

The Case of the Reappearing Spectacles—The Future Is Not So Bright for International Parallel Importers in the ECJ After *Silhouette International Schmied GmbH & Co. KG v. Hartlauer Handelsgesellschaft MbH*

I. INTRODUCTION	479
II. HISTORICAL BACKGROUND AND ANALYSIS.....	480
III. NOTED DECISION.....	492
IV. ANALYSIS AND CRITICISM	495
V. CONCLUSION	502

I. INTRODUCTION

Austrian company Silhouette International brought an action for interim relief before the Landesgericht Steyr seeking an injunction restraining Hartlauer Handelsgesellschaft from distributing its products in Austria.¹ Silhouette produced fashion spectacles in the higher price ranges and distributed the spectacles worldwide under the word and picture trademark “Silhouette,” which was registered in Austria and in most countries of the world.² When selling its goods in Austria, Silhouette supplied the spectacles to specialist opticians, while in other countries it sold through a system of selective distributorships.³ The defendant, Hartlauer, was a discount seller of spectacles in numerous branches in Austria and solicited customers

1. See Case C-355/96, *Silhouette Int’l Schmied GmbH & Co. KG v. Hartlauer Handelsgesellschaft mbH*, [1998] 2 C.M.L.R. 953, 974. Silhouette argued that it had not exhausted its trademark rights with respect to the products because it did not distribute them within the European Economic Area (EEA). See *id.* It based its claim on paragraph 10a of the Markenschutzgesetz (protection of trademarks), paragraphs one and nine of the Gesetz gegen den unlauteren Wettbewerb (unfair competition), and Article 43 of the Allgemeines Bürgerliches Gesetzbuch (the Civil Code). See *id.* The Landesgericht Steyr is the regional court of Steyr and the Oberlandesgericht Linz is the higher regional court of Linz. See *id.* at 960.

2. See *id.* at 973. “A Community trade mark may consist of any signs capable of being represented graphically, particularly words, including personal names, designs, letters, numerals, the shape of goods, or of their packaging, provided that such signs are capable of distinguishing the goods or services of one undertaking from those of other undertakings.” Council Regulation 40/94 of 20 December 1993 on the Community Trade Mark art. 4, 1994 O.J. (L 11) 1, [hereinafter Regulation 40/94].

3. See *Silhouette Int’l*, [1998] 2 C.M.L.R. at 973. A producer of a high profile product generally seeks to control the distribution of that product by implementing a selective system of distributorships to better protect the upscale image of the product. In such a system, the manufacturer does not just want any company distributing its product, but one which will safeguard its image.

mainly by its low prices.⁴ Hartlauer was not supplied by Silhouette because Silhouette considered sales by Hartlauer to be harmful to the image which Silhouette had created for its products as superior quality spectacles.⁵ After obtaining Silhouette products outside the European Union (EU or Union), Silhouette sought to prohibit Hartlauer from marketing under its trademark spectacles or spectacle frames which were not put in the market in the European Economic Area (EEA) by it or with its consent.⁶ Silhouette's action failed before the Landesgericht Steyr and on appeal to the Oberlandesgericht Linz, both courts holding that there was no violation of trademark laws with respect to exhaustion of rights.⁷ The Austria high court referred the case to the European Court of Justice since it involved interpretation of the Treaty establishing the European Community.⁸ The European Court of Justice affirmed in part and reversed in part the decision of the Oberlandesgericht Linz and *held* that Member States could not create national laws which provided for international exhaustion under Article 7(1) of the Trade Marks Directive, violation of which was not enough for a trademark proprietor to obtain an injunction restraining a distributor from selling the goods in the EEA.⁹ Case C-355/96, *Silhouette Int'l Schmied GmbH & Co. KG v. Hartlauer Handelsgesellschaft mbH*, [1998] 2 C.M.L.R. 953.

II. HISTORICAL BACKGROUND AND ANALYSIS

In his vision for creating a united Europe to remedy the devastating effects of World War II, French statesman Robert Schuman sought to create an economic and political entity that would

4. *See id.* at 974.

5. *See id.*

6. *See id.* In October 1995, Silhouette sold 21,000 spectacle frames of an out-dated model to a firm called Union Trading for the equivalent of \$261,450. *See id.* The sale was arranged by Silhouette's sales representative to the Middle East. *See id.* The sales representative was directed to instruct the purchaser that the frames were only to be sold in Bulgaria or states of the former Soviet Union. *See id.* Although the sales representative informed Silhouette that he had instructed the purchaser accordingly, it is not possible to ascertain whether that actually happened. *See id.* After Silhouette delivered the goods to Union Trading in Sofia in November 1995, Hartlauer somehow acquired the goods and offered them for sale in December 1995. *See id.* In its advertising campaign, Hartlauer stated unequivocally that they were not supplied by Silhouette but was able to obtain 21,000 Silhouette frames from abroad. *See id.*

7. *See id.* at 974.

8. *See Silhouette Int'l* (1998) 2 C.M.L.R. at 975. The European Court of Justice is the highest court of the European Union and has jurisdiction pursuant to Article 177 of the EC Treaty over all matters involving interpretation of the Treaty. *See Treaty Establishing the European Economic Community* Mar. 25, 1957, O.J. (C91) 5 (1992) (as amended by the Treaty on European Union) [hereinafter EC TREATY].

9. *See Silhouette Int'l*, (1998) 2 C.M.L.R. at 972, 976.

have minimal internal barriers to trade.¹⁰ At a time when weakened European powers feared another devastating war, Schuman's bold proclamation recognized that the best way for Europe to face the future was to unify its collective power.¹¹ To this day, over fifty years later, the quest for unity has not gone without its twists and turns. During the embryonic stages of the European Community (EC or Community), there was much concern that the enforcement of trademarks could and would be used as a barrier to trade between Member States.¹² This potential problem threatened the harmonization and free movement of goods principles essential to the effective functioning of the EEA.¹³

In the 1960s, when market integration became a fundamental principle regarding competition policy in the EC, large firms and trademark proprietors feared that they would no longer be able to divide the common market through export bans and other similar measures.¹⁴ Attention turned to the use of intellectual property rights in the 1960s when trademark owners realized they could use such

10. See generally WILLIAM DIEBOLD, JR., *THE SCHUMAN PLAN: A STUDY IN ECONOMIC COOPERATION* 1-2 (1959). This vision, announced on May 9, 1950, was known as the Schuman Plan. See *id.* at 4. It was inspired by Jean Monnet, the French proponent of European integration. See *id.* at 8. Under this plan, all Franco-German steel production would be placed under a common High Authority composed of independent persons named by the participating national governments, but acting within an organization open to participation by other European countries. See TREATY ESTABLISHING THE EUROPEAN COAL AND STEEL COMMUNITY, April 18, 1951, O.J. (C191) 44 (1992) [hereinafter ECSC TREATY].

11. See DIEBOLD, *supra* note 10, at 2-3. After a decade of planning, on March 25, 1957, France, Germany, Belgium, the Netherlands, Luxembourg, and Italy signed the Common Market Treaty which gave birth to the European Economic Community (EEC). See *id.* at 649-50. Its purpose was to provide for closer economic ties between the Member States and the establishment of a single customs union among the Member States. See *id.* at 650-51. Formed after the experience of the two World Wars, it was envisaged that the Common Market Treaty would eliminate nationalism and thus promote peace and prosperity. See *id.* at 651.

