

COMMENTS

When is Copyright Exhausted by a Software Licence? *UsedSoft v Oracle*

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☞ Distribution right; EU law; Exhaustion of rights; Licensing agreements; Resale; Software

The Grand Chamber of the European Court of Justice held in UsedSoft GmbH v Oracle International Corp (C-128/11) (July 3 2012) that a software licence which is granted for an unlimited period in return for a fee constitutes a sale of that copy of the software program, exhausting the copyright owner's right to object to the resale of that particular copy. This applies whether the software is sold on a physical medium or downloaded. However, where the licence covers multiple copies the licensee is not permitted to divide the licence and resell the rights to individual copies. This judgment brings a degree of clarity to this area of law on the specific facts of this case, but more fundamentally demonstrates a commitment by the ECJ to ensure that technological change does not reintroduce territorial restrictions in Europe.

Facts

Oracle develops and markets computer software. In the EU, computer software is protected by copyright as a literary work under Directive 2009/24.¹

Article 4 of that Directive reads:

- “1. Subject to the provisions of Articles 5 and 6, the exclusive rights of the rightholder within the meaning of Article 2 shall include the right to do or to authorise:

(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 authorisation by the rightholder;

(b) the translation, adaptation, arrangement and any other alteration of a computer program and the reproduction of the results thereof, without prejudice to the rights of the person who alters the program;

(c) any form of distribution to the public, including the rental, of the original computer program or of copies thereof.

2. The first sale in the Community of a copy of a program by the rightholder or with his consent shall exhaust the distribution right within the Community of that copy, with the exception of the right to control further rental of the program or a copy thereof.”

Article 5 of the Directive reads:

“In the absence of specific contractual provisions, the acts referred to in points (a) and (b) of Article 4(1) shall not require authorisation by the rightholder 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.”

The software at issue in this case was “client-server” software, which was stored on a customer’s server and accessed by users from their individual workstations. In most cases (85 per cent of the time), customers downloaded the software on to their server free of charge from Oracle’s website, although in a minority of cases the software was distributed on physical media (CDs).

In order to use the software, the customer also had to purchase a licence from Oracle to cover the required number of users. The licences were offered in bundles of 25 users for a single fee. As the ECJ noted, a customer requiring licences for 27 users would have to buy two licences (which would cover up to 50 users). The licences stated:

“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.”

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¹ Directive 2009/24 [2009] OJ L111/16. The Directive codifies Directive 91/250 [1991] OJ L122/42.

UsedSoft purchased and resold used licences or part of them (in the example above, for the other 23 users), including an “Oracle Special Offer” in October 2005. Unsurprisingly, Oracle objected to that practice and brought proceedings for copyright infringement.

In response, UsedSoft claimed that Oracle’s copyright had been exhausted. UsedSoft sought to rely on the *OEM-Version* judgment of the German Federal Court of Justice.² In that case, the court had found that copyright was exhausted where software was distributed on physical media, notwithstanding the breach of any limitations in the distribution agreement (the software there was an original equipment manufacturer (OEM) version which was only to be supplied with computer systems). UsedSoft said the same approach must apply where software is distributed by downloading.

That exhaustion argument was rejected by the Munich courts at first and second instance both in interim proceedings³ and the main proceedings.⁴ The Düsseldorf and Frankfurt courts followed the Munich courts,⁵ although the Hamburg District Court accepted UsedSoft’s argument in an unfair competition case brought by a Microsoft dealer.⁶ The issue has also arisen more broadly: Adobe has taken action against UsedSoft before the Frankfurt courts⁷ and in Switzerland,⁸ while similar issues have also been fought in France and the Netherlands.⁹

In the case brought by Oracle in the Munich courts, UsedSoft appealed on a point of law to the German Federal Court of Justice, which referred the following questions to the ECJ on February 3, 2011:

- “1. Is the person who can rely on exhaustion of the right to distribute a copy of a computer program a ‘lawful acquirer’ within the meaning of Article 5(1) of Directive 2009/24?
2. If the reply to the first question is in the affirmative: is the right to distribute a copy of a computer program exhausted in accordance with the first half-sentence of Article 4(2) of Directive 2009/24 when the acquirer has made the copy with the rightholder’s consent by downloading the program from the internet onto a data carrier?
3. If the reply to the second question is also in the affirmative: can a person who has acquired a ‘used’ software licence for

generating a program copy as ‘lawful acquirer’ under Article 5(1) and the first half-sentence of Article 4(2) of Directive 2009/24 also rely on exhaustion of the right to distribute the copy of the computer program made by the first acquirer with the rightholder’s consent by downloading the program from the internet onto a data carrier if the first acquirer has erased his program copy or no longer uses it?”

The case was allocated to the Grand Chamber of the ECJ (indicating that the case was regarded as particularly complex or important) and was heard on March 6, 2012. Oracle’s position was supported by the European Commission and by Spain, France, Ireland and Italy.

Opinion of Advocate General Bot

A.G. Bot’s Opinion was delivered on April 24, 2012. He said that the second question referred (is there exhaustion?) should be answered first, which he did by considering the concepts of “sale” and then “distribution right” in art.4(2), before considering together the first and third questions.

First, he indicated that “sale of a copy of a program” in art.4(2) was an autonomous concept of EU law which had to be given a uniform interpretation and not be a matter of (varying) national laws. He rejected Oracle’s argument that the distinction drawn in that article should be between sale and licence but rather said that it should be between sale and rental. Recital 12 of the Directive defined rental as “the making available for use, for a limited period of time and for profit-making purposes, of a computer program or a copy thereof”. That supposed the payment of a periodic fee and ultimate return of the copy of the computer program. By contrast, therefore, he said that sale should be construed broadly to cover transactions (whether described as a licence or otherwise) which involve the transfer of ownership of a copy of the computer program, for an unlimited period of time, in return for a one-off or lump sum payment.

Secondly, he considered Oracle’s argument that the “distribution right” which was exhausted was limited to the distribution of a program incorporated in a tangible article such as a CD, based (inter alia) on Recitals 28 and 29 of the Directive. Again, he rejected that argument on various grounds, including the basis that art.4(2) must be

² Case I ZR 244/97 *OEM-Version* [2001] GRUR 153.

³ Case 7 O 23237/05 (Munich District Court, January 19, 2006); Case 6 U 1818/06 Munich Higher Regional Court, August 3, 2006).

⁴ Case 7 O 7061/06 (Munich District Court, March 15, 2007); Case 6 U 2759/07 (Munich Higher Regional Court, July 3, 2008). See also Case 30 O 8684/07 (Munich District Court, November 27, 2007).

⁵ Case I-20 U 247/08 (Düsseldorf Higher Regional Court, June 29, 2009); Case 11 W 15/09 (Frankfurt Higher Regional Court, May 12, 2009).

⁶ Case 315 O 343/06 (Hamburg District Court, June 29, 2006), upheld on the different ground that the legal uncertainty was made clear (Hamburg Higher Regional Court, February 7, 2007).

⁷ Case 2-06 O 556/09 (Frankfurt District Court, November 25, 2009 and January 6, 2010); Case 11 U 13/10 (Frankfurt Higher Regional Court, June 22, 2010); Case 2-06 O 428/10 (Frankfurt District Court, April 27, 2011).

⁸ Case ES 2010 822 (Zug Cantonal Court, May 2011).

