

**EXHAUSTION OF TRADEMARKS
AND OTHER INTELLECTUAL PROPERTY RIGHTS**

UNICE COMMENTS

I. **INTRODUCTORY REMARKS**

UNICE is surprised that the recent decision of the European Court of Justice in the “Silhouette Case” did not put an end to the present tendency at EU level to discuss alleged advantages of international exhaustion in the area of trademarks and more generally for intellectual property rights.

In this paper, UNICE would like to voice the particular concerns of intellectual property rightholders. The manufacturers of branded products represented by UNICE are extremely concerned about the consequences that changes in the Community exhaustion regime could have for intellectual property rights in general. Apart from the specific consequences in the field of trademarks, it would inevitably have a repercussion on designs, patents, copyright and other IPRs. The whole intellectual property framework could be affected and the outcome of such a change would be a general dilution of these rights, which are vital to innovation and economic growth.

II **DEFINITION OF EXHAUSTION**

1. The theory of exhaustion of IPRs has been developed by courts. Exhaustion doctrines establish the limits of territorial distribution rights of intellectual property owners after the first sale of their protected goods/works.
2. In the EU, a regional exhaustion theory prevails. It means that if a rightholder has first sold goods on which he has IPRs in the market of one EU member state, or given his consent to do so, his rights on that good are deemed to be “exhausted” and he cannot oppose its import to, or sale in, any other EU member states. This regime is based on one of the cornerstones of the European Community: the creation of a single market. Since this market is considered as an area without internal frontiers, goods, services, persons and capital should move freely.
3. Under international exhaustion, the rightholder loses its exclusive right of distribution after the first sale or distribution of a protected product anywhere in the world.

4. The ECJ has confirmed on many occasions the well-enshrined principle of EU regional exhaustion. Legal arguments are not questioned. The debate is now centred around economic consequences of a choice of exhaustion and UNICE will focus its comments on these aspects.

III. ECONOMIC ARGUMENTS AGAINST INTERNATIONAL EXHAUSTION

1. UNICE would like to recall that the countries covered by the WTO Agreement do not constitute a customs union and economic area such as the European Union, or even a free-trade area. There are still many tariff and non-tariff barriers, and important differences in economies, legal systems, wealth and development, state price controls and regulations.
Product prices within a given market are still affected by such matters as company taxation, state regulations and other infrastructure expenses, salary levels determined by local conditions and interference of local governments with the normal operation of markets.
International exhaustion is therefore not consistent with economic reality in the present state of global trade.
2. If prices are established not by the free market but by state intervention, international exhaustion can have devastating effects since it can lead to partial expropriation of rightholders' rights. This arises in particular where prices are controlled in the country of first sale (as with price-controlled pharmaceuticals).
3. International exhaustion creates barriers to international trade. To protect themselves from its effects, innovators are in effect barred from selling in, or transferring technology to, countries where prices are low. Developing countries will also be negatively affected since rightholders will not grant licences in low-price countries or in countries with non-existent or low intellectual property protection.
4. It has been argued that the USA and Japan follow the international exhaustion principle. This is a misinterpretation of the US and Japanese exhaustion regimes. As the NERA study points out in the few cases where international exhaustion is applied in these countries, it concerns only certain categories of products and often on a case by case basis.
Whatever Europe does, UNICE is of the opinion that the USA is unlikely to follow if that is contrary to US trade interests. Any country that adopts international exhaustion in circumstances where the US does not, will not only shoot itself in the foot by holding back technology transfer and the export and import of goods at reasonable prices; it will also give a competitive advantage to US trading corporations and to US exporters to low-price countries.
5. The increase in parallel imports resulting from a move to international exhaustion would be an open door for counterfeit goods. Since the Commission is willing to reinforce the fight against counterfeiting, it should carefully assess the impact of a change in exhaustion regimes on counterfeiting.

