

THE EU COMPETITION LAW IMPLICATIONS OF AGREEMENTS TO KEEP PARALLEL IMPORTS OUT OF THE EEA

The use of agreements or concerted practices to keep parallel goods out of the European Union may result in a competition-law violation. Regardless of the status of the intellectual property rights embodied in goods first sold outside of the European Economic Area (EEA), the combination of restrictive agreements prohibiting export to the European Union, combined with a selective distribution system within the EEA that is in a position to exploit the resultant higher price in the market, could be found to violate Article 81 of the EC Treaty. As the European Court of Justice slowly delineates the complexities of intellectual property exhaustion, the competition-law issues raised by global parallel trade may come to overshadow the intellectual property considerations that have driven Court of Justice jurisprudence.

I. INTRODUCTION

THE European Court of Justice has narrowed the legal issues concerning the status of parallel goods originating from outside of the European Union.¹

¹ Hereafter the “EU,” as opposed to the European Economic Area, the “EEA”, established by treaty reprinted at [1992] 1 CMLR 921, the combination of the European Community and the European Free Trade Association, the “EFTA.” The EU is “the market” under consideration. However, it should be kept in mind that the parallel-importation rules applicable to the EU are, by necessity, applicable to the EEA. Goods in free circulation with the EEA member countries that are not members of the EU (commonly referred to as EFTA states: Norway, Liechtenstein, and Iceland) are considered to be in free circulation throughout the EEA and, hence, throughout the EU as well. See *Mag Instrument, Inc v California Trading Co, Norway, Ulsteen*, Case E-2/97, [1997] Report of the EFTA Court 129; [1998] 1 CMLR 331. Furthermore, the First Council Directive (89/104 EEC) of 21 December 1988, to approximate the laws of the Member States relating to trademarks [1989] OJ L40/1, 11 February 1989, hereafter “the Trade Marks Directive” or “the Directive,” is effective in EFTA countries through Art 65(2) and Annex XVII, point 4(c) of the EEA treaty. Additionally, Art 2(1) of Protocol 28 on intellectual property provides:

“To the extent that exhaustion is dealt with in Community measures or jurisprudence, the Contracting Parties shall provide for such exhaustion of intellectual property rights as laid down in Community law. Without prejudice to future developments of case law, this provision shall be interpreted in accordance with the meaning established in the relevant rulings of the Court of Justice of the European Communities given prior to the signature of the Agreement.”

The use of national intellectual property rights to block the importation or dissemination of extra-market goods² does not violate the free movement of goods principles³ embodied in Articles 28, 29, and 30 of the EC Treaty.⁴ Nor does it necessarily require a resolution of the issues concerning the international exhaustion of intellectual property rights.⁵ While an intellectual property owner's control over the intellectual property embodied in parallel goods may give the intellectual property owner cause to keep such goods off the market, there is a resultant effect upon the market as a result of the exercise of that control that implicates the competition laws, particularly Article 81.

II. WHAT ARTICLE 81 PROHIBITS IN RESPECT OF PARALLEL IMPORTS

Article 81(1) provides:

“1. The following shall be prohibited as incompatible with the common 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 common market, and in particular those which:

² Extra-market goods are goods that have at least some portion of their commercial life outside of the EU market. These goods are of two types: imports and re-imports. No distinction is necessary for purposes of the present discussion. Let us suffice to say that imports are extra-market goods that begin their commercial existence outside of the political boundaries of the market. Re-imports are goods that begin inside of the market by being sold for export out of the market, are sent out of the market, and then are re-imported into the market, usually against the wishes of the owner of any intellectual property rights carried by the goods.

³ *EMI Records, Ltd v CBS (UK) Ltd*, Case 51/75, [1976] ECR 811; [1976] 2 CMLR 235, paras 10, 22.

⁴ Treaty Establishing the European Community, Rome, 25 March 1957, TS 1 (1973), Cmnd 5179, as amended by the Treaty on European Union. This is a state of law rather than of fact. Once parallel goods are in free circulation within the market, it is impossible for purchasers to tell from where they came. Customs clearance is no guarantee that an intellectual property owner gave its consent for intellectual property protected goods to be imported from outside of the market. The potential for national legislatures to adopt rules requiring certificates of legality for extra-market goods is prohibited. Therefore, absent some indication of the legal status of goods printed directly onto the protected goods themselves by the intellectual property owner, the parallel-importation problem and the collateral threat of an infringement action from dealing in infringing, imported goods tends to hinder the movement of all intellectual property protected goods within the market.

⁵ As described in Cornish, *Intellectual Property: Patents, Copyright, Trade Marks and Allied Rights* (4th ed) (Sweet & Maxwell, London, 1999) pp 47-49, 767-770.

- (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.”⁶

Article 81(1) prohibits all agreements and concerted practices between competitors, actual or potential, that may affect trade between Member States and that lead to a distortion of competition within the market.⁷ In the early years of Common Market jurisprudence, there was a conceptual division in how the Article 81(1) prohibitions would be applied to transactions involving intellectual property.⁸ One portion of the division was said to be the existence of intellectual property rights. This existence was, and still is, protected by Article 295⁹ of the EC Treaty and has remained immune from the application of the competition laws in all but the most extreme cases.¹⁰ The other portion was the exercise of intellectual property rights.¹¹

⁶ EC Treaty, no 4 above, Art 81(1).

⁷ *Ibid.*

⁸ *Etablissements Consten, SA and Grundig-Verkaufs-GmbH v EC Commission*, Case 56, 58 [1966] ECR 299; [1966] CMLR 418. This development is addressed in Whish, *Competition Law* (3rd ed) (Butterworths, London, 1993) pp 331, 631 *et sub*, and discounted in Tritton, “Articles 30 to 36 and Intellectual Property: Is the Jurisprudence of the ECJ now of an Ideal Standard?” [1994] 10 EIPR 422.

⁹ EC Treaty, *supra*, note 4, Art 295, formerly Art 222, which states, “This Treaty shall in no way prejudice the rules in Member States governing the system of property ownership.”

¹⁰ *Radio Telefis Eireann (RTE) and Independent Television Publications, Ltd v EC Commission*, the “Magill” case, Joined Cases C-241-242/91, [1995] ECR 808; [1995] 4 CMLR 718. This case was decided on an application of EC Treaty Art 82, abuse of a dominant position, to facts wherein a copyright owner had effectively total control of the market for television programme listings.

¹¹ The majority of this discussion, like any discussion concerning parallel importation, focuses primarily on trademarks as the form of intellectual property embodied in parallel goods. Apart from specific pieces of legislation that are aimed exclusively at marks, such as the Trade Marks Directive, *supra*, note 1, the European principles of trademark exhaustion apply to other forms of intellectual property. Most importantly, where a particular product enjoys

It is to the exercise of rights, particularly in blocking parallel imports, that Article 81(1) has been applied.

The *Consten and Grundig* case¹² gave the contours of the application of Article 81 to intellectual property. Agreements between competitors that attempt to minimize competition can, in principle, distort trade within the market.¹³ This distortion of trade may be between the parties to the agreement or between them and third parties.¹⁴ It may take the form of restricted competition in a particular product throughout the market.¹⁵ It may take the form of territorial restrictions for particular areas within the market.¹⁶ It may combine the two in an attempt to control the quantity of goods available, the manner in which they are presented to consumers, and their selling price.¹⁷ What gives these agreements the ability to distort competition in face of counter-balancing parallel importation is the use of intellectual property rights embodied in the imported goods to stop parallel trade. Therefore, it is the exercise of intellectual property rights to enforce otherwise valid agreements that gives the combination of the two the anti-competitive character that the European Court of Justice considers as violating Article 81.¹⁸

There are two parts to the restrictive practice of blocking parallel importation within the market. The first part is the agreement between undertakings evidencing an intention to distort competition. The second is the anti-competitive act itself: the use of intellectual property rights to enforce what may be an otherwise legally-permissible agreement.¹⁹

more than one form of intellectual property protection, the exhaustion of one intellectual property right is deemed to exhaust all other forms. *Merck & Co, Inc and others v Primecrown, Ltd and others*, Joined Cases C-267&268/95, [1996] ECR I-6285; [1997] 1 CMLR 81; *Merck & Co, Inc v Stephar, BV and Petrus Staphanus Exler*, Case 187/80, [1981] ECR 2063; [1981] 3 CMLR 463.

¹² *Etablissements Consten, SA and Grundig-Verkaufs-GmbH v EC Commission*, *supra*, note 8.

¹³ *Ibid*, at 470-478.

¹⁴ *Ibid*.

¹⁵ *Ibid*, at 478.

¹⁶ *Ibid*, at 474.

¹⁷ *Ibid*, at 473; see also *Hasselblad (GB) Ltd v EC Commission*, Case 86/82, [1984] ECR 883; [1984] 1 CMLR 559.

¹⁸ *Etablissements Consten, SA and Grundig-Verkaufs-GmbH v EC Commission*, *supra*, note 8.

¹⁹ This analysis takes on a criminal law-like character. The anti-competitive agreement evidences the *mens rea*, or guilty mental state, of the parties, and the use of intellectual property rights to enforce the intention is like the criminal action, the *actus reus*. There are no criminal sanctions under European Union competition law, apart from the heavy fines and injunctive orders available under Council Regulation 17: first Regulation implementing

For the most part, the exercise of intellectual property rights is entirely legitimate. Because this is so, it was necessary for the Court of Justice to define in general terms the allowable uses of intellectual property in such a way as to distinguish them from those which would implicate prohibited practices. In *Centrafarm v Sterling Drug*,²⁰ the court defined the “specific object” of trademark rights as being to allow the mark owner to put its branded goods onto the market for the first time and to prevent others from pirating the mark.²¹ Once a trademark owner has consented to a first sale in the market, its trademark based rights are exhausted and the underlying goods may be sold and resold throughout the market without restriction. How the market is defined is the second great issue involved in Community-based parallel importation.²² At one time, prior to the adoption of the Trade Marks Directive, it did not matter under the national trademark laws of most Member States where branded goods were sold. Those laws recognized the international exhaustion of trademark rights after a volitional first sale any where in the world.

