS., EUROPEAN COMPETITION LAW ANNUAL: 2005 THE INTERACTION BETWEEN COMPETITION LAW AND INTELLECTUAL PROPERTY LAW 49-58, Hart Publishing 2007)
[677] Id.

*basis of specified criteria and where these distributors undertake not to sell such goods or services to unauthorized distributors within the territory reserved by the supplier to operate that system*.[678] Inspiration behind the retainment of SDSs by the manufacturers of goods are a multitude. This, well possibly, ranges from the reasonably justifiable objectives of retaining the brand image -that has been eloquent created- throughout the entire supply chain or reducing, to some extent, the risk of counterfeit goods blending in the market to detriment of the brand image, all the way to particularly anticompetitive goal of keeping the third-party traders out of the business thus reducing intra-brand price competition created by such traders.

In the involvement of contrasting motives involved, a monotype treatment of selective distribution systems, particularly under competition rules, falls illogical and practically incorrect. However, the practical perils entailed in SDSs that are liable to affect the trade between Member States were, for the most part, addressed by the community exhaustion doctrine, as we have already pointed out that doctrine relates to continuous circulation of the goods once they are put on the market and is as only as effective as the goods are accessed by the third-party traders. SDSs however capable of (i) evading the exhaustion principle, by effect, to the extent that it places the goods out of the reach of third-party traders and (ii) enabling to the originator a proper ground for seeking remedy against its distributors on the basis of the underlying agreement (selective distribution agreement) when products have leaked to the outside the distribution chain even if the exhaustion has occurred (internal relations). Moreover, the arrangements of this sort typically envisage exclusive territorial areas or clusters of customers to each member of the distribution network and impose them not to supply to traders in that designated area and/or not to supply to the customers in the area of other distributor of the same network. Restraints to trade and competition follows from that prospect and it necessarily implies cross border effect between the Member States.[679] Thus given the inherent anticompetitive potential the agreement presenting the foundation of such distribution systems are also subject to competition rules, particularly Art.101(1).

Necessary to note at the outset, although intellectual property rights do not rest at the center of the conflict between SDS arrangements and competition rules, the said conflict and the reconciliation thereof retains clear connotations for further commercialization of trademarked goods. To that end, this represents the area wherein the collective interference of

[678] Regulation 330/2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices
[679] KUR, ET AL., *supra* note 14 at 469

exhaustion principle and competition rules is most significant. In this subsection we shall confine our interest, first, to general treatment of commercialization of goods through SDSs under competition rules and, secondly, to a contemporary issue thereunder, namely, restrictions to online sales imposed by selective distribution agreements.

### 2.1. General Treatment of SDSs Under Art. 101(1)

Early jurisprudence of the ECJ contributed to the general perception of the SDSs from the viewpoint of competition rules; imaginably, however, the area neither *ex ante* prompts competitive risk, nor is it unreservedly outside the provinces of competition rules.

As articulated in *Metro*, the conformity of SDSs with Art. 101(1), primarily, depends on resellers being chosen on the basis of objective criteria of a qualitative nature as regards the technical qualifications of the reseller and his staff and the suitability of his trading premises and that such conditions are laid down uniformly for all potential resellers and are not applied in a discriminatory fashion.[680] Further qualifying the compatibility analysis, in *L'Oréal v. De Nieuwe AMCK*, the Court expressed two additional focal points that needed to be taken into account. Firstly, it was necessary to observe whether the product in question necessitate a selective distribution system in order to preserve its quality and ensure its proper use and, secondly, it must be ensured that the selection criteria do not go beyond what is necessary.[681]

The subtext could be summarized as follows: brand image, inter alia that ascribed to trademark, deserves protection against potential degeneration created by the conditions in which subsequent traders market the goods in question. To that end the supplier has reasonable benefit in retaining a SDSs in order to reduce the aforesaid risk. On the counterbalance, this benefit can be upheld only to the extent that it does not function as a leverage for anticompetitive behavior such as to affect the trade between the Member States. It is for this very reason that the selection of resellers must be based on qualitative criteria - quality that aligns with the brand image and characteristics of the goods - instead of quantitative ones[682]; it must be *uniform, proportionate* to the that legitimate objective and applied in a *non-discriminatory* nature. Above all, the retainment of an SDS must be necessary in the first place.

[680] Case 26/76: Metro SB-Großmärkte GmbH & Co. KG v Commission of the European Communities, para. 20
[681] Case 31/80: NV L'Oréal and SA L'Oréal v PVBA "De Nieuwe AMCK", para. 16
[682] It was also noted by the Court, in L'Oréal, that implementation of quantitative criteria, in principle, brings the SDSs under the prohibition of Art. 101(1) [para. 17]. To that effect see also: Case 56/65: Société Technique Minière v. Maschinenbau Ulm

On the other hand, the higher quality, luxury or technology involved in the goods the more likely the brand image is harmed by traders marketing the goods under inferior conditions. Therefore, there presumably appears, on the part of the supplier, an enhanced necessity and justification for marketing via selective distribution. A similar consideration, contemplating the justification of that interest, was also articulated by the Court. Accordingly, there are legitimate requirements, such as the maintenance of a specialist trade capable of providing specific services as regards high-quality and high-technology products, which may justify a reduction of price competition in favor of competition relating to factors other than price.[683] Price competition weakened by the SDSs are counterbalanced by (qualitative) competition as regards the quality of the services supplied to customers, which can only be perpetuated through the adequate profit margins safeguarded by SDSs.[684] From a general stand point, this follows that price competition as a corollary to general (non-selective) distribution settings is not the only form of competition, nor is it the sole indicator of net competitive outcome. Quite the contrary, other pro-competitive outcomes which can solely be attained through SDSs might take precedence over mere price competition. Consequently, SDSs, to the extent that they are aimed at the attainment of a legitimate goal capable of improving competition in relation to factors other than price, are regarded as an element of competition which is in conformity with Art. 101(1) of the Treaty.[685] Should the conditions resultant from *Metro* and *L'Oréal* jurisprudence (hereinafter Metro criteria) be met, they are considered to have aim at that legitimate goal capable of improving competition.

The bottom line of the Court`s jurisprudence predicates the existence of a certain degree of competition-enhancing impact -even if that does not particularly relate to intra-brand price competition- rendered by SDSs, particularly as regards inter-brand competition, leading different brands of similar products to compete in quality. By the same token, conformity of SDSs with Art. 101(1) is necessarily judged by the net competitive effect of that particular system following a balance test on pro and anti-competitive implications. Crucial to note that observance of Metro criteria keeps the SDS in question out of the scope of Art. 101(1) at the outset, but not *vice versa*. The actual significance of the balancing test, thus, presents itself

[683] Case 107/82: AEG-Telefunken AG v Commission, para. 33
[684] Case 75/84: Metro SB-Großmärkte GmbH & Co. KG v Commission of the European Communities (Metro II), para. 45
Among these lines of argument there exists a subtle reference to the original motive of competition rules: the consumer welfare that is advanced through availability of high-quality products. Also insinuated, though intellectual property rights and trademarks in particular are not spoken out, an envisagement akin to incentive theory of intellectual property rights
[685] Case 107/82: AEG-Telefunken AG v Commission, para. 33

when the *Metro* criteria are failed, in which case, exemption is sought under Art. 101(3) on the basis of that test.

Against the judicial background thus illustrated, the balance test was subsequently[686] institutionalized by the Vertical Restraints Block Exemption Regulation (VBER) outlined below.

### 2.2. Vertical Restraints Block Exemption (VBER)[687]

Complementary to the judicial framework, VBER set out a formalistic modality for the application of exemptions [within the meaning of Art. 101(3)] in relation to distribution agreements. Distribution agreements whereby the market share of each party, individually, does not exceed 30% shall enjoy the block exemption;[688] this is regardless of whether the SDS is qualitative or quantitative in nature.[689] Below this threshold SDSs are entitled the exemption, despite some restrictions they entail, provided that active selling by the authorized distributors to each other and to end users is not restricted.[690] At any rate, restrictions contained in a selective distribution agreement must not encroach on 'hardcore restrictions' listed in the Regulation.[691] These include *inter alia* the restriction of the territory into which, or of the customers to whom, a buyer -party to the agreement- may sell the contract goods or services.[692] However in line with the very purpose of SDSs, restrictions may be imposed as regards (i) active sales[693] by a buyer party to the agreement to a territory or a customer group which has been allocated exclusively reserved to the supplier itself or to another buyer; (ii) sales by a wholesaler -party to the agreement- to end users, in order to allow the supplier to segregate the wholesale and retail level of trade; (iii) sales, at any level of trade, to unauthorized distributors located in any territory where the system is currently operated or where the supplier does not yet sell the products; (iv) sales, by a buyer party to the system, of the component of the goods

[686] Although by the time the Court`s jurisprudence took shape an antecedent of VBER, namely the Regulation 19/65/EEC was in place, the latter was of a legal-basis nature, authorizing the Commission to apply competition exemptions in respect to certain agreements. Synopsis of that Regulation did not practically reach far beyond the abstract idea of exempting certain distribution agreements from the scope of Art. 101(1), albeit without providing an actual framework.
[687] Regulation (EU) No 330/2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices (VBER)
[688] Id. Art. 3(1)
[689] Guidelines on Vertical Restraints (Guidelines), para. 176
[690] Id.
[691] These are listed out in Art. 4 of the VBER
[692] Id. Art. 4(b)
[693] Active and passive sales are defined as follows: (i) Active sales mean actively approaching individual customers by for instance direct mail, including the sending of unsolicited e-mails, or visits as well as by promotion and advertisements that is tailored for a particular group of customers. (ii) Passive sales connote responding to unsolicited orders from individual customers. See: Guidelines on Vertical Restraints, para. 51

to competitors.[694] As indicated above, it is also constitutes a breach of the hardcore restrictions when active or passive sales to end users by members of a selective distribution system operating at the retail level of trade are restricted.[695] Be that a hardcore restriction, however, the Regulation made a reservation for the possibility of prohibiting a member of the system from operating out of an unauthorized place of establishment. That is to say, it is permissible, for the purposes of block exemption, to stipulate in distribution agreement that the distributors only sell the goods from a place of establishment authorized by the manufacturer.[696] Correspondingly, restrictions can be imposed on the distributor`s ability to determine the location of his business premises, it may be, likewise, prevented from operating its business from different premises or from launching new premises in other locations.[697]

### 2.3. Restriction on Online Sales

The early cases discussed above related to classic market modalities hinged on brick-and-mortar businesses which, ever since, has lost an immense ground to digital shopping experience. So much so that, it is reported, in present days online shopping, in specific sectors, prevails over the habit of visiting physical stores; and overall ratio is rapidly nearing to a tie.[698] Selective distribution agreements pose unique challenges on the end of competition as far as digital platforms are at the stake.

According to the Regulation, members of an SDS must be free to sell the goods to the end users both actively and passively;[699] the contrary would offend against the hardcore restrictions enlisted. However, as noted above, active sales by the distributors to a particular area or a particular group of customers can be restricted insofar as those are exclusively appointed to another member of the distributions system.[700] On the other hand, sales on the internet are typically regarded as to fall in passive category.[701] Such follows that an outright ban on online sales, or a provision having that effect, stipulated by a distribution agreement

[694] VBER, Art. 4(b)(i),(ii),(iii),(iv)
[695] Id. Art. 4(c)
[696] Anne C. Witt, *Restrictions on the use of third-party platforms in selective distribution agreements for luxury goods*, 12(2-3) Eur. Compet. J. 435, 451 (2016)
[697] Guidelines, para. 57
[698] For a contemporary note, it is also observed these days, due to the COVID-19 global pandemic, the shopping habits in most traditional sectors, such as foodstuff, are also getting under digital influence.
[699] VBER, Art. 4(c)
[700] Id. Art. 4(b)(i)
[701] Guidelines, para. 52

would *prima facie* constitute a hardcore restraint[702], provided that the characteristics of the online sales do not assimilate to active sales.[703]

Much like the requirements stipulated *vis-à-vis* becoming a part of the SDS, the supplier might set quality standards for the use of the internet site to resell his goods.[704] Having recourse to the case law of the Court, SDSs are justified to the extent that they are proportionate and necessary, to preserve the brand image and quality; correspondingly, the requirements, in order to be justified, are supposed to present a qualitative nature. The problem arises where the requirements, in a qualitative disguise, have their objective in preventing the online sales of the goods which, in turn, implies a restriction, at very least, to passive sales. Therefore, applicability of the block exemption depends on the extent to which the conditions stipulated in distribution agreements imply restrictions to online sales and to which such restrictive stipulations conform with the legitimate objectives of SDSs. Jurisprudence of the ECJ has progressively shed light to this particular issue.

***Pierre Fabre Dermo-Cosmétique[705]***

The dispute originated from the distribution agreement framing the sales of cosmetic and personal care products supplied by Pierre Fabre. The said agreement stipulated that the sales must exclusively take place in a physical realm in the presence of a qualified pharmacist.[706] This, in effect, precluded all forms of selling on the internet as affirmed by the referring court.[707] In that regard, the question referred was whether a general and absolute ban on selling the goods to end users via the internet constituted a "hardcore" restriction of competition by object within the meaning of Art. 101(1) and whether that is not covered by the block exemption but is potentially eligible for an individual exemption within the meaning of Art. 101(3).[708]

In response, the ECJ reiterated the relevance of Metro criteria at the outset; accordingly, distribution agreements pose a restriction to competition, by their object, unless those criteria are met.[709] Also apparent from the wording of the Court, Pierre Fabre submitted, as the

[702] Giuseppe Colangelo & Valerio Torti*, Selective distribution and online marketplace restrictions under EU competition rules after Coty Prestige*, 14(1) Eur. Compet. J. 81, 88 (2018)
[703] Guidelines, para. 53, 57
[704] Id. para. 54
[705] Case C-439/09: Pierre Fabre Dermo-Cosmétique
[706] Id. para. 12, 13
[707] Id. para. 14
[708] Id. para, 31
[709] Id. para. 41

justification of that stipulation, the need to maintain the prestigious image of the products at issue.[710] Interestingly however, the Court did not hesitate concluding that the aim of maintaining a prestigious image is not a legitimate aim for restricting competition, therefore the contractual provision in question cannot avoid falling within the prohibition in Art. 101(1) of the Treaty.[711] Consequently, the contractual provision requiring sales of cosmetics and personal care products to be made in a physical space where a qualified pharmacist must be present, thus resulting in a ban on the use of the internet for those sales, amounts to a restriction by object within the meaning of that provision.[712]

Having thus established the applicability of Art. 101(1), the Court then went on to examine whether the provision should benefit from the block exemption. This consideration was particularly important in the present case since the national competition authority, which ordered Pierre Fabre *inter alia* to revoke the relevant contractual provision, had found that that provision constituted a hardcore restriction within the meaning of Art. 4(c) of VBER, therefore it cannot enjoy the block exemption. In opposition, Pierre Fabre asserted, the internet amounts to an unauthorized business place within the meaning of (the second part of)[713] that article, to that end, ban on the online sales was equivalent to a prohibition on operating out of an unauthorized establishment, which it was entitled to restrict.[714] The ECJ was not convinced by that argument. It found in that regard that a contractual clause prohibiting *de facto* online sales, at the very least, has as its object the restriction of passive sales to end users located outside the physical trading area of the relevant member of the selective distribution system;[715] it is therefore bluntly constituted a hardcore restriction pinned down by Art. 4(c) of the VBER. Moreover, the argument that internet implies an unauthorized place of establishment cannot be upheld insofar as the latter term covers only outlets where direct sales take place.[716] Thus the Court concluded that the block exemption was not applicable; however, exemption might be sought individually under Art. 101(3) the Treaty.

Arguably, the judgement of the Court arose a greater doubt than the clarity it rendered. Devoid of a context reference, observation of the Court *"The aim of maintaining a prestigious*

[710] Id. para. 45
[711] Id. para. 46
[712] Id. para. 47
[713] VBER, Art. 4(c): "…without prejudice to the possibility of prohibiting a member of the system from operating out of an unauthorised place of establishment"
[714] C-439/09: Pierre Fabre, para. 55
[715] Id. 54
[716] Id. para. 56

*image is not a legitimate aim for restricting competition…"* exhibited a fundamental controversy to its earlier case law where it had recognized the legitimate interest of the supplier in retaining SDS in order to preserve brand image and quality and, particularly, to ensure the proper use of the product. Moreover, due to the same observation, it has exhibited self-contradiction to the effect that it also cited the said earlier case law. Despite the foregoing, the benefit of the ruling resides at the clarity it yielded on the following points: (i) the internet cannot be regarded as an unauthorized business establishment and (ii) an absolutory ban on the online sales, even if that is not directly stipulated but flows from another contractual stipulation, precludes the application of the block exemption. Some of the doubts remained in the sequel of *Pierre Fabre* had yet to be obviated in the ensuing judgement of the Court in *Coty Germany*.

***Coty Germany***[717]

The dispute underlying the preliminary reference proceedings arose when Akzente - an authorized distributor of Coty products - refused signing the agreement amending their existing selective distribution agreement. The amendment included *inter alia* a provision prohibiting the distributors from selling the products on third party platforms (the platform at issue in that case was *Amazon*), confining the online sales to 'electronic shop window' of the authorized store. Coty, on that ground brought an action whereby it sought an order to prohibit Akzente from distributing through third party platforms. The German court in appellate hearing referred to the ECJ the following questions: (i) Do SDSs aimed at distribution of luxury goods and concerned ensuring "luxury image" for the goods constitute an aspect of competition that is compatible with Art. 101(1)? (ii) If so, is it permissible under that article to prohibit the use of third-party platforms for the sales of the goods? (iii) Does that prohibition amount to 'restriction to passive sales' within the meaning of Art. 4(c) of the VBER?

In answering to the first question, the ECJ reaffirmed the relevance of compliance with *Metro* criteria. Subject to fulfillment of that condition, the Court found the SDSs, whose objective is to preserve the luxury image of those goods, to be compatible with Article 101(1) of the Treaty.[718] Of particular importance in view of the ruling in *Pierre Fabre*, the Court held that seemingly contradicting findings in these two judgements as to the objective justifiability of the aim of 'maintaining prestigious image' were not in fact at odds. This was because the contexts in the two disputes were significantly different, and context matters in interpretation

[717] Case C-230/16: Coty Germany v. Parfümerie Akzente
[718] Id. para. 29

of the said objective. Two distinction were identified: (i) in Pierre Fabre, the goods at issue were cosmetic and body hygiene goods which are not necessarily luxury goods; (ii) the ban on online sales at that case was comprehensive (absolutory) in effect, whereas in the present case in concerns only third-party platforms. In other words, the considerations in *Pierre Fabre* solely related to the goods at issue; therefore, an implication for luxurious goods, such as in the present case, cannot be inferred from that judgement.[719]

As regards the second question, it was observed that the proportionality of the contractual provision prohibiting the sales on third-party websites must be determinant insofar as it is discernible from the material at hand that the provision is objective, uniform and non-discriminatory. The sales on third party websites where the supplier cannot check the conditions in which those goods are sold entails a risk of deterioration of the online presentation of those goods in a way as to harm their luxury image.[720] Proportionality was, according to the Court, fulfilled to the effect that the ban on online sales in the present case covered only those third-party platforms where the aforesaid risk existed,[721] thus not constituting an absolute ban on online sales. To that end, the prohibition does not go beyond what is necessary, therefore complying with *Metro* criteria and with Art. 101(1) of the Treaty.

The third question, sought to clarify whether the ban in question would constitute a hardcore restriction within Art.4(c) of VBER; in other words, it sought to clarify whether the ban amounted to a restriction to passive sales to end-users which in turn would render the block exemption inapplicable. Therefore, it only relates to the scenario where the referring court finds, in a substantive analysis, that one or more of the conditions are not satisfactorily met. This is because, the SDS would not fall foul of Art.101(1) in the first place if the conditions were met.

Interlinked to its observations as regards the other questions, the Court found that even if the contractual provision in question limits a specific kind of online sales, it does not amount an absolutory ban since it allows the authorized distributors to advertise on third-party platforms [722] and to use online search engines, hence customers are able to access the online offer of authorized distributors.[723] As a result, the Court held that it does not constitute a hardcore restriction within the context of the VBER when contractual provision in a selective

[719] Id. para. 32-35
[720] Id. para. 46
[721] Id. para. 52
[722] Perhaps advertisements such as to link the customers to the original website of the distributor.
[723] Coty Germany, para. 67

distribution agreement, for luxury goods, prohibits the distributors from selling the goods on third-party platforms. Result being that even if the agreement comes falls under Art. 101(1), that does not necessarily preclude the application of block exemption.

***Remarks***

The judgement is Coty evacuated a major part of the fallacies *Pierre Fabre* left behind. Moreover, it added an undeniable certainty to the application of VBER as regards the interpretation of hardcore restrictions therein. It follows from the holding that the breaking point in the assessment in both cases was 'proportionality' which, alongside the 'necessity' criterion, inherently warries according to the nature of the goods at issue. These are subjective elements to be assessed in each case. Beneath that subjective elements, however, a more objective set of reference points have been provided for by the Court by indicating two dichotomies. These are (i) luxury vs. non-luxury goods; (ii) outright ban vs. qualitative ban on online sales. The latter dichotomy retains a self-contained reasoning and arises very little ambiguity: a complete ban on the online sales, or other provisions *de facto* creating that result, is aimed at drying up that source therefore it cannot be deemed qualitative, thus falling under the scope of Art. 101(1) at the outset. Furthermore, an outright ban, even if *de facto*, shall also exclude the opportunity of benefiting from the block exemption insofar as in excludes passive sales to the end-users, hence constituting a hardcore restriction. Given the severity of the restriction, it is also unlikely to find an individual exemption under Art. 101(3).

The first dichotomy, however, is prone to exhibiting an obstacle to the comprehension of the Court`s jurisprudence in a linear manner. While it is eminent on the face of the early cases that 'the characteristics of the product in question should necessitate' an SDS (one of the *Metro* criteria), the sequel of *Coty* seemingly indicates that 'the characteristic of the product' for that purpose merely refers to character of luxury. On the other hand, it was made explicitly clear in *Coty* that the Court did not retract its view in *Pierre Fabre*, and distinguished it by the non-luxurious character of the goods involved. This naturally raises the question whether the Court`s conclusion would be the same if the ban in question on that judgement was not absolutory, or would the Court still take the same view on the sole ground that the goods are not classified as luxury products. The constant reference to the luxurious nature of the goods in *Coty* further intensifies the importance of that question. Secondly, one cannot help but wonder -if the element of luxury was the ultimate criterion as suggested in *Coty*- why the Court had not made a single reference to luxury/non-luxury distinction in *Pierre Fabre* judgement.

Finally, it is rather apparent that the judgement in Coty comes -comparatively- fortunate on the end of legal certainty, after the judgement in *Pierre Fabre*. This however does not change the reality that a question mark -a big one- was still left behind: Are SDSs that stipulate restrictions to online sales over third party platforms, only permissible to the extent that they relate to luxury products? And if so, what should be regarded as a luxury threshold? Does fame or a fine brand image, albeit not outstandingly luxurious, still justify SDSs online? Important to note that certain national courts had simultaneously taken initiative in interpreting that question. Particularly in *Nike* judgement (which was released before the Coty ruling), Dutch courts took the view that famous brand`s ban on sales on third party platform did not offend against Art. 101(1).[724] However the decision of Dutch courts is a representative of the proposition that the 'necessity' cannot rightly be judged merely by the luxury element, further and unified clarity on that point, on the EU level, is inherently needed.

### 3. Refusal to License and Abuse of Dominant Position: General Outlines

Exclusive rights on intellectual property protected subject matter have two foremost appearances: first, to solely exploit whatever is protected and, second, the discretion to determine who else can exploit. The latter, by extension connotes an exclusionary selection inferring the cluster of third parties who are denied exploiting the protected subject matter. The initial *obiter dictum* as to refusal to license, thus, shall be that it is of the very essence of intellectual property rights. This is irrebuttable from the perspective of intellectual property law; nonetheless a parallel concern is raised on the end of competition law, given that refusal to license is practically viable to lock down the competition (i) in the very market for the protected subject matter as well as (ii) in downstream markets whose activity is firmly interlinked to that upstream market.

The inherent unilateral character exhibited in the practice of refusal to license, categorically, brings the potential competition law concerns thereunder to the domain of the Art. 102. For that provision to come into play, in reliance to the early jurisprudence of the Court, what is primarily and cumulatively sought is for there to be a dominant position; that position being abused; and that abuse being such as to impact the trade between the Member States.[725] Reading together the imperatives above, it falls unlikely that the exercise of

[724] Jacopo Liguori, *Selective Distribution: The Consequences for Non-luxury Products*, MONDAQ (11 Dec. 2020) <https://www.mondaq.com/italy/antitrust-eu-competition-/1014736/selective-distribution-the-consequences-for-non-luxury-products>
[725] Case C-24/67: Parke, Davis and Co. v. Probel, pp.72

intellectual property rights, in form of excluding the others from exploitation thereof, insofar as such prerogative comprises the very purpose of that right is unlikely to amount to an abuse of dominant position. The question, thus, boils down to whether refusal to license is liable to constitute abuse of a dominant position and -if so- under what circumstances. The initial considerations and the ground rules on that matter have been laid in two cases that centered around design rights.

***Volvo v. Veng*[726] and *CICRA v. Renault*[727]:** Both cases before the ECJ concerned production and marketing of spare car parts, in particular body panels, without the authorization of the original car manufacturer who held design rights to the said parts. In the first case, Volvo refrained from licensing the respective design rights to Veng, even though the latter was willing to pay a reasonable royalty to the right holder for the articles sold under that license. Veng, in turn, asserted that Volvo abused its dominant position by refusing to license. In the second case, however, the third-party manufacturer had no such apparent intention to obtain a license; it rather sought annulment of the respective design rights which, in its opinion, covered a subject matter, i.e. car body parts, that had lacked any aesthetic value in order to be so protected. On that occasion it was the referring Italian court that doubted the compatibility of the exercise of design rights with Art. 102 (then Art. 86) given that such exercise enables the right holder to eliminate competition from third-party manufacturers of spare parts. However in the latter case the particular element of refusal to license did not present itself, the common question was whether the exercise of the rights in a way to exclude the others from producing and marketing protected substance would offend against Art. 102 to the effect that such exercise forecloses the competition.

The Court, having followed the same pattern in both cases, highlighted that the right to prevent third parties from manufacturing and selling or importing, without its consent, products incorporating the design constitutes the very subject-matter (or substance) of his exclusive right.[728] Neither the mere possession thereof would amount to a dominant position,[729] nor their exercise by default would pose an abuse of a dominant position. In particular case of refusal to license the Court found that an obligation imposed on the right holder to grant to third parties, even in return for a reasonable royalty, a license would lead to the right holder being deprived

[726] Case C-238/87: AB Volvo v Erik Veng (UK) Ltd
[727] Case C-53/87: CICRA and Others v Renault
[728] Volvo v. Veng, para. 8; CICRA v. Renault, para. 11
[729] CICRA v. Renault, para. 18

of the substance of his exclusive right, to that end refusal to grant such a license cannot *per se* constitute an abuse of a dominant position.[730]

An abuse for that purpose, however, requires an extra element that is found among the characteristics of a particular exercise of the rights. That element is broadly conceptualized by the Court as 'certain abusive conduct' that is engaged in by an undertaking in dominant position. Within the context of the cases at hand exemplified by an arbitrary refusal to supply spare parts to independent repairers, or setting up an unfair level of prices for the parts supplied, or discontinue the production of spare parts for a particular model despite that model of cars are widely being in circulation.[731] Abstractness of that concept is outright; in a way, it seems to plainly suggest that 'a refusal of license amounts to an abuse of a dominant position when it is abusive'. It is equally obvious that it is not intended to lay a general test. Its actual significance however is found in the distinguish thus put between the rule and exception.

*The ground rule and the exception:* Neither there is a built-in dominant position in the possession of intellectual property rights -a point which was already eminent from the earlier case law-, nor does the normal exercise thereof implies abuse of a dominant position. An extra element is sought: certain abusive conduct. The latter notion is further clarified by the subsequent judgements.

***Magill*[732]*:*** In Magill the ECJ has demonstrated over a positive example the circumstances whereunder 'certain abusive conduct' appears. Significantly, the Court has addressed these as 'exceptional circumstances' and somewhat systematically offered a set of objective criteria as opposed to indistinct notion of 'certain abusive conduct' which was previously inserted in *Volvo* and merely approximated to car spare parts in line with the context of the occasion.

Each one of British and Irish television broadcasters involved in the dispute (BBC, ITP and RTE)[733] individually published its own television guides which contained exclusively their own program schedule. These schedules were also provided to other media outlets, such as newspapers, on demand, however only on a daily basis and under strict license conditions.[734] The end result being that, at the time, there were no weekly television guides available on the

[730] Volvo v. Veng, para. 8
[731] Id. para. 9; CICRA v. Renault, para. 16
[732] Case C-241/91: Radio Telefis Eireann (RTE) and Independent Television Publications Ltd (ITP) v Commission of the European Communities (Magill)
[733] According to the finding of the referring court, the broadcasters had held significant access rate in respect to the countries concerned, that are Ireland and Northern Ireland. See. Id. para. 6
[734] Though in the observance of the license conditions the daily schedules were provided to those media outlets free of charge.

relevant market other than that of the broadcasters; and a full weekly guide to these major broadcasters` programs was hinged upon purchasing those three guides separately. It was Magill that attempted to offer such a weekly comprehensive television guide that was missing on the market. This attempt was interrupted by the injunctions obtained by those broadcasters who held copyrights in respect to their program schedules and refused licensing thereof.