⁹ For commentary, see T. Heydn et al., “Dealing with Used Software: Ingenious Business Model or Piracy?” (2006) 1(3) W.C.R.R. 29; J. Pohle, “Selling Used Software Licences” (2006) 159 *Copyright World* 8; F. Moos, “The Copyright Minefield of Second-hand Software” (2006) 165 M.I.P. 38; M. Huesch et al., “Germany: intellectual property — copyright” [2007] C.T.L.R. N30; T. Heydn, “Dealing with ‘Used’ Software Licences: Update on the Battle in Germany” (2008) 3(10) W.C.R.R. 32; A. Wiebe, “The Principle of Exhaustion in European Copyright Law and the Distinction Between Digital Goods and Digital Services” [2009] GRUR Int 114; T. Overdijk et al., “Exhaustion and Software Resale Rights” (2011) 2 CRi 33; J. Kolczynski, “Exhaustion of copyright of computer software online: a European (Polish, German Austrian) and US perspective” [2011] E.I.P.R. 578.

interpreted in line with art.36 of the Treaty on the Functioning of the European Union (TFEU), which limits restrictions on free movement of goods to those which are necessary to safeguard the specific subject-matter of (in this case) copyright.¹⁰ He doubted that the right to prevent resale of software by a lawful acquirer could be so justified, particularly in the light of the ECJ's judgment in *FAPL*¹¹ (which held that the specific subject-matter does not guarantee the right to the highest possible remuneration but only reasonable remuneration), and said the right to prevent resale would extend the monopoly granted by copyright beyond its specific subject-matter.

Therefore the answer to the second question was that copyright in a copy of a computer program is exhausted where the right holder allowed the copy to be downloaded from the internet to a data carrier (or otherwise made that copy available in the European Union, in any form and by any means) and granted, for consideration of a lump-sum payment, the right to use that copy for an unlimited period of time.

Although this appeared to be a bad result for Oracle, the Advocate General then returned to the first and third questions. He found that the sale of the copy of the program only exhausted the distribution right under art.4(1)(c) of the Directive and did not exhaust the reproduction right under art.4(1)(a). Moreover, he found that the concept of the "lawful acquirer", who had the right to reproduce under art.5(1), was restricted to someone who had acquired a copy of the program under a contract with the copyright owner. Therefore he concluded that a subsequent purchaser could only use a program already incorporated into a data carrier by the original purchaser and could not make a fresh copy, regardless whether the original purchaser erased his copy or no longer used it.

The Advocate General recognised but accepted the significant practical limitations of this finding in his Opinion:

"I am aware that confining the rule in this way only to copies materially incorporated in a data carrier after being downloaded from the internet will severely limit its scope in practice but, although justifiable on grounds of the need to preserve the effectiveness of the exhaustion rule and to give precedence to the free movement of goods and services, the converse solution, which would have the effect of widening the scope of the exhaustion rule beyond that envisaged by the EU legislature, cannot, in my view, be adopted without jeopardising the principle of legal certainty, which requires the rules of EU law to be foreseeable."¹²

Judgment of the ECJ

The Grand Chamber's judgment was handed down very quickly on July 3, 2012. Although it considered the questions in the same order as the Advocate General, and generally agreed with his conclusions on the second question (with an important addition), it took a different view on the first and third questions.

As regards the second question, the court's ultimate ruling was:

"Article 4(2) ... must be interpreted as meaning that the right of distribution of a copy of a computer program is exhausted if the copyright holder who has authorised, 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."¹³

Although not mentioned in that ruling, in its judgment the court held that the original purchaser of a multi-user licence did not have the right to divide the user rights under the licence.¹⁴ If the subsequent purchaser did not already have a copy of the program, he could only install one by reproducing the original purchaser's copy, which would only be permissible if the original purchaser made his own copy unusable. Even if the subsequent purchaser already had a copy of the program on its server, any purchased user rights could not be used in relation to that existing copy in which rights had been exhausted. Either way, the user rights could not be divided.

However, that mention of making the original copy "unusable" indicated that the court regarded this as relevant to the other questions referred. Unlike the Advocate General, it was not willing to interpret the Directive in a way which would "prevent the effective use of any used copy in respect of which [the copyright owner's] distribution right has been exhausted". Instead, it held that the person acquiring the used copy was a lawful acquirer under art.5(1) and so was entitled to reproduce the copy. However, the court noted that the original purchaser would infringe the copyright owner's reproduction right if it did not make its existing copy unusable at the time of resale. The court also noted that the copyright owner could use all technical means and protective measures at his disposal, such as product keys, to ensure that the original purchaser did not continue to use that copy.

As regards the first and third questions, the court's ultimate ruling was:

¹⁰ On the ambiguity of the legislation, and the likelihood it would be interpreted by reliance on the Treaty, see C. Stothers, *Parallel Trade in Europe* (Hart Publishing, 2007), pp.48–52 and 58–59.

¹¹ *Football Association Premier League v QC Leisure* (C-403/08 and C-429/08) [2012] Bus. L.R. 1321, discussed in C. Stothers, "Copyright Owners Cannot Require Satellite Broadcasters to Impose Territorial Restrictions on the Use of Decoder Cards" [2011] J.I.P.L.P. 265.

¹² *UsedSoft GmbH v Oracle International Corp* (C-128/11) A.G. Opinion April 24 2012 (C-128/11), A.G. Opinion, April 24, 2012 at [99], echoing M. Leistner, "Used" software before Europe's top court — the German Federal Supreme Court refers the Oracle v UsedSoft case to the European Court of Justice" (2011) 42(5) I.L.C. 503, 504: "[If the lawful acquirer of a re-distributed tangible copy of a computer program cannot perform those (normal) acts of use that are necessary to use that copy in accordance with its intended purpose], the exhaustion principle would indeed be almost meaningless with regard to computer programs."

¹³ *UsedSoft GmbH v Oracle International Corp* (C-128/11) [2012] E.C.D.R. 19 at [72].

¹⁴ *UsedSoft v Oracle* [2012] E.C.D.R. 19 at [69]–[71].

“Articles 4(2) and 5(1) ... must be interpreted as meaning that, in the event of the resale of a user licence entailing the resale of a copy of a computer program downloaded from the copyright holder’s website, that licence having originally been granted by that rightholder to the first acquirer for an unlimited period in return for payment of a fee intended to enable the rightholder to obtain a remuneration corresponding to the economic value of that copy of his work, the second acquirer of the licence, as well as any subsequent acquirer of it, will be able to rely on the exhaustion of the distribution right under Article 4(2) ... and hence be regarded as lawful acquirers of a copy of a computer program within the meaning of Article 5(1) ... and benefit from the right of reproduction provided for in that provision.”¹⁵

Analysis

Following the recent *FAPL* decision, this is the second major judgment of the Grand Chamber of the ECJ in just nine months which considers how the European single market should treat the distribution of copyright works in non-material form.¹⁶ If these judgments are followed, which seems highly likely given they were decided by the Grand Chamber, these two cases will become fundamental decisions on the interaction between intellectual property rights and the European single market in the online world, in the same way that *Consten and Grundig* and *Deutsche Grammophon* set the current framework in relation to physical goods in the 1960s and 1970s.¹⁷

The cases arise from highly specific facts which occurred some time ago: use of Greek decoder cards to show satellite broadcasts of English football matches in English pubs between 2004 and 2007, and an unusual German business reselling the right to use sophisticated business software in 2005. However, both judgments show a continuing commitment by the ECJ to ensure that technological change does not reintroduce territorial restrictions in Europe.

That commitment is likely to have a much broader impact than satellite decoder cards and business software. For instance, there are currently 21 appeals pending before the EU General Court against the Commission’s 2008 *CISAC* decision, which prohibited territorial restrictions in the contracts of music collecting societies.¹⁸ After the appeals are decided by the General Court, the inevitable further appeals will go to the ECJ. Territorial restrictions applied by collecting societies were said by the Commission to be one reason why music from Apple’s

iTunes store was and is not available to consumers across the EU, meaning that these appeals could have significant implications for consumers.¹⁹

Quite aside from the territorial issues, the ECJ’s suggestion that the specific subject-matter of copyright is limited to “appropriate” remuneration which corresponds to the economic value of the copy of the work, following *FAPL*,²⁰ could raise further concerns for intellectual property owners. As provided in art.4(1), intellectual property normally provides an exclusive right (an absolute right to exclude others from using the intellectual property) and not just a right to “reasonable” royalties. The actual value of the rights is then determined by negotiation in the marketplace.