Arts 81 and 82 of the Treaty, as amended by Reg 1216/1999 of June 10, 1999 amending Reg No 17, [1999] OJ L148/5. The criminal law analogy more closely applies in other systems of anti-trust law, such as under the Sherman Act of the United States, where criminal penalties may be applied to anti-competitive behaviour. If the Art 81(1) prohibitions were to be criminalized in the parallel-importation context, the crime would be that of the exercise of intellectual property rights in furtherance of an anti-competitive conspiracy. Cf Odulu, “Interpreting Article 81(1): object as subjective intention” (2001) 26 EL Rev 60.

²⁰ *Centrafarm, BV and Adriaan De Peijper v Sterling Drug, Inc*, Case 15/74, [1974] ECR 1147; [1974] 2 CMLR 480.

²¹ *Ibid*, para 8.

²² See sections E and F below.

National Laws on Trade Mark Exhaustion

A. Recognising International Exhaustion of Trade Marks:
Austria
Belgium
Denmark
Luxembourg
The Netherlands
Norway
Sweden
B. Probably Recognising International Exhaustion of Trade Marks:
The United Kingdom
Ireland
C. National Law Unclear as to International Exhaustion:
France
Spain
D. Recognising National Exhaustion Only:
Italy

All that is required to exhaust the intellectual property protection of the goods is the intellectual property owner's consent for the first sale.²³ The commercial realities of that sale, such as the price received, are in most cases²⁴ irrelevant to the exhaustion of the intellectual property rights.²⁵ It

²³ What it is that constitutes consent is the question of the moment in parallel-importation law. See *Zino Davidoff, SA v A&G Imports, Ltd* [1999] 3 All ER 711, hereafter "*Davidoff*," currently on referral to the ECJ for a ruling on the consent issue, as to the English position on the issue. Compare *Zino Davidoff, SA v M&S Toiletries, Ltd; JOOP! GmbH v M&S Toiletries, Ltd*, [2000] SLT 683, for a differing Scottish position on the same issue. The cases and national positions are compared in MacQueen, "International Exhaustion of Trade Mark Rights: A Scottish Contribution to the Debate" [2000] 4 IPQ 414; Swift, "Davidoff: Scottish Court Declines to Follow English Ruling on Parallel Imports" [2000] 8 EIPR 376. For the existing position – to the extent that there is one – of the ECJ, see *Sebago, Inc v GB Unic, SA* [1999] 2 CMLR 1317.

²⁴ *Centrafarm, BV and Adriaan De Peijper v Sterling Drug, Inc, supra*, note 20, para 8.

²⁵ See *CNL-Sucal, N v Hag GF, AG*, Case C-10/89, [1990] ECR I-3711; [1990] 3 CMLR 571.

is, therefore, in the interest of intellectual property owners to be careful about how and where they give consent for the first sale.

To more closely control the giving of first-sale consent, intellectual property owners began using more carefully constructed and more elaborately restrictive agreements. This in turn caused the European Court of Justice to delineate those agreements to which Article 81(1) would apply. The court had held, in *Consten and Grundig*, that no distinction was to be made, for the purposes of applying Article 81(1), as to agreements between parties at the same commercial level²⁶ and parties at different levels in the commercialisation of goods.²⁷ The exception to this rule is that Article 81(1) does not apply to agreements between a parent undertaking and its subsidiaries.²⁸ It does, however, apply to agreements between intellectual property owners and independent distributors of protected goods.²⁹ A formal, written agreement is not necessary to support a finding of an Article 81(1) violation.³⁰ Any agreement, however informal, that prohibits the parties from allowing intra-market parallel importing, is anti-competitive as a matter of law.³¹ An elaboration on this rule was given in *Almelo v Energiebedrijf Ijsselmis, NV*³² where the Court of Justice held that restrictive agreements, requiring export out of the market and prohibiting re-importation, are not necessarily anti-competitive. The agreements may be anti-competitive if there is a selective distribution system for the goods covered by the agreement in place in the market that, itself, restricts competition, and there is an appreciable difference between the price of the goods outside of the market and inside of the market.³³

²⁶ Horizontal agreements.

²⁷ Vertical agreements. *Etalissements Consten, SA and Grundig-Verkaufs-GmbH v EC Commission*, *supra*, note 8; *Bayerische Motorenwerke, AG v Ald Auto-Leasing D, GmbH*, Case C-70/93, [1995] ECR I-3439; [1996] 4 CMLR 478, para 15.

²⁸ *Centrafarm, BV and Adriaan De Peijper v Sterling Drug, Inc*, *supra*, note 20, para 41.

²⁹ *Tipp-ex, GmbH & Co KG v EC Commission*, Case C-279/87, [1990] ECR I-261; *Bayerische Motorenwerke, AG v Ald Auto-Leasing D, GmbH*, *supra*, note 27, para 19.

³⁰ *Bayerische Motorenwerke, AG v Ald Auto-Leasing D, GmbH*, *supra*, note 27, para 16.

³¹ *Tipp-ex, GmbH & Co KG v EC Commission*, *supra*, note 29, para S1; *Bayerische Motorenwerke, AG v Ald Auto-Leasing D, GmbH*, *supra*, note 27. See also *W Burns Tractors, Ltd v Sperry New Holland*, Commission decision 85/617/EEC, [1985] OJ L376/21; [1988] 4 CMLR 306, para 52.

³² Case C-393/92, [1994] ECR I-1477; see also *W Burns Tractors, Ltd v Sperry New Holland*, *supra*, note 31, para 52; *Camera Care, Ltd v Victor Hasselblad, AB and Hasselblad (GB) Ltd*, Commission decision of 2 December 1981, [1982] OJ L161/18; [1982] 2 CMLR 233, para 55.

³³ *Almelo (Municipality of) and others v Energiebedrijf Ijsselmis, NV*, *supra*, note 32, paras 2-3. It is worth noting at this juncture that there are appreciable differences in the prices of intellectual property protected goods inside and outside of the market. See, generally,

Thus, Article 81(1) prohibits the use of intellectual property rights for enforcing agreements between independent undertakings that intend to prevent parallel importation within the market. The exercise of the intellectual property rights to repel parallel imports in support of an agreement or concerted practice, even if the use of intellectual property rights is the only aspect of the agreement or practice capable of challenging parallel imports, determines the intention of the parties. This is to say that the act itself evidences the intention behind it. Under certain circumstances, Article 81(1) may prohibit the use of intellectual property rights to enforce similar agreements that call for excluding parallel imports by requiring the export of goods out of the market and keeping them out.³⁴

III. SELECTIVE DISTRIBUTION SYSTEMS

The economics of trade creates a continuum of options for intellectual property owners.³⁵ At one extreme is the economy of quantity, available to the mass marketer of protected products in volume. A tendency towards options in this range requires a choice in favour of quantity of sales at the cost of the rarity of the product. As the supply of the product in the market increases, with the demand for the product remaining relatively constant, the per-unit price of the product decreases. The intellectual property owner expects that the increased volume of sales will more than compensate for a decrease in the per-unit profit margin.³⁶ So long as the marginal revenue

National Economic Research Associates, *The Economic Consequences of the Choice of a Regime of Exhaustion in the Area of Trademarks: Final Report for DGXV of the European Commission*, 8 February 1999, hereafter the “NERA Report;” specifically at p 117.

³⁴ *The Community v Konica (UK) Ltd and Konica Europe, GmbH*, Commission decision 88/172/EEC, [1988] OJ L78/34; [1988] 4 CMLR 848, paras 36, 38, 40-41, 45-47; *Nungesser (LC) KG and Kurt Eisele v EC Commission*, Case 258/78, [1982] ECR 2015; [1983] 1 CMLR 278, paras 28-29; *Pabst & Richards, KG v The Bureau National Interprofessional de L’Armagnac (BNIA)*, Case 76/684, [1976] OJ L331/24; [1976] 2 CMLR D63, paras 30-31; *Société de Vente de Ciments et Bétons de l’Est, SA v Kerpen & Kerpen, GmbH & Co, KG*, Case 319/82, [1983] ECR 4173; [1985] 1 CMLR 511, para 6; *Zera-Agrarchemikalien, GmbH and Wilhelm Hinkens v Agrimont, SpA and others*, Commission decision 93/554/EEC, [1993] OJ L272/28; [1995] 5 CMLR 320, paras 103-116.

³⁵ See Posner, *Economic Analysis of Law* (4th ed) (Little, Brown and Co, Boston, 1992) pp 38-45, 665-671.

³⁶ This dynamic is more complicated for brand owners who have a dependency on public perceptions for a significant portion of the value of their intellectual property. Over production, with a resultant over marketing of a product, can cause a perceived degrading of the brand image. See, for example, the now settled dispute involving designer Calvin Klein, reported in “Calvin Klein’s License Battle Goes to Court”, *International Herald Tribune*, 20-21 January 2001, p 11; “Fashion Fiasco Ends on a Kiss”, *International Herald Tribune*, 23 January 2001, p11.

is greater than its marginal cost, the process can continue to a point of competitive equilibrium, where the marginal revenue and marginal cost are equal. An example of this is in the manufacturing and sale of pharmaceuticals. The research, development, and initial production costs for a new drug are approximately the same whether one dose is made or one million doses are made.³⁷ Rather than hoping to recover their costs and make a profit through manufacturing a limited quantity of a pharmaceutical with a very high per-unit price, a manufacturer will make as many doses as the demand in a lucrative market will bear;³⁸ charging a lower price for each unit but expecting that the increased sales at the lower price will give the manufacturer the best return on its investment.³⁹

At the other end of this continuum is a tendency towards scarcity. This is most applicable to designer goods, whether protected by copyrights or trademarks. Much of the value of such goods is not inherent in the goods themselves, but resides precariously in the public's perception of the goods as expressing a degree of desirability. This is the "allure" of designer goods.⁴⁰ The allure is diminished as the goods become more widely available, because the public perception of exclusivity associated with the ability to obtain⁴¹

³⁷ See Hancher, "The European Pharmaceutical Market; problems of partial harmonisation" [1990] EL Rev 9.

³⁸ It is the demand in lucrative markets that defines the measure of the demand for a product that a manufacturer will respond to. Where the product is intellectual property protected, the profitability of market must compensate the intellectual property owner for more than the cash cost of producing the product in order for it to offset other cost factors. See the text accompanying nos 101 – 103 below. There may be a much higher demand in a market that is too poor to pay a profitable price for a protected product. In that case, a manufacturer will ignore the unprofitable demand. For an example of this in the case of pharmaceuticals, see "Africans Plead in Vain for AIDS Treatment", *International Herald Tribune*, 28 December 2000, pp 1, 4.

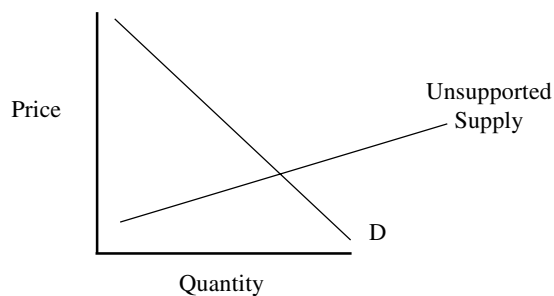
³⁹ This model is complicated by several factors: the health and safety laws applicable to pharmaceuticals, the patent monopoly available to drug developers for at least the first twenty years of the marketing of new drugs, by the possibility of parallel trade in pharmaceuticals, and the public interest in providing affordable health care as expressed in the policies and laws of many states that directly or indirectly restrict the retail price of prescription drugs. See Booer, Edmonds, Glynn, and Oglialoro, "Economic Aspects of the Single European Market in Pharmaceuticals" [1999] ECLR 256; Geddes, "Free Movement of Pharmaceuticals within the Community: The Remaining Barriers" [1991] 16 EL Rev 295.

⁴⁰ See *Davidoff*, *supra*, note 40; where Laddie, J, explains the importance of "allure."

⁴¹ "To obtain" meaning, in practical terms, to afford. In western nations at least, the exclusivity associated with designer goods is not so much directly related to the scarcity of the goods themselves as it is to the wealth necessary to purchase scarce, and therefore more expensive, goods. Brand owners may seek to produce and sell more goods and, simultaneously, maintain higher retail prices up to a point of market saturation, without destroying the public perception

the designer goods is diminished. Therefore, it is in the interest of manufacturers of such goods to limit the supply of the goods available in the market and, with the demand for the goods remaining relatively constant, to charge the highest per-unit price the market will bear.⁴² The manufacturer's emphasis in this case is directed towards achieving the highest profit margin possible for each sale of the product, rather than towards achieving the greatest volume of sales possible.

Illustration 1. Standard Supply-Demand Relationship



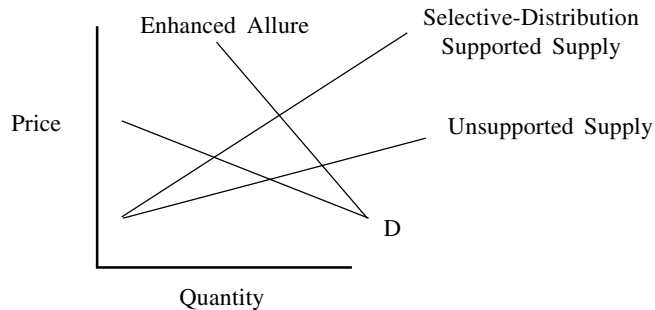
To achieve its aims of increasing the per-unit market price of designer goods, intellectual property owners must control both the manufacture and distribution of those goods. To preserve the public perception of exclusivity and scarcity, and to enhance the allure of their products, intellectual property owners must also control the type of retail establishment through which their products are sold. This control is achieved through the use of selective distribution and sales systems. These systems supply some retailers in the market and exclude others. Whether or not a particular retailer is included in the system depends, in general, on whether the inclusion of that retailer

of exclusivity. The public perception is only altered when there are so many of the products available that market forces which are not under the control of the intellectual property owners, such as parallel traders, are able to begin the discount selling of the goods through lower-priced retail outlets and, thus, informing the public that the goods are not necessarily symbols of wealth or social status.

⁴² The highest price that the market will bear may not be the same for all markets or for different parts of the same market. This possibility creates the potential for parallel importing. The parallel importer buys goods where they are less expensive and sells them where they are more expensive. This is a form of price arbitrage that tends to average prices uniformly within markets and between markets. See Cornish, "Trade Marks: Portcullis for the EEA?" [1998] EIPR 172.

would help or hinder the manufacturer's aim of achieving the highest per-unit price for the limited supply of the goods being sold. The use of these systems creates an ongoing conflict within the market. In a legal sense, the conflict is between the intellectual property owner's understandable desire to make a profit while protecting its product's image and the desire of excluded retailers to have access to the supply of the protected goods and so to compete in the market.⁴³

Illustration 2. Restricted Supply – Enhanced Demand Relationship



Because of this conflict, the European Court of Justice has had several opportunities to define what is and what is not a permissible use of a selective distribution system.⁴⁴ In applying Article 81(1)⁴⁵ to commercial practices involving such systems, the court has held that a violation can occur if the agreements creating the system directly or indirectly, actually or potentially affect interstate trade.⁴⁶ To determine what effect the agreements have on interstate trade, the court considers the type of product involved, the market

⁴³ See generally Dixon and Mueller, "Antitrust in the Common Market: Marx, Monopoly, and the 'Chill Winds of Competition'" [1996] 42 Antitrust L & Econ Rev.

⁴⁴ The ECJ functions as the legal arbiter between the desires of brand owners to exclude competition at the intra-brand, retail level and the desires of excluded retailers to compete in the market for branded goods. In a commercial sense, parallel importers fulfil the same function as the ECJ. Parallel importers commercially arbitrate on the basis of price – a basis comparable to the ECJ's legal province – between the brand owners' desire to sell their products at the most profitable price available to them in a particular location and the desires of excluded retailers to buy branded goods and resell them at a profit.

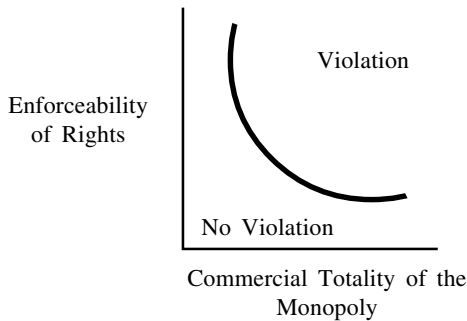
⁴⁵ EC Treaty, *supra*, note 4, Art 81(1).

⁴⁶ *Salonia v Giorgio Poidomani and Franca Baglieri (née Giglio)*, Case 126/80, [1981] ECR 1563; [1982] 1 CMLR 64, para 12; *La Technique Minière v Maschinenbau Ulm, GmbH*, Case 56/65, [1966] ECR 235; [1966] CMLR 357 at 375.

position and market share controlled by the grantor of the agreements, the isolated occurrence or repeated nature of the agreements, the severity of the restrictions created for collateral trade in the products in question, and the opportunity for competition from outside of the selective distribution system.⁴⁷ This is to say that the court will consider, for Article 81(1) purposes, the entirety of the agreements creating a selective distribution system and the surrounding commercial circumstances, as well as the cumulative effect of a network of agreements.⁴⁸

The less room the commercial realities of the trade in a particular product leave for the growth and development of effective competition, the greater will be the effect of the enforcement of legal rights, particularly of exclusive rights such as those of intellectual property owners, upon competition. This is to say that the greater the convergence between a legal, intellectual property-based monopoly and an economic monopoly, the greater will be the anti-competitive effect of the monopoly.⁴⁹

Illustration 3. Enforceability of Rights and Likelihood of Violation



A mechanism used to give the agreements effect and to shield the resulting selective distribution system from unwanted competition is the body of applicable, national intellectual property laws. Therefore, the territoriality

⁴⁷ *La Technique Minière v Maschinenbau Ulm, GmbH*, *ibid*, at 375-376.

⁴⁸ *Delimitis v Henninger Bräu, AG*, Case C-234/89, [1992] 5 CMLR 210.

⁴⁹ See the *Magill* case, *supra*, note 10, for an example of a complete convergence of legal and economic monopolies, giving rise to an EC Treaty, Art 82, competition-law violation. Art 82 provides, in part:

“Any abuse by one or more undertakings of a dominate position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market insofar as it may affect trade between Member States. ...”

inherent in selective distribution systems is often defined along national lines. The court has held that the combined, exclusionary effects of selective distribution systems and national laws can violate Article 81(1).⁵⁰ The more exclusionary the selective distribution system, the more likely the use of national laws to support it is to violate the article.⁵¹ The criterion for the inclusion or exclusion of potential retailers may violate Article 81(1),⁵² particularly if it is based on quantitative measures.⁵³ In making a determination about the influence of quantitative restrictions in agreements creating a selective distribution system, the court will consider, as before, the potential of the restrictions to affect inter-state trade, the nature of the products, the market position of the parties to the agreement, and the isolated or wide-spread nature of the restrictions.⁵⁴ Where parallel importation is concerned, the guiding principle is that of intellectual property exhaustion: a consensual sale in any part of the EU exhausts an intellectual property owner's right to further control the intra-market movement of the underlying goods.⁵⁵ It does not matter which intellectual property rights are involved. The exhaustion of one intellectual property right exhausts all other rights expressed in a product.⁵⁶

Consideration of the size of the market share that is controlled by the parties to selective distribution agreements is a recurring theme for the Court of Justice. Market share, itself, is dependent upon the definition of the particular market for the products involved. In defining the relevant market, the court will consider the definition of the market for the products that is used by their manufacturer,⁵⁷ the physical and qualitative character of the market, the type of uses for which the products are suited, the range of accessories available for the products, and the price of the products – all factors which may restrict sales to certain categories of customers.⁵⁸

⁵⁰ *Procureur du Roi v Benoit and Dassonville*, Case 8/74, [1974] ECR 1183; [1974] 2 CMLR 436, para 12.

⁵¹ *Ibid*, para 11; *Officier van Justitie v Adriaan de Peijper*, Case 104/75, [1976] ECR 613; [1976] 2 CMLR 271.

⁵² *Hasselblad (GB) Ltd v EC Commission*, *supra*, note 17, para 51.

⁵³ *Lancôme and Cosparfrance Nederland, BV v Etos, BV and Albert Heijn Supermart, BV*, Case 99/79, [1980] ECR I-2511; [1981] 2 CMLR 164, paras 21-24.

⁵⁴ *Ibid*.

⁵⁵ *Merck & Co, Inc v Stephar, BV and Petrus Staphanus Exler*, *supra*, note 11, para 14.

⁵⁶ *Ibid*.

⁵⁷ But see FORM A/B, section 6, Regulation 3385/94 [1994] OJ L377/28; FORM CO, section 6, Regulation 447/98 [1998] OJ L61/1, where the product market is defined in terms of the goods that the customers consider to be substitutes, "All those products and/or services which are regarded as interchangeable or substitutable by the consumer, by reason of the products' characteristics, their price and their intended use."

⁵⁸ *Hasselblad (GB) Ltd v EC Commission*, *supra*, note 17, para 21.

Once the relevant market is defined, elements of selective distribution agreements or practices based upon the functioning of the selective distribution system that attempt to limit sales of the product to discrete territories within the market become suspect. Agreements prohibiting exports violate Article 81(1),⁵⁹ as do informal understandings between dealers within a selective distribution system not to supply parallel importers.⁶⁰ In general, selective distribution systems lose the exemptions given to them under Article 81(3)⁶¹ if elements within the system attempt to restrict the supply of the products to other dealers within the market.⁶² These considerations are not limited to finished products. The exemption is not available for selective distribution agreements involving intermediary products that have the object or effect of restricting competition.⁶³

The terms of an agreement creating a selective distribution system are important for determining whether an Article 81(1) violation has occurred,⁶⁴

⁵⁹ *Ibid*, para 46.

⁶⁰ *Ibid*, paras 27-29; *Société d'Hygiène Dermatologique de Vichy v EC Commission*, Case T-19/91, [1992] ECR II-415, para S1; *Re 'Pioneer' Hi-Fi Equipment*, Commission decision of 14 December 1979, [1980] 1 CMLR 457, paras 60-63, 77-80.

⁶¹ EC Treaty, *supra*, note 4, Art 81(3). This section of Art 81 provides for exemptions to the prohibitions of Art 81(1). These exemptions were, for the years during which much of the current case law was handed down, specifically set out in three regulations: Commission Regulation 1983/83 (concerning exclusive distribution) [1983] OJ L173/1, [1983] 1 CLE 262; Commission Regulation 1984/83 (concerning exclusive purchasing) [1983] OJ L173/5, [1983] 1 CLE 255; Commission Regulation 4087/88 (concerning franchising) [1988] OJ L359/46. These have now been amended. See *Commission Green Paper on Vertical Restraints in EC Competition Policy*, COM(96) 721; *Communication from the Commission on the Application of the Community Competition rules to Vertical Restraints – Follow-up to the Green Paper on Vertical Restraints*, COM(98) 544. These amendments are well explained in Whish, "Regulation 2790/99: The Commission's "new style" block exemption for vertical agreements" [2000] 4 CML Rev 887; Whish, "Recent developments in EC competition law 1998/99" [2000] EL Rev 219; Ehlermann, "The modernization of EC antitrust policy: A legal and cultural revolution" [2000] 3 CML Rev 537.

⁶² *Hasselblad (GB) Ltd v EC Commission*, *supra*, note 4, paras 30, 35.

⁶³ *Bureau National Interprofessionnel du Cognac v Clair*, Case 123/83, [1985] ECR 391; [1985] 2 CMLR 430; *Re the Application of the Federación Nacional de Cafeteros de Colombia*, Commission decision 82/860/EEC, [1982] OJ L360/31; [1983] 1 CMLR 703, paras 38-39, 43. This point is developed further in the text accompanying notes 121-122 below.

⁶⁴ *Ford-Werke, AG and Ford of Europe, Inc v EC Commission*, Case 25-26/84, [1985] ECR 22725; [1985] 3 CMLR 528, para 32. Even disclaimers and severability clauses written into a selective distribution agreement, which seek to eliminate an agreement's potential illegality under the competition laws, will not save the parties to the agreement if their conduct is anti-competitive. *Parker Pen, Ltd v EC Commission*, Case T-77/92, [1994] ECR II-549; [1995] 5 CMLR 435, para 55; *Re Deere and Company, John Deere Export and others: National Farmers Union v Cofabel, NV*, Commission decision 85/79/EEC, [1985] OJ L35/58; [1985] 2 CMLR 554, para 27.

but the terms of the agreement are not the only facts that will be considered.⁶⁵ Details of the operation of a selective distribution system that are left to the discretion of the grantor or manufacturer, and which are later acted upon unilaterally, will be treated as part of the agreement creating the system and are subject to the prohibitions⁶⁶ of Article 81(1). These actions alone, such as excluding from the distribution system some retailers who are otherwise capable of preserving the product's public image,⁶⁷ can constitute the factual basis for finding an Article 81(1) violation.⁶⁸

IV. ANTI-COMPETITIVE PRACTICES WITHIN THE MARKET

The competition laws apply not only to the formal, agreement-based operation of distribution systems, but also to the behaviour of the parties to informal understandings in respect of competitors. As a general rule, any form of collusion between competitors that is capable of affecting intra-market trade is prohibited by Article 81(1) as a concerted practice.⁶⁹ A concerted practice has been defined as a form of co-ordination between undertakings⁷⁰ that, without going so far as to amount to a proper, formal agreement, knowingly substitutes for the usual risks of competition a practical cooperation between the undertakings.⁷¹ "Knowingly" is the requisite mental state, the *mens rea*. Accidental or negligent conduct is presumably not the basis for finding a Article 81(1) violation, though parallel conduct – meaning risk-minimizing actions taken simultaneously by competitors – may serve as partial proof of a concerted practice.⁷² Like all mental-state requirements, there is a need for proof. This proof is usually provided by circumstantial evidence.⁷³

⁶⁵ *Ford-Werke, AG and Ford of Europe, Inc v EC Commission*, *supra*, note 64, para 33.

⁶⁶ *Ibid*, para 21.

⁶⁷ *Groupement d'Achat Édouard Leclerc v EC Commission*, Case T-19, 88/92, [1996] ECR II-1851; [1997] 4 CMLR 995.

⁶⁸ *Ford-Werke, AG and Ford of Europe, Inc v EC Commission*, *supra*, note 64, para 46.

⁶⁹ *Völk v Etablissements Vervaecke, Sprl*, Case 5/69, [1969] ECR 295, [1969] CMLR 273, para 3.

⁷⁰ An "undertaking" is any entity, including a public body, that is engaged in commerce. See, *eg, Almelo (Municipality of) and others v Energiebedrijf, Ijsselmis, NV*, *supra*, note 32.

⁷¹ *ICI, Ltd v EC Commission*, Joined Cases 48, 49, and 51-57/69, [1972] ECR 619; [1972] CMLR 557, para 64.

⁷² *Ibid*, para 66. Implicit mental-state requirements in the competition laws is an area that bears further investigation, particularly in light of the heavy penalties that may be imposed for a violation of the competition laws and the possibility of using an absence of proof of a required mental state as a defence.

⁷³ This subject is treated in Hays, "The Burden of Proof in Parallel-Importation Cases," [2000] 8 EIPR 353.

The European Court of Justice has said, that in determining whether there is a concerted practice, the facts of the situation should be considered as a whole after taking into account the market in question.⁷⁴ This means that nearly anything may be considered in determining whether collusion between competitors has occurred. The burden of proof is on the Commission of the European Communities,⁷⁵ and the burden may be divided into two parts: proving from the actions of the competitors that suspect behaviour has occurred, and proving that, under the relevant circumstances, that behaviour is capable of distorting competition within the market.

In meeting the first part of its burden, the Commission may use:

1. Evidence of agreements concerning the competitors themselves and evidence of agreements concerning third parties;
2. Evidence of an informal sharing of plans between competitors;⁷⁶
3. Correspondence between the competitors and third parties,⁷⁷ and documentary hearsay evidence from third parties;⁷⁸
4. Evidence of a competitor acting on complaints of unwanted competition by a third party⁷⁹ or of price fixing through requiring specified resale prices by a competitor and a third party;⁸⁰
5. Evidence of agreements between competitors concerning sales to a third party that show an intention to stop the third party from competing.⁸¹

Specific to selective distribution systems, the operation of the system can provide evidence of a distortion of competition if:

1. Existing dealers are unable to branch into other territories;

⁷⁴ *Re European Sugar Cartel: Coöperative Vereniging "Suiker Unie" UA and others v EC Commission*, Cases 40-48, 50, 54-56, 111, 113-114/73, [1975] ECR 1663; [1976] 1 CMLR 295, para 28.

⁷⁵ *Ibid*, para 363.

⁷⁶ *Ibid*, paras 173-174.

⁷⁷ *Ibid*, para 164.

⁷⁸ *Ibid*, paras 272-332.

⁷⁹ *Camera Care, Ltd v Victor Hasselblad, AB and Hasselblad (GB) Ltd*, *supra*, note 32, paras 42, 47.

⁸⁰ *Ibid*, para 49.

⁸¹ *Compagnie Royale Asturienne des Mines, SA and Rheinzink, GmbH v EC Commission*, Joined Cases 29, 30/83, [1984] ECR 1679; [1985] 1 CMLR 688.

2. The manufacturer or granter refuses to supply prospective new dealers in an area unless sales by the existing dealers in that area fall short of a preset amount;
3. The supplying of a prospective new dealer in an area is made dependent on that dealer making a compensation payment to an existing dealer; or
4. There is a restriction placed on a dealer against sales to certain categories of customers.⁸²

Furthermore, the operation within a distribution system of restrictions on advertising,⁸³ sales rebates and discounts,⁸⁴ and repair guarantees⁸⁵ may provide evidence of a concerted practice aimed at restricting competition.

The second part of the Commission's burden, proving the capacity of a concerted practice to affect competition within the market, is less qualitative and more quantitative. There is a *de minimis* exception for concerted practices that are incapable of affecting the market in any meaningful way.⁸⁶ In order to determine whether an agreement can affect the market, the relevant market sector must be defined.⁸⁷ A market share of as little as five percent has been held to be significant enough for an associated concerted practice to affect the market for Article 81(1) purposes.⁸⁸ What the market is depends on the goods involved. Generally, a substantial market share in any national market within a Member State is enough to elevate the capacity of competition-distorting, concerted practices above the *de minimis* threshold.⁸⁹ For horizontally or vertically restrictive agreements, market-share thresholds

⁸² *Re the Agreement of Ivoclar, AG*, Commission decision, 85/559/EEC, [1985] OJ L369/1; [1988] 4 CMLR 781, paras 15-16; *Compagnie Royale Asturienne des Mines, SA and Rheinzink, GmbH v EC Commission*, *supra*, note 81.

⁸³ *Camera Care, Ltd v Victor Hasselblad, AB and Hasselblad (GB) Ltd*, *supra*, note 32, para 60.

⁸⁴ *Gosmé, SA v Distribution Martell Piper, SA*, Commission decision IV/32.186, [1991] OJ L185/23; [1992] 5 CMLR 586, para 34.

⁸⁵ *Camera Care, Ltd v Victor Hasselblad, AB and Hasselblad (GB) Ltd*, *supra*, note 32, para 56.

⁸⁶ *Völk v Etablissements Vervaicke, Sprl*, *supra*, note 69, para 3.

⁸⁷ *Miller Int'l Schallplatten, GmbH v EC Commission*, Case 19/77, [1978] ECR 131; [1978] 2 CMLR 334, para 10. See also FORM A/B, section 6, Regulation 3385/94; FORM CO, section 6, Regulation 447/98, *supra*, note 57.

⁸⁸ *Ibid*, paras 9-10.

⁸⁹ *Ibid*, paras 448-542; *Miller Int'l Schallplatten, GmbH v EC Commission*, *supra*, note 87, paras 7-14.

of five and ten percent, respectively, are enough to make the agreements susceptible to the Article 81 prohibitions.⁹⁰

Once the particular market segment has been defined, and it is determined that the market segment is capable of being affected by the restrictive practices generally, it remains for the Commission, in the first instance, to decide whether the particular restrictive practices under consideration have, as their object or effect, a counter-competitive purpose. For restrictive practices to affect intra-Community trade, it must be foreseeable that the practice is likely to have an influence of some kind on the pattern of trade between Member States.⁹¹ Therefore, practices carried out with the intent of making the export of goods to a Member State more expensive and less profitable for others, or which discourage third parties from exporting goods to a Member State, and which have the aim of maintaining higher prices in the destination country – meaning shielding the market segment in the destination country from competition – are prohibited by Article 81(1).⁹²

The application of intellectual property rights to these general principles is only secondary. The use of intellectual property rights can be an enforcement mechanism for restrictive practices. Their use is not a restrictive practice in and of itself. If the underlying restrictive practice is prohibited, so will be the use of national intellectual property rights to give effect to the distortion of competition. For example, intellectual property protected goods sold with the consent of the intellectual property owner in one Member State are freely re-sellable in all Member States.⁹³ National intellectual property rights cannot be used to stop the free movement of these goods across national frontiers.⁹⁴ Likewise, intellectual property rights cannot be used to protect a national market from imports when the intellectual property owner or its licensee has placed the imported goods in circulation.⁹⁵

⁹⁰ *Commission Notice on Agreements of Minor Importance* [1997] OJ C372/13.

⁹¹ *Remia, BV, Verenigde Bedrijven Nutricia, NV and another v EC Commission*, Case 42/48, [1985] ECR 2545; [1987] 1 CMLR 1, para 22.

⁹² *Gosmé, SA v Distribution Martell Piper, SA*, *supra*, note 84, para 34.

⁹³ *Etablissements Consten, SA and Grundig-Verkaufs-GmbH v EC Commission*, *supra*, note 8.

⁹⁴ With qualification, this principle has remained true since *Consten* and *Grundig*. See Beier, “Industrial Property and the Free Movement of Goods in the Internal European Market” [1990] 2 IIC 131; Jones, “Does an Opportunity Still Exist for the Development of a Doctrine of International Exhaustion at a Community Level under Articles 28 and 30” [2000] EIPR 171. See also *Pharmon, BV v Hoechst, AG*, Case 19/84, [1985] ECR 2281; [1985] 3 CMLR 775.

⁹⁵ *Keurkoop, BV v Nancy Keen Gifts, BV*, case 144/81, [1982] ECR 2853; [1983] 2 CMLR 47.

V. AGREEMENTS WITH PARTIES OUTSIDE OF THE MARKET

From the previous sections, it appears that the foundation for the operation of Article 81(1) is the principle that, in order to be actionable, attempts to distort competition, in whatever form, must be capable of having an effect on the intra-EU market. Agreements between a party within the market and a party outside of the market can have such an effect.⁹⁶ The first statement is the rule in competition law and the second is its natural corollary. Both are reasonable because it is the effect of distorted competition that Article 81 is intended to prevent, and if that is the aim of the competition laws, then it should not matter from where a participant to a competition-suppressing arrangement happens to operate at any particular time.⁹⁷

This extra-territorial aspect of Article 81 has been extended further. Not only can Article 81(1) prohibitions be applied to persons outside of the EU, but also the prohibitions can be applied to actions taken outside of the EU.⁹⁸ Again, this extension is logical because concerted practices that restrict competition can be carried out through more varied mechanisms than formal agreements.⁹⁹ They may be implied from the actions of competitors and third parties.¹⁰⁰ Therefore, arrangements, formal or informal, expressed or implied, that are given effect outside of the market may violate Article 81(1) if they distort competition within the market.¹⁰¹

There are three elements to the marginal cost of intellectual property protected goods that are subject to the potential for parallel importation:

1. The production cost of the protected products themselves;
2. The loss of first-sale distribution control;

⁹⁶ *Béquelin Import Co and another v GL Import Export, SA*, Case 22/71, [1971] ECR 949; [1972] 1 CMLR 81, paras 11-12; *Community v Konica (UK) Ltd and Konica Europe, GmbH*, *supra*, note 34, para 47; *Re French and Taiwanese Mushroom Packers*, Commission decision 75/77/EEC, [1975] OJ L29/26; [1975] 1 CMLR D83, para 21.

⁹⁷ The legal residence of a party is not particularly important for the operation of Art 81(1), and the competition laws may be applied to a party to a prohibited agreement that resides outside of the EU. See *ICI, Ltd v EC Commission*, *supra*, note 71, para 11; *Re Aluminium Imports from Eastern Europe*, Commission decision 85/206/EEC, [1985] OJ L92/1; [1987] 3 CMLR 813, para 9.2.

⁹⁸ *Re Franco-Japanese Ball bearings Agreements*, Commission decision 74/634/EEC, [1974] OJ L343/19; [1975] 1 CMLR D8, paras 15-16.

⁹⁹ *Ibid*, para 25.

¹⁰⁰ See the text accompanying notes 70-73 above.

¹⁰¹ *Nederlandse Vereniging voor fruit en Groentenimporthandel and Nederlandse Bond van Grossiers in Zuidvruchten en Ander Geïmporteerde Fruit 'Frubo' v EC Commission*, case 71/74, [1975] ECR 563; [1975] 2 CMLR 123.

3. The forfeiture of the negative intellectual property right as to those goods.

The production cost of the product is just that, the per-unit cost of manufacturing, including the cost of warehousing and transporting the goods to the point of sale. The first-sale distribution cost is reflected in a loss of control over the presentation of the protected product to consumers – a diminution in the allure of the product resultant from sales of legitimate examples outside of an authorised distribution system. Its effect is qualitative. The cost of forfeiture of the negative intellectual property right is reflected in the loss of certainty as to the future commercialisation of previously protected products after a volitional first sale.¹⁰² Its primary effect in relation to parallel imports is quantitative, as reflected in the number of goods available in commerce. Where an intellectual property owner's profit margin is supported by a selective distribution system for its products and by sales in multiple markets with a degree of segregation between them, profitability in any one market is affected by variations in the marginal cost of the goods to the intellectual property owner across all markets so long as there is potential for parallel trade serving as a link between markets.

One way in which such arrangements can potentially distort competition within the EU market is through restricting the possibility of exports to the market.¹⁰³ For example, a ban on exports to the EU could be carried out through setting an artificially high sale price for goods sold outside of the market. This would violate Article 81(1) if it could be shown that the purpose for the high price is to discourage exports to the EU.¹⁰⁴ The selling price of products abroad would affect trade within the market, particularly where the selling price within the market is greater than the marginal cost of the goods. High prices abroad have an effect on competition within the market if they are kept high for the purpose of preventing a supply of the goods becoming available for export to the market.¹⁰⁵ This would be the case where the external price of goods was kept equal to or greater than the market price for the same goods. The intellectual property

¹⁰² Intellectual property rights are essentially negative rights. Intellectual property gives its owner the right to keep goods embodying the intellectual property out of circulation. See Cornish, *intellectual property*, *supra*, note 5, pp 6-7. Intellectual property rights do not give their owners an affirmative right to do anything.

¹⁰³ *Ibid*; *Re Franco-Japanese Ball bearings Agreements*, *supra*, note 98, paras 15-16, 39.

¹⁰⁴ *Re Franco-Japanese Ball bearings Agreements*, *supra*, note 98, paras 15-16; *Re French and Taiwanese Mushroom Packers*, *supra*, note 96, para 11.

¹⁰⁵ *The Community v Franuc, Ltd and Siemens, AG*, Commission decision 85/618/EEC, [1985] OJ L376/29; [1988] 4 CMLR 945, paras 24-26.

owner's aim in keeping external prices high would be to support lower marginal costs for the same or similar goods within the market through a greater retention of distribution control and avoidance of the legal implications from the forfeiture of negative intellectual property rights. The result is to allow an intellectual property owner to increase demand for a protected product while maintaining a constant level of supply in an environment of scarcity – an increased per-unit profit margin.

This is an inherently unstable position and is only possible through the enforcement of intellectual property rights. As the commercial tension increases in proportion to the discrepancy between the supply of and the demand for the product, the intellectual property owner must exercise increasingly greater control, not so much over the price aspect of its marginal cost, for that may remain constant, but over the distribution control cost and the cost to its negative intellectual property rights.¹⁰⁶ Where these efforts at control become conspiratorial, substituting the certainty of an agreement or concerted practice for the uncertainties of competition across multiple segments within a market and across multiple markets – perhaps because the intellectual property owner is unable to exert the needed control itself – Article 81 applies. This sort of price support, through effectively preventing exports to the EU, is anticompetitive because its intention is to isolate the market from a source of potentially cheaper goods through manipulation of the external supply.¹⁰⁷

This market manipulation is at the opposite extreme to the type of fact patterns that are usually involved in parallel-importation cases. Normally, intellectual property protected goods are offered for sale outside of the EU at much lower prices than prevail in the market, giving rise to the source of cheaper priced, authentic goods that become the object of parallel trade. Apart from exercising EU-based intellectual property rights, the obvious way for intellectual property owners to prevent parallel trade is to raise the price of their goods sold abroad, eliminating the price differential that makes parallel trading profitable. If the price rise abroad is too great, then the goods will be priced out of the foreign market, resulting in a loss of foreign sales to the EU-based intellectual property owner. But that loss may be more than offset by a resulting trade advantage if it results in global market sharing. If there were coordination in pricing between a foreign

¹⁰⁶ *Deutsche Grammophon, GmbH v Metro- SB- Großmärkte, GmbH & Co, KG*, Case 3 U 108/1970, Hanseatische Oberlandesricht, 28 October 1971; [1972] CMLR, part 54, 107, where the German court found that the consent necessary to exhaust the protection in question was supplied by the unauthorised actions of an employee.