12. See GUY TRITTON, *INTELLECTUAL PROPERTY IN EUROPE* 144 (1996).

13. See *id.* at 145. Pursuant to the preamble of the EEA Agreement, the EEA consists of the EEC, European Coal and Steel Community, Belgium, Denmark, Germany, Hellenic Republic, Spain, France, Ireland, Italy, Luxembourg, Netherlands, Portugal, United Kingdom, Austria, Finland, Iceland, Liechtenstein, Norway, Sweden, and Switzerland; these nations and entities are referred to as the Contracting Parties. See Agreement on the European Economic Area, January 3, 1994, 1994 O.J. (L 1) 3 [hereinafter EEA Agreement]. The general objective of the EEA is "to promote a continuous and balanced strengthening of trade and economic relations between the Contracting Parties with equal conditions of competition and the respect of the same rules with a view to creating a homogeneous European Economic Area." TRITTON, *supra* note 12, at 24. The fundamental provisions of the EEA Agreement are essentially the same as the EC Treaty, although the EEA Agreement includes more technical provisions with respect to intellectual property. See *id.* In addition, the EEA consists of Contracting Parties which are not members of the EC, and the European Court of Justice has held that provisions of the EEA Agreement which are identical to the EC Treaty should not be interpreted identically. See *id.* at 24-25.

14. See Valentine Korah, *Exhaustion of Trademarks in the European Communities*, Sixth Annual Conference on International Intellectual Property Law & Policy 2 (Apr. 16-17, 1998).

measures to divide the market.¹⁵ As the use of intellectual property rights increased during the 1970s, the European Court of Justice was forced to reconcile the desire for a harmonized internal market with creating incentives to invent and manufacture by the grant of exclusive intellectual property rights.¹⁶

The Court created a distinction between the grant of the trademark right, which was subject to national law of individual Member States, and the exercise of the right itself, which was subject to Community law.¹⁷ Following this logic, the Court protected the "specific subject matter" of the trademark right, while preventing proprietors from using intellectual property rights to partition the common market.¹⁸ Trademark proprietors could not restrict the import of goods put on the market in another Member State by them or a third party with their consent, unless justified by the "specific subject matter" of the right.¹⁹

Exactly what constituted "specific subject matter" was established in the *Centrafarm* cases.²⁰ In its interpretation of Articles 30 and 36 of the EC Treaty, the Court established for trademarks and other forms of intellectual property a principle of Community-wide exhaustion.²¹ The principle of exhaustion limited the rights of a trademark owner to control the resale of a product bearing the trademark after the goods had been put on the market by the trademark owner or a third party with his consent.²² Community exhaustion of trademarks was established in *Centrafarm v. Winthrop*.²³ In *Centrafarm*, a Dutch subsidiary of a British-owned pharmaceutical company sold the same product at a higher price in Holland than in the United Kingdom.²⁴ *Centrafarm*, a Dutch

15. *See id.*

16. *See id.* at 3.

17. *See id.*

18. *Id.*

19. Korah, *supra* note 14, at 3.

20. *See id.* at 3-4.

21. *See* EC TREATY arts. 30 and 36. Article 30 of the EC Treaty provides that "[q]uantitative restrictions on imports and all measures having equivalent effect shall, without prejudice to the following provisions, be prohibited between Member States." Article 36 of the Treaty provides that "[t]he provisions of Articles 30 to 34 shall not preclude prohibitions or restrictions on imports, exports or goods in transit justified on grounds of public morality, public policy or public security. . . . Such prohibitions shall not, however, constitute a means of arbitrary discrimination or a disguised restriction on trade between Member States."

22. *See* Jesper Rasmussen, *The Principle of Exhaustion of Trade Mark Rights Pursuant to Directive 89/104 (and Regulation 40/94)*, 4 EUR. INTELL. PROP. REV. 174 (1995).

23. Case 16/74, *Centrafarm v. Winthrop*, 1974 E.C.R. 1183, 1197-98.

24. *See id.* at 1184. *Winthrop* marketed the drug "Negram" in the Netherlands for Sterling Drug. *See id.*

wholesaler, purchased the product in quantity on the British market and resold it on the Dutch market at a higher price than it was purchased for in the United Kingdom and a lower price than it was sold for on the Dutch market.²⁵ Centrafarm functioned as a parallel importer; that is, the company purchased goods in quantity where the price was lowest and resold the goods in another part of the EC where the price was higher, and thus, undercut the price of the trademark proprietor.²⁶ The European Court of Justice, in a landmark decision, held that under Article 36 the trademark owner's exclusive rights to the trademark ceased to exist once a trademark owner, or a third party with its consent, placed a product on the market.²⁷ Reasoning that a trademark owner could partition national markets and erect barriers to free trade without the principle of Community exhaustion, the Court determined that the sale in the Community of trademarked goods, by the trademark owner or with his consent, necessarily exhausted the trademark rights throughout the Community.²⁸ As a result, the proprietor of the trademark lost his right to oppose the use of the mark by others in subsequent transactions throughout the Community.²⁹

In the second *Centrafarm* case, *Hoffmann-La Roche v. Centrafarm*, the Court held that "specific subject matter" entails the exclusive right of the trademark proprietor or a third party with his consent to put the products on the market for the first time.³⁰ This, the Court reasoned, protected the trademark owner from free riders using the trademark in connection with counterfeit products and avoided confusion by customers as to the origin of the trademark.³¹ With these protections granted to the proprietor, the Court justified the exercise of intellectual property rights under Article 36 of the EC Treaty.³²

The Trade Marks Directive of 1989, formally known as First Council Directive 89/104, established the exclusive right conferred upon trademark owners by Member States in Article 5 and substantiated the Community doctrine of exhaustion as established by

25. *See id.* Centrafarm took advantage of a considerable price differential in importing the product from Great Britain. *See id.* Court records indicated that "Negram" was sold in Great Britain at half the price for which it was sold in the Netherlands. *See id.*

26. *See id.* at 1193.

27. *See id.* at 1197-98.

28. *See Centrafarm v. Winthrop*, 1974 E.C.R. at 1193-94.

29. *See id.* at 1194.

30. *See Korah*, *supra* note 14, at 3-4.

31. *See id.* at 4.

32. *See id.*

the *Centrafarm* cases.³³ Passed on December 21, 1988, the Trade Marks Directive served to codify the Court's case law regarding exhaustion of Community rights.³⁴ Article 7(1) of the Directive provided that a trademark did not entitle the proprietor to prohibit the trademark's use in relation to goods which have been put on the market in the EC under that trademark by the proprietor or with his consent.³⁵ By virtue of the EEA Agreement, the principle of exhaustion was extended beyond the Community to cover the entire EEA.³⁶ The Trade Marks Directive was adopted under Article 100a of the EC Treaty to further the functionings of the internal market.³⁷ The preamble stated that the general purpose of the Directive was primarily to prevent the distortion of the free market caused by the variance in trademark laws throughout the Community.³⁸

The Directive essentially harmonized the "general conditions for obtaining and continuing to hold a registered trade mark."³⁹ While binding in most respects, Contracting Parties were given discretion to decide whether to adopt certain provisions of the Directive, for example, with respect to refusal to register or invalidate a trademark, and whether to provide protection to a trademark with a reputation.⁴⁰ In the context of trademark exhaustion, Articles 5 and 7 of the Directive are of special importance.⁴¹ Article 5, entitled "[r]ights

33. See First Council Directive 89/104 of 21 December 1988 to approximate the laws of Member States relating to trade marks, arts. 5 & 7, (1989) O.J. (L 40) 1 [hereinafter Directive 89/104].

34. See *id.* Pursuant to the EC Treaty, the Council and Commission have the power to "make regulations and issue directives, take decisions, make recommendations or deliver opinions." EC TREATY art. 189. Regulations have general application and are binding and directly applicable in all Member States. See *id.* A directive is binding in all Member States as to the ends which it seeks to accomplish, but leaves to the individual states the methods it wishes to employ to achieve these ends. See *id.* A decision is binding only upon those countries to which it is addressed. See *id.* Neither a recommendation nor an opinion has binding force. See *id.*

35. See Directive 89/104, *supra* note 33.

36. See generally EEA Agreement, *supra* note 13, 1994 O.J. at 8.

37. See Directive 89/104, *supra* note 33. Article 100a of the EC Treaty provides that "[t]he Council shall, acting in accordance with the procedure referred to in Article 189b and after consulting the Economic and Social Committee, adopt the measures for the approximation of the provisions laid down by law, regulation or administrative action in Member States which have as their object the establishment and functioning of the internal market."

38. See Directive 89/104, *supra* note 33. The ninth recital, in particular, states that "[w]hereas it is fundamental, in order to facilitate the free circulation of goods and services, to ensure that henceforth registered trademarks enjoy the same protection under the legal systems of all the Member States; whereas this should however not prevent the Member States from granting at their option extensive protection to those trademarks which have a reputation." *Id.*

39. *Id.*

40. See *id.*

41. See Case C-355/96, *Silhouette Int'l Schmied GmbH & Co. KG v. Hartlauer Handelsgesellschaft mbH*, [1998] 2 C.M.L.R. 953, 958 (opinion of Advocate General Jacobs).

conferred by a trade mark,” provides that a registered trademark confers numerous exclusive rights to the proprietor of that trademark.⁴² Article 7(1) outlines the parameters of Community trademark exhaustion, and Article 7(2) enumerates possible exceptions to the exhaustion of rights conferred by a trademark.⁴³

Further guidance on the interpretation of the Trade Marks Directive is provided by the Community Trade Mark Regulation.⁴⁴ The Trade Mark Regulation provides for a single Community mark throughout the Community and contains a provision virtually identical to the Trade Marks Directive regarding exhaustion of rights.⁴⁵ Like the Trade Marks Directive, the Trade Mark Regulation provides only for Community exhaustion and excludes references to international exhaustion.⁴⁶ It is doubtful that the Regulation leaves much, if any, discretion to the Member States in determining trademark actions.⁴⁷

Unlike the succinct EU policy regarding Community exhaustion, none of the EU institutions, including the Court, Council, and the Commission, have been able to create a consistent policy regarding international exhaustion.⁴⁸ The principle of international exhaustion provides that a trademark proprietor cannot stop the importation of goods bearing this trademark if such goods have been marketed in any other country by the proprietor or with the proprietor’s consent.⁴⁹

Much of the Court’s case law on exhaustion of rights has been developed in the context of the Community and not the world market.⁵⁰ In *EMI Records v. CBS United Kingdom*, the Court held that its case law under Articles 30 and 36 should not apply to imports

42. Directive 89/104, *supra* note 33.

43. *See id.* Article 7(2) of Directive 89/104 provides that “[p]aragraph 1 shall not apply where there exist legitimate reasons for the proprietor to oppose further commercialization of the goods, especially where the condition of the goods is changed or impaired after they have been put on the market.”

44. *See Silhouette Int’l*, [1998] 2 C.M.L.R. at 968 (opinion of Advocate-General Jacobs).

45. *See* Regulation 40/94, *supra* note 2, 1994 O.J. at 3.

46. *See id.* at 6. Article 13(1) of Regulation 40/94 provides that “[a] Community 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 trademark by the proprietor or with his consent.”

47. *See Silhouette Int’l*, [1998] 2 C.M.L.R. at 969 (opinion of Advocate-General Jacobs).

48. *See id.* at 962-68.

49. *See* Rasmussen *supra* note 22, at 174. Advocate-General Jacobs phrased the principle of international exhaustion as “whether Community law requires Member States to provide for exhaustion only when the goods have been marketed in the EEA, or whether Member States may (or perhaps even must) provide for exhaustion when the goods have been marketed in a third country.” *Silhouette Int’l*, [1998] 2 C.M.L.R. at 957 (opinion of Advocate-General Jacobs).

50. *See Silhouette Int’l*, [1998] 2 C.M.L.R. at 967 (opinion of Advocate-General Jacobs).

from non-Member States.⁵¹ Following this logic, the *Centrafarm* doctrine that provided for a principle of Community exhaustion could not be extended to third countries. The *EMI* case involved a dispute over whether an American company which had a mark registered in the United States could use that same mark in Europe.⁵² Normally this would not be a problem, except that a European company already had the same mark registered in the United Kingdom.⁵³ The Court found that prohibition on the use of a trademark from a third country did not constitute an unwarranted limitation or restriction on the free movement of goods within the EEA.⁵⁴ Furthermore, the Court determined that Articles 30 and 36 did not prevent the proprietor of a trademark in a Member State from exercising its rights under the national law of that State to prevent the sale of goods imported from outside the Community bearing that same mark.⁵⁵ Moreover, the proprietor could not prevent the manufacture in that Member State by a proprietor entitled to use the mark outside the Community.⁵⁶

Even prior to the Directive and Regulation, the principle of international exhaustion was viewed unfavorably by the Court and the Community at large.⁵⁷ Later cases in the European Court of Justice seemed to indicate a similar bent: as long as there was preservation of free movement of goods in the Community, then the principle of international exhaustion was irrelevant. In *Bristol-Myers Squibb v. Paranova A/S*, the Court held that Article 7(1) of the Directive precluded the proprietor of a trademark from preventing an importer

51. See Case 51/75, *EMI Records v. CBS United Kingdom*, 1976 E.C.R. 811, 845 ("Consequently the exercise of a trade-mark right in order to prevent the marketing of products coming from a third country under an identical mark . . . does not affect the free movement of goods between Member States and thus does not come under the prohibitions set out in Article 30 *et seq.* of the Treaty.")

52. See *id.* at 816.

53. See *id.* The Court was requested to answer the following questions by the High Court of Justice, London:

Should the provisions of the [EC Treaty] and in particular the provisions laying down the principles of Community law and the rules relating to the free movement of goods and to competition be interpreted as disentitling A from exercising its rights in the trade-mark under the appropriate national law in every Member State to prevent: (i) the sale by B in each Member State of goods bearing the mark X manufactured and marked with the mark X by B outside the Community in a territory where he is entitled to apply the mark X, or (ii) the manufacture by B in any Member State of goods bearing the mark X?

Id. at 816-17.

54. See *id.* at 866-67.

55. See *id.*

56. See *id.*

57. See *Silhouette Int'l*, [1998] 2 C.M.L.R. at 959 n.4, (opinion of Advocate-General Jacobs).

from marketing a product, which was put on the market in another Member State by the proprietor or with his consent, even if the importer repackaged the product and affixed a trademark label without the owner's consent.⁵⁸ In analyzing Article 7(2), the Court stated that the trademark owner may oppose further efforts by the importer to market the repackaged products, unless this opposition would lead to an artificial partitioning of the markets.⁵⁹ With regular products, as well as with repackaged products, an owner's exclusive right to affix a trademark at a certain point would be considered exhausted, as it would enable parallel importers to create a better market for consumers.⁶⁰ Such an admission of repackaged goods was not a derivation of Article 36 of the EC Treaty.⁶¹

The Court took a step closer to addressing the issue of international exhaustion in *Phytheron Int'l SA v. Jean Bourdon SA*.⁶² In *Phytheron*, a product was imported from a non-member state into a Member State by a parallel importer, and the transaction was not authorized by the proprietor of the trademark.⁶³ The parallel importer in the first Member State sought to sell the product to a French company, in whose country it could not be imported.⁶⁴ Apparently, the product was approved under trademark law in Germany, but not in France.⁶⁵ Since Germany and France did not approximate similar national rules regarding importation of goods, the Court had to address whether a product, which is covered by a protected trademark and lawfully acquired in one Member State by a trader of another Member State where this trademark is also marketed, could be lawfully imported from the second Member State and marketed in the first Member State.⁶⁶ To determine the appropriate standard in which

58. See Joined Cases C-427/93, C-429/93 and C-436/93, *Bristol-Myers Squibb v. Paranova A/S*, 1996 E.C.R. I-3457, I-3530, [1997] 1 C.M.L.R. 1151.