Any suggestion that the ECJ or national courts should intervene to ensure remuneration demanded for intellectual property is “appropriate” or “reasonable” could have serious implications for a wide range of fields, from compulsory licensing of pharmaceuticals to trolls asserting patents over electronics and telecommunications. However, this would likely be reading too much into the ECJ’s language. As in *FAPL*, the court really seems to be saying little more than that there is no right to any remuneration which could be obtained by asserting rights which go beyond the “specific subject matter” of the intellectual property right. In turn that “specific subject matter” is no more than the scope of right which the ECJ considers compatible with the EU Treaty and, in particular, the Treaty’s various prohibitions of territorial restrictions. Put more simply, the ECJ is saying that you cannot justify extending the scope of a right by pointing to the additional remuneration you would get if it were extended. That is hardly controversial, although it does not provide any guidance on how to determine that scope.

For software itself, the ECJ’s judgment in *UsedSoft v Oracle* will clearly be disappointing for many developers and will have surprised some in the light of the (overall) more positive Opinion of the Advocate General. However, the judgment itself, given its limited scope, is not as disastrous as might first be thought, although software developers do still need to pay heed to the direction the ECJ is taking.

First, the right to prevent division of licences to resell “unused” user licences is important. If such licences could lawfully be resold, that would have the potential to undermine the multi-user licence model, which would increase complexity of licensing and require more careful pricing of additional licences to avoid cannibalisation of sales. By excluding such sales, the judgment is effectively limited to “used” or “second hand” software.

¹⁵ *UsedSoft v Oracle* [2012] E.C.D.R. 19 at [88].

¹⁶ Discussed previously in C. Stothers, “Copyright and the EC Treaty: music, films and football” [2009] E.I.P.R. 272.

¹⁷ *Consten and Grundig v Commission* (56/64 and 58/64) [1966] E.C.R. 299; [1966] C.M.L.R. 418; *Deutsche Grammophon v Metro SB* (78/70) [1971] E.C.R. 487; [1971] C.M.L.R. 631.

¹⁸ Commission Decision C(2008) 3435 of July 16, 2008, appealed as *CISAC v Commission* (T-442/08) et al.

¹⁹ Commission Press Release IP/08/22 (January 9, 2008). See also the Commission’s proposed Directive on collective management of copyright and related rights and multi-territorial licensing of rights in musical works for online uses in the internal market COM(2012) 372 final (July 11, 2012).

²⁰ *FAPL v QC Leisure* [2012] Bus. L.R. 1321 at [105]–[109].

Secondly, most developers will be able (if necessary) to change their distribution model from that used by Oracle in 2005 in order to circumvent the direct impact of the case. In particular, developers may provide for periodic royalty or rental payments and return of the software at the end of the term, or more fundamentally may provide software as a service (SaaS) or other forms of “cloud computing” where the software is not stored by the customer.

That said, developers using other distribution models in the EU must still think carefully about potential risks to those models the light of the ECJ’s judgments. Despite the concern raised by A.G. Bot to apply the legislation as it stands, to avoid “jeopardising the principle of legal certainty, which requires the rules of EU law to be foreseeable”, the ECJ itself focused more on preserving the effectiveness of the exhaustion rule and the European single market.²¹ Given that stance, developers would be well advised to consider whether their contractual restrictions could now be regarded as anti-competitive under art.101 TFEU or could be disregarded under the free movement provisions. In particular, before implementing any particular rental or cloud model, developers should assess the risk that the ECJ may hold that the right to use of software provided under that model is transferrable notwithstanding any contractual provisions to the contrary. That can then be factored into decisions about which model to use, and the value of applying different prices or other conditions in different territories within the EU.