¹⁰⁷ *Ibid.*

undertaking and one in the market, both concerned with potentially competing goods, whereby each maintained the price of their goods in the other's market at such a level as to not undercut the other's domestic price, then the concerted practice would have the double effect of both eliminating a price differential for parallel trading and supporting prices at the highest level in each market.

Regional-market division is possible where there is an inherent barrier to market entry, as where the cost of entry is prohibitive for potential competitors who are not already active in the particular product market, and where the technology utilized by or the aesthetic appeal of the product is protected by intellectual property rights for which there are no available substitutes. This is to say that competitors, one in the EU and one abroad for example, could each exercise their similar intellectual property based monopolies to exact the highest price possible for their protected products in their home markets.¹⁰⁸ This is the essence of the intellectual property monopoly; the economic reward for inventiveness and creativity. The affront to the competition laws – Article 81(1) in particular – comes from the intellectual property owners refraining from competing with each other so as to avoid price retaliation in their home markets, with the effect that prices for intellectual property protected products and their substitutes remain uniformly high and the natural course of competition is distorted. To use the Court of Justice's method of analysis from *Consten and Grundig*,¹⁰⁹ an intellectual property owner's influence over the price of goods abroad, in an attempt to extend that influence to the price of similar goods in their domestic market, is not a part of the specific subject matter of their intellectual property rights.¹¹⁰ It is, rather, an impermissible exercise of intellectual property rights in an attempt to substitute cooperation, in a negative, informal way, for the risks of competition.¹¹¹

The preceding are extreme examples. The simplest option for the intellectual property owner, if it were possible, would be passive, non-com-

¹⁰⁸ This is a permissible exercise of an intellectual property right.

¹⁰⁹ *Etablissements Consten, SA and Grundig-Verkaufs-GmbH v EC Commission*, *supra*, note 8.

¹¹⁰ See *Allen & Hansburys Ltd v Generics (UK) Ltd*, Case 434/85, [1988] ECR 1245; [1988] 1 CMLR 701, paras 11-13, as to patents; *Centrafarm, BV v American Home Products Corp*, Case 3/78, [1978] ECR 1823; [1979] 1 CMLR 326, paras 10-13, as to trademarks; *Collins v Imtrat Handelsgesellschaft, mbH*, Cases C-92, 326/92, [1993] ECR I-5145; [1993] 3 CMLR 773, para 20, as to copyright.

¹¹¹ This informal cooperation, if it were to be expressed in an agreement, would be something on the order of, "Since we control between us the available substitutes for each other's intellectual property protected products, we agree not to compete with each other by undercutting the other's monopolistic price in their home markets."

petition – to not sell its protected products outside of its chosen markets and so to negate the possibility of parallel importation. The intellectual property owner would never be guilty of an impermissible exercise of their intellectual property rights in respect of foreign markets because there would be no such exercise. While there is no affirmative obligation on undertakings under the competition laws to compete, there is usually an obligation on intellectual property owners, at least with respect of industrial property, to exercise their intellectual property rights. Patents must be worked. Trademarks must be used. There may be negative legal implications for not exercising intellectual property rights: compulsory licences of patents or de-registration of marks. The effect of non-use in a particular market would be to increase the intellectual property owner's overall marginal cost through an increase in the loss of control over distribution and from the forfeiture of the negative rights in the particular market where it could have competed and where it formerly enjoyed intellectual property protection, but choose not to compete.¹¹²

In the early drafts of the Council Regulation (EC 40/94) of 20 December 1993, on the Community trademark,¹¹³ the European Commission noted the potential for the use of Community-based, national intellectual property laws to isolate the internal market from external sources of protected goods to the detriment of internal competition and, ultimately, of consumers. The Commission said:

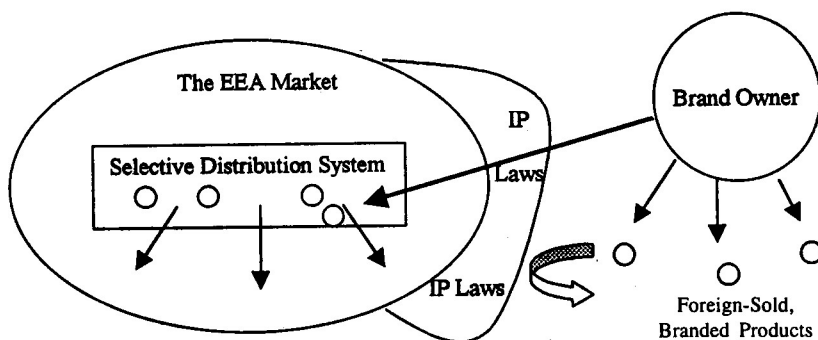
[The obligation to ensure undistorted competition] could clearly not be observed if the Commission were to propose rules laying down the principle that the proprietor of a Community trademark had the right to use it in order to compartmentalize the world market. There is a real danger that undertakings whose principle place of business

¹¹² Within the EU, the intellectual property owner that chooses not to compete receives some protection from the side effects of its choice on its intellectual property rights in some national markets. For example, goods manufactured under a compulsory licence are not deemed to have been put into circulation by the intellectual property owner, who can defend against their importation into the markets where it does compete. *Allen & Hansburys, Ltd v Generics (UK) Ltd*, *supra*, note 110, paras 11-13; *Generics (UK) Ltd and Harris Pharmaceuticals, Ltd v Smith Kline and French Laboratories, Ltd*, Case C-191/90, [1992] ECR I-5335; [1993] 1 CMLR 89, para 24; *Pharmon, BV v Hoechst, AG*, Case 19/84, [1985] ECR 2281; [1985] 3 CMLR 775, para 26; *Re Compulsory Patent Licences: EC Commission v United Kingdom*, Case C-30/90, [1992] 2 CMLR 709, paras 25-27; *Theftord Corp and another v Fiamma, SpA and others*, Case 35/87, [1988] ECR 3585; [1988] 3 CMLR 549, paras 24-25; *Volvo, AB v Erik Veng (UK) Ltd* Case 238/87, [1988] ECR 6211; [1989] 4 CMLR 122, para 8.

¹¹³ [1994] OJ L11/1, 14 January 1994, the "Trade Mark Regulation."

could well be in a non-member country would prevent their products from being imported into the Community at more favourable prices, which would be detrimental to Community consumers.¹¹⁴

Illustration 4. The Commission's Example of Market Manipulation



The Commission's answer to this problem was to propose a rule of the global exhaustion of marks after a first sale of the underlying goods:

The application of the principle of the exhaustion of the right to the trademark ties in with the attaining of two tasks which are entrusted to the Community by the [EC] Treaty: the abolition, as between Member States, of obstacles to freedom of movement of goods and services, and the institution of a system ensuring that competition in the common market is not distorted.¹¹⁵

The Commission changed its position in favour of only Community-wide exhaustion of marks, but without any explanation of what had become of its former concerns for internal competition:

On the question of international exhaustion of the rights conferred by a Community trademark, the Commission has formed the opinion that the Community Legislator should refrain from introducing this principle and make do with the rule of Community-wide exhaustion.¹¹⁶

¹¹⁴ *Proposal for a First Council Directive to Approximate the Laws of the Member States Relating to Trade Marks*, 19 November 1980, COM(80) 635 final, p 34.

¹¹⁵ *Ibid.*

¹¹⁶ *Amended Proposal for a Council Regulation on the Community Trade Mark*, [1984] COM(84) 470 final, pp vi-vii, referring to Art 11 (now Art 13).

As has long been recognised by the Commission and the Court of Justice, price competition is only one form of competition.¹¹⁷ Competition may be increased or decrease through the manipulation of the distribution of goods.¹¹⁸ Thus, while the price of goods may remain unaffected, an intellectual property owner can increase or decrease competition within a market, including a foreign one, by increasing or decreasing the effectiveness of the distribution of their products. An intellectual property owner could avoid retaliatory competition from an otherwise-cooperative, foreign intellectual property exploiter by only selling comparable goods in the foreign market through a distribution mechanism that does not compete directly with the distribution system of the local intellectual property exploiter.¹¹⁹ Here again, the benefit to the exporting intellectual property owner is two fold: retaliatory competition is avoided and the goods are placed in commerce in a way that minimizes the supply available for profitable parallel trade.¹²⁰

These extra-market applications of Article 81(1) are not limited to finished products. Agreements, or their equivalents, formed outside of the market

¹¹⁷ *Metro-SB-Großmärkte, GmbH & Co KG and Verband des SB-Großhandels eV v EC Commission*, Case 26/76, [1977] ECR 1875; [1978] 2 CMLR 1, para 21; *Re the Agreement of Ivoclar, AG*, Commission decision 85/559/EEC, [1985] OJ L369/1; [1988] 4 CMLR 781, paras 22-24.

¹¹⁸ *The Distillers Company, Ltd v EC Commission*, Case 30/78, [1980] ECR 2229; [1980] 3 CMLR 121; *Re the Agreement of Ivoclar, AG*, *supra*, note 82, paras 15-16; *Re the Franchise Agreements of Yves Rocher*, Commission decision 87/14/EEC, [1987] OJ L8/49; [1988] 4 CMLR 592, paras 57-64.

¹¹⁹ For example, a brand owner that markets its goods only through speciality, high-street shops in its domestic market, might choose to sell its goods through high-volume discount stores in a foreign market so as to avoid retaliatory competition in kind from a foreign brand owner that also prefers to use boutique sales points. Objectively, the products are substitutes for one another, just as generic drugs are objectively substitutes for brand-name pharmaceuticals. Subjectively, the allure of the discounted goods is diminished to the point of their appearing to consumers as being of a different class of product from those presented through speciality shops. Commercially, the production costs of the products may be the same, but the marginal cost to its intellectual property owner of the discounted product would be higher, considering the loss of distribution control and forfeiture of its negative right to withhold goods from the market.

¹²⁰ Minimising the supply of goods available in a foreign market for parallel trade through the manipulation of the distribution of those goods is relatively simple in theory. The manufacturer instructs its distributor in the foreign market to only sell the goods in such a way that makes it practically impossible for a parallel importer to obtain a large quantity at a sufficiently low price to make parallel trading profitable. An example of this would be the requirement that the goods only be offered for sale at retail; that no wholesale lots of the goods are to be sold to third parties. This will work if the manufacturer's control is sufficiently effective and if the foreign distributor follows instructions. See *Davidoff, supra*, note 23, for an example of an attempt to manipulate the distribution of an intellectual property protected product so as to eliminate parallel trade that went wrong.

or involving parties from outside of the market, that fix the price of an intermediary product, can violate Article 81(1) if it is the object or effect of the agreements to restrict intra-market competition in finished products that utilize the intermediary.¹²¹ Thus, an agreement between potential competitors that sets the sale price of raw materials in the global market may violate Article 81(1) if the agreement has the effect of limiting the intra-market price of finished products to the higher end of the sale-price spectrum. This would be a form of vertically-integrated trust, whereby the producers of a commodity secondarily manipulate the retail price of finished goods through their control over the price and supply of a necessary precursor. This distorts competition in the finished products uniformly throughout the market by eliminating alternative sources and prices for a raw material required for the finished product.¹²²

A partial restriction on exports to the market can be a feature of competition-distorting agreements. This takes the form of intra-market territorial assignments in which sole distributorships are created. Exports of products to the market are allowed, but only through a selective distribution and sales system. Arrangements of this type, whether formal or informal, are agreements for Article 81(1) purposes.¹²³ These agreements can violate Article 81(1) if they hinder competition within the market.¹²⁴ As with many selective distribution systems, intellectual property rights are the enforcement mechanism that is used to stop unauthorized importation and sales. At least in the case of trademarks, where an intellectual property owner knows that its importation-restricting agreements are contrary to the competition laws, the bringing of an infringement action against an unauthorized importer

¹²¹ *Re Wood Pulp Cartel: A Ahlsröm Oy and others v EC Commission*, Cases 89/85 etc, [1993] 4 CMLR 407, para 142; see text accompanying note 63.

¹²² Trademarks have become, conceptually, a raw material like petroleum or wood pulp. Just as crude oil can be processed so as to make up parts of more valuable products as diverse as pharmaceuticals and ear rings, so can a single trademark elevate the value of products as diverse as cigarettes and neckties. Some undertakings exist only to license a trademark that no longer is tied to a particular product or to products made by a particular manufacturer. See *eg*, “A Bankrupt Converse Plans Restructuring”, *International Herald Tribune*, 23 January 2001, p 12. In considering agreements concerning the restrictive pricing and importation of trademark protected goods from outside of the EU, the trademark aspect of those goods should be treated, conceptually, as an intermediary product or raw material.

¹²³ *Tepia, BV v EC Commission*, Case 28/77, [1978] ECR 1391; [1978] 3 CMLR 392, para 41.

¹²⁴ *Musique Diffusion Française, SA, C Melchers & Co, Pioneer Electronics (Europe) NV and Pioneer High Fidelity (GB) Ltd v EC Commission*, Cases 100-103/80, [1983] ECR 1825; [1983] 3 CMLR 221, paras 74-75.

will be treated as an aggravating circumstance in an Article 81(1) proceeding,¹²⁵ and it may be punishable under the enforcement regulations.¹²⁶ The *de minimis* exception applies, but the hindrance to competition must be extremely small. A market share of as little as 3.18% is sufficient to support a finding of an Article 81(1) violation from attempts to prevent unauthorized distribution within the market.¹²⁷

The origin of the products involved is irrelevant for purposes of the application of Article 81(1) when those products are subject to a competition-distorting agreement that seeks to prevent unauthorized imports. In *Javico v Yves Saint Laurent*,¹²⁸ the Court of Justice held that Article 81(1) precludes agreements that are intended to prevent the re-importation of goods originating within the EU, if the agreements prevent, restrict, or distort competition within the market or are liable to distort intra-market trade.¹²⁹ This is true even if the selective distribution system within the market for the products in question is exempt from the operation of the competition laws under Article 81(3). Agreements with a distributor outside of the market, wherein re-importation is excluded, are not entitled to exemptions based on Article 81(3) and are prohibited by Article 81(1).¹³⁰

VI. APPLICATION TO EXTRA-MARKET PARALLEL IMPORTS

This discussion has shown, in general, that agreements or concerted practices involving a party outside of the market may contravene Article 81(1). It remains to apply that principle to parallel imports from outside of the EU. *EMI v CBS*¹³¹ was a case of intellectual property protected, parallel imports coming into the EU from abroad. The Court of Justice held:

A restrictive agreement between traders within the Common Market and competitors in third countries that would bring about an isolation of the Common Market as a whole which, in the territory of the

¹²⁵ *Tepia, BV v EC Commission*, *supra*, note 123, para 64.

¹²⁶ *Ibid*, para 70; Council Regulation 17, Art 15 – First Regulation implementing Arts 81 and 82 EC Treaty [1999] OJ L148/5, as amended. See note 19 above.

¹²⁷ *Musique Diffusion Française, SA, C Melchers & Co, Pioneer Electronics (Europe) NV and Pioneer High Fidelity (GB) Ltd v EC Commission*, *supra*, note 124, para 86.

¹²⁸ *Javico Int'l and Javico, AG v Yves Saint Laurent Parfums*, Case C-306/96, [1998] ECR I-1983; [1998] 5 CMLR 172.

¹²⁹ *Ibid*, paras 22-27.

¹³⁰ *Ibid*, paras 30-31.

¹³¹ *EMI Records, Ltd v CBS United Kingdom, Ltd*, Case 51/75, [1976] ECR 811; [1976] 2 CMLR 235.

Community, would reduce the supply of products originating in third countries and similar to those protected by a mark within the Community, might be of such a nature as to affect adversely the conditions of competition within the Common Market.

In particular if the proprietor of the mark in dispute in the third country has within the Community various subsidiaries established in different member-States which are in a position to market the products at issue within the Common Market such isolation may also affect trade between member-States.¹³²

This is to say that an agreement to block parallel imports from outside the EU may violate Article 81(1) if:

1. One of the parties to the agreement is commercially active inside of the market;
2. The mechanism to block the importation is a market-based intellectual property right;¹³³
3. The effect is to isolate the market as a whole from an external supply of the protected goods or their substitutes;¹³⁴
4. The intellectual property proprietor has a selective distribution system within the market, through which it can exploit the resultant higher, intra-market price.

The *EMI* decision is a fusion of the principles considered in the preceding discussion. Intellectual property based restrictions on parallel importation that isolate the internal market from less expensive sources of a product are an acceptable attribute of the exploitation of the intellectual property

¹³² *Ibid*, para 28-29.

¹³³ *EMI v CBS* involved a trademark. Conceptually, there may not be a reason to distinguish between the various forms of intellectual property. *Music-Vertrieb Membran, GmbH and K-Tel Int'l v GEMA*, Cases 55, 57/80, [1981] ECR 147; [1981] 2 CMLR 44, paras 11-12. However, it is not clear how the ECJ will address this issue for competition-law purposes. There is a case to be made that the future development of Community law in this area will show a divergence in the treatment of the different types of intellectual property rights. See Norman, "Parallel Imports from Non-EEA Member States: The Vision Remains Unclear", [2000] 4 EIPR 159.

¹³⁴ The *EMI* decision specifically mentions "similar" goods, at para 28. "Similar" is taken here as being a substitute for "substitute" goods. Thus, it is reasonable to extrapolate from the *EMI* decision that it should apply to substitute technologies, such as might be patent protected. See, eg, Byrne, "Exhaustion of Patent Rights in EEC Competition Law" [1979] EIPR 150.

monopoly that becomes unacceptable under the competition laws when combined with a co-existing selective distribution system within the market – an example of synergism. Such a state of affairs is unacceptable because it is not only a reaction against existing competitive forces, it also seeks to prevent the development of new avenues of competition in the future.

An embedded issue is that of what degree of isolation of the internal market is required. This isolation should be gauged by considering the global strength of the intellectual property rights controlled by the party within the market who is attempting to keep out the parallel imports. The broader the market-basis of the intellectual property rights, the more effective they will be at repelling near-substitute products and the greater will be the market's sequestration. The measure of market seclusion that will trigger Article 81(1) sanctions should be analogous to the measure of the effect on competition utilized in applying the *de minimis* standard. Any degree of isolation above a negligible amount would be actionable.¹³⁵ At any rate, the burden remains with the Commission to prove, in any given instance, that the repulsion of extra-market goods is having an effect on intra-Community trade.¹³⁶ The fact that the goods in question may come from outside of the market should not matter for competition law purposes. If the associated intellectual property rights were exhausted as to the goods in question, the only issue as to their importation would be that of the customs laws.¹³⁷ Once the goods were within the market, the free-movement provisions of the EC Treaty would be controlling.¹³⁸

The conflict is between the competition laws and the growing body of parallel-importation related, intellectual property laws. The competition laws, in some instances, prohibit objections to the importation of goods when that importation is necessary to assure a supply of the goods to fuel competition.¹³⁹ The intellectual property laws address parallel importation, but only from an intellectual property perspective. The argument is not joined.

¹³⁵ An example of a negligible degree of market isolation would be that resulting from a global conspiracy to isolate the Common Market from parallel trade in square automobile tires – assuming there was intellectual property protection within the market for such a product. Because the internal market for square tires is so small, and because the round-tire substitutes are so widely available, the restraint on competition within the market would be *de minimis*.

¹³⁶ *Groupment des Fabricants de Papiers Peints de Belgique and others v EC Commission*, Case 73/74, [1976] 1 CMLR 589.