59. See *id.* at I-3541-42. The Court addressed each of the three joined cases in turn, each of which had similar fact scenarios, using essentially the same logic with respect to the partitioning of markets. See *id.*

60. See *id.* at I-3554.

61. See *id.* at I-3529.

62. See *Phytheron Int'l SA v. Jean Bourdon SA*, 1997 E.C.R. I-1729.

63. See *id.* at I-1742. *Phytheron* and *Bourdon* entered into a contract whereby *Bourdon* agreed to purchase a plant health product which was imported from Germany, but was originally from Turkey. See *id.* *Bourdon* canceled the order prior to delivery, claiming that the product could not be marketed in France until the trademark proprietor agreed to consent. See *id.* The trademark owner never consented and *Phytheron* brought action for breach of contract. See *id.*

64. See *id.*

65. See *id.*

66. See *id.* at I-1743. The issue was subject to certain conditions regarding the product: That the product was genuine, had not undergone any processing, had not undergone any alteration in packaging, and also had been approved in the first Member State. See *id.*

to frame this question, the Court had to determine whether Article 7 of the Trade Marks Directive precluded application of a national rule in France, where a trademark proprietor could prevent the importation of a product from a nonmember state.⁶⁷ Considering all these issues, the Court held that Article 7 did preclude application of such a national rule in a Member State.⁶⁸

The Court based its decision on two primary reasons.⁶⁹ First, the Court determined that Article 7 banned Member States from enacting national rules to prevent the importation or marketing of a product which had already been imported in the Community lawfully through another Member State by the trademark owner or through a third party with the trademark owner's consent.⁷⁰ The Court's opinion suggested that such a rule would threaten the free movement of goods in the internal market.⁷¹ Second, the Court reasoned that in accordance with Articles 30 and 36 of the EC Treaty, under Article 7(2) of the Directive, the exhaustion of rights doctrine did not apply if the trademark owner had legitimate reasons to oppose the further commercialization of the products.⁷² In *Phytheron*, it was clear that although the Court sought to protect the rights of the trademark owner, it also attempted to strike a balance between the scope of those rights and the desirability of a harmonized internal market.

In *Parfums Christian Dior SA v. Evora BV*, the Court addressed a similar situation involving a reseller who was not a part of the proprietor's selective distribution system.⁷³ Evora employed independent advertising to bring attention to the trademarked goods which it was selling.⁷⁴ Dior found this advertising to be inconsistent with the upscale, prestigious image it sought to convey to

67. See *Phytheron Int'l*, 1997 E.C.R. at I-1747. This rule also assumes that the product has been acquired lawfully in the other Member State by an independent parallel exporter, who has sent it to the first Member State. See *id.*

68. See *id.* at I-1749.

69. See *id.* at I-1747-48.

70. See *id.* at I-1747-48.

71. See *id.*

72. See *Phytheron Int'l*, 1997 E.C.R. at I-1748. Reasons for opposing further commercialization of the product include when the condition of the products has been severely changed or impaired since they were initially put on the market. See *id.* This situation might have occurred if the pills were no longer in the condition as they were when initially marketed by Phytheron.

73. See Case C-337/95, *Parfums Christian Dior SA v. Evora BV*, 1997 E.C.R. I-6013, I-6037.

74. See *id.* In a Christmas promotion, the defendant advertised the sale of the plaintiffs' products and depicted in advertising leaflets the packaging and bottles of some of those products. See *id.*

consumers.⁷⁵ Moreover, Dior claimed that the use of its mark by Evora was damaging to its reputation.⁷⁶ Evora responded that this type of advertising was customary for resellers in its position.⁷⁷ More importantly, Evora argued that this type of advertising did not infringe Dior's exclusive rights, and consequently, Dior could not rely on its trademark to prohibit Evora from advertising the products it marketed.⁷⁸

Before reaching its decision, the Court noted that a balance had to be struck between the interests of the proprietor and the potential damage to the trademark's reputation, on the one hand, and the reseller's interest in being able to resell the goods, on the other.⁷⁹ The Court held that a parallel importer must be able to sell his goods or else the proprietor would be able to partition the market.⁸⁰ Relying on *Bristol-Myers-Squibb*, the Court agreed that Article 7 of the Directive should be interpreted in the same light as Article 36 of the EC Treaty, relating to the free movement of goods.⁸¹ The Court reasoned that if the right to make use of advertising to draw attention to a product were not exhausted in the same way that the right to sell items is exhausted, then resale would be made more difficult and the purpose of Article 7 would be undermined.⁸² Consistent with this logic, the exhaustion of rights doctrine would hold no real power and markets could potentially be partitioned.⁸³ Accordingly, the Court interpreted Articles 5 and 7 of the Trade Marks Directive to permit a reseller to resell goods and to make liberal use of a proprietor's trademark to advertise and bring to the public's attention the existence of these goods. Previously, however, these trademarked goods could be placed in the Community only by the trademark proprietor or a third party with its consent.⁸⁴

75. *See id.*

76. *See id.* at I-6038. ("Dior claimed in particular that the use made by Evora of its trade marks was contrary to the provisions of the Uniform Benelux Law on Trade Marks in force at that time and was liable to damage their luxurious and prestigious image.").

77. *See id.* at I-6039.

78. *See Parfums Christian Dior*, 1997 E.C.R. at I-6039.

79. *See id.* at I-6047.

80. *See id.* at I-6051.

81. *See id.* at I-6013. ("[T]he purpose of the 'exhaustion of rights' rule is to prevent owners of trade marks from being allowed to partition national markets and thus facilitate the maintenance of price differences which may exist between Member States.").

82. *See id.*

83. *See Parfums Christian Dior*, 1997 E.C.R. at I-6013.

84. *See id.* From a slightly different approach, the Court also considered Article 5 in its analysis: "If the right to prohibit the use of his trade mark in relation to goods, conferred . . . under Article 5 . . . , is exhausted [pursuant to Article 7], the same applies as regards the right to

Another area of concern for trademark proprietors arose when parallel importers attempted to repackage the trademark owner's original products.⁸⁵ In *MPA Pharma GmbH v. Rhone-Poulenc Pharma GmbH*, the Court addressed a situation involving a parallel importer who bought a trademarked product in another Member State with the proprietor's consent, and subsequently repackaged the product and reattached the trademark on the importer's label.⁸⁶ The plaintiff Rhone-Poulenc owned the trademark to a drug that it marketed in Germany and sold as a prescription in packets of different sizes.⁸⁷ Pharma purchased the same drug on the Spanish market at a lower price, then repackaged it in a larger volume, and sold the product at a cheaper price than the plaintiff.⁸⁸ Rhone-Poulenc regarded the marketing of the repackaged pills as trademark infringement since it considered the way it marketed its product an acceptable prohibition or restriction under Article 36.⁸⁹ In marketing pharmaceuticals, Rhone-Poulenc considered repackaging of pills as a threat to health of humans, an exception to measures restricting trade under Article 36.⁹⁰ Pursuant to Article 36, however, a trademark proprietor could not use the protection of health and life of humans as a restriction on imports if it was used as a "disguised restriction on trade between Member States."⁹¹

In addressing whether a proprietor could use this exception to Article 36 to bar a reseller's use of the trademark, the Court looked principally to the essential function of a trademark, "which is to guarantee to the consumer or end user the identity of the trade-marked product's origin by enabling him to distinguish it without any risk of

use the trade mark for the purpose of bringing to the public's attention the further commercialization of those goods." *Id.* at I-6046.

85. *See* Case C-232/94, *MPA Pharma GmbH v. Rhone-Poulenc Pharma GmbH*, 1996 E.C.R. I-3671, I-3677.

86. *See id.*

87. *See id.*

88. *See id.* Pharma imported "Orudis retard" in parallel from Spain and marketed it in Germany. *See id.* In order to obtain packages of fifty tablets, it repackaged the product in new external packaging that it designed and that was distinct from the Rhone-Poulenc packaging. *See id.* The external packaging noted the origin of the product, its manufacturer, and Pharma's status as a parallel importer. *See id.* at I-3678.

89. *See id.* at I-3679. Rhone-Poulenc sought an injunction to prevent repackaging a pharmaceutical product which was put on the market in another Member State. *See id.*

90. *See generally*, *MPA Pharma*, 1996 E.C.R. at I-3671.

91. *Id.* at I-3681. Trademark proprietors also may not justify restrictions on trade between Member States on the basis of public morality, public policy, or public security; the protection of national treasures possessing artistic, historic or archaeological value; or the protection of industrial and commercial property. *See* EC TREATY art. 36.

confusion from products of different origin.”⁹² Since the Court found it obvious that consumers would associate the trademark with the identity of the trademarked product’s manufacturers, the Court held that Rhone-Poulenc was trying to use this exception as a restriction on trade.⁹³ Furthermore, the Court stated that Rhone Poulenc’s action constituted an artificial partitioning of the market between Member States.⁹⁴ The Court found this case of partitioning to be particularly egregious since Rhone-Poulenc marketed the product in different types of packaging throughout the EC.⁹⁵ Ultimately, the Court determined that a parallel importer could repackage a product to meet particular national rules, such as the number of pills per container.⁹⁶

Using similar logic to the *Rhone-Poulenc* case, the Court never found the failure to practice international exhaustion to be contrary to the Agreement on Trade-related aspects of Intellectual Property Rights (TRIPs).⁹⁷ For the purposes of dispute settlement, nothing in TRIPs addressed the issue of exhaustion of trademark rights.⁹⁸ Article 50(1) of TRIPs required that judicial authorities of the Contracting Parties be authorized to order provisional measures to protect the interests of proprietors of trademark rights conferred under the laws of those Parties.⁹⁹ This Article established various procedural rules applicable to applications for the adoption of such measures.¹⁰⁰ In *Hermes International v. FHT Marketing Choice*, the trademark proprietor of designer ties marketed through a selective distributorship seized ties from FHT in the belief that it was

92. *MPA Pharma*, 1996 E.C.R. at I-3683. Here, Rhone-Poulenc attempted to oppose the use of the trademark by a third party (Pharma) after the product had been repackaged. *See id.* at I-3679.

93. *See id.* at I-3691.

94. *See id.* at I-3684-85.

95. *See id.* at I-3685. Rhone-Poulenc sought to eliminate parallel importers using the Article 36 exception. *See id.* at I-3676-78.

96. *See id.* at I-3685. (“Where . . . the trade mark owner uses many different sizes of packaging in that State, the finding that one of these sizes is also marketed in the Member State of exportation is not enough to justify the conclusion that repackaging is unnecessary. Partitioning of the markets would exist if the importer were able to sell the product in only part of his market.”)

97. *See* Case C-53/96, *Hermes Int’l v. FHT Marketing Choice BV*, No. C-53/96, [1998] ECJ LEXIS 1353, at *19 (June 16, 1998). *See also* Council Decision 94/800 of 22 December 1994 Agreement on Trade-related Aspects of Intellectual Property Rights, 1994 O.J. (L 336) 1.

98. *See* *Silhouette Int’l Schmied GmbH & Co. KG v. Hartlauer Handelsgesellschaft mbH*, [1998] 2 C.M.L.R. 953, 968 (opinion of Advocate General Jacobs).

99. *See* *Hermes Int’l* [1998] ECJ LEXIS 1353, at *13-14.

100. *See id.* at *14.

marketing copies of Hermes's ties.¹⁰¹ Hermes alleged trademark infringement by FHT.¹⁰² The Court proceeded to outline a procedure which would serve a proprietor who sought to put an end to an alleged infringement of the proprietor's trademark.¹⁰³ This procedure provided that the measure was characterized under national law as an immediate provisional measure and that its adoption was required on the ground of urgency.¹⁰⁴ For the purposes of dispute settlement under the TRIPs, the Court held that nothing (subject to certain provisions) could be used to address the issue of the exhaustion of intellectual property rights.¹⁰⁵

III. NOTED DECISION

In the noted case, the European Court of Justice was asked by the Oberster Gerichtshof (the High Court of Austria) to assess whether the Oberlandesgericht Linz (an Austrian district court) properly dismissed Silhouette's cause of action against Hartlauer contending violation of Article 7(1) of the Trade Marks Directive.¹⁰⁶ Emphasizing the need to maintain the free movement of goods within the EC, the Court concluded that Member States should not be allowed to create national laws which provided for international exhaustion.¹⁰⁷ The Court also found a trademark proprietor could not use Article 7 of the Trade Marks Directive alone in seeking to obtain an injunction against a parallel importer.¹⁰⁸ An affirmative case did not rest on exhaustion of trademark cases, but on other issues such as infringement and unfair competition.¹⁰⁹ Ultimately, the Court concluded that it would be a threat to the internal market if Member States created their own laws with respect to international exhaustion.¹¹⁰

101. *See id.* at *9. On December 21, 1995, Hermes seized the ties with the consent of the President of the Arrondissementsrechtbank (district court). *See id.* Only 10 ties were in FHT's possession, while 453 were held by PTT Post BV to the order of FHT. *See id.*

102. *See id.*

103. *See id.* at *16.

104. *See Hermes Int'l*, [1998] ECJ LEXIS 1353, at *16. Other requirements of the procedure include: the opposing party summoned; the decision adopting the measure reasoned; and the decision accepted by the parties as a final resolution of their dispute. *See id.* at *16-17.

105. *See id.* at *17-24.

106. *See Case C-355/96 Silhouette Int'l Schmied GmbH & Co. KG v. Hartlauer Handelsgesellschaft GmbH*, [1998] 2 C.M.L.R. 953, 975.

107. *See id.* at 979.

108. *See id.* at 979-80.

109. *See id.* at 972.

110. *See id.* at 977.

The Court began its analysis with an examination of relevant precedent.¹¹¹ Justice Gulmann, writing for the Court based on Advocate General Jacobs's opinion, stressed that while Article 7 of the Trade Marks Directive did not provide for international exhaustion, it alone was not enough to obtain an injunction against a parallel importer.¹¹² A trademark owner must show, in addition to an Article 7(1) violation, elements of trademark infringement and unfair competition.¹¹³ National courts in Austria and other Member States applied the doctrine of international exhaustion, which the Court stressed worked counter to the principles of harmonization since not all Member States provided for such exhaustion.¹¹⁴

Specifically, the court addressed two questions.¹¹⁵ First, the Court asked whether Article 7(1) was to be interpreted such that the trademark entitled its proprietor to prohibit a third party from using the mark for goods in the EEA put on the international market under that mark in a State that is not a Contracting State.¹¹⁶ Second, the Court asked if the proprietor of the trademark could, on the basis of Article 7(1) alone, seek an order that the third party cease using the trademark for goods which have been put on the market under that mark in a state which is not a Member State.¹¹⁷ In response to the first question, the Court held that national provisions providing for international exhaustion "were contrary to Article 7(1) of [the Directive]."¹¹⁸ In response to the second question, the Court held that if a parallel importer exercised use of the principle of international exhaustion, then Article 7(1) alone "could not be interpreted as meaning that the proprietor of a trademark was entitled . . . to obtain an order restraining a third party from using his trade mark."¹¹⁹ Thus,

111. See *Silhouette Int'l*, [1998] 2 C.M.L.R. at 973. By order of October 15, 1996, the Oberster Gerichtshof referred the matter to the Court for a preliminary ruling under Article 177 of the EC Treaty. See *id.*

112. See *id.* at 979-80. Before addressing the international exhaustion of rights, the Court noted the relevant statutes, including Article 7 of the Directive and the EEA Agreement. See *id.* at 973.