It is striking that the US courts have adopted a very different approach from that of the ECJ, holding that the first sale doctrine (exhaustion) does not apply to software licences.²² In particular, the Ninth Circuit held in *Vernor* that neither of the factors subsequently relied upon by the ECJ (the right to use for an unlimited time and the absence of recurring licence payments) would make the transaction a “sale” for the purpose of that doctrine. However, it should be borne in mind that the legislation is much more specific in the United States, where §109(d) of the Copyright Act expressly precludes exhaustion in the case of “any person who has acquired possession of the copy ... by rental, lease, loan or otherwise, without acquiring ownership of it”.²³ More generally, the US courts do not have the same mandate to integrate jurisdictions which is provided to the ECJ by the Treaty on the Functioning of the European Union, which underpinned the judgment in *UsedSoft v Oracle* and led the court to adopt its

“purposive” construction of the legislation. Therefore the marked difference of approach between the European and US courts may well lead over time to different distribution models, in the absence of legislative change in the US or Treaty change in Europe.

Filtering for Copyright Enforcement in Europe after the Sabam cases

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© Copyright; Electronic monitoring; EU law; File sharing; Fundamental rights; Injunctions; Internet service providers; Online infringement; Privacy; Social media

Sabam, a Belgian collective rights management organisation, wanted an internet access provider and a social network site to install a filter system to enforce copyrights. In two recent judgments, the Court of Justice of the European Union decided that the social network site and the internet access provider cannot be required to install the filter system that Sabam asked for. Are these judgments good news for fundamental rights? This article argues that little is won for privacy and freedom of information.

Introduction

In the *Scarlet v Sabam*¹ and *Netlog v Sabam*² judgments, the Court of Justice of the European Union dealt with the question of whether an obligation to install a mechanism to filter out copyright protected works is in line with EU law. In these judgments, the court struck through a general obligation to filter out copyrighted material. Some have greeted the judgments with enthusiasm.³ But are these judgments indeed good news for privacy and information freedom? This article argues that little is won for these fundamental rights.

The second section provides background information to the cases, and the third section places the cases in the context of European case law on the liability of internet

²¹ Such an extreme purposive approach by the ECJ is not a new development. Consider, for instance, *Davidoff v Gofkid* (C-292/00) [2003] E.C.R. I-389; [2003] 1 C.M.L.R. 35, where the ECJ decided that the phrase “in relation to goods or services which are not similar to those for which the trade mark is registered” in art.5(2) of the Trade Mark Directive 89/104 (now Directive 2008/95 [2008] OJ L299/25) could be ignored entirely, on the basis that the Directive “must not be interpreted solely on the basis of its wording, but also in the light of the overall scheme and objectives of the system of which it is a part”.

²² *Vernor v Autodesk* 621 F. 3d 1102 (9th Cir. September 10, 2010), cert. denied 132 S. Ct 105 (2011); *Apple v Psystar* 658 F. 3d 1150 (9th Cir. September 28, 2011), cert. denied (2012). On the sale/licence distinction, see also *MDY Industries v Blizzard Entertainment* 629 F. 3d 928 at [3] (9th Cir. December 14, 2010).

²³ A point well made by A. Ruttenberg et al., “What Effect Will the *UsedSoft v Oracle* Decision Have on US Software Companies” (August 9, 2012), *Cooley Client Alerts*, <http://www.cooley.com/what-effect-will-the-usedsoft-v-oracle-decision-have-on-us-software-companies> [Accessed September 5, 2012].

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¹ *Scarlet v Sabam* [2012] (C-70/10) E.T.M.R. 4.

² *Sabam v Netlog* (C-360/10) [2012] 2 C.M.L.R. 18.

³ For instance, European Digital Rights (EDRI) calls the *Scarlet v Sabam* judgment “a vital victory for internet freedoms”, EDRI, http://www.edri.org/scarlet_sabam_win [Accessed September 5, 2012].