¹³⁷ *Phytheron Int'l, SA v Jeans Bourbon, SA*, Case C-352/95, [1997] ECR I-1729; [1997] 3 CMLR 199, para 21; see also, Prändl, "Exhaustion of IP Rights in the EEA Applies to Third-Country Goods Placed on the EEA Market" [1993] 2 ECLR 43

¹³⁸ *Bristol-Myers Squibb and others v Paranova, AS*, Joined Cases C-427, 429, 436/93, [1996] ECR I-3457; [1997] 1 CMLR 1151.

¹³⁹ See text accompanying notes 103-115 above.

It has not been determined what should happen when the circumstances and Article 81(1) combine to prohibit the exercise of intellectual property rights to block parallel imports from outside the market in an instance where the intellectual property rights embodied by the imported goods have not been exhausted.

The leading case of the moment, from the intellectual property law point of view, is *Silhouette v Hartlauer*.¹⁴⁰ There is ample published commentary discussing this case.¹⁴¹ But *Silhouette* does not address the situation where the competition laws forbid the exercise of a not-exhausted, intellectual property right in respect of goods originating from outside of the market. This is because *Silhouette* and its progeny, *Sebago v G-B Unic*¹⁴² and *Davidoff*,¹⁴³ are concerned with the exhaustion of rights. An intellectual property right is said to be exhausted when its owner has fully exercised its rights under the laws that create the right in the first place.¹⁴⁴ Thus,

¹⁴⁰ *Silhouette International Schmied, GmbH & Co, KG v Hartlauer Handelgesellschaft, mbH*, Case C-355/96, [1998] ECR I-4799; [1998] 2 CMLR 953; [1998] All ER (EC) 769. Hereafter “*Silhouette*.” This case involved trademark protected spectacles that were intended for retail sale in Bulgaria. Instead, they were parallel imported into Austria, which, at the time, considered a volitional sale anywhere in the world of intellectual property protected goods to exhaust the Austrian intellectual property protection in those goods – a principle known as international or global exhaustion. The Court of Justice ruled to the contrary, holding that it was against the purpose of the Common Market for individual Member States to adopt rules of international exhaustion.

¹⁴¹ See Hays, “The Silhouette Case: The European Union Moves to the Highest Common Denominator on the Gray Market Question” [1998] TMR 234; and better: Carboni, *Zino Davidoff, SA v A&G Imports, Ltd: A Way Around Silhouette?* [1999] EIPR 524; Hann, *Silhouette v Hartlauer – “Fortress Europe?”* [1999] J World Intell Prop 809; Pagenberg, “The Exhaustion Principle and “Silhouette” Case” [1999] 1 IIC 19; Woolridge, “The Silhouette Case: The Trade Marks Directive and International Exhaustion” [1998] 4 IPQ 436.

¹⁴² *Sebago, Inc and Ancienne Maison Dubois et Fils, SA v G-B Unic, SA*, Case C-173/98, [1999] 2 CMLR 1317, hereafter, “*Sebago*.” The ECJ’s decision in this case was a natural consequence of the court’s prior decision in *Silhouette*. If a first sale of goods outside of the market does not exhaust the intellectual property owner’s rights as to those goods within the market, then when goods, first sold outside of the market, are imported and resold within the market without the consent of the intellectual property owner, the further intra-market commercialisation of the goods would be an infringement of the intellectual property rights. The issue in *Sebago* was whether a retailer within the market, where the intellectual property owner sold some of the shoes in question, had to prove that there was consent for each example in a mixed batch of the goods, where some may have originated from within the market and some from without. The Court of Justice held that trademark exhaustion and the need for consent was specific to each example of an otherwise intellectual property protected product.

¹⁴³ *Davidoff*, *supra*, note 23.

¹⁴⁴ Cornish, *Intellectual Property*, *supra*, note 5, at 41 *et sub*; Hays, “The L’anza Decision”, [1998] 8 Ent L Rev 313. A good portion of the debate concerning the exhaustion of rights concerns what it means to fully exercise the right. If intellectual property is seen as a bundle

the exercise of rights described by a United Kingdom patent exhausts patent protection for the goods concerned in the United Kingdom and, out of necessity for the integration of the Common Market,¹⁴⁵ everywhere else in the EU.

One may deduce from these cases that exhaustion is a matter internal to the market, a local issue for local rights. Competition law, on the other hand, is global in both cause and effect.¹⁴⁶ What is known about the relationship between these two bodies of laws, and what has been known since *Consten and Grundig*, is that questions about the existence of a right – such as whether a right, in a given circumstance¹⁴⁷ and in relation to particular goods,¹⁴⁸ has been exhausted by the actions of its owner¹⁴⁹ – are effectively subordinate in commercial terms to issues of their exercise, as defined by Article 81. The intellectual property right may continue to exist, as in *Silhouette*, but its use may be prohibited, as in *Consten and Grundig*, and this prohibition can apply in respect of goods embodying the right and originating from outside of the EU.

VII. CONCLUSION

Agreements or concerted practices which are capable of distorting competition within the EU are prohibited by Article 81(1). A principle mechanism used to give effect to such competition-distorting agreements, particularly where intellectual property protected goods are concerned, is selective distribution systems within the market. One of the ways in which these

of a nearly infinite number of privileges to do various things, then it is difficult to determine when all of the privileges have either been exercised or forfeited. On the other hand, if intellectual property is a negative right to exclude goods embodying the attributes described by the intellectual property from the stream of commerce, then the presence in commerce of legitimate goods to which the exclusionary right has been waived is a clear indication that the right has been previously exercised and, therefore, exhausted.

¹⁴⁵ *Dansk Supermarked, A/S v Imerco, A/S*, Case 58/80, [1981] ECR 181; [1981] 3 CMLR 590, para 12; *Gesellschaft zur Verwertung von Leistungsschutzrechten, mbH v EC Commission*, Case 7/82, [1983] ECR 483; [1983] 3 CMLR 645, para 39; *Keurkoop, BV v Nancy Keen Gifts, BV*, *supra*, note 95, para 24; *Merck & Co, Inc and others v Primecrown, Ltd*, *supra*, note 11, paras 36-37; *Polydor, Ltd and RSO Record Shops, Ltd v Harlequin Record Shops, Ltd and Simons Records, Ltd*, Case 270/80, [1982] ECR 329; [1982] 1 CMLR 677, paras 7, 17.

¹⁴⁶ Cocuzza and Montini, "International Antitrust Co-operation in a Global Economy" [1998] 3 ECLR 156; Ham, "International Cooperation in the Anti-Trust Field and in Particular the Agreement Between the United States of America and the Commission of the European Communities" [1993] CML Rev 571.

¹⁴⁷ The issue in *Silhouette*, *supra*, note 140.

¹⁴⁸ The issue in *Sebago*, *supra*, note 142.

¹⁴⁹ The issue in *Davidoff*, *supra*, note 23.

systems may be used to distort competition is through frustrating parallel trade. For Article 81(1) purposes, it does not matter if some or all of the parties to an anti-competitive agreement or concerted practice are located outside of the market.¹⁵⁰ The important and legally cognisable fact is that extra-market commercial behaviour is capable of distorting the development of competition within the market. The same threat to internal competition from the use of trademark rights to isolate the market from external sources of goods was recognised by the Council in the first drafts of the Trade Mark Regulation.¹⁵¹

It follows that extra-market agreements or concerted practices, that seek to prevent parallel importation from outside of the EU into the market, and that utilize EU-based intellectual property rights to isolate the market from external sources of legitimate, intellectual property protected, parallel goods, and that employ a market-based selective distribution system to benefit from higher intra-market prices and lower intra-market non-price costs, are anti-competitive and prohibited by Article 81. The ECJ recognized this relationship between restrictions on extra-market parallel imports and distortions of internal competition in *EMI v CBS*,¹⁵² where the court said that the use of national intellectual property rights to repel imports from outside of the EU might adversely affect competition within the market if the intellectual property owner operated a selective distribution system with the market.

The subsequent case law of the Court of Justice has only addressed the question of whether the intellectual property rights in extra-market parallel imports were exhausted. The court has yet to consider the circumstance where the intellectual property rights embodied by parallel imports from outside of the EU are not exhausted¹⁵³ – the rights still exist in respect of the goods in question – but the exercise of the rights is prohibited by Article 81(1). Under the law of the venerable case of *Consten and Grundig*, the two issues may coexist. The non-exhausted intellectual property right embodied by extra-market parallel goods may continue once the goods have been brought into the market, but their exercise should be prohibited where necessary to preserve the unfettered development of competition within the market.

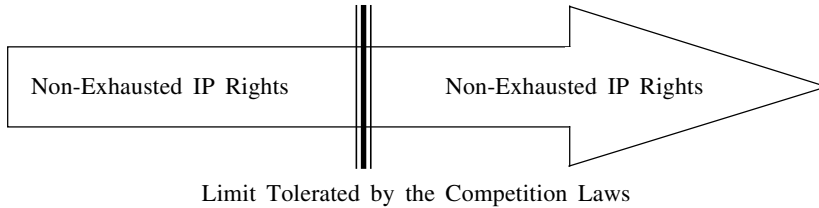
¹⁵⁰ *Community v Konica (UK) Ltd and Konica Europe, GmbH, supra*, note 34, para 47; *Béguelin Import Co and another v GL Import Export, SA, supra*, note 96, paras 11-12; *Re French and Taiwanese Mushroom Packers, supra*, note 96, para 21.

¹⁵¹ See the text accompanying notes 113-115.

¹⁵² *Supra*, note 131.

¹⁵³ As in *Silhouette, Sebago*, and, perhaps, under the ECJ's future decision on the referral of *Davidoff*.

**Illustration 5. Range of Commercial Behaviour in
re. Enforcement of Rights**



Once the European Court of Justice has delineated the exhaustion-of-rights issues, compensating for the definitional deficiencies in such Community legislation as the Trade Marks Directive, and once the Court has given guidance to intellectual property owners on how they may assure that their rights are not exhausted in respect of extra-market goods, the application of the EU competition laws to extra-market, parallel goods will become a point of contention between intellectual property owners and parallel traders, including those retailers who benefit from parallel trade. This is particularly true now that competition law enforcement has devolved to the national courts of the Member States,¹⁵⁴ giving potential competition law litigants a local forum for their disputes. The next battle in the struggles over intellectual property-protected goods in global circulation may be fought at the national court level using the competition laws and relevant defences.

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¹⁵⁴ Under Art 84 of the EC Treaty, *supra*, note 4.

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