Legally Flawed but Politically Sound? Digital Exhaustion of Copyright in Europe after UsedSoft

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Abstract

The principle of exhaustion, or the first sale doctrine (US), in copyright means that once a copy of a work is put on the market with the consent of the right holder he or she will not be entitled to control the further distribution of the copy. It is well settled that the exhaustion rule applies to the distribution of tangible copies (books, CDs, DVDs etc), but its application to the online context is controversial. In the UsedSoft case (case C-128/11) the Court of Justice of the European Union nevertheless applied the exhaustion rule of the Computer Software Directive to a situation where ‘used licenses’ of computer software were passed on to third parties enabling them to download the software from the right holder's website. The article discusses the legal premises and the policy implications of the decision, contrasting it also to the ReDigi decision of the US District Court of the Southern District of New York.

Keywords: Intellectual property; copyright; distribution right; exhaustion; first sale doctrine; free movement of goods and services

1. Introduction

The exhaustion of rights is one of the ‘hot topics’ of intellectual property (IP) law. The principle of exhaustion and the equivalent US first sale doctrine go to the very heart of what IP law is about: a concrete reflection of the trade-off between the interests of the rights holders and the general public. In the copyright field, exhaustion traditionally relates to the distribution right, meaning that when a copy of a copyright-protected work (or other related subject matter) is sold or otherwise put on the market by the copyright holder or with his or her consent, the right holder may not invoke his or her exclusive right to control the further distribution of the copy. After the emergence of digital technology and the Internet, the question arose as to whether or to what extent exhaustion applies to the online environment. In EU law, the question might have seemed resolved by the 2001 European Copyright Directive (EUCD), which states that exhaustion does not occur. Yet, the topic has still been subject to discussion after the adoption of the Directive. Furthermore, in 2012 the Court of Justice of the European Union...
Union (CJEU) (Grand Chamber) delivered a remarkable decision in the *UsedSoft* case, applying the exhaustion rule in the 2009 Computer Software Directive (CPD) Article 4(2) to digital downloads. As expected, the decision led to immediate reactions from legal scholars and the case has already been subject to extensive analyses.

In part, what follows from these analyses is that the decision perhaps leaves open as many questions as it answers, not least regarding its scope and possible future consequences. The concern I raise here relates to the legal grounds for the decision. Many commentators have discussed the fact that the CJEU pushes the exhaustion criterion in CPD Article 4(2) beyond what was clearly the purpose behind the corresponding provision in EUCD Article 4(2) and the sustainability of the Court’s *lex


3 Case C-128/11 *Axel W. Bierbach, administrator of UsedSoft GmbH v Oracle International Corp*, ECR report forthcoming (*UsedSoft*).


specialis argument in this respect. Less attention has been given to the fact that the CJEU concentrates solely on the interpretation of the criterion for exhaustion, pursuant to Article 4(2), and hardly discusses the scope of the right which is subject to exhaustion according to the ruling – ie the distribution right. My contention is that the arguments put forward by the CJEU for applying CPD Article 4(2) in the online environment, although controversial per se, are in any case not sustainable grounds for letting the distribution right (Article 4(1)(c)) apply to the same environment. If this is true, on the face of it, the authority of the decision is clearly weakened. On the other hand, one should take into consideration the possibility of reaching the same result with a different reasoning. The discussion in the subsequent sections takes on both tasks – giving a critical analysis of the legal reasoning of the CJEU and at the same time investigating possible alternative routes to the solution reached.

It is pertinent to recapitulate briefly the facts and result of the UsedSoft case before starting the analysis. In Germany, software reseller UsedSoft was sued by the producer Oracle for infringement of its copyright. UsedSoft specialises in the marketing of used software licenses, including user licenses for Oracle’s so-called client-server software. This allows the licensee to store a copy of the programme on its server in order to give a certain number of users access to the programme by downloading it to their workstation computers. Oracle offered group licenses for a minimum of 25 users each. The licenses stipulated that they were non-transferrable and to be used exclusively for the licensee’s internal business purposes. UsedSoft nevertheless acquired user licenses from customers of Oracle and offered ‘used licenses’ for the Oracle programmes on its website. Consequently, UsedSoft customers were able to download a copy of the programme from the Oracle website after acquiring a used license, or – if they already had the software – to purchase further licenses for additional users.

Oracle brought proceedings in German courts seeking an injunction against UsedSoft. An injunction was allowed by the Regional Court of Munich, but the decision was appealed to the German Federal Supreme Court (Bundesgerichtshof (BGH)), which referred questions to the CJEU for a preliminary ruling. The questions were – in short, slightly rephrased and in the order the Court answered them – as follows: (1) is the right to distribution exhausted pursuant to CPD Article 4(2) when the acquirer of a computer programme has made the copy with the right holder's consent by downloading the programme from the Internet onto a data carrier?; (2) is the person who can rely on exhaustion of the distribution right a ‘lawful acquirer’ within the meaning of CPD Article 5(1) (with a pertaining right to reproduction)?; (3) can a person who has acquired a ‘used’ software license as ‘lawful acquirer’ also rely on exhaustion of the right to distribute the copy of the computer programme made by the first acquirer, in order to download it onto a data carrier if the first acquirer has erased his or her programme copy or no longer uses it?

The CJEU answered the three questions in the affirmative with certain qualifications. In short, the Court accepted that the exhaustion of the distribution right pursuant to CPD
Article 4(2) occurs insofar as the following qualified situations of online transactions are concerned: (i) where the software is made available (with the consent of the right holder) for download without time restrictions; (ii) the first acquirer makes his or her own (downloaded) copy unusable at the time of the resale; and (iii) the first acquirer transfers his or her license to use entirely to the second acquirer. In such a situation, the Court held, ‘a restriction of the resale of copies of computer programmes downloaded from the internet would go beyond what is necessary to safeguard the specific subject matter’ of the copyright to the computer programme.

