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Exhaustion Doctrine: Close to the Ultimate Aim of Copyright

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Abbreviations

ACC	Australia Copyright Council
CLRC	Copyright Law Review Committee
EU	European Union
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
ICESC	International Covenant on Economic, Social and Cultural Rights
IP	Intellectual Property
MC	Marginal Cost
MR	Marginal Revenue
PSA	Price Surveillance Authority
TRIPS	Agreement on Trade-Related Aspects of Intellectual Property Rights
UDHR	Universal Declaration of Human Rights
UK	United Kingdom
U.S.	United State of America
WCT	WIPO Copyright Treaty
WPPT	WIPO Performance and Phonograms Treaty
WTO	World Trade Organisation
WIPO	World Intellectual Property Organisation

1 Introduction

1.1 Short Presentation of the Subject

The exhaustion doctrine (also known in some jurisdictions as the “first sale doctrine¹”) is one of the basic rules of intellectual property (IP) system, and is applied to many IP rights, from copyright to trademark. The term “exhaustion” or “first sale” describes the concept of this rule, where, after the “first sale” of a particular legitimate work, the IP owner may no longer control or restrict the use or resale of a work use, because his IP rights to the work is exhausted.

The exhaustion doctrine is generally grouped into two kinds, territorial exhaustion and universal exhaustion, or, national and international exhaustion². The distinction between international and national exhaustion depends on the treatment of their legal status, according to the importing nation’s laws, when those legitimate goods have been imported without the authorization of local IP Right(IPR)’s holder.

With regards to copyright, for quite a long time in copyright history, there was only the doctrine of national exhaustion. Since the copyright system was created, the national authorities have played an important role in granting copyright to authors before the first modern copyright law - 1710 Statute of Anne in the U.K, protection similar to modern copyright was granted nationally to the Stationers’ Company as a privilege³. Since then, most countries developed their own copyright system, varying from the 1834 Royal Law on Printing in Spain to the *Urhebetrecht* in Germany⁴.

The territorial system built upon the boundary line of the countries dominates copyright legislation until the development of new technology that largely quickened the speed of the copy’s reproduction and distribution. In terms of increasingly trans-national markets, territorial protection turned out to be the obstacle preventing the author from receiving remuneration in countries other than where their creative activities had taken place⁵. In order to protect the benefit of the author in the international context, in the end of

¹ See U.S. Copyright Code Section 109(a)

² J.A.L. Sterling, *World Copyright Law* (Sweet & Maxwell, London, 2003) Section III – 1001.

³ W. Cornish and D.llewelyn, *Intellectual Property: Patent, Copyright, Trade Marks and Allied Right* (Sweet & Maxwell, London, 2007) p. 377.

⁴ M. Woodmansee, ‘The Genius and the Copyright: Economic and Legal Condition of the Emergence of the “Author”’, in W.T.Gallagher (ed.), *Intellectual Property* (Ashgate, The England, 2007) pp. 4-26.

⁵ See W. Cornish and D.llewelyn, *Supra* note 4, pp.379-280, *eg.* The UK, the commercial position as a considerable exporter of copyright materials and strong interest in reciprocal copyright arrangement other countries and its colonies.

nineteen century, the international community entered into a multilateral agreement for copyright, the Berne Convention for the Protection of Literary and Artistic Works of 1886. The nature and scope of copyright was for the first time proposed and universal accepted. Since that time, copyright has experienced a process of internationalization. Even today, we are still undergoing this process, as does the exhaustion doctrine. The rule that a copyright is exhausted when the copyrighted work first placed at market anywhere in the world is becoming accepted under national law.

1.2 General Purpose

This article is not aimed at whether or not copyright protection, as a whole system is desirable, but rather how to adjust this system such as exhaustion rule to full fill the needs of the original intention of the creation of copyright system. Copyright protection in the main is intended to enhance human society's well-being by providing economic and moral rewards for the contributions of authors and artists. How to realize the enhancement of social knowledge accumulation, to large extent, depends upon the efficiency of the distribution of knowledge protected by copyright.

The purpose of this article is to analysis the impact from the exhaustion rule of copyright on the distribution of knowledge and improvement of the human well being.

1.3 Research Question

Copyright provides that the owner has the exclusive economic right to copy, sell perform and import his work. The excise of those rights is subject to many limitations and exceptions in copyright law, for the purpose of reaching a balance of the needs of all human being well and the exclusive ownership. The exhaustion doctrine is one of them, and whether the exhaustion doctrine should be internationalized makes it more controversial at the level of domestic legislation.

The national exhaustion rule could no longer function well to meet the increasing need of knowledge distribution by providing enough access to creative work, and from time to time, it has been used as the barrier to block the trade of intellectual property goods. Since the international instruments leave the freedom to members to determine their own policy, I discuss the countries' attitude to international exhaustion.

1.4 Method

The article mainly concerns the exhaustion doctrine at which level has more impact that is positive on the knowledge distribution. The comparative analysis method has been conducted to examine the issue through the main part of the article.

The comparative process in the article involves the textual and jurisprudential aspects. The textual comparison is employed to ascertain different legislations on the exhaustion issue. The jurisprudential comparison may be more complex. In the article, it contains the historical jurisprudence, the economic jurisprudence and legal philosophy, which applies the cross-disciplines studies.

The historical jurisprudence refers to a study of the historical development and growth of the copyright exhaustion rule, and the changes involved in that growth, such as the development about Article 6 in the TRIPS and Australia copyright reform. The economic jurisprudence investigates into the effects on the application of the exhaustion of the economic phenomena such as price discrimination and parallel trade. To sum up, the studies on those cross-disciplines are applied in order to have a comprehensive understanding of the exhaustion issue.

1.5 Structure

The article is organized as follows: in this chapter the basic introductory concepts are briefly presented, such as international exhaustion. In the Chapter 2, from the cross-disciplinary perspective, I discuss the exhaustion rule's impact on the distribution of knowledge in the philosophic, economic and human rights point of view. In Chapter 3, I briefly review the text of exhaustion doctrine in the context of normative legislation. In Chapter 4, I consider the domestic law plays the determinative role, and I review the U.S, EU and Australia copyright law on the exhaustion. In Chapter 5, I turn to the international legal framework governing the exhaustion rule and parallel importation, including the TRIPS and WIPO treaties. In Chapter 6, I analyze the reform in Australia copyright law that as an example for international exhaustion. In Chapter 7, I summarize the various exhaustion legislations, and review the two exhaustion related issues. Concluding remarks are in Chapter 8.

2 Background Theories

2.1 Philosophy Analysis

2.1.1 John Locke's Theory

In John Locke's *Two Treatise of Government*, property especially, private property with the individual's labour upon them constitutes a strong argument against a monarchy. In a state of nature, the every man has nothing but his "labour", and goods are held in common of which the *enough and as good* condition is normally treated as descriptive, the goods which he removes out of the common, and he mixes his labour with it, and joined to it that is his own property.⁶

Through putting individual efforts upon the goods from common, the individual converts these goods into private property. This value-add labour allows the individuals to be enjoyed as human beings.⁷ Regardless of whether the labourer is motivated by some benefit, reference to "value-added" theory, "when labour produces something of value to other-something beyond what morality requires the labourer to produce- then the labourer deserves some benefit for it."⁸ Deserving the benefit by the labour here does not mean that because the labour produce the benefit, but labour adds the value to the social value, and this social value production deserves the benefit or reward. In Locke's theory, the add-social value treated as same as the enhancement of the common, as far as the common itself is concerned, each individual's usage of goods in the common will not result in the shortage or influence other people's work on it, and those add-social value belongs to the common.

While the intention of intellectual property legalisation illustrates that the enhancement of the "public good" justifies the rewards the exclusive right to the labourer who produced it by his or her intelligent efforts. From common point of view, the incentive is a main function of intellectual property rules that is aimed at encouraging more contribution to the common or social knowledge accumulation. Once a new piece of intellectual work is authorized the exclusive property ownership, once it is known by other

⁶ J. Locke, *Two Treatise of Government: An essay concerning the true original extent and end of civil government* (Oxford, 1946) pp.3-10

⁷ See J. Hughes, 'The Philosophy of Intellectual Property', *The Georgetown Law Journal*, (1988-1989), claiming the conceptual description of common also could be applied to human being, pp.287-366

⁸ Becker, The Moral Basis of Property Rights, IN PROPERTY, NOMOS XXII, quoted by *Ibid* p. 305

people, it has led to an expansion of the common, or of the accessible of common.

In the context of copyright, the labour consist two parts, creating of the idea and the expression of the idea. Coming up with an idea is the first step to create an intellectual product. Secondly, the value of this intellectual product perceived by society is through idea's expression. One of the most influent theories of the twenty century, $E = mc^2$, the theory of relativity, was first introduced in Albert Einstein's 1905 paper "On the Electrodynamics of Moving Bodies"⁹. Take this as a instance, $E = mc^2$, in the term of idea, is a part of the common. Basing on the labour of Einstein, it has expressed in the form of a thesis "On the Electrodynamics of Moving Bodies". From the Lockean point of view, the common is with the *enough and as good* condition. Therefore, the labour of Einstein does not increase the common as much as it increases the ability of other people to take from the common. In other words, the idea such as $E = mc^2$ already exist and the labour which adds social value is transporting idea from "the ethereal reaches" to physical world where idea could be used.¹⁰ Taking the pre-exist nature of the idea into consideration, only value labour is expression, which consist of transporting, translation the idea into accessible knowledge. It is the labour that to which the copyright system favour granting exclusive property rights, on the ground that the labour enhances the accessibility of knowledge in the common.

However, the extent of exclusion entailed in copyright impacts on that how the creation of property affects accessibility or distribution of the common.¹¹ The absolute exclusion of copyright limits other people's ability to retrieve knowledge from the common, which influences "as good and as many" of the common for remain individuals. According to Locke's theory on the common, the common had enough supply with similar quality that each person's extraction from it will not result in the shortage when other people need same quality and quantity. In the context of copyright, the distribution of the common depends on whether the copyright system could work alone with the nature of common. Therefore, the *enough and as good* is not only a condition to the common, but also a criteria can be used to examine the exclusion of copyright. The import of exhaustion of distribution right is consistent with the condition to the common.

2.1.2 Robert Nozick's Development

In Robert Nozick's *Anarchy, State and Utopia*, he observed the relationship creation of property and exclusion in the way of *reductio ad absurdum*: he asks whether the owner of a can of tomato juice who dumps it into the sea

⁹ *Theory of relativity*, <www.en.wikipedia.org/wiki/Theory_of_relativity>, visited on 8 April 2009.

¹⁰ Hughes, *Supra* note 8, p. 312

¹¹ *Ibid*, p. 315

could claim ownership of all the high seas¹². He argued that “social considerations favour establishment of private property and a free market system would not violate Locke’s proviso that “*enough and as good*’ remain in the common”.¹³

The *enough and as good* condition guarantees that remain individual’s needs would not rely on property holders to actively introduce them into the common. Otherwise the public can be worse off if a creation is offered and then limited in its use than it would have been had the creation never been made.¹⁴ While due to the free flow of information, today people are better off by the reason that more ideas are available which provides the “shoulder” to be stood by early expression work. New expression, no matter which reflects new or old ideas, even most become private property, benefit the common by unlimited distribution and availability to all. The free circulation delimits the right of author in the face of claims by consumers and other people from the common.

2.1.3 Hegel’s Alienation Theory

In Hegel’s alienation theory, one could be alienate any of his universal element, by the reason that “alienating the whole of my time, as crystallized in my work, I would be making into another’s property the substance of my being, my universal activity and actuality, my personality”.¹⁵ Moreover, “the reason I can alienate my property is that it is mine only insofar as I put my will into it.”¹⁶ However, what makes his theory complex is alienation is more than abandoning something, the act of alienation involves the choice of where and how the property will be used in the future.¹⁷ To maintain the sense of continuity over time and to exercise one’s liberty—that is treated as a key element of person in Hegel’s theory, one should have an ongoing relationship with external world. “Copyright may be justified either on the ground that they shield from appropriation or modification artifacts through which authors and artists have expressed their “wills” (an activity thought central to “personhood”) or on the ground that they create social and economic conditions conducive to creative intellectual activity, which in turn is important to human flourishing.”¹⁸

Using the personality to justify the limitation on his property, Hegel analogues the absolute alienation without limitation to slavery and suicide,

¹² R. Nozick, *Anarchy, State and Utopia*, (Oxford, 1978) pp.175-83.

¹³ *Ibid*

¹⁴ W. J. Gordon, ‘A Property Right in Self-Expression: Equality and Individualism in the Nature Law of Intellectual Property’, 1533 *Yale Law Journal* (1993)

¹⁵ G.W.F. Hegel, *Philosophy of right*, (translated by S.W.Dyde) (Amherst, 1996), p. 69

¹⁶ *Ibid* p.67

¹⁷ Hughes, *Supra* note 8, pp.344-345

¹⁸ W. Fisher, *Theories of Intellectual Property*, also see M.J. Radin, *Reinterpreting Property* (University of Chicago Press, Chicago,1993); J. Waldron, *The Right to Private Property* (Clarendon, Oxford, 1988).

because they are the surrender of a “universal aspect of one self”, because even inalienable types of property that constitute one’s own private personality.¹⁹

In the context of copyright, the property creator’s purpose of alienation of copies usually is to gain exposure of his idea, which is a non-economic form of the idea of recognition.²⁰ Author must have the right to claim his work’s identification and integrity in order to keep the “substantive characteristic, which constitute...private personality and the universal essence of ...self-consciousness.”²¹ Hegelian’s personality justification has influenced the civil law countries to quite large extent, which results in the right of author has been more focused on and the moral right of author rather than the common law community. Although moral right has been long expressly protected in civil law countries on the ground of limitation to alienation, the limitation does not extend to the distribution of protected work, to the contrary, from the Hegelian perspective, payments from copyright user to copyright owner are acts of the recognition. The payment acknowledges the claim from individual over the property. This acknowledges is a relationship connects individual with external world, which full fills personality justification from the owner’s point of view. Any other limitation upon user means the diminution to user’s personality, from the perspective of user’s personality.

2.1.4 Summary

By observing the intention of various legislation of copyright, the common predominant philosophical framework is utilitarian. The philosophical framework always intertwined with the intention of the legislation, although these are some difference in the entitlement of labour between the natural rights perspective and utilitarian perspective. Both perspectives have no conflict about enrichment of the public social value.

Locke’s theory treats the labour of the person in producing justifies his property entitlement, and at same time emphasizes the importance of keep the nature of the common. To meet those ends including the social benefit, the distribution plays a crucial role. John Locke justified property rights as moral entitlements to the fruits of one’s labour provided the valuable product and the creator benefit from it without violating other’s right and needs²². Hegel’s philosophy of right perceives the alienation of property as expression of personality to the object and other, alienation of property should be subject to limitation of personality, but this restriction should not

¹⁹ Hegel, *Supra* note 16

²⁰ Hughes, *Supra* note 8, pp.349-350

²¹ Hegel, *Supra* note 16

²² E. U. Petersmann, ‘Human Right of International Trade Law: Defining and Connect the two field’ in T. Cottier, J. Pauwelyn, and E. Burgi (eds.), *Human Right and International Trade* (Oxford, 2005) p. 48

influence the distribution, through which individual could be continuously connect with external world. Reference to the philosophical justification, the copyright law should act as an instrument guarantee the protection, in respect of the distribution of copyright work.

2.2 Human Rights

The justification of copyright law is based on, if not derived from, human right. Besides that many human right instruments claim the protection of copyright in the light of property argument, the history of copyright law indicates that the modern copyright statues could be perceived as elements of a certain triumph of the authors' freedom of expression and diffusion of knowledge over control exerted by the stationers, in England, or through the privilege holders, in pre-Revolution France.²³ The authors enjoy the freedom of publishing and receiving the revenue from his creation under the protection of copyright law.

A major justification for copyright protection is that incentives and rewards to authors resulted in benefit the needs of society. Combination with the property justification, copyright as a kind of basic human right is addressed in the fundamental international human right instrument Universal Declaration of Human Rights (UDHR):

Article 27(2): Everyone has the right to protection of the moral and material interests resulting from any scientific, literary or artistic production of which he is the author.

And also in its parallel article in the International Covenant on Economic, Social and Cultural Rights:

Article 15 (1) (c): The States Parties to the present Covenant recognize the right of everyone....to benefit from the protection of moral and material interests resulting from any scientific, literary or artistic production of which he is the author.

In order to make sure the achievement of these goals, the Covenant mandates that State parties undertake a series of steps²⁴. While “to be consistent with full provision of Article 15, the type and level of protection afforded under any intellectual property regime must facilitate and promote cultural participation and scientific progress and do so in a manner that will broadly benefit members of society both on an individual and collective level.”²⁵

With the coming of information era, the period of updating the generation of knowledge is getting significantly shorter, which requires the much quicker and shorter period of information diffusion in order to keep updating knowledge.

²³ Y. Gendreau, 'Copyright and Freedom of expression in Canada', in P. L.C. Torremans (ed.), *Copyright and Human rights*, (Kluwer Law International, the Hague, 2004), pp.21-36

²⁴ International Covenant on Economic, Social and Cultural Rights (ICESC), Article 15,(2);(3);(4)

²⁵ A.R. Chapman, 'Approaching Intellectual Property as a Human Right (obligation related to Article 15(1)(c))' XXX:3 *Copyright Bulletin*, (2001) pp. 4-36.

On the other hand, copyright is expanding according to digital era. For example, the rental right, article 7(1) of the WIPO Copyright Treaty gives an “exclusive right of authorizing commercial rental to the public of the originals or copies of their works” to “Authors of (1) computer program; (2) cinematographic works and (3) works embodied in phonograms”. The expanding copyright, to some extent more or less, limits those diffusion and expression. Yet if authors are indeed protected, their protection is already in itself limited by rules whose existence owes much to concerns about human rights such as the freedom of expression of third party²⁶, and freedom of expression safeguards a person’s right to affect and receive information. If go a little bit further, freedom of expression allows individuals to gather the information necessary for making various choices as part of the democratic process²⁷. Therefore, the balance between the broad public interest of society and interest of individual right holder changed as well.

Enjoying the “benefit from the protection of moral and material interests from...” in ICESCR Article 15 does not mean the enjoying the protection of copyright without any restriction. As Paul Torremans puts it: “the balance between the public and private interests is not external element for copyright. On the contrary, it has been internalized by copyright and it is part of its fundamental nature.”²⁸ The exhaustion clause in copyright regime could effectively limit right holder abuse exclusive right to liberate the legislative and necessary diffusion and expression of knowledge.

The implementation of exhaustion doctrine in the international human right context, not only be entitled the public’s right to access to the creation, but also grant the buyer of copyrighted works the freedom to trade his possession. The right to dispose of one’s property as basic property right can be justified as precondition for individual autonomy and for a free, informed and accountable society, from the human right point of view²⁹.

The freedom of trade as human right is protected by the constitution. The Germany and Switzerland explicitly protect trade freedom as a constitutional right of citizens.³⁰ Inside the EU, the free movement of goods and non-discrimination as “the fundamental freedoms” at the same level as other “fundamental rights” has been encoded into the 2004 EU Treaty Constitution.³¹ When turning to trans-national or cross-community freedom of trade with third countries, the national constitution and EU law seem to

²⁶ Gendreau, *Supra* note 3

²⁷ A. Meiklejohn, ‘The First Amendment is An Absolute’, *Supreme Court Review* (1961) p. 245.

²⁸ P. L.C. Torremans, ‘Copyright as a Human Right’ in P. L.C. Torremans (ed.), *Copyright and Human rights*, (Kluwer Law International, the Hague, 2004), pp.1-21.

²⁹ E. U. Petersmann, *Supra* note 23 pp. 48-49

³⁰ M. Hilf and E.U. Petersmann, *National Constitutions and International Economic Law*, (1991)

³¹ See Article I-4 (Fundamental freedom and non-discrimination), I-9,II-75 (Freedom to choose and occupation and right to engage in work), II-76 (freedom to conduct a business), and II-76 of the EU 2004 Treaty Constitution

provide less protection rather than national trade or trade inside the community.³²

However, after the Second World War, the history shows that trade liberalization partly goes hand in hand with improved enjoyment of protection of human rights.³³ Trade regulation expanded into the field of intellectual property under the World Trade Organization (WTO). Although some human rights lawyer expressed the fear that WTO rules elevate free trade over and above the human rights protection and promotion,³⁴ with regard to the right to freedom trade, a basic human right is the main content that the WTO law aims to protect and promote. There is no conflict between the copyright arrangement on trade and the aboard human right standard. Taking the different ways, but they are aims to the same destination. “While human rights clearly are predominant in terms of setting goals of aspiration” ...the economic law such as copyright arrangement “provides important tools”.³⁵

The freedom to trade, from the basic need perspective, is external liberty and important human right.³⁶ “Everyone, as a member of society, has the right to social security and is entitled to realization, through national effort and international co-operation and in accordance with the organization and resources of each State, of the economic, social and cultural rights indispensable for his dignity and the free development of his personality.”(Article 22 of UDHR) The regulation as the tool facilitates the freedom to trade meets the requirement of human rights in terms of UDHR. According to Article 28 of UDHR, “Everyone is entitled to a social and international order in which the rights and freedoms set forth in this Declaration can be fully realized.”

³² See Article 2 of German Basic Law and Article 131-133of EC

³³ T. Cottier, J. Pauwelyn, and E. Burgi, ‘Linking Trade Regulation and Human Rights in International Law: An Overview’ in T. Cottier, J. Pauwelyn, and E. Burgi (eds.), *Human Right and International Trade* (Oxford, 2005) pp. 1-29

³⁴ *Ibid*, p.3

³⁵ *Ibid* p. 19

³⁶ Petersmann *Supra* note 31 p.57

2.3 Economic Analysis

“Human rights undeniably intertwine copyright, but the predominant forces that have shaped the law are economic. Global communities of economic interest among copyright owners have been far more potent than ideology.³⁷” As Paul Goldstein points out, the economic significance of exhaustion doctrine lies in practices of many areas, such as price discrimination. Price of copies differs from one country to another in the light of cost of manufacture; average consuming affordable level and the publisher’s international marketing strategy. From the economic perspective, the attention to a legislation used to be highlighted on the cost, rent seeking and social welfare³⁸. This section presents an economic analysis of exhaustion doctrine in the copyright.

The analogy mentioned in the philosophical perspective does not apply here in the light of unique nature of intellectual property. As Plant pointed out, “the institution of private property make for the preservation of scarce goods, tending ... to lead us to ‘make the most of them’... there is not sufficient concentration of ownership of the supplies of a particular good, and of all the easily substitutable alternatives for it, to enable the owners to control the prices of the property they own. Neither the withholding, nor the disposal of the property of any one owner will in general affect appreciably the price of the commodity in question.”³⁹

2.3.1 Monopoly position

It is an economic truism that the ownership of physical property will not necessarily ends up the monopoly in the market, so how about the ownership of the intangible property such as copyright? Some scholars do not agree to equate IP protection, especially copyright protection with monopoly. On the ground that unlike patent, the copyright does “not provide any protection from independently created competition work no matter how similar they may be.”⁴⁰ Furthermore, the monopolistic competition is appropriate since there is free entry,⁴¹ let alone granting the copyright owner

³⁷ P. Goldstein, *International Copyright Principle, Law, and Practice* (Oxford, 2001) pp. 306-7

³⁸ W. M. Landes and Richard A. Posner, *The Economic Sturture of Intellectual Property Law*, (Havard University Press, 2005) pp.1-11

³⁹ A. Plant, ‘The Economic Theroy concerning Patents for Inventions’, in A. Plant *Selected Economic Essays and Addresses* 57 (University of Chicago Press, 1994) p.36

⁴⁰ S. J. Liebowitz, *Is the Copyright Monopoly a Best-Selling Fiction?* For the SERCI Annual Congress, June 2008

⁴¹ Y. Christopher S, ‘Copyright and Product Differentiation’, *79: New York University Law Review* (2004) pp. 212-280.

a monopoly on making copies of the owner's particular work does not mean that there is necessary any economic monopoly or any deadweight loss.⁴²

No matter whether there is any economic monopoly, in fact, due to the special mechanism of copyright, legislation designed to meet the unique requirement of copyright protection, at least "a monopoly market advantage" would be resulted from the ownership of copyright. Because intangible property has the characteristics of what economists call a "public good" which may be used by many people without depletion, and it is very difficult to prevent free-rider from using it since it has been published. The lighthouse has been widely used as an example. It says the use of the lighthouse, which is built by some ship-owners, does not deplete the value of its hazard warning to other, and the prevention of nonpayer from using its warning system would be insufficient, in this case, the market will undersupply if the producers cannot reap the marginal value of their investment.⁴³ The example in the context of copyright is the musical clip in the cyber environment. Through the digital technology, an infinite number of copies can be reproduced at close to zero cost. What's more, additional users reduce neither the quality nor even the quantity of the original protected work.

The protection with the "monopoly market advantage" can be justified with the name of preventing the price of work from declining to the marginal cost of producing an additional item. That is the reason why in all legislations no country excludes the reproduction right from copyright of owner after the first sale. Because such a clause would result in either very high license fee, which would further influence the enough dissemination of the knowledge, or as mentioned above no one in the market willing to invest into creation.

However, different from the reproduction right, the distribution right does not facilitate the nonpayer. The exclusive monopoly rights to copyright owners precludes the users from taking advantage from the author's creation cost by using a comparative low price to reap the marginal value, which is not exhausted. Even in the context of price discrimination, the owner could still at least benefit from the price in the low-consuming level countries.

Concerning the public interest, unlike the right to reproduction, the limitation distribution right could be depleted the market power of the copyright owners. In contrast, the overprotection of copyright owners' market power can give rise to anti-competitive conduct that lowers economic efficiency. Referring to international trade of copyright protected works, such as entertainment product, "the inclusion of a distribution right, in which the creator of a copyright product can control its distribution

⁴² E. W. Kitch, 'The Nature and Function of the Patent', 20: *Journal of Law and Economics* 265 (1977) pp. 265

⁴³ R. H. Coase, *The Lighthouse in Economics, in the Firm, the Market, and the Law*, (University of Chicago Press, Chicago, 1988) pp.53-106

beyond the first sale, may introduce one such distortion.”⁴⁴ Exhausting the distribution right aims to limit the market power of copyright owners but not, to the extent, erase the exclusive monopoly position of owners.

2.3.2 Market segmentation and price discrimination

Price discrimination is a term related to monopoly behaviour. Charge different prices to different countries for the similar protected work- a practice known as third-degree price discrimination, by which the lower price opens the new market, and facilitates more access to new products. What’s more, to the copyright owners, the new open markets come with the increased output, scale and learning economies that result in decline of marginal cost of new products.⁴⁵

The price discrimination could result in the Pareto improvement from a new opened market.⁴⁶ When economists mention the third-degree price discrimination, the oligopoly setting and complete market segmentation weight heavily on their minds. By introducing the concept of the exhaustion, more or less it would influence those pre-requirements. Here there are two markets, the market 1 and the market 2 (new open market), the market 1 serves the higher price say, P_{m1} , and P_{m2} is the price in market 2. I assume that the two demands functions are nonsubstitutable and the lowering the price in the new opened market does not influence the original price of the former market.

Suppose the marginal cost (MC) is constant, if the copyright owner implements price discrimination between them, the output of copyrighted works in the opened market 2 has increased, which equals the consumer surplus in market 2 has increased. While based on the assumption above, the consumer welfare in market 1 is unchanged, and because of the scale and learning economies, the marginal cost tends to decreasing rather than constant. Taking increased profit of the copyright owner from market 2 into consideration, the total output under (P_{m1}, P_{m2}) is “unambiguously greater” than the output under (P_{m1}, P_{m1}) . To reach the profit-maximizing point ($MR=MC$) for the copyright owner, and the price would be lowered below (P_{m1}, P_{m2}) . Therefore, there is a Pareto Improvement that means the situation of both the consumer and the copyright owner would be better off.

Figure 1⁴⁷:

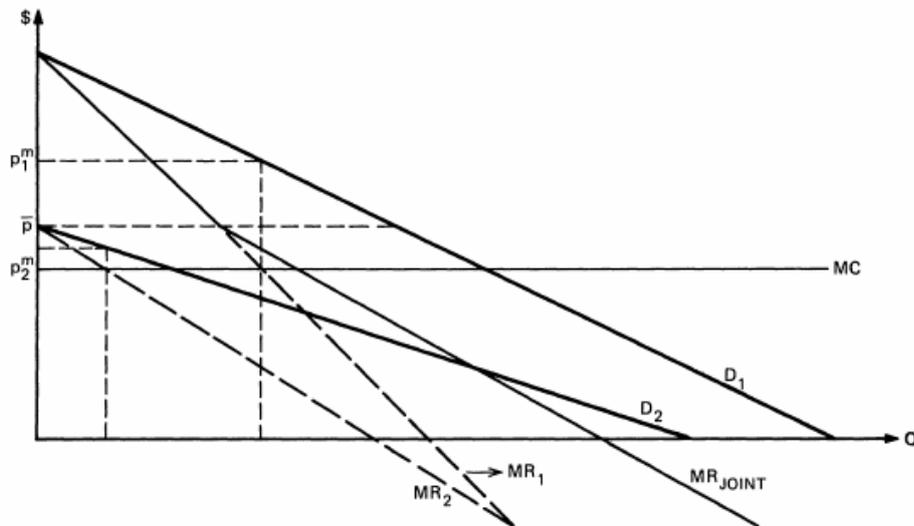
⁴⁴ T. Papadopoulos, ‘The First-Sale Doctrine in International Intellectual Property Law: Trade in Copyright Related Entertainment Products’, 2: 2 Summer, *Entertainment Law*, (2003), pp.40-60

⁴⁵ J. A. Hausman and Jeffrey K. Mackie-Mason, ‘Price Discrimination and Patent Policy’, 19:2 Summer, *RAND Journal of Economics* (1988), pp. 253-265

⁴⁶ *Ibid*

⁴⁷ *Ibid* analogy the structure of model in Hausman’s paper, which was used to analyse the patent issue.

PARETO IMPROVEMENT FROM A NEW MARKET



However, why most copyright owners do not prefer this Pareto Improvement, because the assumption is difficult to reach or with very high cost that almost prevents the copyright owner to do so. According to Figure 1, although at the joint demand the joint marginal revenue is higher than marginal cost, the price of market 1 charges \bar{p} is lower than P_{m1} by the reason that the close substitutability of both demands cause the certain amount loss from the copyright owner from market 1.

Therefore, from the analysis we could find that the market segmentation actually is more artificial for the possible worse off revenue from the higher consuming level market. However, it is need to notice is that although the close substitutability of both demands, they do not, in any case or at any time, make the copyright owners worse off in the higher price market.

Firstly, the substitutability of both demands is close but not completed. Non-substitutability is caused by the individual works are not perfect substitution for each other. A publisher will charge higher prices for hard-covered editions, and later reduce the price for the market that is willing to wait for the paper-covered editions.⁴⁸ Taking the publisher Prentice Hall and Pearson as an instance, it has low cost editions of textbooks for countries such as India, the textbook from which is often printed on cheaper paper, is paperbacks and priced at 15-20 per cent of the dollar price.⁴⁹

Secondly, reimport takes time, so there will be an interval during which the works at high price will not face competition. For the works which are ephemeral or very frequently updated, where the demand is initially very high but falls dramatically after a short period, the books about internet technology could be a good example. For that kind of work, the fixed cost of the work has to be recouped over a brief period otherwise the updated

⁴⁸ Landes and Posner, *supra* note 39, p.39

⁴⁹ *Price Discrimination*, <www.en.wikipedia.org/wiki/Price_discrimination> visited on 23 April 2009

competitors will soon take over the market, so possibly that period could be shorter than time reimport needed. Aware of this, in order to prolong time-lag between the higher price market and the lower price market, the most copyright owners cause a artificial delay of release the work in the lower price market.

Thirdly, the lower price reimported work contributes the copyright owner with monopoly advantage in lower price market in the same territory of higher market. At the same time, it increases the output in lower price market in the same territory, and it provides competitive substitution of pirated works, so it efficiently prevents the piracy.

2.3.3 Summary

Comparing with the copyright owner's pursuit of profit maximum, the policy makers should not only pay attention on the incentive function, but also the social welfare should be weighted heavily on their mind, on the ground that the social welfare is the intention of the copyright, as well as the reason why the incentive is provided. Therefore, with regards to exhaustion rule in copyright, the challenge for policy maker is to set the appropriate level of market power by a mean that balance the users and owners of copyright. Overprotected market power of the owners means a limitation in the dissemination of creative work that reduces consumption level.

Minimize the copyright protection could encourage the dissemination that enhance the consumer welfare. Many scholars have been attempted to identify the optimal level of protection with the method of economic analysis.⁵⁰ The supply of the copyright protected work (q) as a function of price (p) and a hypothetical index of copyright protection (z)⁵¹:

$$q = q(p, z)$$

The consumption of the copyright protected work (c) as a function of price (p) and a hypothetical index of copyright protection (z):

$$c = c(p, z)$$

The consumption is inversely related to copyright works price and protection, while the supply is directly related to copyright works price and protection, therefore⁵²:

$$w = w[c(p, z), q(p, z)]$$

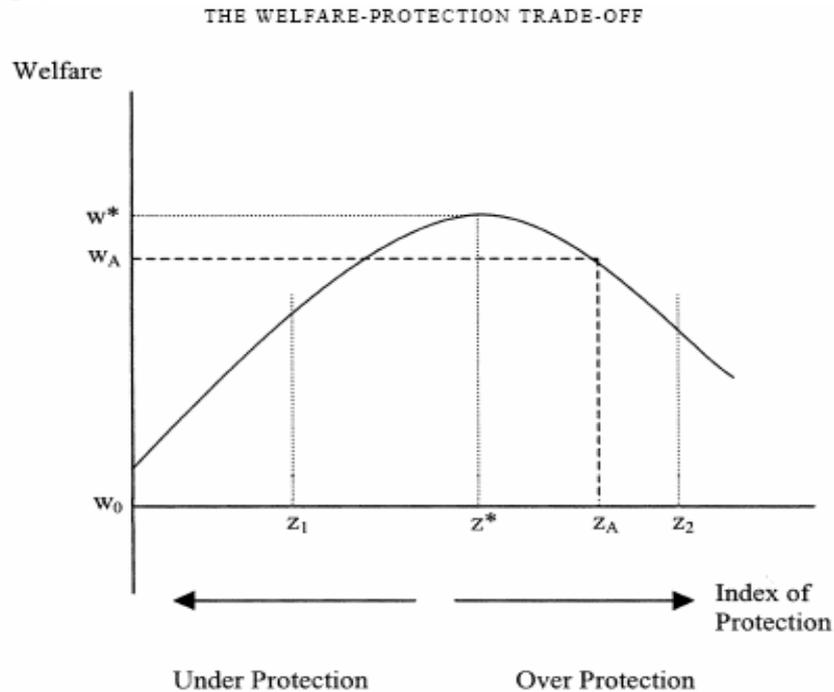
⁵⁰ See Papadopoulos, *Supra* note 44; also see W. M. Landes and Richard A. Posner, 'An Economic Analysis of Copyright Law', XVIII, *Journal of Legal Studies* (1989), pp.325–63

⁵¹ Papadopoulos, *Supra* note 44

⁵² *Ibid*

The copyright owner could decide the price at the international level according to various facts that might be influence the revenue, unless there is “market failure”, policy maker would not allow to directly intervenes the price of works lay in market. However, the domestic policy maker could take advantage of copyright Law to adjust the level of protection that will lead maximize national welfare (w).

Figure 2⁵³:



According to Figure 2, the key element for policy maker is setting an appropriate level of protection (z) that facilitates the dissemination of works. The lower protection such as at the level of (z_1), obstacles to high level of welfare is form less motivation of creation and worse anticipation from the copyright owner to revenue from the market. The former reason (posner why need copyright)

It could be presented as the weak enforcement to piracy, for example. The over protection at the level (Z_2) on hand increase the revenue to the owner at short term and the supply will increase, on the other hand the dissemination will limit by less access, in the end it will end up the lower welfare.

“The key to economic efficiency lies in blackening the social benefit of providing economic incentive for creation and the social cost of limiting the diffusion of knowledge.”⁵⁴ Although precise economic analysis relies tremendously on the research data, based upon the above the overprotection to distribution right, in the measure of social welfare, could not be a strong convincing policy setting that possible locates at level (Z_A) of protection.

⁵³ *Ibid*

⁵⁴ R.P.Merges, P.S.Menell and M.A. Lemley, *Intellectual Property in the New Technological Age*, (Wolters Kluwer, 2007) p. 13

The enough data and complete information is too far beyond to reach. Nevertheless, it would not stop us from agreeing with what Koboldt states⁵⁵:

The determination of the optimal level of copyright protection is a difficult task and requires lawmakers to possess complete information about the production technologies and demand structures.

In essence, the concept of copyright exhaustion of rights ensures a reward has been obtained before it imposing the constraint. The limitation attempts to serve all interests by equitably restricting copyright powers without severely limiting a copyright owner's economic opportunities.⁵⁶

2.4 Parallel Trade

Without referring to the parallel trade, it is difficult to understand why the international instruments on the exhaustion issue result in today's format. As a matter of fact, it is parallel trade that makes the international exhaustion doctrine so hot-debated. Parallel trade refers to the trade in legitimate works outside the local authority channels of distribution, so called "gray market trade" in U.S.

According to above examination, nowadays major economic powers including U.S. and E.U. do not adopt the international exhaustion, the international exhaustion doctrine on copyright are far to be universal recognized. Many scholars found that it is not surprising that a global rule on exhaustion could not be reached⁵⁷. Due to the nature of intellectual property work, in the early period, it usually requires the author's unique creation and publisher's considerable investment on organizing production facilities before its distribution. However, after the first copy has been placed on the market, the reproduction and distribution cost, so called "variable cost"⁵⁸ compares with the early period "fixed cost"⁵⁹, is much smaller. Books and sound records may be reproduced at very low cost with the advanced technology. What's more, the distribution cost of them with the digital method could be virtually zero cost.

As mentioned in economic analysis part, the copyright holders are willing to take price discrimination measure in different levels' markets, in order to gain optimal revenue. Under the national exhaustion, the cheaper goods

⁵⁵ C. Koboldt, 'Intellectual Property and Copyright Protection', 19:2 *Journal of Cultural Economics* (1995), pp. 131–155.

⁵⁶ D. R. Cahoy, 'Oasis or Mirage?: Efficient Breach as a Relief to the Burden of Contractual Recapture of Patent and Copyright Limitations', 17 *Harv. J. Law & Tec* (2003) p.135

⁵⁷ See M. Ganlandt & K. Maskus, 'Intellectual Property Rights, Parallel Imports and Strategic Behavior', No. 704 *IFN Working Paper*, (2007); also see R. Martin, 'An Elementary Proposition Concerning Parallel Imports', 56 *Journal Of International Economics*, (2002) pp. 233-245

⁵⁸ W. M. Landes and R. A. Posner, *Supra* note 39, p. 47

⁵⁹ *Ibid*

flow to the market without the authorization, constitute the gray market. If the doctrine of international exhaustion was adopted, there may well be a large 'dormant market' in parallel trade goods that would be unleashed.⁶⁰ At the same time, it results into the impossibility for the copyright owner to implement the price discrimination between the different markets.

Although there is few ambiguous results referring to how much the welfare of consumers as whole will be improved by the international exhaustion, neither the extent, to which the benefit of the copyright owner will suffer from it. The empirical studies on the copyright exhaustion issues including parallel importation in the international context are sparse, and "quasi-anecdotal"⁶¹, and economics literature that seeks to model the outcome of various approaches⁶². In most cases, this controversial and uncertain topic is representing as the conflict between the interest of the copyright owner and the consumers or the whole society's welfare. The former's main interest is to maximize the benefit from the fixed cost and variable cost, while the interest of later group is public interest such as expand their choices and improve their general well-being.⁶³ The regulation setting for which of them, to large extent, depends on whose interest is policy makers' prior consideration, however, the answer in the real situation is more complicated than "A or B", even more, some time these is no clear groups marked with "A or B".

⁶⁰ F. M. Abbott, 'First Report (Final) to the Committee on International Trade Law of the International Law Association on the Subject of Parallel Importation', *Journal of International Economic Law* (1998) pp.607-636

⁶¹ *Ibid*, p. 613; also see Chard and Mellor, 'Intellectual Property right and Parallel Importation', 12: 69 *World Econ.*,(1989), p. 71; D.A. Malueg and M. Schwartz, 'Parallel imports, demands dispersion, and international price discrimination', 37 *Journal Int'l Econ.* (1994) pp. 167-169,

⁶² Abbott *Supra* note 61, p. 613

⁶³ *Ibid*

3 Text of Exhaustion Doctrine

In copyright law, the doctrine of exhaustion – referred to as the "first sale doctrine"⁶⁴ in the common law countries. It is a fundamental tenet in copyright law, and the limitation on the exclusive rights. It is based on the conception that the copyright holder could no longer control or restrict what a purchaser of a particular legitimate copy use or resale or conduct other forms of action with that copy, as long as it is not against the moral rights.

The traditional exhaustion is subject to the distribution right by the reason of the *right over things* in civil-law countries. Due to this rule, when the ownership of material object conflicts with the distribution right, the ownership enjoys the priority. Therefore, in other words, the distribution right exhausts after its first sale.

The underlying rationale, in short, is that the copyright owner has received his or her "reward" from a sale, and is entitled to nothing more⁶⁵. Different with the purchase, the exhaustion right does not extend to the other rights with the different nature of copyright, such as the rental right. Maybe it does not go to the extreme that re-renting the work from a rental-store needs with the consent of copyright holder, however, saying that "in general rental and lending do not exhaust the distribution right"⁶⁶ usually means the first sale the work does not exhausted the rental right as a exclusive right to the original copyright holder.

The distribution right is a typical right would be subject to exhaustion doctrine. The exhaustion of distribution means once the right owner has authorized the distribution of a particular copy within a certain territory (national or international), the right to authorize further distribution of that copy in that territory has ceased. This definition has two meanings. Firstly, the right of first sale belongs to the author, no one but author has right to disclose his copyrighted work. Secondly, the distribution right could be executed only once, if the article has been entered into public domain by or with the consent of right holder, in other words after so called "first sale", the previous right holder could no longer control the distribution right of the copyrighted work.

But often the first sales rule is confined within the territory covered by the right – it amounts to a principle of domestic exhaustion⁶⁷ (sometime referred to as 'territorially') rather than international exhaustion (or 'universality'). By contrast, the right would be exhausted in any other

⁶⁴ See 17 U.S.C Section 109(a)

⁶⁵ See, e.g. *Borne v. Walt Disney Co.*, 68 F.3d 621, 632-33 (2d Cir. 1995) (noting that the concept of the reward in exchange for the dispossession of the copy is so central that it may constrain a literal interpretation of the statutory language).

⁶⁶ Sterling *Supra* note 2, Section III - 1001

⁶⁷ Sterling *Supra* note 2,

markets in the world after the work has been lawfully put on one market, this rule is under the principle of international exhaustion.

While with more and more countries' national right which is used to rule the copies from other countries, the boundary of a certain territory is easily used as the criteria to categorize the exhaustion principle could implement to what extend. Professor J.A.L. Sterling claims that the exhaustion could be identified into three categories: "the national exhaustion", "the community exhaustion" and "the international exhaustion".⁶⁸ The most common case nowadays is the "national exhaustion", where the national law provides that once the right owner has authorized the distribution of a particular copy within the national territory, the right to authorize further distribution of that copy in that territory has ceased.⁶⁹ The "community" in the term of "Community exhaustion" refers to the European Community. It represents the principle that once a particular copy has been put on the market within the European Community by or with the consent of the right-holder concerned, that copy can circulate freely in the Community, i.e. the right owner cannot prevent further the distribution of that copy in order Member States of the Community. As defined above, the international exhaustion refers to the work can circulate freely in any country, unimpeded by national exercise of the distribution right.⁷⁰ In many countries and European Community, domestic law provides the exhaustion within the boundary of a country or the community. There is few national legislations, so far, on the question of the application of international exhaustion doctrine with regards to authorized copies marketed in another country, and then imported into its territory.

⁶⁸ *Ibid*, 1001-1002

⁶⁹ *Ibid*

⁷⁰ *Supra* note 14

4 National and Community Exhaustion

4.1 National Exhaustion

The doctrine of national exhaustion has been widely accepted in nowadays, which has more or less similar meaning in various legislations. Some countries put exhaustion doctrine under exceptions to distribution right, such as Germany Copyright Law⁷¹, where the exhaustion doctrine is mentioned as a specific limitation to Right of Distribution. In Germany Copyright Law, the consent of the holder, with which the work is put into circulation, could be used to exhaust the distribution right in the national territory. The similar regulation can be found in the Austria Copyright Law Article 16 (3) as well.

While another example is put the exhaustion doctrine under the copyright's limitation as a kind of expectation. For example, in U.S. Section 109 in U.S. Copyright Law about effect of transfer of particular copy or phonorecord, and in Intellectual Property and National Information Infrastructure published by U.S. in 1995, so called "white paper", Part I, A, 7,C Section lists the First Sale Doctrine, both of them are treated as the limitation of copyright. In U.S., different with the exhaustion of patent, the exhaustion doctrine on copyright is codified in the Copyright Act. Section 109 refers to the "Effect of transfer of a particular copy or phonorecord".⁷²

However, unlike the reproduction, translation and adaptation rights, the right to distribution copies of literary and artistic works has historically received less than universal endorsement⁷³. Such as in France and Belgium, there is no distribution right, and the distribution right in those countries is partially approximated by the so-called "right of destination", the author's right of "reserving for a very specific purpose, reproductions of his work that have been put on the market."⁷⁴

⁷¹ Article 17 (2) in Germany Copyright Law state that:

If the original work or copies thereof have been put into circulation in the territory of the European Union or of another Contracting State of the Convention Concerning the European Economic Area through sale thereof with the consent of the holder of the distribution right, their further distribution shall be permissible with the exemption of rental; Copyright, Law (Consolidation), 09/09/1965 (23/06/1995)

⁷² 17 U.S. Copyright Act 109(A) (2000) state that:

...the owner of a particular copy or phonorecord lawfully made under this title, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy or phonorecord.

⁷³ Goldstein *Supra* Note 38 p. 254

⁷⁴ *Ibid*, p.257

Except of those, the exhaustion of distribution right has wildly been recognized in the modern world. In US and Germany as mentioned above, and UK as well its 1988 Copyright, Designs and Patent Act, the exhaustion of distribution has been listed.

4.1.1 The Exhaustion Doctrine of Copyrighted Work Distribution in U.S.

4.1.1.1 U.S.'s interest on copyright industry

In the U.S., the copyright industries (including movies, TV, home video, music, publishing and computer software) are America's greatest trade prize.⁷⁵ The study shows that in 2004 the core US copyright industry has contributed USD 760.49 billion to the US economy, takes up 6.48 per cent in total gross US domestic product; in 2005 this industry has contributed USD 819.06 billion, it takes up 6.56 per cent in total GDP⁷⁶. The value of copyright industry to gross US domestic product has grown 360 percent from 1977 to 1999.⁷⁷ The actual revenue generated from the exports of US copyrighted goods by the core industry was at least \$106.2 billion and \$110.8 billion in the 2004 and 2005 respectively⁷⁸. Therefore, no wonder why Jack Valenti (president of the Motion Picture Association of America) made the comments that: "we bring in more revenue than aircraft, more than agriculture and auto parts. What is more astonishing and more valuable is that the Copyright Industry has a surplus balance of trade with every single country in the world. No other American business enterprise can make that statement, particularly in view of a \$400 billion trade deficit in 2000."⁷⁹ Therefore, having this in mind, no matter how hard and cautiously the U.S. policy makers try to make sure the revenue from the copyright industry, they are all understandable.

4.1.1.2 The Exhaustion Doctrine of Copyright Work Distribution in U.S.

With regards to distribution right of U.S. right owner, once the copyright owner transfers ownership of a particular copy (a material object)

⁷⁵ A. Strory, 'Copyright: TRIPS and International Educational Agenda', in P. Drahos and R. Mayne (eds.) *Global Intellectual Property Rights, Knowledge, Access and Development* (Oxfam, 2002) pp. 125-143

⁷⁶ *Copyright Industry In The US Economy Report, The 2006 Report*, The International Intellectual Property Alliance, <http://www.iipa.com/pdf/2006_siwek_full.pdf>, visited on 24 April 2009.

⁷⁷ *Copyright Industry In The US Economy Report, The 2001 Report*, The International Intellectual Property Alliance, <http://www.iipa.com/pdf/2001_siwek_full.pdf> visited on 24 April 2009.

⁷⁸ The International Intellectual Property Alliance, *Supra* note 78

⁷⁹ Motion Picture Association Of America, Valenti Warns of Potentially Devastating Economic Impact of Copyright Theft. 2001, in Strory *Supra* note 77

embodying a copyrighted work, the copyright owner's exclusive right to distribute copies of the work is "extinguished" with respect only to that particular copy. This limitation on the copyright owner's distribution right allows wholesalers who buy books, in the national territory, to distribute those copies to retailers and retailers to sell them to consumers and consumers to give them to friends and friends to sell them in garage sales and so on -- all without the permission of (or payment to) the copyright owner of the work.⁸⁰ By the provisions of the Act, a purchaser can sell, lease, or destroy any individual authorized copy, regardless of the fact that such an act may interfere with the market for new goods covered by the copyright owner's intellectual property interests.⁸¹ Of course, there are several exceptions to this rule, for example, one of them was carved out for owners of copyright in sound recordings and computer software.⁸²

Besides that, according to the case law, the U.S. Supreme Court seems to have not held Section 109(a) subject to other supplementary rights given to copyright owners in various provisions of the Act, in any other conditions.

Firstly, as long as first sale happened inside the territory of US, the court's decision complies with the Section 109 about the exhaustion doctrine. In the case of *Quality King Distributors, Inc. v. L'Anza Research International Inc.*, copyrighted goods lawfully made in U.S, are shipped abroad, then the foreign purchaser imported them back into US. The first sale happened in the U.S. at the price of U.S. market, the U.S. copyright holder had been rewarded the benefit from the work. Therefore, the Supreme Court determined that a provision giving copyright owners exclusive rights over the importation of copyrighted goods is subject to the limitations in Section 109 (A). On the ground that the Court found it immaterial that the importation of so-called "grey market" goods into the United States could affect a copyright owner's domestic sales market.⁸³

However, with regards to copyright goods made abroad, such as in the case, *Columbia Broadcasting System, Inc. v. Scorpio Music Distributors, Inc.* The imported goods in this case were lawfully produced by an authorized copyright holder in overseas, which means they are legitimate goods. The court held that the first sale defense is not available, and the goods were unlawfully imported back into U.S., even seller was authorized to produce goods abroad. The defense of first sale could apply to the copyright goods made abroad only when the goods have been sold in the U.S. by the copyright owner or with his consent⁸⁴. Section 602 (a) of U.S copyright makes goods acquired outside which then unauthorized import into US

⁸⁰ 17 U.S. Copyright Acts 109(A) (2000): in Intellectual Property and National Information Infrastructure Part I, A, 7,C

⁸¹ 17 U.S. Copyright Act 109(A)(b)(1) (2000)

⁸² *Ibid*

⁸³ 523 U.S. 135, 150-51 (1998).

⁸⁴ *DeBiccare U.S.A. Inc. v. Toys "R" Us, Inc.*, 84 F 3d 1134; 519 U.S. 873 (1996)

constitute an infringement of the exclusive distribution right. The court held that section 109(a) is not available to importer.⁸⁵

Although copyright ownership does not contain the right to exclude the "use" of copyrighted material per se⁸⁶, the right to exclude public display and performance is somewhat analogous.⁸⁷ A narrow first sale-like limitation exists for public display right, but not for the public performance right. That limitation allows the owner of a lawful copy of a copyrighted work to publicly display it, directly or by projection, to viewers present at the place where the copy is located. The idea is essentially the same as the aforementioned limitation on distribution control; the two can easily be considered together.⁸⁸

4.1.1.3 Summary

With strong export interests in copyright, it is not surprise that America would have banned parallel imports anywhere. According to U.S. law, the territorial distinction is obviously applies to the first sale rule. When it happens abroad, the sale of the legitimate produced work does not exhausted the exclusive right of distribution which still entirely belong to the copyright holder in the U.S.

4.2 Community exhaustion

The community exhaustion which in the context of the European Community, refers to the principle that once a particular copy has been put on the market within the European Community by or with the consent of the right-holder concerned, that copy can circulate freely in the Community, i.e. the right owner cannot prevent further the distribution of that copy in order Member States of the Community.

The Article 28 EC Treaty establishes the principle of free movement of goods that requires the cause such as the need of copyright protection cannot stand in the way of it. However, copyright as a form of property, Article 295 of EC Treaty elucidates that EC Treaty shall in no way prejudice the rules in Member States governing the system of property ownership, which requires acknowledge the right of copyright holder to control exploitation of his legislative property. In order to handle with this conflict, some kinds of copyright such as reproducing right and rental right may not be exhausted after first sale of article.

⁸⁵ 514 U.S. 1004 (1995)

⁸⁶ 17 U.S.C. S102(b) (2000) Since copyrights are not, by definition, utility oriented, see, a broad right to exclude "use" would make no sense

⁸⁷ Cahoy *Supra* Note 57

⁸⁸ *Ibid*

Besides that, in the context of EC, some scholars categorize the situation after first sale of copyrighted work into several kinds⁸⁹. Firstly, the copyright protected work marketed in an EEA State by or with the consent of the right owners in that State, and then imported by a third party into another EEA State. In the case of *Deutsche Grammophon GmbH v Metro-SB-Grossmarkte GmbH & Co.K.G*⁹⁰, a German company held a copyright on certain records that its French sales subsidiary marketed in France, those goods were later purchased by the defendant and imported back into Germany where competes with German authorized holder. The Court Said:

“If a right related to copyright is relied upon to prevent the marketing in a Member State of products distributed by the holder of the right or with his consent on the territory of another Member State on the sole ground that such distribution did not take place on the national territory, such as prohibition, which would legitimize the isolation of national markets, would be repugnant to the essential purpose of the Treaty, which is to unite national markets into a single market.

That purpose could not be attained if, under the various legal systems of the Member States, nationals of those States were able to partition the market and bring about arbitrary discrimination or disguised restrictions on trade between Member States.

Consequently, it would be in conflict with the provisions prescribing the free movement of products within the common market for a manufacturer of sound recordings to exercise the exclusive right to distribute the protected article, conferred upon him by him or with his consent in another Member State solely because such distribution such distribution did not occur within the territory of the first Member States.”

Secondly, articles marketed in an EEA State without the consent of the right owner, and then imported by a third party into another EEA country, in general, the local right owner will be able to prevent the importation⁹¹.

Turning to articles marketed outside the EEA, if they marketed with the consent of right owner, and then imported by a third party into an EEA country, the local right owner will generally be able to prevent import into an EC State⁹². The European doctrine of exhaustion of rights ...copies only put into circulation outside the EEA may not import into the EEA without authority.⁹³ In the case of *Micro Leader Business v Commission*⁹⁴, Micro leader (independent entity from Microsoft) imported the Microsoft software sold in Canada market and sold them in France. Microsoft France claimed its right to prevent distribution of the items had not been exhausted by the authorized sale of the items in Canada. The Court explained the Article 4(c) of the EC Computer Program Directive and concluded that “the exhaustion

⁸⁹ Sterling *Supra* note 2, p. 775

⁹⁰ C-78/70 (1971) E.C.R. 487; (1971) C.M.L.R. 631 ECJ

⁹¹ *Supra* Note 14

⁹² *Ibid*

⁹³ C. Colston and K. Middleton, *Modern Intellectual Property Law* (Cavendish, London, 2005) p. 341

⁹⁴ T-198098,(2000) E..C.D.R. 217, CFI

of rights takes place only if the products have been marketed in the Community by the owner of such rights or with its consent.... Without prejudice to the application of Article 86 of Treaty (prohibition of price-fixing)...it would have been a legitimate exercise of copyright by Microsoft⁹⁵". Last but not least, the local right owner has right to prevent articles which market outside the EEA without the consent of right owner imported by a third party into EEA States⁹⁶.

With regards to exhaustion of rights in relation to copyright, in general, the rule of exhaustion address like mentioned above, however decisions of ECJ are different in the view of different subject matters which are protected by copyright, what it termed the "specific subject matter" and the "essential function" of the copyright in question. In the case of *Warner Bros Inc. and Another v Christiansen*⁹⁷: The copyright holder of video films in both UK and Denmark markets sought to preclude the buyer of the lawful copies in UK "free and clear" for rental in the UK market from renting out the copies to Danish market. The videos imported from UK where at that time does not have a rental right in copyright into Denmark, there is a rental right, for video hire. The Court hold that without the harmonization of rental rights policy at the Union level, the Danish law would govern the right of the copies owner, therefore, the protection of Danish licensee against rental of video under Danish law on rental right was not contrary to principle of free movement of goods, Danish right holder has right to collect royalties from rental those videos imported from UK. In *Coditel SA v. Cine Vog Films*, a party without the authorization retransmitted in Germany a film public performance in Belgium by a license with the consent of copyright holder. Confronting the issue of exhaustion of film exhibition and broadcast right beyond the boundary of a country, the ECJ explained that the film industry is largely depends on the economic revenue earning from the public performance, so the copyright owner could re-assert his right against every public showing of the film.

According to above cases analysis, in general, in the Europe community, the restriction on the imported goods from non-EU Member States are not subject to the exhaustion rule, but briefly allow the exhaustion rule exists in the internal market of EU, such as referring to the distribution right. However, the certain characteristic of the copyright subject matter has an impact on the exhaustion issue in specific cases. A certain harmonized community law with regard to video rental right may need to be reached before the exhaustion doctrine could be applied. Similar with the performance right of film, the rental right constitutes a specific case for exhaustion analysis.

⁹⁵ *Ibid*, para 34.

⁹⁶ *Supra* Note 14

⁹⁷ C-158/86 (1988) E.C.R.2605; (1988) 3 C.M.L.R 684, ECJ

5 International Instruments

5.1 The TRIPS Agreement

5.1.1 The purpose and Article 6

With the increasing amount of trade from the copyright and entire intellectual property industry, and the need “to the mutual advantage of producers and users of technological knowledge and in a manner conducive to social and economic welfare, and to balance rights and obligation”⁹⁸, TRIPS agreement was designed as a part of whole package agreements under WTO (due to the different interests on the IP issue between the developed and developing countries, the harmonized international IP convention was hardly to reach, so that the developed countries gave up some interesting under textile or agriculture in exchange the compromise of developing countries on the IP issues), in order to extend the membership in international intellectual property right convention.⁹⁹

After the heated debate process, Article 6 of TRIPS has been finally reached to deal with the exhaustion issue as followed:

“For the purpose of dispute settlement under this Agreement, subject to the provisions of Article 3 and 4 nothing in this Agreement shall be used to address the issue of the exhaustion of intellectual property rights.”

According to the text of this Article, except that from blocking turn to DSM with regard to TRIPS, it is difficult to find the limitation on the Member’s freedom to regulate the exhaustion issue with regards to all types of intellectual property rights including copyright.¹⁰⁰

5.1.2 Negotiating history of Article 6

5.1.2.1 Pre-TRIPS Situation

Not only the exhaustion on the patent and trademark goods, but also the copyrighted works’ exhaustion doctrines have far away from being harmonized in the international community before the birth of TRIPS. It is interesting to review the negotiating process of the TRIPS Article 6, by

⁹⁸ Article 7 of TRIPS Agreement

⁹⁹ Papadopoulos, *Supra* note 45, p.48

¹⁰⁰ C. M. Correa, *Trade Related Aspects of Intellectual Property Rights-A Commentary on the TRIPS Agreement* (Oxford 2007), p. 78

doing so, we could observe the divergence of contracting parties on this issue, and on the other hand reflects the complex of this issue.

The interest on the copyright industry and parallel importing varies from country to country, and few systematic investigations and studies had been done on the potential influence of the different level exhaustion rule on international trade and economic development before the TRIPS negotiation¹⁰¹. Negotiating parties had not reached the consensus on in which level the copyright should be exhausted. In US, few decision had been made on the issue of the national or international exhaustion of copyrighted works; in the EU, the Member States maintained the different approaches to international exhaustion on copyrighted works¹⁰² (although under the TRIPS agreement and the negotiating process the EU has been treated as one contracting party¹⁰³); and contracting parties such as the Australia had considered the issue of international exhaustion on the copyrighted works¹⁰⁴.

5.1.2.2 Initial Proposals

The first step before the TRIPS to regulate the parallel imported goods is granting the legitimate status of the goods. In the 1988, according to the Compilation of Written Submissions and Oral Statement issued by the GATT Secretariat, “the parallel imports are not counterfeit goods and a multilateral framework should not oblige parties to provide means of action against such goods”¹⁰⁵, and similar observation had been made concerning the need to preserve right of parallel importation in connection with border measures and safeguards to protect legitimate trade.¹⁰⁶

In 1989, Canada made the proposal, in which it aimed at reaching the international exhaustion to the specific intellectual property goods.¹⁰⁷ Then in 1990, a proposal made from the U.S. to claim that “the exhaustion of right in one territory would not exhaust right elsewhere.”¹⁰⁸ The participants from the small countries expressed their concern about the right of importation, in the light of such right is not required in the Berne convention and might result in the trade distortion which against the intention of the TRIPS and itself Article 7 and 8.¹⁰⁹

¹⁰¹ UNCTAD-ICTSD, *Resource Book on TRIPS and Development* (Cambridge,2005) pp.92-117

¹⁰² *Ibid*,

¹⁰³ Footnote 3 of the Brussels Draft: for the purpose of exhaustion, the European Community shall be considered a single Party.

¹⁰⁴ In 1986, Australia Copyright Law Review Committee (CLRC) had considered whether the change on parallel importing was needed.

¹⁰⁵ Trade in Counterfeit Goods: Compilation of Written Submissions and Oral Statement, MTN. GNG/NG11/W23, 26 April 1988.

¹⁰⁶ UNCTAD-ICTSD, *Supra* note 103

¹⁰⁷ Note by the Secretariat, Meeting of Negotiating Group of 30 Oct.-Nov. 1989, MTN. GNG/NG11/W/68, 29 March 1989.

¹⁰⁸ Note by the Secretariat, Meeting of Negotiating Group of 2,4 and 5 April 1990, GNG/NG11/20, April 1990.

¹⁰⁹ *Ibid*

5.1.2.3 The Anell Draft

In the July of 1990, Lars E.R. Anell (the Chairman of the TRIPS Negotiation Group) presented a composite text that was taken from the various delegations' proposals to Negotiation Group.

In the text, it stated that: "... establish procedures according to which a right holder, who has valid grounds for suspecting that the importation ofpirated copyright goods... may take place. ...This provision does not create an obligation to apply such procedures to parallel imports."¹¹⁰

Although not specifically mentioned the copyright goods, but the comments on trademarked goods could have the analog understanding to the copyrighted goods, which provided that "right shall be subject to exhaustion if the trademarked goods or services are marketed by or with the consent of the owner in the territories of the PARTIES."

5.1.2.4 The Brussels Draft

In the Brussels Ministerial Conference, the draft text on the exhaustion had been transmitted as followed:

"Subject to the Provisions of Article 3 and 4 above, nothing in this Agreement imposes any obligation on, or limits the freedom of, PARTIES with respect to the determination of their respective regimes regarding the exhaustion of any intellectual property rights conferred in respect of the use, sale, importation or other distribution of goods once those goods have been put on the market by or with the consent of the right holder."

Compared with the final text on the exhaustion, this draft was trying to define the scope of the exhaustion that has a great impact on the copyrighted works on the ground that there are various rights under copyright with regard to various subject matters. There are considerable debates referring to the regulation on the scope of the exhaustion rule throughout the Uruguay Round.¹¹¹ Countries that are sympathetic for the international exhaustion rule did not wish to preclude the application of the doctrine to from certain areas, by the reason that a defined scope of the exhaustion limits the freedom to choose applying the exhaustion rule on the other subject matters of intellectual property protected rights.

5.1.2.5 The Dunkel Draft

¹¹⁰ Section 4; 15A, Status of Work in the Negotiating Group, Chairman's Report to the GNG, MTN. GNG/NG11/W/76.

¹¹¹ UNCTAD-ICTSD, *Supra* note 103

In the Dunkel Draft the final text has been encoded into the TRIPS Agreement as we can see today. As Mr. Adrian Otten summarized, the text of Article 6 reflects “a compromise between governments favouring an explicit recognition of national discretion in regard to exhaustion practices, including the choice of national or international exhaustion¹¹²”...not as the earlier proposal, came out the rule neither “for a specific rule providing rights against parallel imports in the copyright area”, nor the international exhaustion rule on the area such as trademarked goods. The final text touched upon the issue of exhaustion in the TRIPS and “both sides to the negotiations preferred the final formula.¹¹³”

5.1.3 Interpretation of Article 6

5.1.3.1 Dispute Settlement and the Scope of Article 6

Although the Article excludes the issue of exhaustion from being addressed for the purpose of dispute settlement under the TRIPS agreement, the words do not prevent the issue from being subject to other purposes under other instruments of WTO. As mentioned in the beginning of the TRIPS, the intention of TRIPS is to “to ensure that measures and procedures to enforce intellectual property rights do not themselves become barriers to legitimate trade”.¹¹⁴ The national copyright regulation may have the same effect as a barrier to the legitimate copyrighted works, and it is possible for a Member to claim that the national exhaustion that facilitates the copyright holder to block the parallel imports is not consistent with GATT rule, and the GATT panel could be involved into this issue.¹¹⁵ Therefore, there is a possibility that the issue of exhaustion could be subject to dispute settlement under the WTO rules. It is necessary to maintain the application of dispute resolution mechanism (DRM) of the WTO on the exhaustion issue, on the ground that the DRM was lacking the WIPO treaties, and it would provide the measure for the effective implementation of enforcement against the breach of TRIPS in order to protect the interest of parties involved in international trade.

¹¹² Oral description of negotiations from the Secretary to the Trade negotiating Group during Uruguay Round, at a 1998 meeting on the subject of exhaustion of rights and parallel importation, see *ibid*; also see Remarks of Adrian Otten in F.M. Abbott, Second Report to the Committee on International Trade Law of the International Law Association in the Subject of the Exhaustion of Intellectual Property Right and Parallel Importation, presented in London, July 2000 at the 69th Conference of the International Law Association, rev. 1.1.

¹¹³ *Ibid*

¹¹⁴ Preamble in the TRIPS

¹¹⁵ UNCTAD-ICTSD, *Supra* note 103: Exhaustion of Rights P104, under Article XI, GATT 1994, “No prohibitions or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export license or other measures, shall be instituted or maintained.”

By modification of the Brussels Draft, the question arises as to if the exhaustion may be applied to all exclusive rights, or only refer to certain scope of intellectual property was left to individual Member to determine at a national level. Though the Article 28¹¹⁶ seems to indicate that patent owner has exclusive right on importing that makes the Member unable to adopt the international exhaustion rule. However, the footnote of the “importing” states that right conferred is subject to the Article 6 that with regard to acts of commercialization or distribution of imported goods with the owner’s consent. While the Article does not further prescribe that how to determine the consent from the owner, it could be interoperated that the consent of owner depends on the Member’s attitude to the exhaustion. If Members have adopted the international exhaustion, the consent may affect the goods when it was placed on the market anywhere in the world.¹¹⁷

5.1.3.2 Application at the National Level

Besides the determination of the owner’s consent - the circumstance in which exhaustion may be deemed to have occurred; the Article has left the open to Members to interpret the exhaustion on copyrights according to national legislation or before the national court. In other words, the Article 6 provides that Members are free to incorporate the principle of international exhaustion into their national legislation, without breaching the TRIPS obligation. It has a significant meaning to the developing countries and small economies¹¹⁸. The primary objective for developing the freedom to application exhaustion rule at the national level is understood by some scholar as the balance that the WTO is trying to reach between the freedom of trade and the increased protection of intellectual property.¹¹⁹

What's more, the Berne Convention does not contain the importing right, and explicitly expresses the distribution right as an exclusive right to the author or artist. Article 8¹²⁰ of TRIPS guarantees the right of Member to adopt the national rule to prevent abuse of IPR by holders.

5.2 The WIPO Treaties

¹¹⁶ See Article 28 (b) “the subject matter of a patent is a process, to prevent third parties not having the owner’s consent from the act of using the process, and from the acts of: using, offering for sale, selling, or importing for these purposes at least the product obtained directly by that process.”

¹¹⁷ UNCTAD-ICTSD, *Supra* note 103, p.105

¹¹⁸ See a submission to the Council for TRIPS, IP/C/W/280, P6

¹¹⁹ Bronckers, The Exhaustion of Patent Rights Under WTO Law, *Journal of World Trade* 1998. P144

¹²⁰ Article 8 “Appropriate measures ... may be needed to prevent abuse of IPR by holders or the resort to practices, which unreasonably restrain trade or adversely affect the international transfer of technology.”

Besides the TRIPS Agreement, another set of international law with respect to intellectual property right is managed by World Intellectual Property Organization (WIPO).

However, exhaustion doctrine has not been explicitly expressed by any WIPO treaties¹²¹. The WIPO Secretariat has argued that a certain authorization of copyright holder in one country does not make the goods produced according to that authorization lawful in other countries, for example in Berne Convention, the Article 16 (seizure of infringing copies not necessarily infringing the copies in the country from which they are import) as well as the Article 13(3) concerning the sound recording.¹²² “The right of first distribution is an inseparable corollary to the right of reproduction.”¹²³ The right holders have to have the power to control the importation of copies in order to enjoy the right of the reproduction.

The only exception is Article 6(5) of the Treaty on Intellectual Property in Respect of Integrated Circuits (IPIC). It exhausts the exclusive right when a layout-design has been put on the market by, or with the consent of right holder.¹²⁴

Turning to the WIPO Copyright Treaty (WCT) and WIPO Performances and Phonograms Treaty (WPPT), the member states of both treaties determine their own exhaustion doctrine on the copyright subject matters, either international or national. The identical exhaustion rules are stated in Article 6(2) of WCT and Article 8 of WPPT as followed:

“Nothing in this Treaty shall affect the freedom of Contracting Parties to determine the conditions, if any, under which the exhaustion of the...right ...applies after the first sale or other transfer of ownership of the original or a copy of the work with the authorization of the author.”

5.3 Summary

“The benefits that might flow from allowing parallel imports to be blocked is insufficient to justify the potential inhibition of trade¹²⁵”, and the restriction of parallel imports of legitimate goods obviously constitutes the non-tariff barrier to trade and a direct contravention of the WTO or early

¹²¹ D. Gervais, *The TRIPS Agreement-Drafting History and Analysis*, (London Sweet&Maxwell, 2005) p. 115

¹²² Document prepared for the Committee of Experts on Possible Protocol to the Berne Convention, BCP/CE/II/2, March 1993, quoted by Ibid.

¹²³ *Ibid*

¹²⁴ Article6(5) of IPIC: “[Exhaustion of Rights] Notwithstanding paragraph (1)(a)(ii), any Contracting Party may consider lawful the performance, without the authorization of the holder of the right, of any of the acts referred to in that paragraph where the act is performed in respect of a protected layout-design (topography), or in respect of an integrated circuit in which such a layout-design (topography) is incorporated, that has been put on the market by, or with the consent of, the holder of the right.”

¹²⁵ Abbott, *Supra* note 61, p. 607

GATT rules. Nevertheless, under the strong push from some developed countries such as U.S. with huge interest in exports of copyrighted work for a global regime of national exhaustion, so far at the level of international instruments, none of them, neither the WIPO treaties nor the WTO TRIPS, finally could reach the international harmonized rule on the exhaustion doctrine.

Although so far none of international instruments can enshrine the international exhaustion on copyright issue, they neither list any particular obligation on it. The freedom is left for member states to decide their own policy. Even under the Berne Convention that implies the national exhaustion, the member states remain free to apply the Convention as they see fit.¹²⁶

Therefore, from the last decade of twenty century, Australia has promoted by the interest-related groups, after conducting comprehensive inquiries by establishing the special policy advisory bodies, the policy makers decided to reform the Australia copyright law in order to exhaust the distribution right of copyright protected works category by category. The following part of article will examine the copyright exhaustion reform in Australia..

¹²⁶ A.A. Yusuf and A. Moncayo von Hase, 'Intellectual Property protection and international trade: Exhaustion of Right Revisited', 127 *World Competition*, (1992), quoted by JAL Sterling, p. 114

6 International exhaustion- Australia Copyright Act

The copyright in Australia did not accept the exhaustion on copyrighted work in the beginning. Since 1968 when the Copyright Act has been published, for decades Australian copyright owners depend on this legislation to protect their economic exclusive privilege on a wide range of rights, including the right to reproduction, the right to translation, the right to perform, and the right to distribution and so on. These rights are essentially to provide the incentive to creative production and prevent the free-rider taking advantage with very low even zero cost.

Among all those articles listed in 1968 Copyright Act, to preclude the any parallel importation of copyright protected works into Australia, the Australian copyright owners were able to rely on two sections in this Act, which are Section 37 and Section 102, respectively on the infringement by importation for sale or hire of books and the Infringement by importation for sale or hire of copyright in other subject-matters. They state in the almost same words:

The copyright in a literary, dramatic, musical or artistic work is infringed by a person who, without the licence of the owner of the copyright, imports an article into Australia for the purpose of:

- (a) Selling, letting for hire, or by way of trade offering or exposing for sale or hire, the article;
- (b) Distribution the article:
 - (i) for the purpose of trade; or
 - (i i) for any other purpose to an extent that will affect prejudicially the owner of the copyright; or
- (c) By way of trade exhibiting the article in public;

If the importer knew, or ought reasonably to have known, that the making of the article would, if the article had been made in Australia by the importer, have constituted an infringement of the copyright.

Based on 1968 copyright Act, the Australian copyright owner was authorized wide range of protection that to some extent was over the boundary of protected copyright works is the main content of the article. The most typical case is *RA & A Bailey & Co Ltd v Boccaccio Pty Ltd*.¹²⁷ The case concerned the importation of authentic bottles of Baileys Original Irish Cream cocktail a liqueur manufactured in the Republic of Ireland and intended for the market in Holland. In this case, the Court denied the claim of trademark infringement by the sale in Australia with labels intended for

¹²⁷ *RA & A Bailey & Co Ltd v Boccaccio Pty Ltd*, 84 FLR 232; 4 NSWLR 701; 77 ALR 177; 6 IPR 279; 1986 WL 590688; Supreme Court of New South Wales

the Australian market, according to doctrine of exhaustion¹²⁸. The claim of copyright infringement succeeded on the basis of the copyright in the label, and as a result product bearing the label could be used as the ground on which the parallel trade had been prevented.

However, since last decade of twenty century, promoted by the interest-related groups, the policy makers decided to reform the Australia copyright law in order to liberalize the trade in copyright products. The reform has progressed in a stepwise fashion for individual product classes¹²⁹, conducted comprehensive inquiries by establishing the special policy advisory body facilitates voices and opinions from the various aspects.

6.1 1991 Copyright Amendment Act

6.1.1 Background

In 1983 the Attorney-General asked the Copyright Law Review Committee (CLRC) to consider whether the change on parallel importing was needed.¹³⁰

In 1988, CLRC has issued a report on the importation provisions of the 1968 Copyright Act. This report focused on a the critical question “which the Committee has had to consider is whether the importation provisions of the Copyright Act should be modified, so as to make it lawful to import articles which are parallel imports as distinct from articles which are pirate copies.”¹³¹ Facing the obstacles result from the protectionism and limited inquires, the report asserted that repeal of the restriction on parallel imports of foreign books will lead to cheaper price¹³² and increased availability of copyright material in Australia¹³³.

¹²⁸ *Ibid*, The exhaustion theory whereby once the trade mark owner has put his goods on the market his control is exhausted and the territorial theory which demands that the owner's rights in one jurisdiction must have no bearing upon those in another.

¹²⁹ L. Longdin, ‘Parallel Importing Post TRIPS: Convergence and Divergence in Australia and New Zealand’, 50 *International and Comparative Law Quarterly*, (2001) pp.54-89

¹³⁰ S. Carey, ‘Between Two Worlds: Australian Publishing on the Horns of an Import Dilemma’, LLC *Springer Science Business Media*, (2008) pp.156-164

¹³¹ CLRC, The Importation Provisions of the Copyright Act 1968, Conclusion P234, Para190,

¹³² Though it delacaer that to what extend the price will be inflencene by the reform is unable to predict. Australia Pice Surveillance Authority, Inquiry into book prices: final report, 1989. See Longdin *Supra* Note 131, it states Australia paid more for books and had a more restricted choice of titles, an outcome wich could only partly be attributed to market size or what one Autralia historian called ‘the tyranny of distance’. See S. Carey *Supra* Note 132, According to the Pice Surveillance Authority, Australians were paying 50 per cent more for their paperback fiction than Americans, and 12 per cent more than the British

¹³³CLRC *Supra* Note 133 Para 192, 193

6.1.2 1991 Copyright Amendment Act

In 1991, the Australia Parliament issued the Copyright Amendment Act 1991 to enable access to books that have been published overseas but are not available in Australia¹³⁴. Provided that copyright owners could guarantee supply works within 30 days after its first publishing or within 7 days the publisher notifies in writing that order would be filled within 90 days, the copyright owner retain exclusive right without exhaustion. Otherwise, as long as the book is non-infringing book that means a book otherwise than under a compulsory license, without infringing the copyright subsisting in any “work” or “published edition” in a country and not included an elimination list¹³⁵, the parallel importing of the book is allowed.

6.1.3 Impact of the 1991 Amendment

The Act was amended to facilities the Australian booksellers to parallel import copies of a copyright protected work if the authorized copyright holder-usually the publisher- in Australia fails to meet the certain requirements.

The rule such as 30 days no doubt provides an incentive to the publishers in Australia to release titles promptly to guarantee the copyrights on their titles. Otherwise, as before 1991, the publishers could pursue the Australia copyright on a foreign book and delay the release of the title. Therefore, in 1995, the Price Surveillance Authority (PSA) conducted a public inquiry on the effects of 1991 Amendment on the price and availability of books. According to that, the 1991 Amendment has improved distribution efficiencies and the speed with which most new releases became available in Australia.¹³⁶

As mentioned in the report submitted to PSA by Australia Copyright Council (ACC), the ACC claimed that they had no special knowledge about the price of books in Australia or comparisons with price overseas.¹³⁷ However, many commentators asserted that from 1989 to 1999, “a steady decline ‘in book price’ to a point where they are currently on average

¹³⁴ Australia Copyright Council (ACC), Price Surveillance Authority(PSA) Inquiry into the Impact of 1991 Amendments to the Copyright Act 1968 , Allowing Parallel Importation of Books in Certain Circumstances,1995 ; the books including paperback version where only the hard back version is available in Australia.

¹³⁵ The book does not mean: (a) a book whose man contain is one or more musical works with or without any related literary, dramatic or artistic work;
or (b) a manual sold with computer software for use in connection with software ;
or (c) a periodical publication

¹³⁶Carey *Supra* Note 132, P 159

¹³⁷ ACC *Super* note 136

cheaper here than in the UK or the US”¹³⁸. In the report, PSA favoured to a complete repeal of importation limitation without the restriction on parallel trade.

6.2 1998 Copyright Amendment Act

As mentioned above, Australia Government did not stop by only lifting the parallel importing restriction on the books. In 1998 Australia move to amend the Copyright Act to insert the “non-infringing accessory” and to allow parallel importing of sound recording.

6.2.1 1998 Copyright Act Amendment, NO. 104

This Amendment was aimed at the copyright on the labelling and packaging of imported goods. The label and some forms of package being an artistic work which is vested in one or other of the copyright owner is no disputes¹³⁹. However the copyright on them were used to as a course to restrict the parallel importing the same goods, such as in the *RA & A Bailey & Co Ltd v. Boccaccio Pty Ltd*. The Amendment NO. 104 has removed those temptation by inserting non-infringing accessory at subsection 10(1).¹⁴⁰

¹³⁸Carey *Supra* Note 132, footnote 4, Gallagher P, “Our bookshelves are among world’s best,” letter in *The Australian*, 30 June 2001. The ACCC’s evidence was “heavily criticised,” according to Jim Dwyer, Partner of Allens Arthur Robinson: “Senate passes Copyright Amendment (Parallel Importation) Bill—28 March 2003,” client briefing published by Allens Arthur Robinson. www.aar.com.au/publications

¹³⁹ *Supra* Note 129, *A Bailey & Co Ltd v Boccaccio Pty Ltd* Case P*241

¹⁴⁰ Australia Copyright, Act (Amendment), 30/07/1998, No. 104, WIPO CLEA, Article 44 C as followed ha been added into the Act.

44C : Copyright subsisting in accessories etc. to imported articles

(1) The copyright in a work a copy of which is on, or embodied in, a non-infringing accessory to an article is not infringed by importing the accessory with the article.

(2) Section 38 does not apply to a copy of a work, being a copy that is on, or embodied in, a non-infringing accessory to an article, if the importation of the accessory is not an infringement of copyright in the work.

6.2.2 1998 Copyright Act Amendment, NO.105¹⁴¹

The importation provisions in the Act allow owners of Australian copyright in a sound recording to prevent legitimate copies of that program from being imported except through distribution channels approved by the local authorized copyright holder. Due to the outcome of PSA inquiry that the Australian sound recording prices were higher than in other countries including the United Kingdom, the United States, Canada and New Zealand, Australia decided to allow parallel importing of sound recordings subject only to certain minimal limitation.¹⁴²

Although facing the fierce lobbying by the music industry, the Australia compromised with the “sweetened medicine”¹⁴³, no doubt the repeal of

¹⁴¹ Australia Copyright, Act (Amendment), 30/07/1998, NO. 105, WIPO CLEA, Article 44D as followed has been added into the Act.

44D Import of non-infringing copy of sound recording does not infringe copyright in works recorded

(1) The copyright in a literary, dramatic or musical work is not infringed by a person who:

(a) imports into Australia a non-infringing copy of a sound recording of the work; or

(b) does an act described in section 38 involving an article that is a non-infringing copy of a sound recording of the work and has been imported into Australia by anyone.

Note: In a civil action for infringement of copyright, a copy of a sound recording is presumed not to be a non-infringing copy of the sound recording unless the defendant proves it is. See section 130A.

(2) This section applies to a copy of a sound recording only if, when the copy is imported into Australia, the sound recording has been published:

(a) in Australia; or (b) in another country (the *publication country*) by or with the consent of:

(i) the owner of the copyright or related right in the sound recording in the publication country; or

(ii) the owner of the copyright or related right in the sound recording in the country (the *original recording country*) in which the sound recording was made, if the law of the publication country did not provide for copyright or a related right in sound recordings when publication occurred; or

(iii) the maker of the sound recording, if neither the law of the publication country nor the law of the original recording country (whether those countries are different or not) provided for copyright or a related right in sound recordings when publication occurred.

Note: Subsection 29(6) deals with unauthorised publication.

(3) In subsection (2):

owner of the copyright or related right in the sound recording means the owner at the time publication of the sound recording occurred.

(4) The copyright in a work a copy of which is on, or embodied in, a non-infringing accessory to a non-infringing copy of a sound recording is not infringed by importing the accessory with the copy.

(5) Section 38 does not apply to a copy of a work, being a copy that is on, or embodied in, a non-infringing accessory to a non-infringing copy of a sound recording, if the importation of the accessory is not an infringement of copyright in the work.

¹⁴² Longdin *Supra* Note 131, p. 25

¹⁴³ *Ibid*,

parallel importing restriction control the distribution of the sound recording legitimately produced overseas has a significant meaning¹⁴⁴.

6.3 Copyright Amendment (Parallel Importation) Act 2003

Software program has been put forward as next categories in the Act reform. In 2002, the parliament of Australia presented the Bill 2002 that aimed at amending the Copyright Act 1968 to enable the legal parallel importation and subsequent commercial distribution of computer software products. This Bill extended the application of the Amendment of the Act on sound recording, since from 1998, with the rapid development of cyber technology, the software products has proliferated which is protected by copyright with regard to international instruments such as TRIPS.

The provisions of the Copyright Act allowed a software holder to take action for infringement of copyright that is not in the exception list that including such as book and sound recording, where a person imports or subsequently commercially deals with imported copyright material of that software holder. According to the Explanatory Memorandum of the Bill 2002, “these provisions effectively allow these firms to charge higher prices for their products in the Australian market than in other major markets and possibly to restrict the range of goods entering the Australian market.”¹⁴⁵ By the conclusion that remove the provision to exhausted distribution right, the Industry Commission in a report recommended that Australia should allow the international exhaustion of distribution right on software.¹⁴⁶ Similar findings as on books and sound recordings, the Australian Competition and Consumer Commission found that Australia consumers had been paying more on the computer program than U.S. consumers had.

Therefore, the Copyright Amendment (Parallel Importation) Act 2003 emerged after a long debate, it removes the distribution right on software after the first sale from the exclusive right of copyright holder, and enable the parallel importing for commercial distribution in Australia. Further more, it uses regulation on the enhanced CD plug the loophole left by sound recording Amendment.

¹⁴⁴ The Australian IP Review Committee has recommended in its Interim Report 23 that restriction in parallel importation in the copyright legislation be repealed both as between types of copyright material and as between the industries and activities that rely on copyright protection and those that do not.

¹⁴⁵ *the Explanatory Memorandum of Copyright Amendment (Parallel Importation) Bill 2002*,

<<http://www.comlaw.gov.au/ComLaw/Legislation/Bills1.nsf/frame lodgment attachments/A1CEB4E578FFD484CA256F720030448E>> visited on 7 May 2009

¹⁴⁶ Industry Commission 1995 Report, Computer Hardware, Software and Related Service Industries

6.4 Bilateral Agreement - AUSFTA

Since the WTO rules grant the exception from the non-discrimination policy, it allows the creation the free-trade agreement when the members exchange a most extensive set of positive preferences that “is offered to one party is an effective act of negotiation discrimination as to another, and visa versa”¹⁴⁷. On the February 8 2004, the U.S. and Australia have reached the Australia-United States Free Trade Agreement (AUSFTA) that touched upon the copyright issue in the detailed intellectual property chapter¹⁴⁸. The U.S.’s willing to reach a free trade agreement with Australia on one hand is it’s continuation of bilateral trade policy¹⁴⁹, on the other hand, the Australia policy reforms such as on copyright raises as the impact on US trade, and the need to use trade and economic integration strengthen the military operation by Bush’s administration.¹⁵⁰ While Australia’s motivation to promote the trade agreement is more from the pressure, it feels the competition from Asia.¹⁵¹

With regard to the content of copyright in the AUSFTA, besides that both parties are required be subject to multilateral treaties such as WCT and WPPT¹⁵², the addition of the “TRIPS-plus” and “WIPO treaties-plus” obligations are worthy to pay attention. The criminal penalties have been added with regard to the distribution of encoded broadcast.¹⁵³ The achievement of the exhaustion from Australia copyright reform seems to be unscratched so far as by this chapter. However, AUSFTA safeguards the freedom of contract. It requires that economic rights in copyright be “freely and separately” transferable by contract, and person-acquiring copyright shall “enjoy fully the benefits derived from that right.”¹⁵⁴ This provision presents a number of different interpretations,¹⁵⁵ from the perspective of the exhaustion rule, there is possibility that it leaves the freedom of the copyright owner to draft the contract caters to the vertical distribution of copyrighted works.

¹⁴⁷ J.H. Mathis, *Regional Trade Agreement in the GATT/ WTO: Article XXIV and the Internal Trade Requirement*. (T.M.C. Asser Press, 2002), p.1

¹⁴⁸ Chapter 17 of AUSFTA

¹⁴⁹ See Andrew Stoeckel, David Pearce & Gary Banks, *Western Trade Blocs: Game, Set or Match for Asia-Pacific and the World Economy* 55 (1990) (discussing the various attempts by the United States to establish a trade agreement with Australia from 1980 to the early 1990s), quoted by R. Burrell and K. Weatherall, ‘Exporting Controversy? Reactions To The Copyright Provisions Of The U.S.-Australia Free Trade Agreement: Lessons For U.S. Trade Policy’, 259, *University of Illinois Journal of Law, Technology and Policy*, (2008) pp. 1-61

¹⁵⁰ G. White, ‘Free Trade as a Strategic Instrument in the War on Terror?: The 2004 US Moroccan Free Trade Agreement’, 59 *Middle E. J.*, (2005) p. 597-98

¹⁵¹ C. M. Dent, *New Free Trade Agreement in the Asia-Pacific* (Palgrave Macmillan, 2006) p.66

¹⁵² Chapter 17.1.2 of AUSFTA

¹⁵³ Chapter 17.7 of AUSFTA

¹⁵⁴ Chapter 17.4.6 (a) of AUSFTA, quoted by Burrell and Weatherall,

¹⁵⁵ *Ibid* p. 4

Although the United States Trade Representative (USTR) criticized that Australia's reform that allows the parallel importation of copyrighted goods¹⁵⁶, and there was a strong voice to against the continuation of this policy¹⁵⁷, the AUSFTA did not attempt to make the Australia's exhaustion rule of copyright being in line with the America's. As a matter of fact, from the perspective of the nature of free-trade agreement, rather than change the legislation about parallel importation in Australia, the U.S. should be responsible to internationalize the first sale doctrine in order to waive the interference with the free movement of goods- the rule that allows the copyright holder in a certain territory to control the import. Maybe that is the reason why the voice such as "text of the copyright provisions that the US had made significant gains"¹⁵⁸ can also be heard at the same time.

6.5 Summary

Australia has opted to gradually remove the parallel importing restriction by lifting the obstacles market by market, or on the basis that certain copyright protected products possess certain idiosyncratic feature.¹⁵⁹ Furthermore, in the AUSFTA, Australia remains its achievement from the copyright reform unscratched facing the strong pressure from US that strongly appeals to the national exhaustion. Even so, it is not proper to reach the conclusion that Australia is a country with open market, because it bans the parallel importation of all other categories of copyright works that not mentioned in Section 44 of Copyright Act. Films and DVDs for example, which take up considerable amount in the total annual profit of the entertainment industry, are still relied on the Act to prevent the local traders to import legitimate copies without the permission of Australian authorized copyright holders.

If the legitimate concern on the copyright reform is about the lack of competition or abuse of the monopoly power on the global price discrimination, the competition law rather than copyright law should handle this issue, and such concern could not justify the reform. The distribution right is entitled as exclusive right in the copyright that makes sure the right holder keep the advantage in the trade or market. However, the nature of the exclusive right is to benefit so that the copyright allows dissemination the works through the whole society in order to reap the benefits. The Copyright Act we see today is a compromising and processing middle way that separates the ability to control the after first sale from the underlying

¹⁵⁶ Commonwealth of Australia. Joint Standing Comm. on Treaties, Report 61: Australia-United States Free Trade Agreement 240, 2004 ; quoted by Burrell and Weatherall, p. 22

¹⁵⁷ See Andrew L. Stoler, Australia-US Free Trade: Benefits and Costs of an Agreement, in *FreeTrade Agreements: U.S. Strategies and Priorities* 95, 98 n.6 (Jeffrey J. Schott ed., 2004) (discussing multiple concerns about Australia's lesser protections for IP rights)

¹⁵⁸ Graham Greenleaf et al, 'Not a Fair Trade: Australia's TPM Protection and AUSFTA-Inspired Reforms' (2007) *UNSW Law Research Paper No. 2007-19*. Available at SSRN: <<http://ssrn.com/abstract=977118>> visited on May 31 2009

¹⁵⁹ Longdin *Supra* Note 131, p. 23

exclusive rights enjoyed by the copyright holders, in order to provide kind of balance rather than the limitation of competition. The balance here is between the various property interests of creators (including the commercial protection of their work) and the public interest in ensuring equity of access to this material.¹⁶⁰

¹⁶⁰ Ann Cunningham, Submission to the Productivity Commission commissioned study into the Copyright Restrictions on the Parallel Importation of Books, <http://www.pc.gov.au/data/assets/pdf_file/0004/85810/sub233.pdf>, visited on May 11 2009

7 National Exhaustion or International exhaustion

7.1 National Exhaustion or International exhaustion

By examining the international instruments, neither Berne Convention nor 1996 WIPO Copyright Treaty (WCT); WIPO Performance and Phonograms Treaty (WPPT) nor the TRIPS Agreement explicitly expressed the permission or the prohibition of the parallel importing. They all left the free space for a member state or a signatory country to decide their domestic legislation on the conditions, under which the exhaustion of the right of distribution applies¹⁶¹.

The rules seem to be ambiguous, and WIPO and WTO seem to hesitate to rule on the exhaustion issue, especially the copyright. Such intent may be result from the worries that any creative interoperation that break through existing instrument, to the contrary, it may fail to impose the restriction on the member countries with respect to their ability to rule independently on this issue.¹⁶²

Due to the liberal attitudes from the international instruments, and the ambiguous interpretations of rules on the exhaustion issue, the exhaustion rules are far away from being harmonized. The rules are various from country to country. Comparing with the rule in U.S. and E.U., the Australia exhaustion regulation on categories of copyright right works liberalizes the restriction of parallel importing, which are more appealing to the international exhaustion. In Japan, the case law makes Japan considerable more open than U.S. to parallel importation¹⁶³. Few developing countries has the policy puts the restriction on the parallel importation¹⁶⁴. It is worthy to mention that some developing countries only allow one national distributor in its territory.¹⁶⁵ Therefore, it makes the reimport by other competitors impossible. In May 1998, the government of New Zealand removed all restrictions on the parallel importation of copyright goods¹⁶⁶. It

¹⁶¹ See Article 6 in TRIPS Agreement, and Article. 6(2) of the WCT and Arts. 8(2) and 12(2) of the WPPT

¹⁶² M. Bronckers, 'The Exhaustion of Patent Rights under WTO Law', 32:5 *Journal of World Trade*, (1998) pp.137-159

¹⁶³ Abbott *Supra* note 61,

¹⁶⁴ K. E. Maskus and Y. Chen, 'Vertical Price Control and Parallel Imports', Paper presented at the International Seminar on International Trade, (2000) (Cambridge, MA: National Bureau of Economic Research, 5 June)

¹⁶⁵ *Ibid*

¹⁶⁶ In response, the United States initiated a Special 301 'out of cycle' review of New Zealand (United States Trade Representative, 1999). American trade authorities professed

According to the table from Maskus in 2000 as follows, it shows that Australia, Japan and India to some extent are embracing the international exhaustion as well.

Summary of Exhaustion regimes¹⁶⁷

Country	European Union	United States	Japan	Australia	India
Copyright	Community exhaustion	National exhaustion	International exhaustion except for motion pictures	National exhaustion except for compact disk and books	National exhaustion with exceptions

Sources: National Economic Research Associates (1999) and International Intellectual Property Alliance (1998)

What's more, freedom to choose the exhaustion doctrine in the international instruments should not only be simply interpreted as the freedom to choose between international exhaustion and national exhaustion, but the freedom to choose what form of international exhaustion as well. International exhaustion can have more than one fixed model, given that the diverging views and interests of different national government on this issue. The national government should have the right to choose application of international exhaustion on certain categories subject matters and based on various reasons according to the TRIPS and WIPO treaties with the aim of increase the distribution of knowledge. Taking the instance of New Zealand, after changed its policy, it reduced consumer prices of music compact discs and books, reckoned perhaps 20–30 per cent more expensive in New Zealand than in the U.S.¹⁶⁸

The discrimination price could be taken as an consideration to reform law into international exhaustion in some countries, but it could not persuade all countries to accept the same international exhaustion on copyright. Given that facts such as the artistic and cultural nature of works are various, the harmonization of exhaustion on copyrighted works may be difficult to achieve¹⁶⁹. Due to those natures of copyrighted works, they are deemed to be of national cultural significance, unless there is a homogenized culture where commodification and free trade are dominant value, which is impossible to realize so far. Therefore, that substantial harmonization of national copyright law may be difficult to reach as well.¹⁷⁰

the concern that import deregulation would make it difficult to prevent imports of pirated compact discs. However, major music companies recognized that their ability to enforce high retail prices in a segmented New Zealand market would be impaired. See *Ibid* p. 1274

¹⁶⁷ M. Keith E, 'Parallel Imports', 9 *The World Economy*, (2000) pp. 1269-1284

¹⁶⁸ The Research of New Zealand Institute of Economic, 1998

¹⁶⁹ P. Samuelson, 'Implications of the Agreement on TRIPS for Cultural Dimensions of National Copyright Law', 23, *Journal of Cultural Economics* (2000), pp. 95-107

¹⁷⁰ *Ibid*

7.2 The Contractual arrangement

The Japan allows parallel importation in patented and trademarked goods unless the goods are explicitly barred from parallel trade by contract provisions or unless their original sale was subject to foreign price regulation.¹⁷¹ Although Japanese Law does not list the contractual arrangement as the exception in the parallel importation explicitly, it remains us that contract may be used as a way to preclude the international exhaustion rule. The copyright owner could set clauses that limit the circulation of the protected works in the distribution contract with the local distributor.

However, there is one obvious drawback of this method. It is feasible only if there is few distributor or licensee. As pointed out by Posner, “widespread distribution of a copyrighted work through middlemen is necessary to generate an adequate return to the author”¹⁷². However, the distribution prohibition through the contract could not apply to all the consumers, on the ground that the copyright owner could not have a contract with each potential consumer of copies. