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Copyright vs. Exhaustion of Rights: Application to Used Licenses and Downloads

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The Court of Justice of the European Union's recent decision of July 3, 2012 applying the exhaustion of rights rules to the sale of used licenses for downloaded software has significant implications for the video gaming industry, where a large second hand market for games already exists. One of the take-aways from the decision is that contractual clauses will not be sufficient to avoid or overcome the right for the buyer to resell the license in the downloaded game. However, as always, the devil is in the details. Some of the more salient details in the European Court of Justice's decision are discussed below and should be taken into consideration when drafting and structuring the terms of a license agreement, using technical rights management features in video games, etc.

The case which gave rise to the decision ("CJEU") pitted UsedSoft GmbH ("UsedSoft") against Oracle International Corp. ("Oracle") and involved the marketing by UsedSoft of used licenses for Oracle computer programs.

Oracle distributes 85% of its software via download. The user's right to use the program is governed by a license agreement which provides in relevant part that:

"With the payment for services you receive, exclusively for your internal business purposes, for an unlimited period a non-exclusive non-transferable user right free of charge for everything that Oracle develops and makes available to you on the basis of this agreement" (emphasis added).

UsedSoft markets used software licenses, including licenses acquired from Oracle customers. Oracle's used licenses are sold 'current' in the sense that the maintenance agreement entered into between the original license holder and Oracle is still in force. UsedSoft's customers can either (i) download a copy of the program directly from Oracle's website after acquiring a used license, when they are not yet in possession of the software, or (ii) purchase further licenses for additional users by copying the program to the work stations of those users when they already have that software.

Oracle filed a complaint against UsedSoft in Germany seeking a court order for UsedSoft to cease these practices. The Bundesgerichtshof (German Supreme Court) referred the CJEU for a preliminary ruling regarding the interpretation of Directive 2009/24/EC on the legal protection of computer programs.

At the outset, and for a better understanding of the case, it is necessary to note that Article 4(1) of Directive 2009/24/EC notably provides that "the exclusive rights of the right holder (...) shall include the right to do or to authorize:(a) the permanent or temporary reproduction of a computer program by any means and in any form, in part or in whole; in so far as loading, displaying, running, transmission or storage of the computer program necessitate such reproduction, such acts shall be subject to authorization by the right holder". Article 5 (1)providesexceptions to the restricted acts to the extent that "in the absence of specific contractual provisions, the acts referred to in points (a) (...) of Article 4(1) shall not require authorization by the right holder where they are necessary for the use of the computer program by the lawful acquirer in accordance with its intended purpose, including for error correction" (emphasis added).

Article 4(2) also provides that the "the first sale in the Community of a copy of a program by the right holder or with his consent shall exhaust the distribution right within the Community of that copy" (emphasis added). Under the exhaustion rule, the intellectual property right holder who has put goods into circulation in the territory of a Member State loses the right to rely on his or her exploitation monopoly in order to oppose their importation into another Member State.

In this context, UsedSoft argued that the exhaustion rule shall apply to online software transfers, whereas Oracle countered that the distribution right can be exhausted only where the ownership of a tangible object is transferred, which rules out the intangible operation of downloading.

In this matter, the CJEU held that:

1. "(...) The right of distribution of a copy of a computer program is exhausted if the copyright holder who has authorized, even free of charge, the downloading of that copy from the internet onto a data carrier has also conferred, in return for payment of a fee intended to enable him to obtain a remuneration corresponding to the economic value of the copy of the work of which he is the proprietor, a right to use that copy for an unlimited period".
2. "(...) In the event of the resale of a user license entailing the resale of a copy of a computer program downloaded from the copyright holder's website, that license having originally been granted by that right holder to the first acquirer for an unlimited period in return for payment of a fee intended to enable the right holder to obtain a remuneration corresponding to the economic value of that copy of his work, the second acquirer of the license, as well as any subsequent acquirer of it, will be able to rely on the exhaustion of the distribution right (...) and hence be regarded as lawful acquirers of a copy of a computer program side effects to clomid (...) and benefit from the right of reproduction provided for in that provision (emphasis added).

To reach these findings, the CJEU notably noted in relevant part that limiting the application of the principle of the exhaustion of the distribution right "solely to copies of computer programs that are sold on a material medium would allow the copyright holder to control the resale of copies downloaded from the internet and to demand further remuneration on the occasion of each new sale, even though the first sale of the copy had already enabled the right holder to obtain an appropriate remuneration" (paragraph 63). Such a restriction of the resale of copies of computer programs downloaded from the internet would indeed go beyond the necessary measures to safeguard the specific subject-matter of the intellectual property.

In this context, the CJEU justifiably pointed out that the sale of a computer program on CD-ROM or DVD and the sale of a program by downloading from the internet are similar from an economic point of view since the on-line

transmission method is the functional equivalent of the supply of a material medium (paragraph 61).

The CJEU specified in addition that the exhaustion of the distribution right extends to the copy of the computer program sold as corrected and updated by the copyright holder.

However, in order to avoid an infringement of the exclusive reproduction right of a computer program under Article 4(1)(a) of Directive 2009/24/EC, the CJEU ruled that an original acquirer who resells a tangible or intangible copy of a computer program for which the copyright holder's right of distribution is exhausted must make his or her own copy unusable at the time of its resale (paragraph 70).

In this context, and as pointed out by Oracle, ascertaining whether such a copy has been made unusable at the time of its resale may be difficult. On this point, the CJEU again compares computer programs downloaded from the internet and computer programs on a material medium such as a CD-ROM or DVDfor which an author has to face the same problem,to the extent that he or she cannot realistically verify and/or enforce that the original acquirer has not made copies of the program. To address this problem, the CJEU expressly held that it is permissible for a distributor to make use of digital rights management.

Finally, insofar as the copyright holder cannot oppose the resale of a copy of a computer program for which his or her distribution right is exhausted, notwithstanding the existence of contractual terms prohibiting a further transfer, the CJEU concludes that a second acquirer of that copy and any subsequent acquirer are "lawful acquirers". Consequently, the new acquirer would in which event be able to download onto his or her computer the copy sold to him of her by the first acquirer. Such a download must according to the CJEU be regarded as a reproduction of a computer program that is "necessary for the use of the computer program" in accordance with its intended purpose within the meaning of the Directive.

In the present matter, the CJEU only partially followed the opinion of the Advocate General, who considered that "the right to distribute the copy of a computer program is exhausted if the right holder, who allowed that copy to be downloaded from the internet to a data carrier, also granted, for consideration, a right to use that copy for an unlimited period of time", but that "in the event of resale of the right to use the copy of a computer program, the second acquirer cannot rely on exhaustion of the right to distribute that copy in order to reproduce the program by creating a new copy, even if the first acquirer has erased his copy or no longer uses it" (emphasis added).

As the Advocate General himself wrote in his opinion, his position would have blocked the effects of the exhaustion of rights.

The CJEU also rejected the argument put forward by Oracle and the Ireland, French and Italian Governments according to which the concept of "lawful acquirer" only relates to an acquirer who is authorized under a license agreement concluded directly with the copyright holder, to use the computer program (paragraphs 82 and 83).

For now it seems that the exhaustion rule would not apply if the software is offered as a service rather than a product, since the CJEU differentiates between the product as such and services offered in respect of that product.

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