2. The Problematic Legal Reasoning of the CJEU

2.1. The CJEU fails to discuss the scope of the distribution right

In the UsedSoft decision, the CJEU started out by addressing the question ‘whether and under what conditions the downloading from the internet of a copy of a computer programme, authorised by the copyright holder, can give rise to exhaustion of the right of distribution of that copy in the European Union within the meaning of Article 4(2) of Directive 2009/24’. This was the second question referred to the CJEU by the BGH, and the Court answered it by interpreting the sale criterion of Article 4(2) – the meaning of ‘first sale’, which leads to the exhaustion of the distribution right for computer programmes. The entire interpretation of the Court is at this point exclusively linked to Article 4(2) and not to the concept of distribution pursuant to Article 4(1)(c). The Court’s approach may seem to be a result of the questions referred to it by the BGH, as the latter asked whether the distribution right was exhausted by the downloading of the programme, without expressly addressing whether the distribution right applies to the

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6 UsedSoft (n 3) paras 70 and 78. It may indeed be difficult to prove whether this is the case, but as the CJEU rightly observes, the right holder is faced with the same problem when distributing tangible copies of the programme – also in this situation ‘it is only with great difficulty that he can make sure that the original acquirer has not made copies of the program which he will continue to use after selling his material medium’ (para 79). On the other hand, the CJEU underlines that ‘a copyright holder such as Oracle is entitled, in the event of the resale of a user licence entailing the resale of a copy of a computer program downloaded from his website to ensure by all technical means at his disposal that the copy still in the hands of the reseller is made unusable’ (para 87). The approach of the Court has been criticised as ‘cynical’ with reference to the putative fact that ‘it is a big difference for the hen between the two cases: where the fox should go after it if he wants to get the hen and when the hen is placed in the foxes’ cage in the zoo with the inscription ‘you should swear you do not eat it!’: see Mihály Fiscor, ‘Relevance of Exhaustion of Rights in the Digital Environment’, powerpoint presentation at the 2013 ALAI Congress, <http://www.alaicartagena2013.com/index.php/congress/papers> (slide 55). The analogy to this version of the hen and the fox story is, however, hardly striking. Since the user will run the computer programme on his or her computer even in the ‘tangible copy’ situation, the hen is as much ‘in the cage’ in this situation as in the downloading situation. The problem in both situations is ‘to prove that the fox did not eat the hen’, and there is hardly any difference between the two in this respect. Thus, the Court’s comparison seems more realistic than cynical.

7 Thus, the Court explicitly states that ‘if the licence acquired by the first acquirer relates to a greater number than he needs ..., the acquirer is not authorized ... to divide the licence and resell only the user right for the computer program concerned corresponding to a number of users determined by them’: UsedSoft (n 3) para 86.

8 UsedSoft (n 3) para 63.
transaction enabling the download. The latter problem is, however, implied in the third question referred – whether the acquirer of the ‘used license’ can rely on the exhaustion of the right to distribute the copy of the computer programme made by the first acquirer to download the programme onto a data carrier as a ‘lawful acquirer’. If the distribution right does not apply to the transfer of (ownership to) intangible copies, the second acquirer consequently cannot rely on the exhaustion of the distribution right to download the programme as a ‘lawful acquirer’. Contrary to this, an alternative ground would be needed in order to make the downloading lawful. This demonstrates that the CJEU should have addressed the scope of the distribution right as a starting point of its analysis before addressing the application of Article 4(2), and that it would have been unnecessary to the analysis to rephrase the questions of the BGH.

The rights scheme of the Directives dealing with copyright in the online environment, including the Computer Programme Directive (CPD), cannot be properly understood without first examining the Copyright Directive (EUCD). This Directive, which bases its exploitation rights on the rights scheme of the 1996 World Intellectual Property Organisation (WIPO) Copyright Treaty (WCT), enumerates three kinds of rights: the reproduction right, the distribution right and the communication right, which includes the right to make availability on demand. While the reproduction right applies both to the digital and the analog environment, it is evident for several reasons that the distribution right provided for was meant to be limited to the distribution of tangible objects, and that any kind of online dissemination is regulated by the right to communication to the public. First, it follows explicitly from the Agreed Statement to WCT Article 6 that the ‘expressions “copies” and “original and copies”, being subject to the right of distribution … refer exclusively to fixed copies that can be put into circulation as tangible objects’. At the same time, the communication right pursuant to WCT Article 8 covers any act of communication to the public by wire and wireless means – in other words, any act of online transmission. Admittedly, the WCT does not prevent contracting parties from implementing the obligations under the treaties through a different rights scheme – for example, by way of a broad distribution right that covers certain acts of online transmissions and thus implements the communication right in this way, akin to the situation in the USA. Yet, as long as the EU has adopted the WCT rights scheme, which the CJEU confirms both in UsedSoft and its earlier decision in the Peek & Cloppenburg case, this scheme should be followed.

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9 According to the Vienna Convention on the Law of Treaties Art 31(1), a treaty ‘shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose’. The context for the purpose of interpretation shall, inter alia, comprise ‘any agreement relating to the treaty which was made between all the parties in connexion with the conclusion of the treaty’ (Art 31(2)(a)). An agreed statement to the WCT shall be considered as such agreement: see eg Sam Ricketson and Jane Ginsburg, International Copyright and Neighbouring Rights (Oxford University Press 2006) 190–91.

10 This follows from the so-called ‘umbrella solution’ under the WIPO 1996 Treaties: see eg Mihály Fiscor, The Law of Copyright and the Internet (Oxford University Press 2002) 208–09.

Secondly, there are many indications in the EUCD that the distribution right in Article 4 is limited to distribution of tangible copies. Recital 28 of the preamble states that ‘copyright protection under this Directive includes the exclusive right to control distribution of the work incorporated in a tangible article’ and cites the exhaustion rule in the following. Recital 29 emphasises that ‘the question of exhaustion does not arise in the case of services and on-line services in particular’ and that ‘unlike CD-ROM or CD-I where the intellectual property is incorporated in a material medium ... every on-line service is in fact an act which should be subject to authorization where the copyright or related right so provides’. Read in context with the above Agreed Statement to WCT Article 6, WCT Article 8 and EUCD Article 3(3) – the latter of which states that the right to communication to the public shall not be exhausted – the picture becomes quite clear: the distribution right under the Directive applies to the distribution of tangible copies and is subject to exhaustion. Any act of online activity is covered by either the reproduction right or the communication right, to which no exhaustion rule is applicable.