The ECJ, for an initial matter, reiterated that mere ownership of an intellectual property right would not infer a dominant position; in contrast the dominant position in the present case was due to the fact that the broadcasters were the only source to obtain the information on their schedules and that their programs were received from the most households in the countries in question. Consequently, the broadcasters occupied a dominant position in the weekly television magazine market.[735] The actual crux of the case is found in the assessment of the existence of an abuse, which could only be possible under exceptional circumstances. In the present case such circumstances persisted insofar as:

— Refusal to provide the basic information in reliance to copyright protection ascribed thereto precluded the introduction of a *new product* that has a potential demand by consumers.
— There existed *no justification* for such refusal.
— Having refused licensing, the broadcasters exclusively reserved the secondary market of weekly television guides to themselves, *eliminating all competition* therein, since the information denied licensing is *indispensable for that market*.[736]

Albeit it is true that the assessment of exceptional circumstances cannot, at any event, loosen its ties with the case-specific circumstances, the fact remains that threefold approach above tends to offer a relatively objective and predictable framework of 'abusiveness' test to the effect that it is applicable notwithstanding the particular type of intellectual property right in question. This objectivity is also strengthened by the Court`s reasoning for 'new product' criterion, of which, the basis is indicated to be Art. 102(b) limiting the production and market to the detriment of consumers. However along the same lines it should be noted that the new product criterion also intrinsically brings along the necessity of a certain or, at least, determinable novelty threshold which could be particularly problematic in respect to copyright protected works. It is of a little surprise that the latter point kept being a matter of uncertainty

[735] Magill, para. 47
[736] Id. para. 54-56 (emphasis added)

over the subsequent cases and to the present. What surfaces with utmost clarity following the judgement in Magill is the imperative that a dominant position does not put the undertaking under a default obligation of licensing their intellectual property rights; for such an imposition the actual abuse manipulated by intellectual property rights -which occurs under exceptional circumstances- and effect thereof on trade between the Member States are also sought.

***IMS Health*[737]:** The protected subject matter at issue was so called 'the 1860 brick structure' used for a systematic fragmentation of geographic area on the basis of regional pharmaceutical sales data in Germany. Each brick under that system corresponded to a designated geographic area, taking into account several factors such as the municipal boundaries, postcodes, population density, transport networks and the location of pharmacies and medical practitioners.[738] The structure was developed by IMS, a data provider, whose business definition is to collect pharmaceutical sales data and providing thereof to its clients (*inter alia* pharmaceutical laboratories) after having formatted that raw data in accordance with the brick structure. This setting has gradually become a normal industry standard as the clients of IMS set up their information and distribution systems accordingly.[739] The structure was protectable under German copyright law to the effect that it represented a data basis for the purpose of that law.[740] The dispute arose when a competitor (NDC) ended up providing data to its clients using the same brick structure -due to the resistance from the sector towards other data settings- and subsequently faced copyright claim brought by IMS.

The ECJ essentially adhered to the three-factor approach (*i.* refusal is preventing the emergence of a new product for which there is a potential consumer demand; *ii.* that it is unjustified; *iii*. excludes any competition on a secondary market) that it had previously established in *Magill*. Yet, the additional comprehension the Court offered in relation to the notion of 'exceptional circumstances' in line with those factors was not trivial. The Court disposed of any doubt as to the configuration of the three criteria sufficiently forming an abuse. Accordingly, cumulative fulfillment of those conditions is sufficient to find a refusal to license abusive.[741] Semantic range of 'sufficient' on the other hand conveys, that the referred criteria was not an exclusive standard in observation of an abuse. Existence of an abuse embedded in

[737] Case C-418/01 IMS Health GmbH & Co. OHG v NDC Health GmbH & Co. KG
[738] Id. para. 4
[739] Id. para. 6
[740] This point was affirmed by the Frankfurt Higher Regional Court (*Oberlandesgericht Frankfurt am Main*). To that effect, see para. Id. para. 10
[741] Id. para. 38

a refusal to license could be discerned from other factors that are not necessarily in that list; and they are likely be regarded on a case-by-case basis. Crucially, the Court also made an input towards the understanding of new product criterion, albeit implying a rather modest novelty threshold. Accordingly, the undertaking seeking a license should *"not intend to limit itself essentially to duplicating the goods or services already offered on the secondary market by the owner of the intellectual property right"*.[742] Arguably therefore, the new product threshold seems to have been lowered; practically anything beyond a duplication might suffice. This point calls on serious suspicion in the present case *vis-à-vis* whether what NDC intended to offer would satisfy the new product criterion. Unfortunately, this point exceeded the review of the ECJ given that the occasion was a preliminary ruling rather than an appeal to the decision of the Commission and the General Court regarding the underlying competition proceedings.

***Microsoft*:** The long story of antitrust action against Microsoft is traced back to the complaint filed before the Commission by a competitor, Sun Microsystems, in 1998. At the center of the complaint laid, *inter alia*, Microsoft`s refusal to provide interoperability information, that was taken to be prerequisite for Sun to create a work group operating system -rival to that of Microsoft- that could seamlessly operate with Microsoft`s Windows operating systems. Sun contended that, having refused to provide that information, Microsoft abused its dominant position within the meaning of Art. 102. In the sequel of the proceedings initiated[743], the Commission found the practice in question to fall foul of Art. 102 and, besides imposing a great deal of fine, it ordered Microsoft to cease withholding interoperability information.[744] The Commission in its assessment took the express view that the exceptional circumstances constituting the abuse is not necessarily confined to the cumulative criteria the ECJ has set out over its case law; these criteria did not comprise an exhaustive checklist.[745] However, according to *IMS Health* ruling, fulfillment of these criteria 'suffices' for finding exceptional circumstances, the existence of the latter is also distilled from a comprehensive analysis of the entirety of the circumstances surrounding the refusal.[746] This view nevertheless did not hold the Commission back from relying on these criteria as a framework in the assessment of the issue at hand.[747]

[742] Id. para. 49
[743] Case COMP/C-3/37.792 — Microsoft
[744] Id. para. 999
[745] Id. para. 555
[746] Id. para. 558
[747] For the conclusion (i) on 'indispensability' and 'risk of eliminating competition', see: Id. para. 692; (ii) on 'new product' criterion, see: para. 700,701 [Important though the Commission having relied on Art. 102(b)

Microsoft subsequently sought annulment, before the General Court (GC), of the Commission`s decision.[748] The General Court, in essence, found all the findings of the Commission regarding the substance of the case fully accurate; certain points are however worth an additional highlight. For a formal classification of the subject matter at hand, the GC proceeded upon the assumption that the protocols in question, or the interoperability information pertaining to those protocols, are covered by intellectual property rights.[749] Indispensability criterion, according to the GC was dully assessed by the Commission insofar as, given the overall dominance of Windows operating system, non-Windows work group server operating systems cannot continue to be marketed unless they are fully aligned with Windows.[750] As regards the risk of eliminating the competition, it held that neither a demonstration of full elimination of the competition in the relevant market, nor waiting until competitors are actually eliminated would be necessary.[751] What is necessary for that purpose is (i) the 'risk' of eliminating the competition instead of actual elimination thereof; (ii) effective competition being eliminated (or risked) instead of the entire competition.[752] If the contrary was true, Microsoft would have steered cleared that criterion with approx. 10% window it left to the competitors, despite itself holding 90% of the market. Consequently, the Commission had sufficiently substantiated the risk of eliminating effective condition by the refusal to license at issue. On the end of objective justification of the refusal, the GC dismissed Microsoft`s argument that the objective justification must be found in the potential lack of incentive to further create intellectual properties which would be the corollary of its discretion to refuse licensing being taken away. The GC rejected that argument by simply observing that, if that argument was true, it would mean that refusal to license would never constitute an abuse of dominant position.[753]

On a more striking note, the GC held that the appearance of a new product, being a component of *Magill* and *IMS Health* criteria cannot be regarded as the sole parameter of determining whether a refusal to license is viable to prejudice to consumers within the meaning of Art. 102, particularly on the face of the fact that the said provision covers the limitations not

stretched the new product requirement in a way to cover technical development]; (iii) on 'refusal not being objectively justifiable', see: Id. para. 712

[748] Case T-201/04, Microsoft v. Commission

[749] Id. para. 289

[750] Id. para. 388

[751] Id. para. 561-563

[752] Id.

[753] Id. para. 690

only to production but also technical development.[754] The latter was true in the context of the present case insofar as there was no new product at issue whose appearance was hindered;[755] but rather the secrecy of interoperability information did not permit development of a competing product which might or might not wind up being novel. The GC brought this requirement to a more abstract level, such as to cover the hinderance to technical development, on the assumption that the products of competitors would be forced, by the competitive climate, to differentiate from that of Microsoft -hence attain novelty- once the interoperability information is provided and competing products are produced.[756] In the light of foregoing proposition it is noted that, among the conditions under which abuse can be found, 'new product' criterion is of an inferior importance *vis-à-vis* other criteria concerning indispensability and objective justifiability of refusal.[757] Finally on a general note, it also follows from the text of the GC`s decision that the Commission`s hypothesis of non-exclusive checklist as regards *Magill* and *IMS Health* criteria has been implicitly affirmed. That is to say, even if the conditions envisaged in the said decisions are partly missing, 'exceptional circumstances' might nevertheless be deduced from the particular circumstances that surround the refusal at issue.[758]

***Summary***

Initial consideration must be paid to the legal basis: along the general lines of Art. 102, as explicated in *Parke Davies,* what`s cumulatively sought: i) a dominant position; ii) abuse thereof; iii) that abuse being capable of impeding the trade. The latter systematic reveals the general rule and exception: neither IPRs per se confer a dominant position nor their exercise is normally abusive. The basic teaching as regards the interface of refusal to license with the abuse of dominant position within the meaning of Art. 102 is, therefore, that such an abuse is not a default presumption, but rather an exceptional occurrence. The criteria developed in Magill and IMS health relates only to the postulate (ii), i.e. abuse due to the exercise of IPR which can exist only under exceptional circumstances. However through subsequent progress it was made equally clear, perhaps as a reflection of the Commission pressure, exceptional circumstances are not confined to that list established in Magill and IMS. A holistic analysis

[754] Id. para. 647
[755] KUR, ET AL., *supra* note 14 at 479
[756] Case T-201/04, Microsoft v. Commission para. 58
[757] KUR, ET AL., *supra* note 14 at 479
[758] The GC proceeded with the express proclaim that "If [the Court] finds that one or more of those circumstances are absent [it will] proceed to assess the particular circumstances invoked by the Commission." See: para. 336 of the GC judgement on Microsoft

of the circumstances of each case might just as well infer exceptional circumstances; moreover, there is virtually no limit to what can be construed as exceptional. With that the European Commission added a flexible instrument to its toolbox which it eagerly utilizes for substantiating abuse of a dominant position. It is without doubt, the holders of intellectual property rights might have felt a step closer to a general obligation to license.

Such a turn of events is most apparent in the subtext of the holding in *Microsoft.* However comprehensive the GC`s judgement was in Microsoft, it is difficult to assert that it made a contribution to legal certainty as to the treatment of refusal to license under Art. 102; if anything, it seems to have, to some level, compromised the existing legal certainty therein. This is firstly because the GC broadened the scope 'new product' criterion; accordingly, when the refusal represents a limitation of technical development, whether or not a new product will be yielded is of no importance. Particular peril entailed is that the notion of technical development is far less containable than that of new product. Therefore, it is a good fit for a wide interpretation, enriching the portfolio situations where the intellectual property right holder faces the obligation to license. Secondly, the judgement rendered a prospect where the Commission would not even have to stick with the Magill and IMS criteria in the first place so as to find an abuse of dominant position, as long as it can extract some 'exceptional circumstances' from overall circumstances surrounding each case.

## 4.Standard Essential Patents (SEPs) and Abusive of Dominant Position by Bringing Proceedings in Relation to SEPs

Along the general lines the objective of standardization is the identification of voluntary technical or quality specifications with which current or future products, production processes or services may comply.[759] Therefore, it has its effect in setting up the base on a cumulatively higher level so that it will provide an ever-enhancing standard of products to consumers and provide the actors of technology market with a gradually advancing step stone in order for them to build up on the existing technology and developing them beyond the state of art. Along the same lines, with dynamic standardization in place, standards within which the intra-sector competition transpires are gradually set higher. It also ensures interoperability, compatibility of products and services to be offered. In either case the watermark of consumer benefit can be identified in the background.

[759] Recital 1, Regulation (EU) No 1025/2012 on European standardisation.

Despite the voluntary basis in principle, however, in most cases, entry in the market is dependent on compliance with *de facto* or the legally or administratively set technology standards. The competition concern arises where the technical or quality specifications subject to (or achievement thereof strictly depends on) other`s technology rights, in particular patents, hence standard essential patents (SEPs). In that case not only will the entry of the other competitors into the relevant market be dependent on the SEP holder`s will to license, but also, in the absence of that will, any *de facto* entry will intrinsically infer an infringement of SEPs to the effect that its use is the only way to commence in production. Consequently, if the right holder to a standard essential technology is to invoke his rights, no other undertaking can even contemplate existing in the market. This prospect clear reflects the 'indispensability' factor that is involved when refusal to license in general is to be assessed from the view point of abusive conduct.

Centered around this major competition concern, standard setting organizations (SSOs) seek to implement intellectual property licensing frameworks in order to facilitate the compliance with technical standard and specifications in different sectors without the prospective market participants being encumbered by the intellectual property rights that protect the required standard. In that, they require the owners of SEPs commit, beforehand, to license their technology on fair, reasonable, and non-discriminatory terms, also known as FRAND terms.[760]In European experience standards are adopted by the European Telecommunication Standards Institute (ETSI) in information and communication technologies sector; by CENELEX in electrotechnical engineering field and by CEN in remaining sectors.[761] Approaching the matter of access to standard essential technology, European Standardization Organizations commonly impose the obligation on the patent holders (i) to declare any patent or patent application which, according to her/his own judgment, may be considered as an essential patent and to (ii) to commit to making available their patents on FRAND terms.[762]

Among the rationale of standard setting efficiency is of outstanding importance. This entails two dimensions: (i) Following from the general merits of standardization, it seeks out

[760] Hanna Stakheyeva, *Intellectual Property and Competition Law: Understanding the Interplay*, 3, 5 (In ASHISH BHARADWAJ ET AL. eds., MULTI-DIMENSIONAL APPROACHES TOWARDS NEW TECHNOLOGY, Springer 2018)
[761] Legal basis and principle of operation thereof are found at Regulation (EU) No 1025/2012 on European standardisation.
[762] Section 3 and 7.3 of CEN-CENELEC Guidelines (Guide 8) for Implementation of the Common Policy on Patents; Section 4 and 6 of ETSI Intellectual Property Rights Policy

efficiency in resource allocation in research and development in technology sector in order to rid the participants of the burden of inventing around the other's technologies in order merely to access the basic (or default) of the state of art; (ii) efficiency also covers a legal/administrative area in the light of the refusal to license discussions we had above to the effect that SEP schemes, in a way, already presupposes the existence of indispensability criterion in respect to a SEP, drying up at the source the risk that the holder of a standard technology may foreclose the market entry of the others in an abusive way, thus intending to free the competitors from the burden of bringing proceedings under Art. 102 in order to access that indispensable element. Yet, intellectual property policies of these organizations do not set out an autonomous licensing system or substantive licensing terms[763], nor do they revoke the patent holder`s discretion to refuse licensing.

***SEP-based Injunctions***

Against that background a trending issue has been whether it constitutes an abuse of dominant position within the meaning of Art. 102 when the holder of a SEP seeks injunctive relief on the basis of that patent against the other party who is willing to take a license on FRAND terms. Although, at the outset, it is difficult to envisage why seeking injunctive relief *per se* should necessarily imply abuse of dominant position, the nuance, that erupts the possibility of abuse, resides at the commitment that the SEP holder made, on the face of the standardization organizations, to grant licenses on FRAND terms. Commitment as such creates *ex ante* legitimate expectation on the end of the potential licensee that a license can be obtained on reasonable terms. This question was at the focus of *Motorola* and *Samsung* cases whereby the Commission commenced in Art. 102 proceeding against those two telecommunication companies on the basis of the injunctive reliefs that they sought against Apple who sought licensing under FRAND terms.