113. See *id.* at 978-79.

114. See *id.* at 976-77. While Austrian courts provided for international exhaustion, the Oberster Gerichtshof stated that the explanatory memorandum to the Austrian law implementing Article 7 indicated that it was intended to leave the resolution of the question of the validity of international exhaustion to judicial decision. See *id.* at 975.

115. See *id.* at 975. The questions were referred to the Court by the Oberster Gerichtshof. See *id.*

116. See *Silhouette Int'l*, [1998] 2 C.M.L.R. at 975.

117. See *id.*

118. *Id.* at 979. The Directive as amended by the EEA Agreement is still contrary to rules providing for international exhaustion. See *id.* at 977-78.

119. *Id.*

Hartlauer violated Article 7(1) by exercising international exhaustion rights, but that alone was not enough to enable Silhouette to obtain an injunction enjoining Hartlauer from importing the spectacles.¹²⁰

The Court then addressed the parties' main arguments.¹²¹ Silhouette claimed that it had not exhausted its trademark rights under the Directive, as those rights were exhausted only when the products had been put on the market in the EEA by the proprietor or with his consent.¹²² Basing its claim on various aspects of EU law that had been codified into Austrian law, Silhouette argued that Hartlauer had no right to offer spectacles or spectacle frames for sale in Austria under its trademark.¹²³ Hartlauer, in turn, contended that the action should be dismissed since Silhouette had not sold the frames subject to any prohibition of reimportation into the Community.¹²⁴ The Court ultimately concluded that Silhouette's argument was legally correct; but without at least a showing of trademark infringement or unfair competition, granting an injunction on the basis of Article 7(1) would not be feasible since a Directive is not binding on individuals.¹²⁵

The Court employed logical analysis to determine that international exhaustion was contrary to the provisions of the EC Treaty and the Trade Marks Directive.¹²⁶ Relying on the provisions of Article 7(1), the Court refuted Silhouette's contention that the Directive applied only to Community exhaustion.¹²⁷ Next, the Court rejected Hartlauer's argument that the Directive left the Member States free to decide as a matter of national law whether to provide for international exhaustion, since the Directive itself did not resolve this question.¹²⁸ The Court affirmed that rather than providing for differentiation of national laws, the Directive provided for

120. *See id.* at 977, 979.

121. *See Silhouette Int'l*, [1998] 2 C.M.L.R. at 976.

122. *See id.* at 960.

123. *See id.* As noted earlier, the aspects of Austrian law under dispute include protection of trademarks and unfair competition. *See id.*

124. *See id.*

125. *See id.* at 977. The Court noted: "[I]t is to be remembered, first, that, according to settled case-law of the Court, a directive cannot of itself impose obligations on an individual and cannot therefore be relied upon as such against an individual." *Id.* at 979.

126. *See Silhouette Int'l*, [1998] 2 C.M.L.R. at 975-80. The Court first identified when the exclusive rights granted by a trademark are exhausted, subject to the condition that goods have been put on the market by the proprietor or with his consent. *See id.* at 975-76.

127. *See id.* at 976-77. No argument was presented to the Court that the Directive provides for international exhaustion. *See id.* at 976.

128. *See id.* Hartlauer argued that: "Article 7 does not comprehensively resolve the question of exhaustion of rights conferred by the trade mark, thus leaving it open to the Member States to adopt rules on exhaustion going further than those explicitly laid down in Article 7 of the Directive." *Id.*

harmonization of rules of central importance.¹²⁹ This push for harmonization was evident in the first and ninth recitals to the preamble of the Directive.¹³⁰ The Court went further in noting that the Directive “must be construed as embodying a complete harmonization of the rules relating to the rights conferred by a trade mark.”¹³¹

Finally, the Court rejected Hartlauer’s claim that Member States could provide for international exhaustion rights.¹³² In accordance with Article 5 of the Directive, the Court found that Member States had the option to grant more extensive protection to trademarks with a reputation.¹³³ As a result, the Court noted that the Directive could not be interpreted as leaving the option to Member States to provide in their domestic law for international exhaustion.¹³⁴ If the option were left open, the Court observed that some Member States would provide for exhaustion and others would not, which inevitably would create barriers to the free movement of goods and the freedom to provide services.¹³⁵ Ultimately, the Court concluded that the EC was better suited to confront these trademark issues, as it could always extend the exhaustion provided for in Article 7 to products put on the market in nonmember countries.¹³⁶

IV. ANALYSIS AND CRITICISM

The noted case rejected the notion of individual Member States independently creating national laws which provided for the doctrine of international exhaustion.¹³⁷ While the Court effectively prohibited Member States from practicing international exhaustion, its rationale was not based upon a fundamental opposition to the doctrine. Its chief reason for the decision was not based on a desire to protect trademark proprietors, but to preserve the internal market of the

129. *See id.* at 976.

130. *Id.* at 976-77. The first recital of the Directive’s preamble states that since the trademark laws of each Member State differ, this may impede free movement; consequently, it is necessary for the functioning of the internal market to approximate the laws of Member States. *See id.* at 976. The ninth recital states that it is fundamental for the maintenance of the common internal market that trademarks enjoy the same protection under all legal systems, but that Member States may still grant extensive protection to those trademarks with a reputation. *See id.* at 976-77.

131. *Silhouette Int’l*, [1998] 2 C.M.L.R. at 977.

132. *See id.*

133. *See id.* The ninth recital of the preamble actually refers to Article 5(2). *See id.*

134. *See id.*

135. *See id.*

136. *See Silhouette Int’l*, [1998] 2 C.M.L.R. at 977. If the EC were to act in this sphere, then there would be considerably less threat to harmonization.

137. *See id.* at 979.

EEA.¹³⁸ A severe setback to the goals of the Community would occur if each Member State approximated its own trademark laws.¹³⁹ If, however, the European Commission were to adopt a regulation making it legal for importers to purchase their trademarked goods from abroad, then the Court very likely would not oppose this measure since it would create uniform standards throughout the Community.¹⁴⁰ In addition, the Court also seemed to recognize that the bar for determining violation of international exhaustion rights should be high.¹⁴¹ A trademark proprietor needed to use more than Article 7 alone to obtain an injunction, making this a weakened decision. To prove violation of trademark rights, the proprietor must show, in addition to a violation of the exhaustion principle, trademark infringement and unfair competition on the part of the importer.¹⁴²

The Court took a narrow view of the Trade Mark Directive, but was consistent with the *Bristol-Myers Squibb* decision in seeking to preserve the functioning of the internal market above all other considerations.¹⁴³ Still, the Court seemed to recognize that international exhaustion was important to the EC if it hoped to compete successfully with the rest of the world.¹⁴⁴

The policy considerations underlying this decision were important.¹⁴⁵ To some commentators, the exclusion of international exhaustion appeared protectionist and harmful to the functionings of the internal market.¹⁴⁶ On the other hand, others have expressed concern about the possible lack of reciprocity if the Community unilaterally were to provide for international exhaustion.¹⁴⁷ International exhaustion could benefit exporters in third countries which did not recognize this principle, where their markets could remain protected and they could continue to practice monopolistic price discrimination.¹⁴⁸ If, however, a third country already

138. *See id.* at 977. The Court left the option to the Community authorities to extend the doctrine of exhaustion to third countries. *See id.*

139. *See id.*

140. *See id.*

141. *See Silhouette Int'l*, ([1998]) 2 C.M.L.R. at 977.