Turning to the CPD, Article 4(1)(c) provides for the right holder to authorise exclusively ‘any form of distribution to the public, including the rental, of the original computer program or of copies thereof’. This right is enumerated alongside the rights of reproduction and adaptation of the programme. Contrary to EUCD Article 3, the CPD does not provide for any right of communication to the public. This is easily explained by the fact that communication to the public about computer programmes was hardly a viable form of exploitation at the time when the first version of the Directive was adopted in 1991. Admittedly, it could have been possible to include this right when the first Directive was repealed and replaced by the current Directive. On the other hand,

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12 See Hansen and Roczyck (n 5) 909.
13 The Advocate General (AG) held in UsedSoft that ‘a converse reading’ of this sentence ‘implies that that right also includes other forms of distribution’ and that the subsequent reference to the exhaustion rule ‘does not limit exhaustion to one particular form of distribution’ (AG Opinion in UsedSoft (n 3) para 75).
14 Certainly, almost any statement can be read the way one wants it to be read, but it is noteworthy that the sentence states that copyright protection includes distribution of tangible copies and not that the distribution right includes such action. One may therefore wonder why the recital does not explicitly say that copyright protection also includes other kinds of distribution acts if the distribution concept were meant to cover such acts.
15 Again the Advocate General points to the alleged ambiguity of the provision, although he misread it when he says that by virtue of its wording the ‘exhaustion rule should not apply to an online purchase of a CD-ROM in which the copy of the computer program is incorporated’ (para 76). The recital holds a material copy made by the user on the basis of an online service as falling outside the scope of exhaustion – not a material copy sold or purchased online.
17 Cf Stieper (n 5) 668; and Senttleben (n 5) 2925. As both Stieper and Senttleben note, this observation is compatible with the statement made by Jon Bing, ‘Copyright Protection of Computer Programs’ in Estelle Derclaye (ed), Research Handbook on the Future of EU Copyright (Edward Elgar 2008) 401, 415, when discussing CPD Art 5(1), that ‘[i]t may not be unfair to maintain that the Computer Programs Directive is drafted on the understanding that the transaction will involve the acquisition of a physical medium, typically diskettes or compact disks, on which the program is stored’.
18 See on that point Hartmann (n 5) 982.
there was no reason to do so as the EUCD also applies to computer programmes. 18 While Article 1(2) of this Directive explicitly states that the Directive shall leave intact and in no way affect existing Community provisions related to computer programmes, there is nothing that prevents it from supplementing the copyright protection for software. Hence, an interpretation in which the concepts of the distribution right and the reproduction right are understood in accordance with the EUCD and where the communication right of the latter supplements the exploitation rights in the CPD, would not necessarily affect the rights pursuant to the CPD.

The CJEU on the contrary emphasised the role of the CPD as a lex specialis to the EUCD, with reference to EUCD Article 1(2). This was, however, not done in the context of the concept of the distribution right in CPD Article 4(1)(c) but when interpreting the sale criterion under the exhaustion rule in Article 4(2). As is discussed later, the lex specialis argument may make sense in the latter context, 19 but in relation to the rights scheme it is highly problematic. The Court did not discuss this problem. However, the Advocate General addressed this in his Opinion in the case when stating that he did ‘not think that the distribution of a computer program by download from the internet can escape classification as a “distribution right” so as to fall within the definition of the right of communication to the public provided for in Article 3(3) of [the EUCD]’. 20 One of his arguments was rooted in EUCD Article 1(2) as he held that the CPD ‘makes no reference to the concept of right of communication and defines the right of distribution in the broadest sense as encompassing “any form of distribution to the public … of the original computer program or copies thereof”’. He therefore found ‘it difficult to conclude, on a combined reading of those two directives, that the right to make a work available to the public as referred to in art 3(1) of the [EUCD] is applicable to computer programs’. 21 The arguments are unconvincing. As shown above, there are clear reasons why the CPD does not make any reference to communication to the public, and the fact that the Directive speaks about ‘any form of distribution’ says nothing about the very content of the distribution concept.

The only reference the CJEU made to the discussion about the scope of the distribution right, is its holding, when discussing the scope of the sale criterion, ‘that the existence of a transfer of ownership [of a digital copy] changes an “act of communication to the public” provided for in Article 3 of [the EUCD] into an act of distribution referred to in

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18 This follows from the general statement of EUCD Art 1(1) that the Directive concerns the ‘legal protection of copyright and related rights in the framework of the internal market, with particular emphasis on the information society’. The statement in Art 1(2) that the Directive ‘shall in no way affect’ existing provisions, including provisions relating to the protection of computer programmes, means that in such a situation only the latter shall have priority in a case of conflicting provisions. See also EUCD recital 20. The view that the EUCD does not extend to computer programmes – see eg Westkamp (n 2) 54 n 139 – is thus without legislative support.

19 See further section 2.2.

20 AG Opinion in UsedSoft (n 3) para 71. The statement as such is not entirely consistent. The right ‘provided for’ follows from Art 3(1), not the non-exhaustion provision of Art 3(3).