***Motorola***[764]: The alleged infringement in that case transpired from Motorola's pursuit of enforcement of injunctions against a willing licensee, Apple, in relation to a SEP held by the former and that was necessary for implementation for 2G technology. The relevant patent was previously declared essential and the holder committed to the ETSI to license thereof on

[763] Quite the contrary, within the framework of ETSI, these matters are explicitly excluded. In that regard following reservation were made by the ETSI Guide on Intellectual Property Rights (IPRs): (1.1) "In complying with the Policy, the Technical Bodies should not become involved in legal discussion on IPR matters.";
(4.1) "Specific licensing terms and negotiations are commercial issues between the companies and shall not be addressed within ETSI."
[764] Case AT.39985 — Motorola

FRAND terms. With the launch of its first mobile phone in 2007, Apple had implemented 2G standards, subsequently facing injunction proceedings by Motorola. In the course of proceedings Apple made six successive licensing offers to Motorola; however, the latter rejected these offers and chose to pursue the injunction proceedings then set about enforcing the injunction granted, thus pressing severe conditions of settlement agreement to Apple.[765]

In the assessment of that conduct, it was acknowledged by the Commission that seeking and enforcement of an injunction by a patent holder is normally a legitimate course of action; crucially, however, this consideration does not apply to the cases where injunctions are sought and enforced on the basis of SEPs.[766] It also enunciated that 'exceptional circumstances' in the present case followed from the standardization process and Motorola`s commitment to license on FRAND terms.[767] Implicitly, therefore, SEPs within the meaning of SSOs retain built in exceptional circumstances, for the purpose of assessing the infringement of Art.102 by refusal, unless there exist an objective justification. Subsequently the Commission pointed out that an objective justification is not present either where there is a willing licensee;[768] and Apple`s willingness was found apparent from various configurations of licensing offer it submitted. Consequently, in the presence of the potential licensee`s willingness[769] substantiated by the offers it made, there was no need on the end of Motorola to enforce the injunction in order to be appropriately remunerated for the use of its SEPs.[770] To that end Motorola abused its dominant position. Nonetheless, the Commission took the discretion to not impose any fines on Motorola given the lack of a prior consensus on legality of SEP-based injunctions under Art. 102.

Important to note that the Commission has also exemplified certain cases where the enforcement of the injunction could have been justified. This included where (i) the potential licensee is in financial distress and thus unable to pay its debts; (ii) its assets are located in jurisdictions that do not provide for adequate means of enforcement of damages or (iii) it is not

[765] Apple (i) accepted a clause whereby Motorola would be entitled to terminate the agreement in case Apple challenged the validity of any of the licensed SEPs (the so-called 'termination clause'); and (ii) explicitly acknowledged the infringement of the licensed SEPs by all of its devices, including an Apple device that it claimed was not infringing those SEPs., see: Summary of Commission Decision in Case AT.39985 — Motorola, para. 16
[766] Summary of Commission Decision in Case AT.39985 — Motorola, para. 18
[767] Id. para. 21
[768] Id. para. 22
[769] That willingness was substantiated (i) by repetitive licensing offers to the SEP holder and (ii) by the fact that the potential licensee, in those offers, gave the SEP holder the right to set the royalties according to its equitable discretion and according to FRAND principles and proposed a full judicial review of the amount of FRAND royalties, whereby both parties could submit their own evaluations, calculations and reasoning for consideration to the court.
[770] Summary of Commission Decision on Case AT.39985 — Motorola, para. 24

willing to abide FRAND terms to the detriment of SEP holder.[771] Clear from the wording, the list is not intended to be exhaustive but merely exemplary. Arguably, from a general perspective, it is well possible to discern that the list covers other scenarios where objective justification to refusal exists; for which a case-by-case analysis is needed. Nevertheless, in specific case of SEPs where a prior commitment to license and intrinsic 'indispensability' exist, objective justification is likely to occur in rare cases.

***Samsung***[772]: With a different standard essential technology at stake, similar facts were topical in proceedings against Samsung. The latter had committed before ETSI to license its SEP pertaining to UMTS technology on FRAND terms, nevertheless, subsequently sought injunction against Apple who implemented that technology by using Samsung`s patent. Upon the initiation of investigations by the Commission, Samsung responded by offering legally binding commitments. Accordingly, it undertook not to seek injunction for infringement of its SEPs, for a five-year period, against the potential licensees that agrees to (and abides by) a preset licensing framework.[773] The envisaged framework set out *inter alia* a negotiation period up to 12 months and a third-party determination (such as arbitration and the like) of licensing terms on the axis of FRAND in the event that the parties came to no agreement by the end of that 12 months period.[774] Having accepted Samsung`s commitments, the Commission discharged the proceedings.

***Huawei v. ZTE***[775]: Subsequently the ECJ had a say on the issue, offering further clarification, in essence, on whether seeking injunction on the basis of a SEP unconditionally offends against Art.102. In the underlying dispute, negotiations between Huawei, the holder of the SEP in relation to 'Long Term Evolution' standard, and ZTE, the potential licensee, turned out fruitless. The latter nevertheless proceeded with production and marketing of mobile devices incorporating Huawei`s SEP without paying a royalty. Huawei in response brought infringement proceedings before German courts, whereby it also sought an injunction *inter alia* prohibiting the infringement, recall of products and an award of damages.

The Court of Justice followed a top-down methodology in establishing the peculiarity of SEPs. It initially reiterated the earlier case law on refusal to license which in a nutshell set out that abuse of dominant position by the exercise of intellectual property rights is possible

[771] Id. para. 23
[772] Case AT.39939 — Samsung
[773] Summary of Commission Decision on Case AT.39939 — Samsung, para. 15,18
[774] Id. para. 16
[775] C-170/13: Huawei Technologies Co. Ltd v ZTE Corp.

only under exceptional circumstances.[776] Next, it went on to uphold the Commission`s finding in *Motorola* and *Samsung* that the case of SEPs should be distinguished from the general consideration of refusal to license. Accordingly, the distinction was contained in two characteristics: (i) SEPs are indispensable by nature[777]; (ii) the SEP status is a result of declaration of willingness on FRAND terms, thus arising 'legitimate expectations' on the end of potential licensees.[778] Result of that distinguish is while refusal to license in general only *exceptionally* infringes Art. 102, should the refusal concern a SEPs, infringement of that article is *principally* present.

Up until this point the Court`s consideration suggests that refusal to license a SEP *per se* sufficiently poses exceptional circumstances, and principally violates Art. 102. Regard, however, must be had to the fact that, in the present dispute, no straight-forward refusal to license was at issue; the problem rather originated from the disagreement of the parties on the meaning of FRAND terms, in particular the amount of royalty the latter terms imply. On the other hand, it is acknowledged that a patent holder`s right to seek injunction against a *prima facie* infringement is of the substance of that right and enshrined *inter alia* in Article 47 of the Charter of Fundamental Rights, i.e. the right to an effective remedy and to fair trial. This right, the Court emphasized, is not striped off even if the patent in question is declared a SEP, and thus subjected to the commitment of licensing under FRAND terms.[779] Clearly, therefore, a concurrent reading of these considerations indicates the necessity of a balance between the legitimate expectation of third parties and the SEP holder`s right to enforce his intellectual property rights. Accordingly, the patent holder cannot be deemed to have given up on his right to seek injunction, he can nevertheless be obliged to comply with specific requirements before bringing actions against alleged infringers for a prohibitory injunction or for the recall of products.[780]

Those requirements were mapped out by the Court much like a set of procedural guidelines to negotiations, in compliance of which, pursuit of an injunctive relief does not give rise to an infringement of Art. 102. Accordingly:

— The holder of SEP, prior to bringing action, must notify the alleged infringer by specifying the way in which the patent rights were infringed.

[776] Id. para. 47
[777] Id. para. 52
[778] Id. para. 53
[779] Id. 59
[780] Id.

— Should the alleged infringer express willingness to take a license, the holder of the SEP must make a specific, written offer specifying the royalty and the way in which it is to be calculated.
— The alleged infringer, on his part, must respond to that offer diligently and in good faith, without resorting to delaying tactics.
— Should the response of alleged infringer to that offer be negative, he must then make a counter offer with the same qualifications.
— Finally, if the alleged infringer continues using the SEP`s teaching before a license is concluded, he must then provide adequate security after his counter-offer has been rejected.[781]

This follows that the SEP holder can seek injunctive relief without infringing Art. 102 only when he took the steps falling to his part and the alleged infringer continues using the patented technology without complying with above obligations falling on him.

***Concluding Remarks***

Both the GC and ECJ has unmistakably repeated as of early judgements that neither the possession of intellectual property rights as such amount to a dominant position, nor is their exercise intrinsically abusive. Along the same lines, the prerogative to refrain from licensing as a part of the exercise of rights, is not abusive in itself. Nevertheless, the contrary may be the case, subject to exceptional circumstances. It was established with utmost clarity that, in identifying such circumstances, different considerations apply to SEPs on one hand and non-essential patents on the other hand. In the context of non-essential patents (as well as design rights and copyright) exceptional circumstances (without prejudice to other circumstances which may be regarded exceptional) flow from (i) indispensability of the protected subject matter to carrying out activity in the relevant sector; (ii) the fact that refusal to license is liable to hinder the emergence of a new product and (iii) it is likely to exclude all the competition in a secondary market.[782]

As far as SEPs concerned, presumptions are quite the opposite. Exceptional circumstances by default present themselves in that context, particularly because their indispensability is institutionally affirmed and the availability of licenses on FRAND terms is promised at the outset. Against that background, refusal to license a SEP, principally,

[781] Id. para. 61-67
[782] IMS Health, para. 37

constitutes abuse of a dominant position whereas non-essential patents are necessarily tasted against exceptional circumstances. More eccentrically, even the exercise of the right to seek injunction, the fundamental way of enforcing the rights, is likely to give a rise to abuse of dominant position. And this is, in the sequel of the Court`s judgement, not an exceptional case. That is to say, in order to avoid infringing Art. 102 merely by seeking injunctive relief, the right holder is encumbered to follow a rather comprehensive set of requirements.

It is difficult to digest this imperative, especially on the face of the fact that injunctive relief, by its nature, is not an instrument of rendering a conclusive decision but rather a procedural measure. Moreover, the Court deepens the confusion by establishing, in essence, that commencement of proceedings for seeking an award of damages for the past uses or for rendering an account thereof would is not subject to those criteria; such actions cannot constitute an abuse of dominant position.[783] Question thus arises: While the lawsuit seeking an award for damages *per se* is not an abuse of dominant position, why should injunctive relief request -as a part of that lawsuit- constitute such an abuse? The answer resides at the substance of the measures granted as injunctive relief: recall of the products; their definite removal from the channels of commerce or their destruction.[784] In the most lenient scenario, injunctive relief entails the withdrawal of the products of alleged infringer from the market for a definite period, practically eliminating the market presence of the alleged infringer in reliance to the SEP. This prospect is quite a threat on the end of the alleged infringer, especially when the latter is a willing potential licensee. The Commission notes in this regard that a recourse to injunctions may unduly distort FRAND licensing negotiations and allow SEP holders to charge royalties or impose licensing terms which a licensee would not agree to absent the threat of having its products excluded from the market.[785] While the latter postulate offers a comprehendible reasoning, it is unfortunate that the ECJ has omitted making a reference to the reason why seeking injunctive relief connotes abuse; without any reasoning, it simply held it does. In our opinion, even if the Court had simply reproduced the latter expression of the Commission, the decision in *Huawei* could have exhibited a stronger integrity.

On a final note, it needs to be noted that the questions arising from the intersection of SEP licensing and the competition rules of the Union hardly seems to have exhausted. In a

[783] Huawei, para. 76
[784] Article 10(1) of Directive 2004/48/EC of the European Parliament and of the Council of 29 April 2004 on the enforcement of intellectual-property rights
[785] EUROPEAN COMMISSION PRESS RELEASE: Antitrust: Commission consults on commitments offered by Samsung Electronics regarding use of standard essential patents, Brussels, 17 October 2013, pp. 2

recent referral for preliminary ruling, Düsseldorf Regional Court hearing a dispute between Nokia and Daimler,[786] as regards one of the SEPs of the former, directed important question that seek further clarity following the judgement in Huawei. The referring court, among the other things, asks whether the holder of the SEP has the discretion to decide at which degree of the production chain it shall license its standard patent to the licensee who may not be the actual implementer of that technology. Secondly, the German court seeks further clarification of the procedural map[787] that was drawn in the Huawei judgement, particularly regarding the assessment of the 'willingness' of the infringer, through these formal steps, as a potential licensee. On that note, it is reasonable to expect a brighter light to be shed on SEP licensing and competition rules by the Court in the near future, possibly in a way to contribute to the future of this popular intersection that the actors of innovative industries frequently stop by.

## 5. Patent Pooling and Competition Rules

Perhaps one of the most compact definitions suggested for the patent pooling defines it as an arrangement among multiple patent owners to aggregate their patents.[788] Aggregations as such might take a broad scale of organizational forms, ranging from simple contractual arrangements to creation of joint ventures specifically for this purpose or entrusting the transactions concerning the pooled technology to an independent entity. Among the different shapes patent pooling arrangement can take, the common ground is a multitude of patent owners mutually agreeing to waive exclusive rights under their respective patents so as to grant each other rights and/or to grant jointly rights to third parties under their patents.[789] As already stated above, besides pro-competitive rationale and actual impact as such, intellectual property rights naturally entail anti-competitive connotations. Based on the latter aspect, simple logic dictates that the wider the portfolio of exclusive rights gets, the greater exclusionary, thus, anticompetitive effect surfaces. Therefore, it is presumable that centralization of patens is keen to create oligopolies, thus foreclosing the market to potential entrants. And this potential is precursor to an apparent tension between such arrangements and the competition rules.

Much like anti-competitive effects deepen, pro-competitive ones are likewise intensified through collaboration. This point is well reflected by the Commission. On the

[786] The request is registered under the case number C-182/21: Nokia Technologies.
[787] See *supra* note 777
[788] Robert P. Merges, *Institutions for intellectual property transactions: the case of patent pools*, University of California at Berkeley Working Paper 1, 10 (1999)
[789] Roger B. Andewelt, *Analysis of Patent Pools Under the Antitrust Laws*, 53 Antitrust LJ 611, 611 (1984)

account of pro-competitive effects, it observed that technology pooling can produce positive effect *in particular by reducing transaction costs and by setting a limit on cumulative royalties to avoid double marginalization. The creation of a pool allows for one-stop licensing of the technologies covered by the pool. This is particularly important in sectors where intellectual property rights are prevalent and licenses need to be obtained from a significant number of licensors in order to operate on the market.*[790] On the other hand anti-competitive effects are also substantial. According to the Commission *[t]he creation of a technology pool necessarily implies joint selling of the pooled technologies, which in the case of pools composed solely or predominantly of substitute technologies amounts to a price fixing cartel. Moreover, in addition to reducing competition between the parties, technology pools may also, in particular when they support an industry standard or establish a de facto industry standard, result in a reduction of innovation by foreclosing alternative technologies.*[791] Quite naturally, therefore, technology pools represent yet another area where the pro-competitive and anticompetitive impacts need to be put on a scale in order for a compatibility analysis *vis-à-vis* competition rules to be possible.