IV. WHO WOULD BENEFIT FROM INTERNATIONAL EXHAUSTION?

1. UNICE notes that the NERA study shows that parallel trade is not a consumer/price issue. It is a manufacturer/trader issue. The principal question at stake is therefore: who should be allowed to control distribution? Is it innovators or is it traders?

International exhaustion would simply rob innovating companies of the means to finance innovation and research activities since it would prevent them from achieving an adequate return on their investment in innovation. Instead it would divert resources to traders who have made no contribution to innovation.

2. International exhaustion would enable trading companies to buy the product in quantity in a market where prices are relatively low and transport it to a market where prices are relatively high. Parallel traders would maximise their own profit and would sell goods at the highest market price they can, keeping for themselves the lion's share of the price difference.
3. International exhaustion would therefore mainly benefit trading companies, often not based in EU countries.

V. ILLUSORY ADVANTAGES FOR CONSUMERS

1. As shown above, consumers will not benefit in large proportion from a change to international exhaustion. The NERA study confirms the very small effect on retail prices (retail prices may decrease by only zero percent to two percent).
2. In addition, a move to international exhaustion might affect consumer confidence because a product sold under the same brand name in different countries often varies in taste and quality. The product put on the foreign market will be adapted to that market and will often have different characteristics¹.

In addition, brand manufacturers in Europe ensure that their packaging conforms to European or national requirements such as labelling, re-usability and re-cyclability. The same brand sold outside Europe may well be packaged differently because of different local conditions (local packaging requirements, climate, etc.).

All these differences might undermine the rightholder's reputation if goods are put on the wrong market as a result of international exhaustion and parallel trade. The consumer will be disappointed, and the reputation and image of the firm concerned might be affected.

3. Parallel trade resulting from international exhaustion may also affect consumer safety. A product imported into the EU by parallel traders may well contain instructions in non-EU languages. The consumers might end up either with instructions that are not understandable, or no instructions at all if the trader decides to remove them. This would fly in the face of the 1999 Council resolution on operating instructions for technical consumer goods, and in the Commission efforts to strengthen consumer safety.
4. International exhaustion damages selective sales and marketing channels which provide benefits to the consumer from quality control, trained staff, after-sales service, guarantees and product information.
5. UNICE was heavily involved in the discussion concerning the proposal for a directive on the after-sales guarantees on consumer goods. Consumers have been pleading for a high level of

¹ For instance, European brands of toothpaste do not taste as in Asia or Africa; a television for Asian terrestrial reception may not have the full band-width for the European cable network and a European consumer acquiring these products could not use them.

after-sales service and guarantees. In the context, it is difficult to understand that they could favour cheaper products with no after-sales service or guarantee, instead of European products which have to comply with the high standards they have asked for.

VI. CONCLUSION

- The established regime of Community exhaustion, while ensuring free movement of goods in the internal market, guarantees European companies the necessary protection against parallel imports from third countries. This regime is a crucial element in maintaining and protecting EU competitiveness and innovation.
- A move to an international exhaustion system would reduce the economic value of intellectual property rights and would place European companies at a competitive disadvantage vis-à-vis competitors from countries which do not apply this regime. Moreover, if some Member States were allowed to apply international exhaustion, this could ruin the proper functioning of the internal market for trademarks and rental rights.
- Consumers would not benefit in large proportion from parallel trade. UNICE notes that the NERA study shows that parallel trade is not a consumer/price issue. It is a manufacturer/trader issue. Parallel traders want to maximise their own profit and they would sell goods at the highest market price they can.
- The NERA study points out as a consequence to adopting international exhaustion retail prices may decrease by zero percent to two percent. On the other hand, it points out falls in profit for European companies between three and thirty five percent. The figures speak for themselves.
- It remains UNICE's considered opinion that only an exhaustion regime limited to the territory of the European Union can provide the level of intellectual property protection needed by European companies in globalising markets.
- UNICE will therefore continue to oppose international exhaustion as long as there is no single world market with a uniform commercial, economic and legal framework.

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