21 AG Opinion in UsedSoft (n 3) para 72.
Article 4’.

In this respect, the Court referred to the Opinion of the Advocate General where he made his second argument as to why the distribution of a computer programme by download is covered by the distribution right. Here, the Advocate General explicitly emphasised that the right of communication to the public must be interpreted in light of WCT Article 6(1). He pointed to the fact that ‘the treaty refers to the distribution right as being the right to authorize the making available to the public of the original and copies of a work “through sale or other transfer of ownership”’, and added: ‘The wording of that provision is unequivocal. The existence of a transfer of ownership clearly changes a mere act of communication to the public into an act of distribution’. This inference is incomprehensible in light of the explicit expression in the Agreed Statement to WCT Article 6 that the word ‘copies’ in that provision exclusively refers to tangible copies. However, it becomes no easier to understand when considering that the Advocate General, by reference to the arguments of Oracle and the EU Commission, explicitly mentioned the Agreed Statements in his Opinion without discussing the impact of them on the interpretation of Article 6. The Advocate General failed to give any reasons why the distribution concept of Article 6 should not be interpreted in accordance with the Agreed Statement to the provision, indeed because there are none. It thus becomes rather apparent that one cannot have it both ways – arguing on the one hand that the rights scheme of the EU Directives is predicated on the WCT rights scheme, and on the other hand, being in favour of extending the distribution right to the online context, on the account of the communication right. If the distribution right should apply in the online context, it must be because the rights scheme deviates from that under the WCT. The Advocate General’s holding is therefore inconsistent with the WCT.

The Court of Justice’s adaptation of the Advocate General’s reasoning adds a further problem; namely that the Court did not discuss the scope of the distribution right but adhered to the Advocate General’s view when interpreting the sale criterion of Article 4(2). Pointing out that the CPD constitutes a lex specialis to the EUCD, the Court emphasised that ‘even if the contractual relationship at issue might be covered by the concept of “communication to the public” within the meaning of Article 3(1) [EUCD], the “first sale ... of a copy of a program” within the meaning of Article 4(2) [CPD] would still give rise ... to exhaustion of the right to distribution of that copy’. The adherence to the Advocate General’s view that the transfer of ownership changes an act of communication to the public into an act of distribution was presented in this context as an additional argument for why the contractual relationship between the rightholder and its customer, within which the downloading of a copy of the programme takes place, equates with a ‘first sale’ pursuant to Article 4(2) CPD. Thus, even the Court’s statement about the ‘act of distribution’ is in fact an argument in favour of extending the concept of ‘first sale’ to digital downloads.

22 UsedSoft (n 3) para 52.
23 AG in UsedSoft (n 3) para 73.
24 Similarly, see Stieper (n 5) 668.
25 UsedSoft (n 3) para 51.
Consequently, while the Advocate General delivered unconvincing arguments in favour of applying the distribution right to digital downloads, the problem with the Court’s decision is that it failed to discuss the application of the distribution right to the facts in question. The reason for that may be an implicit premise that the distribution concept inherent in Article 4(1)c) and the sale criterion in Article 4(2) correlate. The legal ground for and the sustainability of such a premise is discussed in the following subsection.

2.2. Correlation between the distribution concept and the sale criterion?

In the Peek & Cloppenburg decision, the Court interpreted EUCD Article 4 so as to perform a perfect correlation between the distribution concept and the exhaustion criterion. The Court based its interpretation upon WCT Article 6(1) which defines the distribution right as a right of authors to authorise ‘the making available to the public of the original and copies of their work through sale and other transfer of ownership’ (emphasis added). At the same time, Article 6(2) states that nothing shall affect the freedom of contracting parties to determine the conditions under which the exhaustion of the right applies ‘after the first sale or other transfer of ownership’ (emphasis added). The Court held that paragraphs 1 and 2 of Article 6 ‘form a whole and should be interpreted together’ and stated that ‘since Article 4 [of the EUCD] implements Article 6 of the [W]CT and should be interpreted as a whole, it follows that the term [distribution to the public by sale and] “otherwise” in Article 4(1) … must be interpreted in accordance with the meaning given to it in Article 4(2), that is to say, as entailing a transfer of ownership’.

Much could be said about this statement in the context it is given, but it follows from the discussion above that if this view is transferred to the UsedSoft situation, the result must be that both the distribution concept and the sale criterion are limited to the distribution of tangible copies. As pointed out above, the distribution right called for in WCT Article 6 must be interpreted as limited to the distribution of tangible copies – this follows explicitly from the Agreed Statements to the provision and cannot be circumvented by an interpretation of the sale criterion under the exhaustion rule. So, if the Court bases its rationale in UsedSoft on its holding in Peek & Cloppenburg that the sale criterion equates with the distribution concept, with reference to WCT Article 6, its statement ‘that it does not appear from art 4(2) of [the CPD] that the exhaustion of the right of distribution of copies of computer program … is limited to copies of programmes on a material medium’, is fully unconvincing as long as the Court does not discuss the impact of the Agreed Statements to WCT Article 6 in this context.

However, it does not follow that there is a necessary correlation between the distribution concept and the sale criterion in this respect from WCT Article 6.

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26 Peek & Cloppenburg (n 11) paras 29–36.
27 Peek & Cloppenburg (n 11) para 35.
28 UsedSoft (n 3) para 55.
Admittedly, it is reasonable to read the Agreed Statement to Article 6 as not only applying to the distribution concept in Article 6(1) but also to the exhaustion rule in Article 6(2). Thus, the explicit freedom of the contracting parties ‘to determine the conditions ... under which the exhaustion of the right ... applies after the first sale or other transfer of authorship’ seems to be limited to distribution of tangible copies sold by or with the authorisation of the author. On the other hand, this does not exclude the possibility of extending national or regional exhaustion rules to the distribution of copies that are reproduced on the basis of an online service. It only means that such extension must comply with the three step test in WCT Article 10(2). Therefore, WCT Article 6 is no obstacle to interpreting the sale criterion in CPD Article 4(2) so as to include situations where copies are made on the basis of an online transmission. Nevertheless, as already held, WCT Article 6 cannot possibly serve as an argument in favour of reading both the distribution right and the sale criterion under the exhaustion rule as comprising transfer of ownership on the basis of an online transmission.