As we have already indicated, patent pooling by definition entails (i) collective exploitation of a huge portfolio of technologies (ii) collective exclusion of the third parties, thus, strengthening the pool member's competitive advantage. Two different aspects of technology pools emphasized: firstly, the relationship between the pool members in the form of cross-licensing; and secondly the licensing out the pooled technology to third parties: both might have reverberations on competition. Nevertheless, on both occasions the essence (or the nature) of relationship is an actual licensing transaction; to that end, much like any other licensing agreement that has its objective at technology transfer, they would likely be covered TTBER.[792]

Above the internal and external licenses, however, the distinguish needs to be well emphasized that the agreement forming establishing the patent pools and those concluding

[790] Communication from the Commission — Guidelines on the application of Article 101 of the Treaty on the Functioning of the European Union to technology transfer agreements (2014/C 89/03), para. 245
[791] Id. para. 246
[792] The TTBER principally applies only to the arrangements between two undertakings and the licenses concluded within the context of technology pools usually involve more than two parties; this may lead to the conclusion that intra-pool licenses, insofar as they are concluded between multiple parties, fall outside the scope of the TTBER. Crucial to note that this conclusion is not necessarily correct. On this very matter the Commission has already established that the TTBER shall be applied, by analogy, to licensing arrangements that involved multiple parties as long as they are contextually of the same nature as those covered by the TTBER. See: Communication from the Commission — Guidelines on the application of Article 101 of the Treaty on the Functioning of the European Union to technology transfer agreements (2014/C 89/03), para. 57

licenses within the context of that pool are subject to different considerations of competition law. While the former is likely be covered by the TTBER, the latter is not so covered for two reasons. Firstly, such agreements *per se* do not entail any substantive licensing arrangement; but they rather resemble a framework agreement preceding the actual licensing transactions, in particular addressing the formation organization and operation of the pool envisaged. And secondly, pooling arrangements are multilateral thus expressly excluded from the scope of the TTBER at the outset. Their assessment is therefore subject to general rules under Art. 101 (1)-(3). A detailed guideline for that assessment with a specific focus of technology pooling, including the conditions in which such technology pools are deemed to refuge to a 'safe harbor' from the application of Art. 101(1), has been provided in the Commission`s communication (the Guidelines).[793]

Accordingly, various factors are to be taken into consideration when surveying the competitive risk and efficiencies stemming from the very formation, organization and operation of the pools. These include *inter alia* the transparency of the pool creation process, the selection and nature of the pooled technologies, involvement of impartial experts in the creation and operation.[794] Transparency for that purpose is mainly judged by the openness of the pool to the interested prospective participants; should the openness be ensured, it is more likely that the technologies to be let into the pool are selected on a more objective basis, such as price/quality ratio.[795] A greater importance in this assessment however is ascribed to the nature of the technologies involved in the pool. The nature thereof is potentially identified by two sets of dichotomies: (i) they might be either technological complements or substitutes to one another; (ii) they might, on an individual basis, be either an essential or non-essential technology. Along these lines, the initial observation is that the competition-enhancing impact appears more significantly where (i) the technologies in the pool are more complementary to each other than substitutes; and where (ii) they are essential rather than non-essential. It is not necessarily difficult to read the logic behind such an observation: When the technologies in the pool are substitutes (instead of complements) all the alternatives on the end of the licensee will have gathered in the pool much like a monopoly, thus the licensee will not be able to benefit the competition between the substitute technologies. Secondly in that case, the foremost pro-competitive significance of pooling will practically be undermined to the effect that it will

[793] Communication from the Commission — Guidelines on the application of Article 101 of the Treaty on the Functioning of the European Union to technology transfer agreements (2014/C 89/03)
[794] Id. para. 248
[795] Id. para. 249

cease being a one-stop-shop for the licensee. In the case of pooling of non-essential technologies, it is yet again likely that one-stop-shop function will be pointless given that the pool cannot, in that case, offer the licensee the main technology in that realm but only the auxiliaries. It is noted by the Commission that in such cases the inclusion of significant substitute technologies in the pool will generally be deemed to constitute a violation of Art. 101(1) of the Treaty; and for the same reasons it is not likely to benefit from the exemption set out in Art. 101(3).[796] However, the above referred point is only one aspect of the assessment. The Commission has provided for a checklist of conditions in the fulfillment of which, pooling *per se* and licensing out from that poll shall not be caught by the Art.101(1). Accordingly, fulfillment of the following creates a 'safe harbor':

> (a) participation in the pool creation process is open to all interested technology rights owners;
>
> (b) sufficient safeguards are adopted to ensure that only essential technologies (which therefore necessarily are also complements) are pooled;
>
> (c) sufficient safeguards are adopted to ensure that exchange of sensitive information (such as pricing and output data) is restricted to what is necessary for the creation and operation of the pool;
>
> (d) the pooled technologies are licensed into the pool on a non-exclusive basis;
>
> (e) the pooled technologies are licensed out to all potential licensees on FRAND (fair, reasonable and non-discriminatory) terms;
>
> (f) the parties contributing technology to the pool and the licensees are free to challenge the validity and the essentiality of the pooled technologies, and;
>
> (g) the parties contributing technology to the pool and the licensee remain free to develop competing products and technology.[797]

Finally, it is necessary to note that the failure of the formation, organization or operation of the pool with the 'safe harbor' conditions does not imply a clear-cut breach of Art. 101(1). In those cases, the legitimacy of the technology pool under that provision is to be deduced from

[796] Id. para. 255
[797] Id. para. 261

a comparative assessment of pro and anti-competitive effects flowing from its actual structure, particularly the net competitive effect thereof.

### 6. Reverse Payment (Pay-For-Delay) and Co-Promotion Agreements

Like most types of intellectual property rights, privileges conferred to its holder by patents are limited by time. At the end of the protection term or when the patents are declared invalid, the exclusivities which normally belonged to the patent holder cease existing and the underlying inventions falls into public domain.[798] Naturally on those occasions, any undertaking might enter the relevant market without being hindered by patent exclusivity and without having to invest resources in R&D. Equally clear against this background, the patent holder has obvious benefit in *de facto* exceeding the duration of those privileges to the longest possible extent so as to assure continuous high profit margin. This equilibrium is of utmost significance in pharmaceutical market where the patent holder (the originator) tends to prolong the exclusivity on marketing the product for as long as possible, even beyond the regular patent protection term; and the generic producers seek to remove that exclusivity so as to enter the market, often judicially challenging the validity of patents for doing so. Alternatively, the latter will straight forward commence in marketing its generic products and subsequently challenge the validity of patent over the course of infringement proceeding that the patent holder will bring.[799] Although any attempt of generic entry during the protection term is, at the outset, liable to infringe the patent rights, the outcome of a potential infringement proceeding *vis-à-vis* the existence of an actual infringement and the validity of patent is not always absolutely foreseeable. On that account regard must be had to the fact that pharmaceuticals are often protected under a multitude of patents; that include *inter alia* the active ingredients patents (primary patent) and manufacturing process (secondary patent). Particularly when the main patent has elapsed and the product is being protected by other secondary patents or when there exists certain doubt as to the merits of the existing patent *vis-à-vis* patentability criteria, the generic producer is likely to have strong case. Correspondingly, it is discerned by the patent holder that there is a likelihood 'greater than zero' that the generic product may not infringe the patent rights[800] or the said patent -if challenged- is likely to be invalidated.

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[798] This is in fact viewed as very objective of patent laws: protection to incentivize the perpetual advancement of technology; limited term of protection for the interest of public vis-à-vis access to that technology

[799] SEVILLE, *supra* note 122 at 527

[800] Frank Maier-Rigaud, et al., *Reverse payments: An EU and US perspective* 35,43 (In PABLO FIGUEROA & ALEJANDRO GUERRERO EDS., EU LAW OF COMPETITION AND TRADE IN THE PHARMACEUTICAL SECTOR, Edward Elgar Publishing 2019)

However normally patent settlement agreements connote a more cost efficient and rapid resolution to patent disputes compared to court proceedings, in such cases as described above they tend to commit to the objective of compromising the competition. In that, the originator typically commits to paying a sum (or another value transfer) as consideration for the generic producer for delaying the introduction of the generic product or staying out of the market at all.[801] The end result being the payment by the originator to the competitor, as opposed to a payment by the infringer to the right holder which normally would be the case. Competition is thus preemptively bought off through a 'reverse payment'. Agreements of that nature might be greatly beneficial on the end of both parties, given the price gap between the original patented medicine and the generic one (reportedly approximating 90% in respect to the UK)[802], the potential competitor (introducer of the generic product) might make even greater profit through the settlement than it can make from marketing the generic product. Add to the major litigation costs that are bound to be spent when judicial remedies are sought. That very price gap, which would otherwise be of benefit to consumers, is keen to raise competition law concerns, at very least from the perspective of the objectives of the competition rules as the consumers are deprived of significantly cheaper access to the generic products when their entry into the market is prevented or delayed at the source. More tangibly, there exists an agreement between two market participants and its purpose is to delay or prevent the entry of an alternative, hence competing product, into market; thus, application of Art. 101 likely be attracted.

Settlements of this sort were first brought under a competition-related scrutiny by the Commission with the initiation of a sector inquiry 2008[803] and the competitive risk entailed as such has been incrementally acknowledged ever since.[804] Against that background, the Commission subsequently set about investigating individual patent settlement agreements some of which faced antitrust proceedings and resultant fines on the grounds of violating the competition rules. Some significant examples are summarized below.

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[801] Pablo Ibáñez Colomo, *The legal status of pay-for-delay agreements in EU competition law: Generics (Paroxetine)*, 57(6) Common Mkt. L. Rev. 1933,1933 (2020)

[802] Based on a case specific empirical evidence, it was noted that "[P]rices of generic citalopram dropped on average by 90% in the UK compared to Lundbeck's previous price level once wide-spread generic market entry took place following the discontinuation of the agreements." See. EUROPEAN COMMISSION PRESS RELEASE (Brussels, 19 June 2013) Antitrust: Commission fines Lundbeck and other pharma companies for delaying market entry of generic medicines.

[803] Commission Decision of 15 January 2008 initiating an inquiry into the pharmaceutical sector pursuant to Article 17 of Council Regulation (EC) No 1/2003 (Case No COMP/D2/39.514)

[804] For the history of patent settlement monitoring, including the resultant annual reports, see: https://ec.europa.eu/competition/sectors/pharmaceuticals/inquiry/

In *Lundbeck*[805] the Commission has imposed a total fine over €90 million on *Lundbeck* group, the originator of the antidepressant citalopram; and over €50 million on four generic manufacturers (MercK, Arrow, Alpharma, Ranbaxy). Antitrust proceedings concerned six agreements that were concluded between Lundbeck and the generic competitors and executed between 2002 and 2003. Prior to the conclusion of the agreements, the main patent covering the active ingredient had expired, however Lundbeck was in possession of several process patents. Among the generic competitors one had already commenced in selling its own generic citalopram, and the others were in preparation for doing so. Lundbeck, thereupon, claimed infringement of one or more of its process patents and the generic undertakings, in turn, asserted non-infringement or invalidity of the patents invoked.[806] However before any ruling was delivered on those proceedings, the Lundbeck and the four undertakings concluded the said settlement agreements, whereby the latter agreed not to enter the market in return for substantial payments and other inducements from Lundbeck amounting to tens of millions of euros.[807] The originator, in addition to a significant lump sum payment, had purchased readily manufactured generic medication for the sole purpose of destroying them.[808] Commission held, in the light of these facts, that the agreements, by object, constituted restrictions of competition, hence infringing Art. 101.[809]

The following year, the proceedings in *Servier*[810] culminated in a tremendous fine of €427.7 million. The background facts are boiled down to the intent of Servier, the originator of the cardiovascular medicine Perindopril, to *de facto* prolong its exclusivity over the said product upon the expiry of the primary patent. On that occasion, the portfolio of activities that came under proceedings was however richer: Firstly, there were five patent settlement agreements between Servier and the generic manufactures; and secondly, a technology acquisition by Servier for the purpose of delaying the generic entry. The settlement agreements involved value transfers to the generic competitors in form of lump sum payments ranging from €15,6 to 40 million as well as market sharing with duopoly in certain Member States.[811] As regards the technology acquisition, the originator bought from Azad technology (which was

[805] Case AT.39226 - Lundbeck
[806] Summary of Commission Decision of 19 June 2013 relating to a proceeding under Article 101 of the Treaty on the Functioning of the European Union and Article 53 of the EEA Agreement (Case AT.39226 — Lundbeck), para. 4
[807] EUROPEAN COMMISSION PRESS RELEASE (Brussels, 19 June 2013) Antitrust: Commission fines Lundbeck and other pharma companies for delaying market entry of generic medicines.
[808] Id.
[809] Summary of Commission Decision (Case AT.39226 — Lundbeck), para. 16
[810] Case AT.39612 — Perindopril (Servier)
[811] Summary of Commission Decision (Case AT.39612 — Perindopril (Servier)), para. 7

not covered by the remainder of Servier`s process patents) to produce perindopril, thus removing a close source of competition out of the market.[812] The Commission established that the settlement agreements had their object at restricting the competition within the meaning of Art. 101(1); moreover, the originator was found to exhibit a linear and consistent course of action by buying out potential competitive technology in addition to the settlement agreements. Therefore, the combination of those six transactions, to the effect that it formed an exclusionary strategy, also amounted to a single and continuous abuse of dominant position within the meaning of Art. 102.[813]

More recently, the proceedings in *Cephalon*[814] likewise resulted in imposition of a total fine of €60.5 million on the undertakings, namely Teva and Cephalon, on the grounds of an infringement of Art. 101. The main dispute underlying the settlement centered around Modafinil, a drug for sleep disorder, originated by Cephalon. The latter`s patent to the active ingredient, however, had expired, it nevertheless retained some secondary patents. Teva, on the other hand, held its own patents relating to modafinil's production process, was ready to enter the modafinil market with its own generic version, and it had even started selling its generic in the UK. Upon the legal action brought by Cephalon on the grounds of infringement of its secondary patens, the parties come to agree on a patent settlement whereby Teva undertook, in return of some cash payment and other commercial benefits,[815] not to enter the market with the generic version of the former`s product. The Commission has found that none of the said value transfers would have happened if it was not for the settlement agreement and that Cephalon thus eliminated Teva -the most advanced generic competitor- as a competitor, availing himself the opportunity of maintaining high prices despite its expired primary patent.[816]

In *Fentanyl*[817] infringement of patent rights was not topical, correspondingly no patent settlement arrangement was of issue. However, the agreement between the parties Johnson & Johnson (the originator of fentanyl) and Novartis (the potential competitor) foresaw that the latter would refrain from marketing its generic version of product fentanyl in the Netherlands,

[812] Id. para. 5
[813] Id. para. 24-28
[814] Case AT.39686 — Modafinil (Cephalon)
[815] These reportedly included a distribution agreement, the acquisition of a license on certain Teva patents by Cephalon, purchases of raw materials from Teva, and granting by Cephalon of access to clinical data that were highly valuable to Teva for a different medicine. See: *Press release 26 November 2020, Antitrust: Commission fines Teva and Cephalon €60.5 million for delaying entry of cheaper generic medicine*, EUROPEAN COMMISSION (27 Jan. 2021) https://ec.europa.eu/commission/presscorner/detail/en/ip_20_2220
[816] Id.; Note that the decision of the Commission is not available for the time being.
[817] Case AT.39685 - Fentanyl

despite the latter being on verge of doing so.[818] The originator would in turn commit to monthly payments to Novartis for as long as the latter stays out of competition. The amount paid within the framework is observed to be excessively higher than what could the generic drug could have made if it entered the market.[819] Consequently the Commission found that the agreement the agreement was designated to ensure that the generic product was kept out of the market, thus infringing Art. 101 by object.