142. *See id.* at 978-79.

143. *See id.*

144. *See id.* (Advocate General Jacobs opining that "[i]t seems clear that international exhaustion is one of the matters which most directly affects the functioning of the internal market and which the Directive therefore seeks to harmonise.").

145. *See id.*

146. *See Silhouette Int'l*, ([1998]) 2 C.M.L.R. at 965 (opinion of Advocate General Jacobs).

147. *See id.* at 967 (opinion of Advocate General Jacobs).

148. *See Rasmussen, supra* note 22, at 177.

recognized international exhaustion towards the EEA, then this decision set a troubling precedent and functioned as a barrier to free trade.¹⁴⁹ The principle of exhaustion has worked best when it has been mutual between nations, as in the EC.¹⁵⁰

One way to analyze policy implications is through legislative history and intent. The original proposal of the Commission would have imposed international exhaustion, but due to intense pressure from industry and large firms, the Commission was forced to limit this proposal to Community exhaustion.¹⁵¹ Many analysts have disagreed with the position taken by the Commission and supported by Advocate General Jacobs in construing the Treaty narrowly.¹⁵² The position taken by Jacobs was that Article 7 of the Trade Mark Directive should not vary too much from Article 36 of the EC Treaty.¹⁵³ In addition, Jacobs opposed the notion that the lack of international exhaustion was protectionist, arguing that the notion was more complex in that the doctrine might not be reciprocal.¹⁵⁴

Frederick M. Abbott and D.W. Feer Verkade believed that Jacobs' opinion avoids important policy questions, which the Court should have addressed in its decision.¹⁵⁵ Regardless of the EU policy on international exhaustion, individual Member States would still need to maintain customs procedures and other administrative and judicial remedies with respect to trademarks and other international goods.¹⁵⁶ Furthermore, the authors noted, a uniform EU rule on international exhaustion did not eliminate the need for Member States and the European Union to provide protection for trademark proprietors engaged in international trade.¹⁵⁷ A uniform rule would not result in some Member States having price advantages over others due to the influx of parallel imports.¹⁵⁸ If one Member State allowed for international exhaustion and production could take place at a lower cost in that Member State, then a Member State which did not

149. *See id.*

150. *See id.*

151. *See* Frederick M. Abbott and D.W. Feer Verkade, *The Silhouette of a Trojan Horse: Reflections on Advocate General Jacobs' Opinion in Silhouette v. Hartlauer*, Sixth Annual Conference on International Intellectual Property Law & Policy 22, (Apr. 16-17, 1998).

152. *See Korah, supra* note 14, at 14.

153. *See id.* at 13.

154. *See id.* at 14.

155. *See* Abbott & Verkade, *supra* note 151, at 6. "AG Jacobs says that the subject of the international exhaustion of marks is of the greatest importance to the functioning of the internal market." *Id.*

156. *See id.* at 8.

157. *See id.*

158. *See id.* at 9.

provide for international exhaustion would likely change its policy to enable it to penetrate global markets.¹⁵⁹ The authors ultimately concluded that the suggestion by Jacobs that this issue was political in nature was true; thus, the Court “should leave it as a political matter by leaving to the Member States the freedom to choose . . . the [European Court of Justice] should not make it for all of them on the very weak record before it.”¹⁶⁰

As one of the most fundamental limitations on intellectual property rights, the influence of international exhaustion effects the entire global economy.¹⁶¹ If all nations were to allow this principle, then parallel importers would be able to undercut trademark proprietors, producing lower consumer prices around the world. As the EC determines the future course of international exhaustion, perhaps it should consider the policy of the United States on the same issue.

Unlike the European Court, the U.S. Supreme Court specifically in established certain conditions under which parallel imports would be allowed from abroad.¹⁶² In *K-Mart Corp. v. Cartier, Inc.*, the Supreme Court addressed a similar factual circumstance as the one faced by the European Court of Justice in *Silhouette*.¹⁶³ The Supreme Court was left to decide whether gray market goods should be permitted to be imported in the United States from other countries.¹⁶⁴ Gray market goods in the United States were analogous to parallel imports in the European Union.¹⁶⁵ A gray market good was manufactured abroad, but bore a valid U.S. trademark, and was

159. *See id.*

160. *See* Abbott & Verkade, *supra* note 151, at 11.

161. *See* Darren E. Donnelly, Comment, *Parallel Trade and International Harmonization of the Exhaustion of Rights Doctrine*, 13 SANTA CLARA COMPUTER & HIGH TECH L.J. 445, 447 (1997).

162. *See* *K-Mart Corp. v. Cartier, Inc.*, 486 U.S. 281, 293-294 (1988).

163. *See id.*

164. *See id.* at 285.

165. *See id.* at 285-88. The issue in *K-Mart* was whether the Secretary of the Treasury's regulation permitting the importation of certain gray market goods was a reasonable interpretation of Section 526 of the Tariff Act of 1930. *See id.* at 285. Section 526 prohibits importing

into the United States any merchandise of foreign manufacture if such merchandise . . . bears a trademark owned by a citizen of, or by a corporation or association created or organized within, the United States, and registered in the Patent and Trademark Office by a person domiciled in the United States . . . , unless written consent of the owner of such trademark is produced at the time of making entry.

19 U.S.C. § 1526(a) (1995).

imported without the consent of the U.S. trademark holder.¹⁶⁶ Since the trademark was genuine, a gray market good did not necessarily violate the rights of the trademark owner.¹⁶⁷

In that holding, Justice Kennedy observed that gray market goods and the principle of international exhaustion were not prohibited under certain circumstances.¹⁶⁸ These circumstances are defined in the Customs Service regulation implementing section 526 of the Tariff Act of 1930.¹⁶⁹ Known as the “common-control” exception, it permitted the entry of gray goods manufactured abroad by the trademark owner or its affiliate.¹⁷⁰ The Supreme Court held that the regulation was consistent with section 526 in its exemption from the importation ban goods that are manufactured abroad by the “same person” who held the U.S. trademark, or by a person who was “subject to common . . . control” with the U.S. trademark holder.¹⁷¹

The European Court of Justice would have been well advised to follow the *K-Mart* decision. Not only did the Supreme Court address the validity of Customs regulations, but it left considerable room for parallel imports to continue under section 26 of the Tariff Act and section 42 of the Lanham Act.¹⁷² Subsequent case law has established the rule that legal parallel imports cannot be stopped unless they are “materially different” from those authorized to be sold in the United States.¹⁷³ While U.S. trademark owners may complain that a

166. See *K-Mart*, 486 U.S. at 285. The gray market may arise in any of three contexts. See *id.* at 286. The first and most common context occurs when a domestic firm purchases the rights to register and use as a U.S. trademark a foreign firm’s trademark. See *id.* The second context occurs when a domestic firm registers the U.S. trademark for goods manufactured abroad by an affiliated manufacturer. See *id.* at 286-87. The third context occurs when the owner of the U.S. trademark authorizes a foreign manufacturer to use it. See *id.* at 287.

167. See *id.* at 283-84.

168. See *id.* at 288-89.

169. See *id.*

170. See *id.* at 289. The regulation provides as follows:

(c) Restrictions not applicable. The restrictions . . . do not apply to imported articles when: (1) Both the foreign and the U.S. trademark or trade name are owned by the same person or business entity; [or] (2) The foreign and domestic trademark or trade name owners are parent and subsidiary companies or are otherwise subject to common ownership or control

Id. (quoting 19 C.F.R. § 133.21 (1987)).

171. *K-Mart*, 486 U.S. at 294. The Court upheld the validity of sale of gray market goods in the second context and struck down the third context, so that a foreign manufacturer licensed by the domestic owner of the trademark could not sell the goods in the United States.

172. Section 42 of the Lanham Act provides that U.S. trademark rights will not be exhausted by sales of products bearing those marks that differ in ways material to consumers from those sold in the United States. See 15 U.S.C. § 1124 (1998).

173. See *Grupo Gamesa S.A. De C.V. v. Dulceria El Molino, Inc.*, 39 U.S.P.Q.2d 1531, 1533 (C.D. Cal. 1996) (holding cookies and crackers materially different where different marketing and quality control procedures followed, gray market goods did not indicate that U.S.

“materially different” standard provided a defective shield against gray market goods and defeated the purpose of the enforcement of trademark rights, consumers will ultimately benefit through increased interbrand competition. Interbrand competition, in addition to reducing vertical restraints through the increased number of distributors for a certain product, prevents the trademark proprietor from having a monopoly on the market and ultimately leads to reduced consumer prices.¹⁷⁴

Opponents of gray goods and parallel imports fear that international exhaustion will destroy the purpose of trademark protection.¹⁷⁵ Trademark protection, they argue, provides incentives to develop new products by preventing consumer confusion and by preserving the trademark owner’s ability to obtain economic rewards for development of the product and in establishing the goodwill of the mark.¹⁷⁶ While this argument is certainly valid, parallel imports are healthy for competition and necessary for the protection of consumers. When markets are restricted and interbrand competition is eliminated, consumers literally pay the price, in terms of higher cost for goods and decreased selection in the marketplace.¹⁷⁷ Indeed, consumers and small distributors will suffer most from the lack of international exhaustion as big businesses may continue to control the market.¹⁷⁸ The elimination of parallel imports from the European market eliminates a consumer base and keeps prices high.¹⁷⁹ Without gray market goods, parallel importers are severely limited by what they can import.¹⁸⁰ If trademark proprietors fear parallel imports as a threat to their reputation and goodwill, then they can eliminate the

licensee owned U.S. mark, enriched flour not used as per regulation, and labels did not bear standard nutritional information); *Mavic Inc., v. Sinclair Imports, Inc.*, Nos. Civ. A.93-2444, Civ.A. 93-2448, WL 7703, at *3-6 (E.D. Pa. Jan. 12, 1994) (holding price, warranty and packaging differences not material for bicycle components, injunction ordered that parallel goods have adapters placed on them to conform to genuine goods rather than block importation entirely); *Helene Curtis, Inc. v. National Wholesale Liquidators, Inc.*, 890 F. Supp. 152, 159-60 (E.D.N.Y. 1995) (holding gray market product differed materially from authorized product because it contained ingredients that did not meet New York and California state requirements).

174. See Hugh C. Hansen, *Gray Market Goods: A Lighter Shade of Black*, 13 BROOK. INT’LL.J. 249, 259 (1987).

175. See generally J. THOMAS MCCARTHY, 1 TRADEMARKS AND UNFAIR COMPETITION § 2:1 (2d ed. 1984). When selling a product, a trademark proprietor seeks to exploit the mark as indicative of the value of the product. See *id.*

176. See generally *id.*

177. See Hansen, *supra* note 174, at 259.

178. See generally Nicholas Shea, *Does the First Trade Marks Directive Allow International Exhaustion of Rights?*, 10 EUR. INTELL. PROP. REV. 463 (1995).

179. See Hansen, *supra* note 174, at 251.

180. See *id.*

market by pricing goods uniformly throughout the world.¹⁸¹ Until such time, however, parallel imports should be allowed as a manifestation of the free market.

Trademark proprietors also argue that parallel importers receive a free ride from the goodwill generated by the domestic or Community manufacturer.¹⁸² This argument assumes that the domestic owner bears all costs for product development, advertising, and service. Clearly, this is not the case as *Parfums Christian Dior* adequately demonstrates.¹⁸³ As a result, the reseller, and not the trademark owner, generally bears these costs, as importers often advertise the goods on their own.¹⁸⁴

In applying the doctrine established by the *K-Mart* decision to the *Silhouette* case, Hartlauer probably would not have been enjoined from distributing the spectacles in the European Union. *Silhouette* manufactured the goods in question and there was no “material difference” between these goods and other goods which *Silhouette* produced. Although Hartlauer was not actually enjoined from distributing the spectacles based on the European Court of Justice’s decision, its holding was weak and inconclusive.

Understandably, the Court’s primary objective was to ensure the continuance of the internal market, but it missed a crucial opportunity to clarify and harmonize EU law with respect to international exhaustion. Deference to the discretion of both the Council and Commission was likely a strong consideration in the Court’s judgment. The Court probably anticipated that either one or both of these bodies would address this important issue in the near future. The U.S. Supreme Court, however, realizing that Congress could fall under great political pressure from domestic manufacturers to outlaw gray market goods, left great latitude to foreign manufacturers to create interbrand competition. Unfortunately for consumers, trademark proprietors within the EEA, and parallel importers, the Community’s policy regarding international exhaustion remains inconclusive.

181. *Legislation to Amend the Lanham Trademark Act Regarding Gray Market Goods: Hearings on S.626 Before the Subcomm. on Patents, Copyrights and Trademarks of the Senate Committee on the Judiciary*, 101st Cong., 2d Sess. 11-23 (1990) (oral and written statement of Hon. Warren Rudman, a U.S. Senator from the State of New Hampshire).

182. *See id.*

183. *See id.*

184. *See id.*

V. CONCLUSION

The European Court of Justice's rejection of leaving to Member States the discretion of whether to enforce international exhaustion is consistent with other Court decisions promoting free trade. Maintenance of the internal market is still the most important consideration as the European Union seeks to compete in the global economy. Any impediments to the internal Community market, including inconsistent trademark laws, will hurt Europe in the long term. Despite the Court's adherence to such principles, the noted decision should have been more forceful regarding the necessity of the European Commission to adopt a policy of international exhaustion. Uniform policies are important, but so are policies which reduce vertical restraints, bring a competitive aspect into the economy, and keep consumer prices low. While preserving the internal market, the Court is too cautious in failing to further international exhaustion.

Many commentators expected that *Silhouette* would settle the issues left unresolved by *Phytheron* and other cases involving the principle of exhaustion.¹⁸⁵ While the Court determined that Member States could not individually provide for international exhaustion, it did not use this decision as a bar to the importation of goods.¹⁸⁶ Perhaps the Court would have done better had it enabled Member States to establish national laws providing for international exhaustion. Other Member States which do not provide for exhaustion most likely would have changed course once they noticed its benefits. Instead, the Court chose the vague confines of preserving the internal market by preventing the discretion of the Member States.¹⁸⁷ The noted case, while attempting to provide for the principles of harmonization over the expansion of international trade, only confuses the issue. A trademark proprietor must provide more

185. See, e.g., Eric Gippini-Fournier, Comment, Case C-352/95, *Phytheron Int'l v. Jean Bourdon, SA*, *Judgment of the Court (fifth chamber) of 20 March 1997*, [1997] E.C.R. I-1729, 35 COMMON MKT. L. REV. 947, 965 n.21 (1998).

186. See Case C-355/96, *Int'l Schmied GmbH & Co. KG Silhouette v. Hartlauer Handelsgesellschaft mbH*, [1998] 2 C.M.L.R. 953, 979.

187. See Gippini-Fournier, *supra* note 185, at 963. The author commented:

This interpretation [will] undoubtedly have the advantages of uniformity; to a certain extent, such a uniform solution might be in line with the notion of a common commercial policy towards third countries; however, one would then have to consider carefully whether the Community has competence to harmonize the area to such an extent

Id.

than a violation of Article 7 of the Directive to obtain an injunction.¹⁸⁸ What exactly qualifies as “more” remains to be seen and will surely be the source of future litigation.

William J. Littman

188. *See id.*