If, however, one acknowledges that the distribution right does not apply to this situation, and that Articles 4(1) and 4(2) of the Directives do not ‘form a whole’ but regulate different aspects of the distribution right, much of the Court’s reasoning in the UsedSoft case is legally defensible. Under this premise, it may make sense to hold that it does not appear from Article 4(2) that the exhaustion of the distribution right is limited to tangible copies, but that, by referring to ‘sale’, the provision ‘makes no distinction according to tangible or intangible form of the copy in question’. Under the same premise, it is furthermore understandable that the Court emphasises the role of the CPD as a lex specialis in order to avoid addressing the obvious problem under the EUCD – that recital 29 of the preamble to the Directive explicitly states that ‘[t]he question of exhaustion does not apply to services and on-line services in particular’ and that ‘[t]his also applies with regard to a material copy of a work or other subject-matter made by a user of such a service with the consent of the rightholder’. To be sure, the Court also puts forward more general arguments that may speak in favour of exhaustion of the distribution right by a transfer of ownership of copies downloaded on the basis of an online service. Yet, the result in UsedSoft is based on the CPD and the premise that this Directive does not differentiate between tangible and intangible copies as far as the exhaustion of the distribution right is concerned.

In my opinion, this result is sustainable, if not impeccable, as long as it is recognised that the sale criterion under the exhaustion rule in CPD Article 4(2) does not correspond to the concept of distribution in Article 4(1). The problem with this assumption, however,

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29 This provision states that ‘Contracting Parties shall ... confine any limitations of or exceptions to rights ... to certain special cases that do not conflict with a normal exploitation of the work and do not unreasonably prejudice the legitimate interests of the author’. In the Agreed Statements to the provision, it is underscored that the provision ‘should be understood to permit Contracting Parties to devise new exceptions and limitations that are appropriate in the digital network environment’.

30 UsedSoft (n 3) para 55.

31 UsedSoft (n 3) paras 61–63.

32 See also ibid, paras 56–59.
is that the result would not solve the problem in *UsedSoft*. If the distribution right only applies to the transfer of tangible copies, exhaustion of this right on the basis of a transfer of ownership to intangible copies would mean that the first acquirer of the programme may resell tangible copies (e.g. CDs) reproduced on the basis of the online service irrespective of the distribution right (provided that he or she does not retain any tangible or intangible copies of the programme). On this premise, the exhaustion of the distribution right would not apply to the situation in *UsedSoft*, where UsedSoft customers downloaded the programme from the Oracle website or made digital copies of programmes they already had through additional licenses. As pointed out above, the Court’s application of the exhaustion rule to the *UsedSoft* situation seems to be based on the assumption of a perfect correlation between the distribution concept and the exhaustion criterion. Nevertheless, this assumption alone cannot justify the result in *UsedSoft* and to make matter worse, the Court does not even discuss the sustainability of it in light of the glaring counterarguments.

### 2.3. The insufficiency of CPD Article 5(1)

The final problem with the legal reasoning of the CJEU is its application of CPD Article 5(1), which is the legal ground for permitting the reproduction (downloading) by the acquirers of the programme. The provision states that in the absence of specific contractual provision, reproduction of the programme shall not require authorisation by the right holder where it is necessary for the use of the computer programme by the lawful acquirer. The Court held that the first download by the customer of the copyright owner must be considered as a reproduction necessary for the use of the computer programme by the lawful acquirer. 33 This is hardly to be disputed. Next, it recalled that the copyright holder’s distribution right was exhausted after the first sale of any copy, tangible or intangible, of his or her computer programme. Therefore, the Court held, ‘since the copyright holder cannot object to the resale of a copy of a computer program for which that rightholder’s distribution right is exhausted, it must be concluded that a second acquirer of that copy and any subsequent acquirer are “lawful acquirers”’. As a consequence, the new acquirer of the software license would be ‘able to ... download onto his computer the copy sold to him by the first acquirer’. 34 At this point, the Court deviated from the opinion of the Advocate General. The latter held, in short, that the distribution right applied to the ‘resale of the downloaded copy by the first acquirer’, but not ‘to the assignment of the user license such as that issued by Oracle to its customers’, since this involved ‘the exercise of the exclusive right of reproduction’, as it allowed ‘a new copy of the program to be made by download from the internet or by reproduction from a copy already held by the user’. This obstacle, the Advocate General held, could not ‘be circumvented by recourse to Article 5(1) of [the CPD]’. 

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33 *UsedSoft* (n 3) para 75.
34 *UsedSoft* (n 3) paras 80–81.
35 AG Opinion in *UsedSoft* (n 3) paras 96–99.
The approach of the Advocate General is consistent to some extent with a formalistic point of view. The second acquirer’s copying in the *UsedSoft* case was not a result of any transmission from the first acquirer – in the relationship between the first and the second acquirer it only involved reproduction of the work (downloading from the Oracle website or making new copies). On the other hand, even if the programme had been downloaded from the first acquirer’s website, a reproduction of a *new copy* on the part of the second acquirer must have taken place. If the exhaustion of the distribution right is to apply at all to the transfer of intangible copies, some sort of fictional approach regarding the copy transferred from the first acquirer seems to be necessary if it shall make any sense.\(^{36}\) The paramount reason why Article 5(1) should not be considered as sufficient legal ground for the download is simply that, in EU law, the distribution right does not apply to the transfer of intangible copies. Under this view, therefore, exhaustion of the distribution right does not make an individual who relies on a digital resale a ‘lawful acquirer’ under CPD Article 5(1).

### 2.4. Conclusion

In conclusion, the Court’s ruling in *UsedSoft* is not based on sustainable or consistent legal arguments. On the one hand, it seems to be predicated on the correct premise that the EU Directives follow the rights scheme of the WCT.\(^{37}\) On the other hand, the Court fails to recognise the evident consequence therein; namely that the distribution right under this premise only applies to making available *tangible* copies of the work – which is clearly reflected in Articles 28 and 29 of the EUCD’s preamble. The Court’s arguments in favour of applying the *exhaustion* criterion in CPD Article 4(2) to copies downloaded from the Internet with the consent of the right holder do not solve this problem, and neither does the ‘lawful acquirer’ rule in CPD Article 5(1). The flawed premises for the Court’s ruling consequently weaken its authority as precedent for further cases in the field.

Despite taking into consideration that the Court not only puts forward formal legal arguments but also several policy arguments in favour of its result, the question can be raised whether the policy arguments might be supported on sounder legal grounds. The following section deals with this question.

### 3. Could the Outcome of the CJEU Ruling Be Reached with A Different Approach?

Ever since the *Deutsche Grammophon* case of 1971, EU law has articulated an exhaustion principle based on the rules on free movement of goods (currently laid down in Articles

\(^{36}\) Compare eg Victor F. Calaba, ‘Quibbles ‘n Bits: Making a Digital First Sale Doctrine Feasible’ (2002) 9 Michigan Telecom Tech L Rev 1–34, pointing out on the one hand that the US first sale doctrine (US Copyright Act s 109 which equates with the exhaustion principle) ‘does not apply to digital works’ because ‘in transferring a digitized work, the user is not transmitting her “particular” copy’ (14), but suggesting on the other hand amendments to ‘the Copyright Act so that confusion is resolved as to whether ... [a digital first sale doctrine] exists’ (26).

\(^{37}\) *UsedSoft* (n 3) para 52.
34 and 36 of the Treaty on the Functioning of the European Union (TFEU)). The basic rationale behind the exhaustion rule in the copyright context, which the CJEU confirms in the *UsedSoft* case, is that the control of the resale of copies of work would amount to an illegitimate partitioning of the common market which is not justified as part of the ‘specific subject matter’ of copyright. Until the *UsedSoft* case, the Court’s application of the exhaustion rule was limited to the distribution of tangible copies. Thus, the Court refrained from applying an exhaustion principle on the basis of the rules on free movement of services (currently laid down in TFEU Articles 56 and 57) in the *Coditel I* case (1980), which concerned the cable retransmission of a broadcasted film. The reason was that a film made available to the public by performances ‘may be infinitely repeated’ and that the problems involved were not the same as when a work was distributed in material form. The Court emphasised the legitimate interests the copyright owner had in calculating the fees on the basis of the actual or probable number of performances, the underlying premise being that this interest would not be secured if the right to perform a film were limited to the first broadcasting of it.

Similarly, in *Warner/Christiansen* (1988) regarding the rental of videocassettes, the Court refused to hold that the copyright owner’s right to rental was exhausted under the rules concerning free movement of goods, with reference to the fact that under such a rule it would be ‘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’.

On the other hand, in the *Premier League* case, decided the year before *UsedSoft*, the CJEU held that TFEU Article 56 on free movement of services precluded national legislation to make it unlawful to import and to sell and use foreign decoding devices giving access to an encrypted satellite broadcasting service from another Member State. In that case, the Court held that the right holders would be remunerated for the broadcasting in the Member State where the broadcasting took place and in which an appropriate remuneration would be payable based on the actual and potential audience both in the Member State of broadcast and in any other Member State. Contrary to the opinion of the Advocate General in the same case, the CJEU did not expressly refer to the principle of exhaustion, but the rationale behind the ruling follows that of exhaustion.

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39 *UsedSoft* (n 3) para 62.
41 *Coditel I* (n 40) paras 12–17.
44 *Premier League* (n 43) paras 111–112.
45 AG Opinion in *Premier League* (n 43) para 188.
Consequently, an important factor in distinguishing exhaustion and non-exhaustion in EU law seems to be whether or not the right holder is in a position to calculate the remuneration on the basis of the first act of exploitation. The rights scheme set out in the EUCD is obviously predicated on this premise: exhaustion occurs in the context of distribution of tangible copies (Article 4(2)) but not in the context of the right to communication to the public (Article 3(3)), nor is the reproduction right covered by any exhaustion rule. Further, recital 29 of the preamble underscores the basic rationale behind the scheme:

The question of exhaustion does not arise in the case of services and on-line services in particular ... Unlike CD-ROM or CD-I, where the intellectual property is incorporated in a material medium, namely an item of goods, every on-line service is in fact an act which should be subject to authorization where the copyright or related right so provides.46

What the CJEU actually did in UsedSoft was to put forward arguments in favour of applying the exhaustion rationale to situations where copies of a computer programme are downloaded on the basis of an online service. Thus, the Court held that:

[t]he making available by Oracle of a copy of its computer program and the conclusion of a user licence agreement for that copy are ... intended to make the copy usable by the customer, permanently, in return for payment of a fee designed to enable the copyright holder to obtain a remuneration corresponding to the economic value of the copy of the work of which it is the proprietor.47

According to the Court, ‘from an economic point of view, the sale of a computer program on CD-ROM or DVD and the sale of a program from the internet are similar’ as the ‘on-line transmission method is the functional equivalent of the supply of a material medium’.48 It added that ‘the objective of the principle of exhaustion ... is, in order to avoid partitioning of markets, to limit restrictions of the distribution of those works to what is necessary to safeguard the specific subject matter of the intellectual property concerned.’49 Consequently, the Court held:

[t]o limit the application ... of the principle of ... exhaustion ... solely to copies of computer programs that are sold on a material medium would allow the copyright holder to control the resale of copies downloaded from the internet and to demand further remuneration on the occasion of each new sale, even though the first sale of the copy had already enabled the rightholder to obtain an appropriate remuneration. Such a restriction

46 On this point, see too the Directive’s legislative history, ie the Green Paper on Copyright and Related Rights in the Information Society, COM (95) 382 final, 47–48, and the follow up to the Green Paper, COM (96) 568 final, 19; Commission Proposal (n 15) 27.
47 UsedSoft (n 3) para 45.
48 UsedSoft (n 3) para 61.
of the resale of copies of computer programs downloaded from the internet would go beyond what is necessary to safeguard the specific subject-matter of the intellectual property.\textsuperscript{50}