***Three-factor Assessment***

The assessment of the Commission took as a general basis the structure of the market and the economic and legal context of the agreements. In particular -as it was also commonly applied to the cases above-, so as to identify whether each agreement retained the potential to restrict competition by its very nature the following shall be taken into account:

— Whether the generic undertaking and the originator undertaking were at least potential competitors;
— Whether the generic undertaking committed itself in the agreement to limit, for the duration of the agreement, its independent efforts to enter one or more EEA markets with generic product;
— Whether the agreement was related to a transfer of value from the originator undertaking which substantially reduced the incentives of the generic undertaking to independently pursue its efforts to enter one or more EEA markets with generic product.[820]

It is also worth noting that, the General Court of the EU, in appellate review of *Lundbeck* and *Servier*, upheld the respective decisions of Commission where the above three-factor approach had been employed.[821] While the said decisions of the General Court have been further appealed to the Court of Justice on point of law and both are pending for the time being[822], the Court of Justice recently had the occasion to rule on pay-for-delay agreements for

[818] Id. para. 238
[819] Id. para. 220
[820] Case AT.39226 – Lundbeck, para. 661; Case AT.39612 — Perindopril (Servier), para. 1154; Case AT.39685 – Fentanyl, para. 219
[821] See: T-472/13 - Lundbeck v Commission and T-691/14 - Servier and Others v Commission. Noteworthy though, while the former has been fully upheld by the General Court, the latter has been partially upheld. The General Court, in the latter case, has not observed an extra element inducing an abuse of dominant position; thus the agreements were found to infringe Art. 101 only. See, to that effect, the operative part of the judgement as published in the Official Journal of the European Union (OJ C 462, 22.12.2014)
[822] C-591/16 P - Lundbeck v Commission; C-201/19 P - Servier and Others v Commission

the first time, in relation, however, to antitrust proceedings that were held by the national competition authority of the UK (CMA).

***Case C-307/18: Generics UK v. CMA[823]***

The proceedings concerned three agreement which were entered into by GSK, the originator of Paroxetine on the one hand, and three generic companies that were contemplating entering in the market for that product upon the expiry of GSK`s main ingredient patent on the other hand. The agreements, among other things, secured discharge of ongoing litigations in return for various forms of value transfer from the originator to the generic companies; that included promotional allowance, annual marketing allowance etc. on top of the purchase of already produced generic stocks.[824] The agreements were found to infringe the national equivalent of Art. 101 and 102 of TFEU, hence bringing the CMA to impose fines which subsequently were appealed to before the national court. In answering to a wide array of questions placed by the Competition Appeal Tribunal, the ECJ has shed light to certain concepts in assessment of pay-for-delay arrangement.

As regards the notion of potential competition the Court found that the originator -whose primary patent (that of active ingredient) has fallen to the public domain but process patents exist- and the generic producer are potential competitors, given that the latter has a firm intention and an inherent ability to enter the market, and that market entry does not meet barriers to entry that are insurmountable.[825] Secondly, in the existence of such a potential competition, the agreements made between the originator and generic manufacturers -whereby the former undertakes a value transfer in return for the latter`s promise not to enter market or to challenge the validity of the remainder of the patents- amounts to an agreement which has as its object the prevention, restriction or distortion of competition if that value transfer can have no explanation other than the commercial interest of the parties to the agreement not to engage in competition on the merit.[826] This connotes 'restriction by object' within the meaning of Art. 101(1). On the other hand, 'competition by effect' is judged by the existence of the appreciable potential or real effects on competition created by the agreement in question. Moreover, that analysis necessarily takes into consideration the economic and legal context in which the involved undertakings operate; it likewise regards the real conditions and the

[823] C-307/18: Generics (UK) Ltd and Others v Competition and Markets Authority (CMA)
[824] Id. para. 12-14
[825] Id. para. 58
[826] Id. para. 111

structure of the market in question.[827] However the ECJ established that, finding 'restriction by effect' does not depend on finding -should the agreement be absent- either the manufacturer would probably have been successful in the proceedings relating to the process patent at issue, or the parties to that agreement would probably have concluded a less restrictive settlement agreement.[828] That is to say, the assessment of 'restriction by effect' is to be made with reference to the prospect of competition where the agreement did not exist; though the hypothetical scenarios beyond that -such as the potential sequel of the litigation or possibility of a less restrictive agreement- are irrelevant.

It needs to be finally noted that both Lundbeck and Servier were appealed to the CJEU on point of law and pending for the time being. In the light of Generics UK decision of the CJEU it is plausible that those two decisions were also to be upheld by the CJEU, add to the Opinion of AG Kokott in Lundbeck in that direction.[829] [830]

[827] Id. para. 116
[828] Id. para. 122
[829] AG Kokott in her opinion suggests the dismissal of Lundbeck`s application, thus upholding the Commission`s and the General Court`s views. See: OPINION OF ADVOCATE GENERAL KOKOTT delivered on 4 June 2020 Case C-591/16 P, para. 250
[830] It is important to note that after the initial submission of this dissertation, the Court of Justice delivered its decision on the said case in the same direction as speculated above. The Court of Justice upheld the General Court`s decision (T-472/13 - Lundbeck v Commission) for the most part (except for certain procedural aspect which did not substantively factor into the final holding); thus, retaining the status quo that the earlier line of cases, discussed above, had established. See: Case C-591/16 P: H. Lundbeck A/S and Lundbeck Ltd v. European Commission

# CONCLUSIONS

Despite the *acquis communautaire* often exclusively regards the initial and subsequent marketing of incorporeal goods as commercialization, we have been able to demonstrate that commercialization is so much more than this undertaking. Both the activities of bringing intellectual properties into market in form of goods and services and the acts of manipulating (facilitating or impeding) the latter with the use - or negligence to use - of intellectual property rights provide "intellectual property commercialization" with its actual scope. We were also able to pinpoint that the inherent tension between the territorial IP protection and free movement and undistorted competition (the last two combined amounts to the essence of the EU Internal market) is not institutional or passive but rather practically eminent when intellectual property is thus commercialized. Mitigation of that practical tension being an existential matter for the market integration and, in turn, for the entire European integration, we had asserted that the Construction of European IP law was compelled by that the said practical – and political – necessities that surfaced on the axis of what we conceptualized as intellectual property commercialization. We correspondingly purported that the particular intellectual property law and practice emerging from this equilibrium is the "law of economic policy" rather than that of prevailing IP law interest, inevitably rendering the law as an instrument of actualizing pre-determined economic and political mindset. We purported a law of the said nature is highly fluid interrelated to the advancements and progress in technology and creative industries resulting not only in novel types of subject matter but also in novel ways of commercializing thereof. Against that dynamic background, we asserted, the EU law and acquis on intellectual property that we can speak of today has emerged from, shaped by and will, in the future, follow the pattern dictated by the reconciliation of the existing and prospective clash between the fundaments of the internal market and IP protection as reverberates on intra-Union commerce. Thus, the boundaries of intellectual property commercialization, from a legal perspective, dynamically indexed to the realization and preservation of the Internal Market; in particular delineated by the free movement principle and the competition rules of the Union. We finally asserted that the legal comprehension and certainty which, at the outset, were sacrificed to policy objective and accompanying purposive approach gradually gain emphasis, though this tendency is not equally linear in each particular area particularly those which are newly emerging.

The dissertation has tested these propositions on many fronts including – but not limited to – the making of the law and practice, its interpretation and the chronology of the turns and twists in the latter from an analytic perspective that exposes legal versus political reasoning. Both individual focal points that we have analyzed - fragmentally - and the collective reading of these undertakings -holistically- corroborated to the aforesaid initial presumptions we posed, thus offering conclusive and palpable outcomes as regards the undertaking of the study as we shall outline below.

Intellectual property commercialization is a vast continuum that involves all the stages, at least from the product development to the post-sale matters and the different stages of the continuum is characterized by different disciplines. Business aspects and economics of intellectual property often swallow the legal aspects of commercialization thereof. This is because of inherent commercial worth and potential of IPRs on the one hand and that of corporeal goods and services on the other hand. Quite cyclical this commercial worth is owed to the legal identity afforded to intellectual property, which, in a way, institutionalizes and objectifies certain outcomes of human intellect: that is the intellectual property rights. Moreover, we submitted that the commercialization, albeit holistically revolves around the aim of bringing the intellectual property to the market, is not confined to trade of corporeal goods and services. As much as the goods and services that incorporate the intellectual property (IP) the rights protecting thereof (IPR) are commercially worthwhile and are in themselves property objects. To that end, we drew upon the divisibility (separability) of the IPRs and products/services incorporated the rights. Result being that, two ubiquitous modalities of commercialization emerge: (i) commercialization of corporeal goods and services; (ii) commercialization of the rights, as a property object through assignment and licensing or their specific configurations. As the said continuum is not a one-stop-shop, from a commercial perspective, these two types are inextricably linked.

It is through these commercialization acts that the commercial potential of IP rights creates their actual commercial reverberations. However, the first premise to be remembered as regards these reverberations, as we discussed at length, is that the IP rights are, by default, territorial exclusivities. As we explicated at length, the grand total of territoriality and exclusivity, practically, equals to the segregation of national markets, in respect to goods and services incorporate the IPRs, to the detriment of cross-border trade and creation of competitive advantage to the right holder which - if unrestrained - is keen to create monopolies and distort the competitive environment. Applying this general pattern to the particular realm of European

Internal Market, we concluded that the said reverberations are intolerable insofar as the free movement between the Member States and principle of undistorted competition are the integrating and constitutive factors of the Internal Market which, in turn, is the medium of the entire European Integration all along. To that end reconciliation of territorial exclusivities with the free movement principle on the one hand and with the competition rules on the other hand, was a matter of integration. As we demonstrated, this necessity presented itself on the axis of what we conceptualized as intellectual property commercialization. On that note one might go as far as suggesting that the actual conflict area is not the clash of intellectual property protection and free movement principle but, rather, that of intellectual property commercialization, by way of commerce in corporeal goods, and free movement. Yet the primary law of the Union offered very little substantive material to the help of reconciliation of this tension; putting the European judiciary in charge of finding a way around this dilemma.

As we demonstrated, the early responses in that regard, namely the doctrines of existence & exercise of rights and specific subject matter, were a plain reflection of the policy intend such as to defend the functioning of the Internal Market at the sacrifice of intellectual property protection, though devoid of legal merit, certainty and reasoning. However, they were of certain importance to the extent that their objective, conceivable, was to respond as quickly and effectively as possible to the organic conflict between territorial rights and the principle of free movement; and that they, particularly the specific subject matter doctrine, paved the road to the regional exhaustion principle and defined its scope, albeit purposively.

As of *Deutsche Grammophon* the jurisprudence of the ECJ added a valuable and eventual device into its toolbox, which it has utilized ever-since in eliminating the intra-Union commercial reverberations of IP territoriality. To that end, the exhaustion doctrine become one of the foundations for the single European market,[831] hence more of a policy tool than a legal instrument. Over the course of half a century the formulation of that device has been almost identically preserved: once the goods put on the market in one of the Member States by or with the consent of the right holder, further commercialization thereof cannot be opposed to in respect to the Union. The three factors spelled out in that formulation - which more or less uniformly laid out by the jurisprudence of the Court and later by the secondary law of the Union - had to correspond to all scenarios where an IP protected subject matter is commercialized in

[831] Trevor Cook, *Exhaustion–a Casualty of the Borderless Digital Era* 357 (In LIONEL BENTLY ET AL. EDS., GLOBAL COPYRIGHT: THREE HUNDRED YEARS SINCE THE STATUTE OF ANNE, FROM 1709 TO CYBERSPACE, 354-366, Edward Elgar Publishing 2010)

the form of goods. Naturally, each factor was and is in need of interpretative profundity and we fragmentally examined.

The act of putting on the market as the first element of exhaustion, as we discussed, has been surrounded by a terminological scatter; moreover, the complexity of multilayer supply and distribution chains makes it more difficult to pinpoint the precise act of putting on the market. At any rate however, it is intended connote the initial marketing by the right holder and, when determining the exhaustion, the disposal of goods by the right holder in a way to transfer the tittle to a third part is necessarily sought. On the contrary mere importation of goods into the EEA by the right holder with a view to selling them in the Internal Market does not exhaust his rights insofar as such importation itself does not allow the right holder to realize the economic value of trademark. Likewise, offering these goods for sale in the right holder`s own shops or those of an associated company, without actually selling them does not constitute 'putting on the market.[832] Important to highlight however, the transfer of ownership to a third party who is established in the EEA effectuates the exhaustion even if the latter is contractually obliged not to resell the goods in the EEA; result being that non-exhaustion cannot be invoked in case that third party sold the good in the EEA.[833] More recently the Court regarded as not having been put on the market the perfume samples (tester) that were made available by the trademark holder to the resellers without transferring their ownership and that bore phrases 'Demonstration' and 'Not for sale'.[834] It was therefore concluded that the relevant factor in determining whether or not the goods have been put on the market appears to be the transfer of ownership to a third party.

Consent is an iceberg whose tip is barely exposed in the equilibrium of the exhaustion principle, albeit it is the absolute gravity center in determining whether exhaustion has occurred. We have explored the concept of consent from a multitude of perspectives. It was, as shown, less problematic under free movement provisions when the national right holder relied on the IP rights in order to prevent the importation into the state of protection the goods. Free movement principle cannot compel the national right holder to bear the importation of 'other`s goods' that incorporate, say, patent protected invention, confusingly similar mark or the same literary artistic works even if those were lawfully produced and marketed by the others in the exporting Member State. That 'lawfulness' may be due to the independency of the national

[832] C-16/03: Peak Holding v. Axolin-Elinor
[833] Id.
[834] Case C-127/09: Coty v. Simex

rights with the result, for instance, that the same or similar marks belong to two unrelated persons in different Member States; or it may be due to unavailability or expiry of relevant IP rights under the law of the exporting Member State. The bottom line is the national right holder can oppose to importation of the goods originating from (legally and economically distinct) third parties; this, in fact, the bare minimum of the specific subject matter of rights and cannot be sacrificed without killing off the very essence of the rights.

It is less straightforward when it comes to the goods of the right holder. A question of a great magnitude is due to the fact that IP commercialization is not a single-stop continuum; therefore, it is not plainly identifiable in each case who has the discretion to consent within the commercial proximity of the person or entity that is in possession of the rights. In answering to this query, we have shown, consent could be found in vertical and horizontal commercial proximity of the intellectual property right holder. Semantic range of 'with right holder's consent' signifies any marketing activity effectuated by anyone who acts upon the right holder's consent. As we have established, this abstractness (flexibility) in definition helped the Court correspond to any kind of commercial relation that might exist throughout the commercialization continuum, patching up all possible inroads to the exhaustion principle. We have deduced from the case law of the Court that consensual marketing for the purposes of exhaustion includes the marketing by a distributor, a commercial agent, by licensees or by undertakings that belong to the same economic group. Should any one of the aforesaid typified relationship exists, exhaustion occurs in respect to the goods thus marketed. Even more importantly, it was clarified that the object of consent is not limited to these relationships. Legal or economic links that imply a unitary control over the intellectual property right suffice for exhaustion. Economic links saturate a greater area than legal links, leaving very little gap to avoiding the exhaustion by several configurations of territorial assignment of rights while legal links cannot always be clearly identifiable especially in a multinational realm.

However, we also exhibited that the attempts for creating a fool proof exhaustion scheme did not always yield reasonable outcomes; the battle of the legal reasoning and the policy intent was particularly apparent in the context of assignment of IPRs. The Court of Justice inaugurated the debate on the free circulation of goods after the assignment with the rather unfortunate doctrine of 'common origin' whereby it inferred the legal or economic links between the assignor and the assignee from the 'historical' unity of trademarks. In that regard, we found, among other things, that the sequel of this doctrine effectively cancelled out independency and the transactional function of parallel national trademarks, thus rendering

meaningless the commercialization of parallel national trademarks as such. Correspondingly we noted that the latter was one of the most striking examples of the Court`s preoccupancy with favoring free movement almost unconditionally. Retreat from this fanaticism towards a legally comprehendible jurisprudence on this particular matter (which respects the transactional value of the parallel national marks and thus the possibility of commercializing independently) took over two decades and several occasion where the Court directly or indirectly got to touch upon the issue of assignment. More recently, the threshold of economic links has been revisited with the outcome that such a link exists where the assignee, after the assignment of some national rights, has actively and deliberately continued to promote the appearance or image of a single global trade mark or where they coordinate their commercial policies or reach an agreement in order to exercise joint control over the use of the trade mark.[835]

Against that background, from a more general perspective, two important points need to be highlighted: (i) this continuum exhibits the gradual shift from pure purposive approach towards ever-more detailed legal reasoning (ii) reconciliation of intellectual property protection and the free movement principle is an ongoing process whereby multiple layers of interpretative necessities continue emerging from the brief definitions of exhaustion, the doctrine continues developing still due to the necessity compelled by what we conceptualize as IP commercialization.

It was occasionally highlighted that what is guaranteed by the intellectual property right is not the objective attainment of the reward but the possibility - or infrastructure - of doing so. Correspondingly, consent is not weighed against the satisfaction of the IPR holder with the reward achievable (or achieved) by initial marketing but it was identified on the basis of whether the right holder retained the discretion of not putting the goods on the market in the first place. As we have demonstrated, this paradigm is best illustrated by the contrast, *vis-à-vis* exhaustion, between the sales of patented products under compulsory licenses and under governmental price ceilings. As regards the former, the Court made it blatantly clear that the rights shall not exhaust in respect to goods which were marketed in a Member State under compulsory license arrangement; therefore, the right holder could oppose further intra-Union commercialization thereof. This is premised upon the fact that compulsory licensing is not a legal transaction in which respect the right holder retains a contractual liberty including that of

[835] Case C-291/16: Schweppes v. Red Parelela, para. 55

whether or not commencing in the first place; it is rather an administrative tool aimed at providing access to underlying inventions, with public interest concerns. Therefore, it would not qualify as an initial commercialization on the end of right holder, even if some remuneration has been afforded to the latter. On the contrary when the right holder has the discretion not to commence in the initial marketing but nevertheless did so, there is very little to do so as to avoid the exhaustion. The right holders sought refuge to governmentally dictated price ceilings and 'ethical obligation' to market in order to assert non-exhaustion of their rights. The Court persistently refused recognizing as a ground of non-exhaustion any scenario where the right holder could choose whether or not to market. Even more strikingly, it was established that the unavailability of patent protection in the state of first marketing would not prevent the exhaustion. All boils down to the differentiation of legal obligations to market and prevailing circumstances of which the right holders should have been aware while commencing in marketing; under the latter circumstances marketing is a result of the commercial choice of the right holder and the consequences, i.e. exhaustion, must be borne. The question of whether the consent is only relevant factor thus finds an answer: consent relates to putting on the market; consent to the existing circumstances of marketing is not separately sought. Therefore, for the purposes of exhaustion the right to consent is what matters.

An important question in the context of consent is whether marketing by the licensee in breach of the underlying licensing agreement would effectuate the exhaustion or whether the breach should be deemed to have nullified the consent at the outset. We demonstrated that there is no one-fits-all answer to this question; regard must be had first be had to the type of the contractual breach, second to the IPR in question. Non-observances may appear as i) a breach of a contractual provision; ii) an infringement of the subjecting IPR, which may or not accumulate on the same occasion. The former relates to the contractual relations between the parties and the remedies thereto should principally be sought under contract law. The latter on the other hand relates to the *erga omnes* proprietary aspect of IPRs, violation of which exhibits the infringement of intellectual property right. Derogations from the free movement principle concerns the protection of industrial and commercial property and are not aimed at policing the compliance of the parties to intellectual-property-based agreement, which typically is a license. Therefore, while exhaustion relates to the latter, given the consent intrinsic in licensing agreements, we found that there are limited cases where the contractual breach could possibly be as essential as to nullify the consent. Result being that not every non-observance of the

license agreement by the licensee results in nullification of consent; quite the contrary, this is rarely the case.

Secondly, we observed that these limited scenarios differ from one intellectual property right to another. As regards trademarks, the cases where the rights may be invoked against a licensee in breach are explicitly and exhaustively listed by the secondary law on the Union. These include breaches as regards (a) its duration; (b) the form covered by the registration in which the trade mark may be used; (c) the scope of the goods or services for which the license is granted; (d) the territory in which the trade mark may be affixed; or (e) the quality of the goods manufactured or of the services provided by the licensee. And this list is strictly closed given the central role of exhaustion in the functioning of the free movement principle. Amidst the *prima facie* inharmonious jurisprudence, we also purported that the case law of the Court implies that the breach of licensing agreement as regards the quality standard of the goods does not constitute an absolute ground of excluding the exhaustion; conversely, the latter possibility arises only when the right holder (licensor) exhausts all the contractual and practical possibilities to prevent the marketing of inferior quality of goods by the licensee but such marketing nevertheless took place. In turn, we exhibited that similar provisions exist as regards design rights and that a more general clause (any contravention) included in the Plant Variety Regulation has been judicially narrowed down to essential breach, albeit still somewhat remaining ambiguous. Moreover, we found that no legal basis -such as to result in non-exhaustion in case of a contractual breach- existed in the realm of copyright and patents and, similarly, applying the provisions of trademark, design or plant variety rights by analogy to patents and copyrights would likely be devoid of proper legal basis.

As regards the geographical scope of exhaustion we noted that the destiny of further commercialization in general and parallel trade in particular strictly depends on the exhaustion regime applicable. In order for the free movement principle to function, the realm of exhaustion of rights should coincide -at least- the territorial area within which the free movement is envisaged (the Single Market); this was the very essence and benchmark of the regional exhaustion model. This being an irrebuttable point, we exhibited that the question of whether a more liberal exhaustion regime is possible has been a matter of fierce debate. It is rather clear that the said debate is highly political in nature given the sharply different macroeconomic reverberations entailed in each scenario. Should the international exhaustion be permissible, parallel import of IP protected goods into the EEA would have been possible, thus relatively assimilating the price level to the rest of world and practically incapacitating the right holders

to maintain higher price levels in the Internal Market. Nevertheless, as we emphasized, over the course of a series of judgements the Court showed no doubt in taking the view that no more or no less was possible; the regional exhaustion was the exclusive standard.[836] It goes without saying that the consent for the purposes of exhaustion relates to the sales within the Internal Market; initial sales by the right holder outside the EEA would not exhaust the rights in respect to the Internal Market. This is perceived as euro-protectionism creating a fortress of Europe in relation to parallel trade.

We have discovered that the limits of IP commercialization are of a far more complex nature in the realm of copyright. We ascribed this to two main imperatives: firstly, the wide - and ever expanding- scale of creations that fit into the definition of 'work' for the purposes of copyright; secondly as distinct from other types of IP, copyright protected material can be exploited in many alternative ways which are not necessarily preconditioned to distribution of physical products. The latter is inextricably intertwined with the development of communication technologies and unlikely to remain as a closed list. Along the same lines, in present, the dissemination of copyright protected substance is actualized majorly by immaterial means getting less and less dependent on physical substance.

Principally only the distribution of the physical copy of the work comes within the ambit of exhaustion principle while the immaterial dissemination does not. With that, we revealed that the traditional method of reconciling the national rights and market integrity, i.e. the exhaustion doctrine, at the outset falls short of the market related aims of the Union in the realm of copyright and related rights where the protected substance does not necessarily amount to goods (anymore). Moreover, this very prospect brings under question the possibility of complete achievement of the Digital Single Market that has been in the agenda of the Union in recent times.

Against this background we put a particular emphasis on the jurisprudential attempts to expand the exhaustion principle to digital realm. We established that the possibility of application of exhaustion doctrine in respect to the copyright protected digital content is hinged upon the extent to which immaterial dissemination could be approximated to 'distribution'. Subsequently we analyzed two landmark judgements of the ECJ with a particular emphasis to the legal normative background of the rulings which yielded complete opposite results as to the possibility of exhaustion of copyright and related rights in the online realm. We found,

[836] C-355/96: Silhouette v. Hartlauer; C-173/98: Sebago v. G-B Unic; C-414/99: Zino Davidoff and Levi Strauss

firstly, that the Court, in its notorious *UsedSoft* ruling, opportunistically utilized the fact that the legal protection of computer software is subject to a distinct legal instrument (the Software Directive) whose language is incidentally less restrictive on the tangibility requirement for distribution than that of general copyright legislation (the InfoSoc Directive) in order to extend the exhaustion principle to computer software. In turn, we exposed the systematic and doctrinal fallacies of the ruling from the perspective of international law and the Union`s legal order, concluding that this outcome also represented the tendency of suppressing the intellectual property protection with a view to creating new markets for further commercialization of the IP protected substance beside what is traditionally regarded as goods. Next, we analyzed the follow up judgement in *Tom Kabinet,* which had as its subject the possibility of exhaustion in relation to e-books and, coherently, denied such a possibility. We observed that the two judgements exhibited sharp differences not only regarding their outcomes but also, and more importantly, on the point of the approaches taken by the Court in reaching those distinct conclusions. On a comparative reading we concluded that, with the legislative and doctrinal material at hand for the time being, the latter judgement is accurate from a legal perspective. Finally, we arrived at the conclusion that the judgement in *UsedSoft*, besides its endemic and peculiar outcome in the specific field of software, does not by any means open the doors to a generally applicable digital copyright exhaustion.

We were driven to specifically analyze the scope of exhaustion in the realm of trademarks for two apparent reasons: (i) almost all goods that are made commercially available bear trademarks, thus, quantitatively speaking, making this particular intellectual property right the most notorious impediment to intra-Union trade; (ii) the derogation from the free movement principle on the ground of protection of industrial and commercial property (Art. 36 TFEU) was specifically substantiated in the trademark legislation of the Union, entitling the right holder to oppose further commercialization of the goods in the existence of 'legitimate reasons'. Among these legitimate reasons the trademark directive particularly spelled out the cases where condition of the goods is changed or impaired after they have been put on the market. Though, as exhibited, in reality the changes as such comes inevitable or desirable on the end of parallel traders in order to comply with the legal requirements in the target state or to make the goods suitable for the consumer profile there. We posed the question that whether the trademark holder is permitted to oppose further commercialization when alterations as such -generally addressed as repackaging- even if these are legally necessary for the parallel trade

to happen or are to the benefit of the parallel trader. In answering this question, we analyzed the comprehensive set of case law the Court made available over the course of four decades.

We established that within the language of the Court's jurisprudence 'repackaging' has been construed as a broader term such as to cover repackaging, i.e. the change in the external packaging (re-boxing) and re-bundling the content, and relabeling. Moreover, these specific acts subsumed thereunder made no difference from the view point of ascertaining the legitimate reasons to oppose further commercialization. The main principle remains that any interruption with the presentation of goods -pharmaceuticals in particular- is liable to give a rise to the legitimate reason in reliance of which the holder of trademark can derogate from exhaustion. Nevertheless, for the interest of free movement, under certain conditions such alterations to the products cease to be a legitimate reason to oppose further commercialization. Accordingly, following conditions must be cumulatively met: (i) objective necessity; (ii) no effect on the original condition of products; (iii) indication of the repackager; (iv) presentation such as not to liable to damage the reputation of the mark; (v) prior notice to the right holder. We also examined each condition fragmentally with reference to the jurisprudence of the Court; finding, inter alia that the objective necessity is not confined to those arising from the legal framework of the importing country but it is also present in the cases where, without repackaging, the effective access to be market would have been hindered. Important however, the objectivity criterion is not fulfilled when the repackaging is solely attributable to the importer`s attempt to secure a commercial advantage. Consequently, it was revealed that, under these strict conditions, the exhaustion principle could practically extend to exclusive right of affixing the mark to the extent that the repackaging requires re-affixing of the mark. However, this is without prejudice to the indication of origin function of marks; meaning that exhaustion does not at any rate enable the others to affix the marks to the goods that did not originate from the right holder.

Throughout the research we also found that the advertising function of trademarks played an important role in defining the limits of exhaustion. It follows from the holding of the court that the subsequent traders, besides being free to resell those goods, are also free to use the associated trademark to bring to the public's attention the further commercialization thereof. The contrary, according to the Court's purely practical and economic view, would make the further commercialization of the good fairly difficult thus defeating the very purpose of exhaustion principle. However, in a counterbalance, it was established that the further commercialization can be opposed when the use for advertising in the course of further

commercialization is liable to undermine the mark's aura of luxury that associated with certain groups of products. Therefore, we found that the role of advertising function of trademarks implies both expansion and limitations to the scope of exhaustion respectively to the effect that it expands the application of exhaustion towards the exclusive right of using the mark for advertising; and that the aura of luxury was considered as mental condition of the goods and, if impaired, amounts to a ground of legitimate reasons to oppose further commercialization. Moreover, we uncovered that the exhaustion principle is not the only resort for limiting the trademark protection to the benefit or free movement and the freedom to provide services; referential use of trademarks by the others is also permitted beyond the goods of the right holder. Insofar as the exhaustion principle relates to the goods put on the market by the right holder, it facilitates the intra-brand competition by means of further commercialization; meanwhile the fair use limitations, factors into the competition between the brands and sub-sectors. Despite this divergence, they mutually seek to reconcile the interest of free movement of goods and freedom to provide services, thus contributing to undistorted competition environment. From the widest perspective, the common motivation of the both sets of provisions appears to be to make the monopolistic nature of intellectual property right fit into the peculiar characteristics of the internal market.

It was concluded that the domestic premises of intellectual property law, of which the regional exhaustion principle is the main creation, is not the exclusive instrument in demarcating the limits of the IP commercialization in the Internal Market. We had already acknowledged the foundational value of competition rules and identified them as an integrating factor alongside the free movement principle. To that end it was articulated that the competition rules, albeit the IPRs are not their natural or exclusive target, represent an external limit to IP commercialization.

We first explained theoretical and practical interfaces of the two bodies of law, finding that the theoretical and deontological aims of competition laws and intellectual property laws seem to coincide. However, we exposed, this harmony is rather rhetorical; that is to say, in practical terms, this harmony cannot prevent the two bodies of law from coming into conflict. This is premised on the exclusionary character of IPRs which reverberates as the privilege to determine who has the access to protected information or technology both at consumer and competition level as well as to determine under which conditions that access will be provided. In practical terms this enables the holder of the rights to set barriers to the market entry of potential competitors by refraining from licensing an essential technology or information,

therefore cutting the competition at the source. This likewise might pose an obstacle at the outset to the creation of interrelated secondary markets where the use of IP protected substance is the essential requirement. The market actors might, instead of engaging in arduous competitive process, also collude to fix prices, share the markets or limit the production to the disadvantage of the consumer in reliance to those exclusivities. To that end intellectual property rights - particularly the exercise of the exclusivities thereunder- make up perfect instruments to leverage anticompetitive behavior and -if taken to be unrestrained- are likely to assimilate to monopolies. Moreover, some trade practices, such as selective distribution systems, involve the risk of the barriers to further commercialization of the goods, which were normally eliminated by the exhaustion principle, being re-constructed by the market participants. In the view of the foregoing, we explained how the exhaustion principle alone is incapable of providing and preserving the Internal Market, in that we exposed the nuance between the exhaustion principle and the competition rules as regards their influence areas. While the exhaustion principle ensures the free movement and, in turn the integrity of the Internal Market, in respect to 'what has been commercially offered'; IP rights are capable of determining the destiny of 'what can be offered'. In respect to the latter, the exhaustion principle has apparent shortcomings.

On the other hand, competition rules are not concerned with the instrument but they are concerned with the potential and actual anti-competitive effect of behaviors -be that a commercial practice or agreements- such as to affect the trade between the Member States. Competition rules of the Union do not attack IP protection from the point of being 'territorial exclusivities'; nor do they take intellectual property law as a specific realm of intervention. They rather put IP rights on the target to the extent that they are instrument to anticompetitive collusions or behaviors that are liable to affect the trade between the Member States. With that we established that the intersection of IP rights and the competition rules are not confined to typified agreements and practices but, rather, it flexibly covers all the contact points where the exercise of the rights entail anti-competitive results or potential within the meaning of prohibitions of the competition rules of the Union. Therefore, statutory intellectual property exclusivities, although liable to affect competition climate -as they should in line with their theoretical function of advancing innovative competition through rewards and incentives- competition laws set the hand to ensure that this effect is not such as to practically distort the competition beyond their intended purpose. This balance is particularly sought under Art. 101 of the TFEU which in the essence weighs the anti-competitive effects of intellectual property

protection against pro-competitive effects thereof in determining the permissibility of agreements, decisions and concerted practices between the undertakings. Pro-competitive effects thereunder are judged by (i) the contribution to improvement of the production or distribution of goods or to promotion of technical or economic progress; (ii) whether consumers are allowed fair share of the resulting benefit; (iii) whether the agreements and practices are indispensable to the attainment of the aforesaid objectives; and they must not enable the parties to eliminate competition in respect of a substantial part of the products in question. On the other hand, Art. 102 ponders upon whether IP protection confers a dominant position and, in turn, whether such position is abused through the exercise of IPRs in away that may affect the intra-Union trade. On that note, and with a reference to the Court's jurisprudence, we have concluded that the IP rights, in a static sense, are not afoul of the competition rules of the Union but they can be the instrument to the anti-competitive agreements and practices or to abusive conducts. This was, in fact, the very essence of the doctrine of the Court that segregated the existence and the exercise of the rights. Having thus established that the competition rules do not select and approach their target from a legal perspective, but instead, from an economic one, we put on the focus the treatment of specific type of agreements and conducts that revolve around commercialization of the rights and corporeal goods under the competition rules.

As regards the agreements on selective distribution systems (SDS) we submitted the initial observation that the trademark holder might have a legitimate interest in distributing through such systems while these can also be used for keeping the third-party traders out of the business thus reducing intra-brand price competition created by such traders. From early on, the right holder`s legitimate interest in SDS has been found attributable to pro-competitive goals. This is because such systems, although reduce intra-brand price competition, help providing specific services as regards high-quality and high-technology products which can only be perpetuated through the adequate profit margins safeguarded by SDSs, thus leading different brands of similar products to compete in quality. To that end, pro-competitive effect was ascertained by the existence of certain conditions judicially developed. Accordingly, the selection of resellers must be based on qualitative criteria instead of quantitative ones; it must be uniform, proportionate to the that legitimate objective and applied in a nondiscriminatory nature. Above all, the retainment of an SDS must be necessary in the first place. This balance test was subsequently institutionalized by the Vertical Restraints Block Exemption (VBER)

which particularly substantiated, in relation to SDSs, the exemptions enshrined in Art. 101(3) of the TFEU.

Although it is clear under VBER that the restriction on the online sales to the end users disqualifies the SDS from the application of the block exemption, the problem arises where the requirements, in a qualitative disguise, have their objective in preventing the online sales. Situation as such was at the stake in *Pierre Fabre* where the supplier has indirectly prohibited the online sales by requiring the members of the distribution system to make the sales on the physical stores in presence of a pharmacist. The Court found that an absolutory ban on the online sales, even if that is not directly stipulated but flows from another contractual stipulation such as the latter, precludes the application of the block exemption. Moreover, it highlighted that the internet is not regarded as an 'unauthorized business place' wherein the supplier may prohibit a member of the system from operating. In the subsequent judgement the Court held that the ban on online sales on the third-party platforms do not infer absolutory ban, therefore they are justifiable under Art. 101 so long as they are necessary and proportionate. However, in the latter judgement the Court put an immense emphasis on the 'luxurious' character of the goods, on which ground it was found that the sales over third-party platforms entails a risk of deterioration of the online presentation of those goods in a way as to harm their luxury image. And that luxurious character was not the case for the goods that were at the center of the previous ruling. We found in a concurrent reading of the two cases that -although it is conceivable that luxurious character of the goods factors in the analysis of the 'necessity' and 'proportionality' criteria- it remained unclear whether non-absolutory bans on the online sales of non-luxurious goods are permissible; or it should be deemed to have failed fulfilling the 'necessity' criterion at the outset. We also concluded that the sequel of the rulings is problematic to the extent that the threshold of luxury for that purposes is considerably ambiguous especially when the regard is paid to the goods and the marks that are reputable and fine but not outstandingly luxurious and that further and unified clarity on that point, on the EU level, is desirable.

Crucially we observed that the right holder`s refusal to license has been, as it were, the battle field of IP rights and competition rules. This is because the right to exclude the others defines the IP rights; the initial observation as to refusal to license, thus, shall be that it is of the very essence of intellectual property rights. This is irrebuttable from the perspective of intellectual property law; nonetheless a parallel concern is raised on the end of competition law, given that refusal to license is practically viable to lock down the competition (i) in the

very market for the protected subject matter as well as (ii) in downstream markets whose activity is firmly interlinked to that upstream market. We took a dual approach to the matter: we first comprehended the general treatment of refusal to license under the Art. 102 of the TFEU and secondly framed this intersection in particular respect to standard essential patents (SEPs). As regards the former we found neither there is a built-in dominant position in the possession of IP rights, nor does the normal exercise thereof, including the refusal to license, implies abuse of a dominant position. An extra element is sought: certain abusive conduct. The latter notion is further clarified by the subsequent judgements. Accordingly, certain abusive conduct is found under 'exceptional circumstances' which followed from the fact that the refusal precluded the introduction of a new product that has a potential demand by consumers; there existed no justification for such refusal; it eliminated all competition in a secondary market to which the IP in question is indispensable.[837] In the following judgements it was held that the aforementioned list was not exclusive standard of 'exceptional circumstances'; such circumstances could also be discerned from other factors that are not necessarily in that list. Moreover, the new product requirement would have been fulfilled if the intended product is aimed at anything beyond duplicating the goods or services already offered on the secondary market by the owner of the IP right.[838] The interpretative adjustments such as to lower the threshold of abusiveness has been even more ambitiously intensified by the General Court of the Union. It ambiguously broadened the scope of 'new product' criterion, thus, when the refusal represents a 'limitation of technical development', whether or not a new product will be yielded is of no importance. It also found sufficient the 'risk' of eliminating the competition instead of actual elimination thereof; the effective competition being eliminated (or risked) instead of the entire competition. In the light of foregoing, we observed that refusal to license has been put under increasing pressure of competition rules; the exceptional circumstances, so to say, ceased being so exceptional.

As far as SEPs concerned, the scenery is conceivably stricter. We found that the exceptional circumstances by default present themselves in that context, particularly because their indispensability is institutionally affirmed and the availability of licenses on FRAND terms is promised at the outset. Against that background, unlike a non-essential patent, refusal to license a SEP, principally, constitutes abuse of a dominant position. More eccentrically, even the exercise of the right to seek injunction, the fundamental way of enforcing the rights, is

[837] C-241/91: Radio Telefis Eireann (RTE) and Independent Television Publications Ltd (ITP) v Commission of the European Communities
[838] Case C-418/01 IMS Health GmbH & Co. OHG v NDC Health GmbH & Co. KG

likely to give a rise to abuse of dominant position. And this is, in the sequel of the Court`s judgement, not an exceptional case. That is to say, in order to avoid infringing Art. 102 merely by seeking injunctive relief, the right holder is encumbered to follow a rather comprehensive set of requirements.[839] On that note we posed the question while the lawsuit seeking an award for damages is not regarded as an abuse of dominant position, why should injunctive relief request -as a part of that lawsuit- be regarded so? We observed that the answer is not found in the jurisprudence of the Court but in the statement of the Commission. Accordingly, a recourse to injunctions may unduly distort FRAND licensing negotiations and allow SEP holders to charge royalties or impose licensing terms which a licensee would not agree to absent the threat of having its products excluded from the market.[840] Having observed that the ECJ has omitted making a reference to the aforesaid line of reasoning, in fact without producing any reasoning, simply held that seeking injunction under those circumstances is abusive; we concluded that the lack of an apparent reasoning puts the integrity of the Court`s jurisprudence under question.

As regards patent pooling agreements we submitted the initial observation that neither anti-competitive nor pro-competitive effects thereof are *prima facie* dominant. On the one hand, they enable the collective exploitation of a huge portfolio of technologies as well as a collective exclusion of the third parties from that sizable portfolio and thus prone to cartelization; on the other hand, they also represent one-stop-shop licensing in certain sectors, thus reducing the transaction cost as well as facilitating the access to the bundle of interrelated technologies at a presumably lower cost than accumulated cost entailed in the case of individual licensing. We found, in the face of these contrasting outcomes and in line with the general mechanism of Art. 101, pro-competitive and anti-competitive connotations are to be compared in order to make the assessment of the compatibility with that provision. However, we draw attention to two different aspects of patents pools *vis-à-vis* the competition rules: (i) the agreement on the formation of the pool; (ii) the actual intra-pool and external licenses. In that regard we expressed, while the former is likely be covered by the Technology Transfer Block Exemption (TTBER), the latter is not so covered because they do not entail any substantive licensing arrangement; but they rather resemble a framework agreement preceding the actual licensing transactions, in particular addressing the formation organization and operation of the pool envisaged; secondly, pooling arrangements are multilateral thus expressly excluded from

[839] C-170/13: Huawei Technologies Co. Ltd v ZTE

[840] Press Release 17 October 2013, *Antitrust: Commission consults on commitments offered by Samsung Electronics regarding use of standard essential patents*, EUROPEAN COMMISSION (26 Jan. 2021) at 2. https://ec.europa.eu/commission/presscorner/detail/en/IP_13_971

the scope of the TTBER at the outset. Yet, as we noted, the considerations apply to patent pools are found in Guidelines of the Commission[841] which, in the essence articulates that the pools as such are permissible under the competition rules to the extent that they are subject to open participation; they include the essential technology; licenses therein are non-exclusive and the participant are free to further develop competing products.[842]

Finally, we concluded our analysis with the reverse payment settlements that are of utmost significance in pharmaceutical sector and that function for *de facto* extension of expired (or near expired) patents or those which have the risk of being invalidated if judicially challenged. The arrangements revolve around the payments or otherwise value transfers from the owner of patents to the potential competitors who are preparing to enter the market upon the expiry of the patent or who challenge the validity of the patent in order to enter the market; those potential competitors, in turn promise staying out of the market for the agreed term. As clear as the anti-competitive objectives of such arrangements are, we exhibited that, three factors are taken into consideration by the Commission in order to differentiate such arrangements from honest dispute settlement. Accordingly, the agreement is afoul of Art. 101 where the parties to the agreement are at least potential competitors; and the generic producer is committed in the agreement to limit its efforts to enter the market in the EEA; and there existed a value transfer from the originator to the generic producer. We have also noted that 'value' for this purpose penetrates to a wide scale including lump sum payments, promotional allowances and market shares. Moreover, it was also noted that, should the originator exhibit a linear and consistent course of action by buying out potential competitive technology in addition to the settlement agreements, this also constitutes an abuse of dominant position within the meaning of Art. 102.[843]

From all the matter we analyzed, it becomes clear that the free movement principle and competition rules determine the limits of intellectual property commercialization. While the former utilizes the premises of the intellectual property law, particularly the regional exhaustion principle, thus marking the internal frontier of IP commercialization from a legal perspective; the latter sets the outer limits based on its own economically motivated prohibitory premises, without dwelling much on the legal identity of IPRs. This whole setting -the Europeanization of intellectual property- is achieved by sacrifices being made from the

[841] Communication from the Commission — Guidelines on the application of Article 101 of the Treaty on the Functioning of the European Union to technology transfer agreements
[842] Id. para. 261
[843] Case AT.39612 — Perindopril (Servier)

dogmatic classic sense of intellectual property protection. The European IP law above that of Member States was not constructed through an exclusive IP law interest. Quite the contrary, it was compelled by the necessities that appeared on the way of market integration and those necessities were compelled by what we conceptualized as intellectual property commercialization as opposed to mere statics of intellectual property rights. In fact, the Court`s doctrine that differentiated the existence and exercise of the rights amounts to a pure indicator of that realization. That realization led the Court to initially view intellectual property rights as something to suppress in order to effectuate the free movement. Naturally, as we exhibited and as was pointed out by legal scholars, the free movement principle has been at the outset constantly favored in front of IP rights. This proposition is evidenced *inter alia* by the existence/exercise and common origin doctrines of the Court. We have also observed that this fanaticism has left the ground to a more balanced approach that looks out for the interest of free movement on the one hand and that of IP protection on the other hand. Equally clear however, this shift is not linear in every particular sub-domain we examined; not least because some contact (or contrast) points between IP protection and the free movement and competition rules are -as we exhibited- newly emerging, while the others have been at the center since the early stages of market integration. Obviously, this is owed to the reality that the commerce gains a universal identity faster than laws can and this evolution is intensified by ever expanding scope and forms of commercial activities wherein intellectual properties are the major source of value. Therefore, it is comprehendible, in the end, that the legal boundaries of intellectual property commercialization are bound to be dynamic and liquid insofar as the limited legal sources have to correspond not only to novel modalities of IP commercialization but also to novel and, so to say, post-modern attempts of undermining the aims of the Internal Market with the leverage of IP rights.

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