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THE SILHOUETTE OF A TROJAN HORSE: REFLECTIONS ON ADVOCATE GENERAL JACOBS' OPINION IN *SILHOUETTE v. HARTLAUER*

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The Silhouette of a Trojan Horse: Reflections on Advocate General Jacobs' Opinion in *Silhouette v. Hartlauer**

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The European Court of Justice (ECJ) has been asked to decide whether its own seminal jurisprudence on the prerequisites of the completed internal market may be extended into the international arena of trade, or should instead be mandatorily restricted to the European Union (E.U.) market itself.

The ECJ perceived in the 1960s that completion of the internal market as promised by the Treaty of Rome would be threatened if trade mark holders and other holders of intellectual property rights (IPRs) might use those rights to partition the internal market when tariffs and quotas were eliminated within the Community. From that early date the Court has been addressed by attacks against its intra-Union exhaustion doctrine from many sides.

The Court now is asked to define E.U. policy on the subject of the international or worldwide exhaustion of IPRs under the guise of a seemingly minor question of interpretation—namely whether Article 7 of the Trade Marks Directive of 1989 should be understood to have limited the power of the Member States to adopt their own rules regarding international exhaustion in respect of trade marks. Yet underlying this seemingly minor question lies years of intensive lobbying of the Member State governments and the Commission by industry groups concerned to assure that the E.U. does not adopt a policy of international exhaustion, not only in the field of trade marks, but also in the fields of copyright, patent and related rights.

A series of Directives has been set up, each with similar text on the question of exhaustion—each with text that fails to address the international exhaustion issue. Now the Trojan Horse has been wheeled into Luxembourg and the Court is asked

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to construe the text of the Trade Marks Directive. Is the ECJ prepared to foreclose an open world market in IPRs protected goods on the basis of this record? Is the ECJ prepared to open the door in the side of this Trojan Horse?

The factual background

Silhouette v. Hartlauer comes before the ECJ by referral from the Austrian Supreme Court (*Oberster Gerichtshof*).[1] Silhouette is an Austrian producer of fashion eyeglass frames with its trade mark registered in Austria. It sold and exported a quantity of outdated frames at a price below its ordinary wholesale price (for current model frames) to a buyer which took delivery in Sofia, Bulgaria. The buyer in Bulgaria resold the frames to an Austrian discount retailer, Hartlauer, which brought them back into Austria. Hartlauer offered these frames to the public under the Silhouette trade mark, while indicating in its advertisements that Silhouette had not supplied them. Silhouette filed an action seeking to enjoin Hartlauer from marketing the frames under Silhouette's trade mark in Austria.

At the time of the aforesaid transactions, Austria had not yet completed its accession to the E.U. (which took effect on January 1, 1995), and it was then a Contracting State of the European Economic Area (EEA). As a Contracting State of the EEA, Austria was obligated to follow jurisprudence on the subject of the intra-Union exhaustion of trade mark rights. The Austrian Government had adopted the relevant provisions of the Trade Marks Directive,[2] including Article 7 which deals expressly with the subject matter of exhaustion, into its national law (in equivalent language). At the time of the transaction relevant to this case, Hartlauer technically sought to import into a Contracting State of the EEA goods that had been sold outside the territory of the EEA with the consent of the EEA trade mark holder, Silhouette. For all intents and purposes relevant to this case, however, the question is the same as if Austria had then been a Member State of the E.U., and A. G. Jacobs treats this case as such—as hereafter do the authors of this reflection.

Prior to joining the EEA, Austria followed a rule of international exhaustion with respect to trade marks. Once goods bearing an Austrian trade mark had been placed on the market outside the territory of Austria with the consent of the Austrian trade mark holder, that trade mark holder could not use its Austrian trade mark to oppose importation of those goods into Austria. In adopting Article 7 of the Trade Marks Directive into national law, it is said that the Government intended that the question of international exhaustion be "settled by legal

[1] *Silhouette International Schmied GmbH & Co. KG v. Hartlauer Handelsgesellschaft mbH*. These facts are derived from the Opinion of Advocate General Jacobs in this case, delivered January 29, 1998.

[2] First Directive to approximate the laws of Member States relating to Trade Marks (89/104).

practice".[3] The Austrian court of first instance (*Landgericht Steyer*) and intermediate appellate court (*Oberlandesgericht Linz*) ruled in favour of the importer, Hartlauer. The Austrian Supreme Court then put to the ECJ the question whether Article 7(1) of the Trade Marks Directive must be interpreted so as to preclude Austria from continuing to allow international exhaustion in respect to trade marks.

The legal framework

Article 7 of the Trade Marks Directive of 1989 provides:

> "(1) The trade mark shall not entitle the proprietor to prohibit its use in relation to goods which have been put on the market in the Community under that trade mark by the proprietor or with his consent.
> (2) Paragraph 1 shall not apply where there exist legitimate reasons for the proprietor to oppose further commercialisation of the goods, especially where the condition of the goods is changed or impaired after they have been put on the market."

For purposes of the present case there is no indication of a reason to restrict commercialisation under Article 7(2).[4]

Advocate General Jacobs ultimately concludes that the language and context of Article 7(1) of the Trade Marks Directive require the Member States to adopt a uniform attitude toward international exhaustion in the field of trade marks, and to preclude it. In other words, a Member State may not provide that when goods have been placed on a market outside the E.U. (and EEA) with the consent of the

[3] Opinion of Advocate General Jacobs, delivered January 29, 1998 in *Silhouette*, *ibid.* at para. 22.

[4] Several provisions of the Trade Marks Directive may be relevant to the question of international exhaustion. Article 7 should be considered in relation to the basic rights conferred by the trade mark which are enumerated in Article 5, which provides:

> "1. The registered trade mark shall confer on the proprietor exclusive rights therein. The proprietor shall be entitled to prevent all third parties not having his consent from using in the course of trade:
> (a) any sign which is identical with the trade mark in relation to goods or services which are identical with those for which the trade mark is registered;
> (b) any sign where, because of its identity with, or similarity to, the trade mark and the identity or similarity of the goods or services covered by the trade mark and the sign, there exists a likelihood of confusion on the part of the public, which includes the likelihood of association between the sign and the trade mark.
> [. . .]
> 3. The following, *inter alia*, may be prohibited under paragraphs 1 and 2:
> (a) affixing the sign to the goods or the packaging thereof;
> (b) offering the goods, or putting them on the market or stocking them for these purposes under that sign, or offering or supplying services thereunder;
> (c) importing or exporting the goods under the sign;
> (d) using the sign on business papers and in advertising.

trade mark holder, then that trade mark holder may not oppose importation of those goods into that Member State.

The Analysis of Advocate General (A.G.) Jacobs and our reflections on it

The text of the Trade Marks Directive

A. G. Jacobs begins by noting that Article 7 does not mandate that the Member State adopt a rule of international exhaustion.[5] He observes that no party appears to challenge this proposition, and we do not. In support, A. G. Jacobs briefly recounts the legislative history of the Directive.[6] The Commission initially proposed that a rule of international exhaustion be mandatory for the Member States. The Commission subsequently amended its proposal (under heated opposition from industry, we add) in favour of the present neutral formulation. It is without doubt that the express text of Article 7 does not mandate a rule of international exhaustion.

A. G. Jacobs indicates that the language of Article 7 is unclear on the question whether Member States may adopt differing rules on the subject-matter of international exhaustion. He says that it seems logical that if intra-Union exhaustion is required by the Directive, international exhaustion would "naturally" be precluded (or that such a result can be "reasonably inferred")—while accepting that there are other sides to this argument, which he nevertheless finds unconvincing.[7]

It appears that A. G. Jacobs ignores the most reasonable inference from the evidence he presents. The Commission started by proposing an express rule of international exhaustion. The Commission was not ignorant of the issue—it knew it was important. It faced industry pressure and retreated to neutral ground, codifying the existing mandatory E.U. principle of intra-Union exhaustion in the field of trade marks long demanded by the ECJ.[8] If the Commission and Council wished to mandate a rule opposite to that initially proposed by the Commission, they certainly knew how to draft it! Acting with certain knowledge that the Trade Marks Directive would be looked to as a source of instruction on the question of international exhaustion, a neutral rule was adopted without even a single word on the subject in the preamble. The Court should not infer a result precluding international exhaustion from the wording of Article 7 under these circumstances.

[5] Opinion of A. G. Jacobs, at paras 30–31.
[6] *ibid.* at para. 32.
[7] *ibid.* at para. 33.
[8] The official explanation of the Commission to its revised 1985 draft text of the Trade Marks Directive [1995] O.J. C351/4 states: "*La Commission a renoncé à obliger les Etats membres à introduire dans leur législations nationales respectives le principe de l'épuisement international.*"

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In regards to the express text, A. G. Jacobs goes on to say that the now-codified rule of intra-Union exhaustion represents a "derogation" from the rights of the trade mark holder, that permission to the Member States to allow international exhaustion would be a further implied derogation, and that "derogations should not be construed broadly".[9] Leaving aside debate on general principles of interpretation, this argument by A. G. Jacobs starts from a false premise. Article 7(1) codifies the ECJ's jurisprudence on trade marks and the free movement of goods. Trade mark holders in the E.U. did not and do not have the right to partition the market on the basis of their trade mark holdings. Codification of the intra-Union exhaustion rule does not derogate from the rights of trade mark holders. Article 7(1) is not an exception capable of being construed broadly. It is a positive statement of an E.U. rule of law, to be construed as the ECJ would ordinarily construe a positive rule.

The aims and scope of the Trade Marks Directive

A. G. Jacobs accepts that "the terms of the Directive are not conclusive" on the subject of international exhaustion, and he turns to the "aims and scope" of the Directive for interpretative guidance.[10] He acknowledges that the Trade Marks Directive, by its express terms, "does not purport to 'undertake full-scale approximation of the trade-mark laws of the Member States' but aims to approximate 'those national provisions of law which most directly affect the functioning of the common market' ". He adds, "On the other hand, the Directive seeks to ensure, with certain limited exceptions, that trade marks 'enjoy the same protection under the legal systems of all the Member States' ".[11]

Those favouring international exhaustion, according to A. G. Jacobs,[12] suggest that Article 7 was intended only to codify the law of the E.U. on the subject of exhaustion (per Articles 30 and 36 of the E.C. Treaty), and they observe that the ECJ has itself stressed this point. As is well known, Member States followed different approaches to the exhaustion question prior to adoption of the Directive and, absent an express indication to the contrary, this discretion of the Member States should remain intact.

A. G. Jacobs counters this argument by reference to language in the third recital of the Directive's preamble that indicates its purpose to address those aspects of trade marks which "most directly affect the functioning of the internal market". He also quotes another provision (see above) indicating an intention to assure that marks "enjoy the same protection under the legal systems of all the Member States".[13] A. G. Jacobs posits that while the Court may indeed have stressed that

[9] *ibid.* at para. 34.
[10] *ibid.* at para. 35.
[11] *ibid.*
[12] *ibid.* at paras 36–37.
[13] *ibid.* at paras 38–39.

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Article 7 is a codification of its jurisprudence on intra-Union exhaustion,[14] that the Court was speaking only to internal market effects. Thus, he says, "it cannot be assumed that that is the sole function of Article 7".

The next steps in analysis are vital to his conclusions, and we feel constrained to quote:

> "40. If the Directive is seen as establishing the essential terms and effects of trade-mark protection, it is difficult to argue that it leaves Member States free to opt for international exhaustion. The scope of the exhaustion principle is after all central to the content of trade-mark rights.
>
> 41. But even if one takes a narrower view of the character of the Directive, it seems clear that international exhaustion is one of the matters which 'most directly affect the functioning of the internal market' and which the Directive therefore seeks to harmonise. If some Member States practise international exhaustion while others do not, there will be barriers to trade within the internal market which it is precisely the object of the Directive to remove."

This is a peculiar position for A. G. Jacobs to take. The Court has stressed that Article 7 codifies its jurisprudence on intra-Union exhaustion. The Court has not addressed the subject of the mandatory exclusion of international exhaustion in the field of trade marks. If we follow A. G. Jacobs' own principles of interpretation (see above), the "derogation" of Article 7 should be construed narrowly, and the Court should "naturally" stop at the border of its own prior jurisprudence; it should not go on to assume that Article 7 was intended to address another concededly important subject matter.

Beyond this contradiction in reasoning is a more important point. A. G. Jacobs says that the subject of the international exhaustion of marks is of the greatest importance to the functioning of the internal market. If this is true, should not the Commission, Council and other Union organs have addressed it? In the context of a Commission and Council debate over the terms of the Directive, and in which there was intensive industry lobbying on the subject of international exhaustion, the Directive is silent. Why should the Court interpret this silence as a decision by the Union organs to deal in just one way with what we are told is a matter of great import to the Union?

What is the impact on the functioning of the internal market with which A. G. Jacobs and the Austrian, French, German, Italian and United Kingdom governments are so concerned? It is a problem so grave that in 40 plus years of ECJ jurisprudence on the subject of intra-Union exhaustion—and with the Member States maintaining diverse rules on the subject of international exhaustion—it did

[14] A. G. Jacobs is apparently referring to the judgment of the ECJ of July 11, 1996: ECJ Case C–427/93 *Bristol-Myers Squibb v. Paranova A/S*; Case C–429/93 *C. H. Boehringer Sohn, Boehringer Ingelheim KG and Boehringer Ingelheim A/S v. Paranova A/S* and Case C–436/93 *Bayer Aktiengesellschaft and Bayer Danmark A/S v. Paranova A/S*; Joined Cases C–427/93, C–429/93 and C–436/93 Case C–71/94 *Eurim-Pharm Arzneimittel GmbH v. Beiersdorf AG*; Case C–72/94 *Boehringer Ingelheim KG* and Case C–73/94 *Farmitalia Carlo Erba GmbH Pharma GmbH v. Rhone-Poulenc Pharma GmbH*.

not come up before today![15] It is the problem that if the Member States maintain differing rules on international exhaustion, then trade mark holders in some Member States might block parallel imports (as before), while holders in some other Member States might not block parallel imports (as before). This, it is said, may interfere with the functioning of the internal market.

A. G. Jacobs and the above-mentioned governments assume that the Trade Marks Directive will be interpreted to permit those Member States which do not follow a rule of international exhaustion to block imports which have first entered other Member States from outside the Union as parallel imports.[16]

Why is this seen to be such a problem for the proper functioning of the internal market? Irrespective of the rule on international exhaustion that the E.U. ultimately adopts (if it adopts one), the Member States will still need to maintain customs procedures, other administrative procedures and judicial remedies in respect of trade marks and imported goods. On the international side, counterfeiting will continue to pose a potential problem for trade mark holders in the Members States, and mechanisms will be needed to deal with this. In fact, the maintenance of such mechanisms is mandated by the WTO TRIPS Agreement.[17]

[15] The ECJ has ruled in 1976 (ECJ June 15, 1976, 51, 86 96/75; [1976] E.C.R. 811 (*EMI/CBS*)), and 1982 (ECJ February 9, 1982, 270/80; [1982] E.C.R. 707; [1982] C.M.L.R. 677 (*Polydor/Harlequin*), that Member States are permitted to ban extra-Union parallel imports. However, in each case it was decided that the E.C. Treaty does not *mandate* that the Member States do so. The question whether the E.C. Treaty (and whether a Directive based on Article 100a of the Treaty) may require Member States to ban extra-Union imports is a markedly different question which has not been addressed by the Court.

[16] Opinion of A. G. Jacobs, at para. 42. The reasoning behind this interpretation is not set out in the opinion. It is likely to be as follows: Article 7 says that when goods are placed on the market "in the Community" with the consent of the trademark holder, the trademark holder may not oppose the free movement of such goods within the Union. The Court would presumably interpret this to mean that if the law of a particular Member State precludes a trademark holder from opposing the importation of goods bearing its mark that have been placed on the market outside the Union with its consent, then the affected trademark holder has not for purposes of Article 7 *consented* to placement of the goods on the "Community market". In consequence, the goods imported into the Member States following a rule of international exhaustion will not enter into free circulation throughout the Union without the consent of the right holder in the Member State of importation.

The Member State governments which oppose international exhaustion, and A. G. Jacobs, do not accept that Article 7 of the Trade Marks Directive might even be interpreted such that a rule of international exhaustion for one Member State would in effect constitute a rule of international exhaustion for all Member States. Opinion of A. G. Jacobs at para. 42. In other words, if Sweden were to allow parallel imports from non-E.U. countries while France and Germany did not allow such imports, then goods placed on overseas markets with the consent of E.U. trade mark holders would flow into the Union through Sweden, where their entry into the E.U. internal market would assure free movement throughout. Yet if Swedish or Dutch importers had price advantages *vis-à-vis* French importers, and goods that entered the Union through Sweden or the Netherlands were less costly than goods that entered through France, then the European import function might well migrate to Sweden and the Netherlands. If French importers were unhappy to compete with low-price imports from other Member States, they might urge the French Government to adopt a rule of international exhaustion.

[17] See, *e.g.* TRIPS Agreement, arts 42, 44 and 50.

A uniform Union rule on international exhaustion will not eliminate the obligation of the Member States and the Union to provide protection for trade mark holders in international trade.

Furthermore, the intra-Union exhaustion rule by no means eliminates the possibilities for restricting the movement of goods on the basis of trade marks as between the Member States. Trade mark rights remain separate for the Member States, and an identical mark may be held in different Member States by persons with no economic link.[18] In such cases, the holder of the trade mark in one Member State may block importation of goods placed on the market in a second Member State under an identical mark.[19] Moreover, in the context of its intra-Union exhaustion jurisprudence, the ECJ has permitted trade mark holders to block parallel imports under circumstances in which consumer confusion or injury might be foreseen (such as in limited cases involving repackaged pharmaceutical goods),[20] and this jurisprudence is reflected in Article 7(2) of the Trade Marks Directive.[21] It is not the case, therefore, that a single rule barring parallel imports of trade marked goods from outside the Union would eliminate the need for Member States to maintain national regulatory mechanisms in respect to the intra-Union movement of trade marked products, or that an undistorted internal market in trade marked goods would result from such a rule.[22]

The objection that a uniform rule would result in some Member States having price advantages over others in the field of importation runs counter to the view of the single internal market as providing for the most efficient allocation of Union resources. If lower cost parallel imports allow production to take place at lower cost in some Member States, then producers in those Member States will be better able to penetrate global markets. The Union economy as whole will improve. If producers in France find that they are unable to compete with producers in Sweden because the latter have access to lower cost inputs, then French producers may petition their Government to permit parallel imports! If Swedish consumers are able to purchase products at lower prices than French consumers, is this an internal market distortion which should be cured by raising prices in Sweden?

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[18] This is the case under the Trade Marks Directive, though a Community Trade Mark (see discussion, *infra*) is not divisible.

[19] *IHT Internationale Heiztechnik v. Ideal Standard* [1994] 3 C.M.L.R. 857.

[20] See, *e.g.* Judgments of July 11, 1996 referred to in n. 14, *supra*. Note that in these decisions the Court has stressed that any exceptions from the principle of intra-E.U. exhaustion must be justified by specific circumstances that may create risk of harm to the consumer.

[21] See para. 8, *supra* for text.

[22] Under a Union rule which continues to permit Member States to provide for international exhaustion, the parallel importation of trade marked goods into those Members might still be restricted in circumstances in which consumer injury or confusion is foreseeable. This approach to the question of international exhaustion in the field of trade marks has been recommended. *Cf.* Thomas Cottier, *Das Problem der Parallelimporte im Freihandelsabkommen Schweiz-EG und im Recht der WTO-GATT, Revue Suisse de la Propriété Intellectuelle*, I/1995, discussed in the context of the WTO TRIPS Agreement, *infra*, n. 38.

In short, the governments of Austria, France, Germany, Italy and the United Kingdom, with support of the Commission, argue (and A. G. Jacobs accepts) that Article 7 should preclude the Member States from adopting diverse rules on international exhaustion in the field of trade marks because this would adversely affect them. What neither A. G. Jacobs nor these Member States can truly say is that the Council chose to address these concerns in Article 7 of the Trade Marks Directive. The issue was on the table. A rule precluding the Member States from allowing international exhaustion was not adopted. Perhaps the Council can hereafter be persuaded that such a rule is needed. Perhaps not. The point is that the present Trade Marks Directive does not resolve this matter as some would prefer it resolved.

The issue of Union competence

The Trade Marks Directive was adopted on the basis of Article 100a of the E.C. Treaty, and the Government of Sweden argues that Article 100a may not be used as the basis for regulating the subject of international exhaustion. It reasons that international exhaustion is a question of the common commercial policy and should be addressed under Article 113, and that the ECJ in its opinion on accession of the Communities to the WTO[23] decided that external IPRs matters were within the joint competence of the Communities and the Member States.

A. G. Jacobs accepts that certain aspects of the international exhaustion question are better dealt with as common commercial policy issues, such as negotiations regarding exhaustion policies with third states. He also accepts that international reciprocity issues had an influence on the Commission's decision to abandon a rule of international exhaustion for the Union. However, he observes that a rule on international exhaustion will certainly affect trade among the Member States since it will determine whether goods coming into the Union from the outside will be able to move freely.[24]

The question of international exhaustion is substantially more a question of external policy than an internal market question. An effective internal market policy on certain IPRs questions will of course necessitate addressing an international external component. Matters with a mainly external dimension preferably should be dealt with under the common commercial policy. The ECJ must of course tend to the dividing line between internal and external policy with care.

The underlying function of trade mark protection

The Government of Sweden has argued that the function of the trade mark is to assure the consumer of the origin of goods, and not to provide trade mark

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[23] [1994] E.C.R. I–5267.

[24] Opinion of A. G. Jacobs at paras 46–47.