As follows from the discussion in the previous section, basing these arguments on the rule of exhaustion of the distribution right of the CPD involves an inconsistent legal reasoning and is obviously contra legem. The Court should have respected the straightforward decision of the lawmaker to limit the right of distribution of tangible copies and recognise as a point of departure that the right of communication to the public, which includes provisions on availability, is not subject to exhaustion under the rules of the copyright Directives (EUCD Article 3(3)). On the other hand, it follows from the long-standing case law of the Court that restrictions on free movement of goods and services are only permissible if they are necessary to safeguard the specific subject matter of the intellectual property.\textsuperscript{51} Moreover, as also emphasised by the CJEU in previous case law, ‘a directive cannot justify obstacles to intra-Community trade save within the bounds set by the Treaty rules’.\textsuperscript{52} Hence, as long as the Court is of the opinion that restricting the resale of electronic copies of computer programs downloaded from the Internet would go beyond what is necessary to safeguard the specific subject matter of copyright, national rules permitting it will conflict with the Treaty rules on free movement of goods or services as they undoubtedly will have the potential to affect trade between Member States.\textsuperscript{53} Whether the goods or services rules, or both, shall apply to this situation is debatable, although the most consistent view from a free movement perspective is that transactions, such as those in the UsedSoft case, in which the customer is assigned to carry out certain intangible operations (downloading a computer programme), and which do not involve the distribution of tangible objects, should be regulated under the regime for free movement of services, regardless of whether the transaction as a whole is classified as a ‘sale’.\textsuperscript{54}

This solution will not mean that the right of communication to the public or the right to reproduction are exhausted as such. What one can gather from this is that the exhaustion principle based on the free movement rules applies to the extent that its rationale justifies it, and that the statement in recital 29 to the preamble of EUCD that ‘[t]he question of exhaustion does not arise in the case of services and on-line services in particular’ is too broad if it is read as a description of the legal situation also under the rules on free movement of services.\textsuperscript{55} The rights scheme of the Directives would be

\textsuperscript{50} UsedSoft (n 3) para 63.

\textsuperscript{51} It follows from that case law (see eg n 42) that the term ‘specific subject matter’ functions as a demarcation line of what, according to the CJEU, shall be considered as the essence of IP rights which will not be affected by the free movement (or competition) rules.

\textsuperscript{52} See eg joined cases C-427/93, C-429/93 and C-436/93, Bristol Myers Squibb and others v. Paranova A/S [1996] ECR I-3457 para 36.

\textsuperscript{53} See also Senftleben (n 5) 2926–27.

\textsuperscript{54} For a seemingly different opinion, see Senftleben (n 5) 2926.

\textsuperscript{55} To the latter point, also see Westkamp (n 2) 48–49.
supplemented under this approach by the free movement rules, but not be diluted by the application of the same rules.

If the Court had chosen to support its reasoning on the free movement of services instead of CPD Article 4(2), it would at least have reached a legally consistent solution that avoids much of the uncertainty that the UsedSoft decision engenders. This point is revisited in the closing section. Before this, I discuss the soundness of the policy considerations of the decision.

4. Policy Aspects – UsedSoft v Re Digi

As previously pointed out, the UsedSoft decision is based on the policy premise that even the online sale of computer programmes enables the right holder to calculate an appropriate fee for the further use of the programme. A restriction on the digital resale will therefore represent an unjust trade restriction.

The UsedSoft judgment contrasts with the recent ReDigi decision by a US District Court concerning a ‘marketplace for digital used music’. The company ReDigi has set up a service that allows users to sell and buy used digital music files. In accordance with the premises in UsedSoft, the ReDigi service does not allow the seller to retain music that has been sold or uploaded and it contains mechanisms to ensure this. In a partial summary judgment, the District Court still found ReDigi liable both for direct and secondary infringements. Concentrating on the grounds for direct infringement, the District Court held that both the reproduction right and the distribution right were infringed, denying a fair use defence for the former and the application of the first sale doctrine for the latter. The US legal framework is different than the European, and the more formal legal considerations of the District Court will not be highlighted here. Of particular interest, however, are the District Court’s policy-oriented arguments as to why the fair use rule and the first sale doctrine do not apply.

Regarding the fourth factor of the fair use rule in section 107 of the US Copyright Act, the District Court held that ReDigi’s sales are likely to undercut the ‘market for and value of the copyrighted work’. The Court argued that:

[t]he product sold in ReDigi’s secondary market is indistinguishable from that sold in the legitimate primary market save for its lower price. The

56 Capitol Records v ReDigi Inc. (2013), case No 12-0095 (US District Court Southern District of New York). Moreover, the finding of the CJEU that a computer programme license qualifies as a ‘sale’ as long as it is unlimited in time (UsedSoft (n 3) para 45) conflicts with previous US case law, eg Timothy S. Vernor v Autodesk Inc. (2010) F 3d 1102 (9th Circuit).

57 17 USC s 107 puts limitations on the exclusive rights that follow from s 106 where there is ‘fair use’. The assessment of fair use involves considering the following four factors: (1) the purpose and character of the use; (2) the nature of the copyrighted work; (3) the amount and substantiality of the portion used in relation to the copyrighted work as a whole; and (4) the effect of the use upon the potential market for or value of the copyrighted work.
clear inference is that ReDigi will divert buyers away from that primary market.\textsuperscript{58}

Similarly, in discussing the application of the first sale doctrine, the District Court referred to the reasons set out by the US Copyright Office (USCO) in its report on the Digital Millennium Copyright Act for rejecting the extension of the doctrine to distribution of digital works. Here the USCO emphasised the differences between physical copies and digital information in that the latter does not degrade with time and use, and is just as desirable as a new copy of the same work. The report, which the District Court cited on this point, also stresses that the ‘need to transport physical copies of works which acts as a natural brake on the effect of resales on the copyright owner’s market, no longer exists in the realm of digital transmissions’, so that the ‘ability of such “used copies” to compete for market share with new copies is ... far greater in the digital world’.\textsuperscript{59}

Contrasting the CJEU’s arguments in \textit{UsedSoft} with the District Court’s decision in \textit{ReDigi}, one gains a fairly good picture of the various policy considerations at stake. On the one hand, it may be held that the right holder will be in a position to calculate his or her fee for the use of the digital product, provided that the amount of users is stable and does not increase as a result of the digital transfers. At this point, it is possible to simulate the effects of the sale of tangible (digital) copies although the analogy is not necessarily perfect in this respect. On the other hand, it may be claimed that there is no real secondary market for ‘used’ digital files since the quality of the product is the same. This not only differentiates the market situation for digital copies from that of analog ones, there is also a difference between tangible digital copies (like CDs and DVDs) and digital information transferred online. Tangible copies are likely to have a ‘used appearance’ while mere digital information does not have any appearance at all, but will have exactly the same characteristics irrespective of the classification of ‘new’ or ‘used’ products. Accordingly, it is possible to claim that allowing a market for ‘used digital (and intangible) copies’ will undercut the position derived from the right holder’s exclusive right. Hence, the calculated fee will not be ‘appropriate’. From an internal market perspective, the point can be made that an opening for competition from ‘used content stores’ can contribute to countering possible price discrimination between national markets, in a similar way as parallel imports of goods. A possible response from the right holder can be to offer additional services that differentiate the ‘original product’ from the ‘used product’. As far as computer programmes are concerned, after-sale services like maintenance and updates are straightforward examples. Additionally, the CJEU recognised in the \textit{UsedSoft} decision that the exhaustion does not ‘relate to contracts for services, such as maintenance agreements’.\textsuperscript{60} The Court held, though, that

\textsuperscript{58} See section III B 1, Judge Sullivan’s opinion.
\textsuperscript{60} \textit{UsedSoft} (n 3) para 66.
the acquirer can rely on updates at the time of the lawful acquisition of the programme.\footnote{\textit{UsedSoft} (n\ 3) para 67.}

In its decision, the CJEU failed to discuss the counter-arguments that show that the analogy to distribution of tangible copies is far from perfect, a matter that could point in the direction that preventing the sale of 'used digital copies' is part of a specific subject matter of copyright law. Still, the Court has a long tradition for giving priority to free movement considerations even when there are clear objections in favour of a restriction.\footnote{See eg joined cases \textit{C-267/95 and C-268/95 Merck & Co Inc. et al v Primecrown Ltd.} [1996] ECR I-6285, regarding parallel imports of pharmaceutical products in a situation where the pharmaceutical is subject to heavy public price regulation in the exporting State.} Bearing this in mind, the \textit{UsedSoft} decision is not so surprising, even though it means that the policy priorities in Europe will deviate from those that have thus far prevailed in the United States.

5. Conclusion – and Outlook

The \textit{UsedSoft} decision is based on unconvincing legal premises. Firstly, the CJEU has failed to discuss the scope of the distribution right. Secondly, the Court's underlying premise that there exists a perfect correlation between the distribution concept and the sale criterion under the exhaustion rule – a premise that leads to applying both to the transfer of intangible copies – is inconsistent with the ground upon which it is implicitly predicated, namely WCT Article 6(1). However, the policy grounds for applying the exhaustion principle are consistent with the Court's previous case law on free movement of goods, even if that should extend in this case to the free movement of services. Nonetheless, one could wish that the Court had also discussed arguments showing that the analogy to tangible copies is imperfect.

The question that remains after a decision which is not legally convincing but could be supported on different legal grounds, is: what now? The Court's formal arguments are based on the application of CPD as a \textit{lex specialis} to EUCD, which easily leads to the conclusion that the decision does not necessarily extend to other kinds of works than computer programmes.\footnote{See also case \textit{C-355/12 Nintendo Co. Ltd. and others v PC Box Srl}, decision of 24 January 2014 (not yet reported), where the CJEU found that the \textit{lex specialis} rule did not prevent EUCD provisions on technical protection measures (Art 6) from applying to videogames, since they also comprised other kinds of works than computer programmes (para 23 of the decision).} Moreover, the provision in CPD Article 5(1), which is supposed to justify the downloading, also applies exclusively to computer programmes. Apart from an equivalent rule in the Database Directive,\footnote{Directive 9/96/EC on the legal protection of databases [1996] OJ L77/20, Art 6(1).} the EU Directives do not provide for grounds permitting reproduction on the basis of the exhaustion of the distribution right, except for EUCD Article 5(2)(b), which allows Member States to permit private copying for non-commercial purposes on the condition of fair compensation for right holders.
This provision does not, however, help businesses, universities or other undertakings wishing to sell their digital copies to third parties, whether private persons or not. If, on the contrary, the legal grounds for digital exhaustion were switched from exhaustion of the distribution right to the treaty rules on free movement of services, exhaustion of the communication right and the reproduction right would occur to the extent that the rationale for exhaustion provides for it, irrespective of the kind of work or protected subject matter involved. In this situation, the arguments in favour of exhaustion should be weighed against the argument that digital exhaustion can lead to the undercutting of the right holder’s exclusive right when determining whether the right holder is in a position to calculate an appropriate fee. The potential for product differentiation should be taken into account in this context.

Be that at it may, one should hope that the CJEU in later cases reconsiders the application of the distribution right to the transfer of intangible copies. The UsedSoft decision engenders great uncertainty as to the scope of the distribution right in EU law in a situation where many Member States have relied on this right only applying to the distribution of tangible copies. A different issue is that the UsedSoft case is yet another example of the problems that follow from the current categorisation of exploitation rights, and that an alternative approach is desirable. That is an issue for another day. As to the current legal situation, we have to cope with the categorisations, and any deviation to well-established law in this respect is only likely to create chaos under an already complicated rights structure. Hence, it would be easier to relate to a legal situation where ‘exhaustion’, even of the communication right and the reproduction right, as a point of departure, occurs to the extent that the right holder is in a position to calculate an appropriate fee that covers the use subject to exhaustion. That solution would also lead to a shift of focus away from the concept of ‘intangible copies’ and towards the actual use, which is a more realistic approach in the digital environment.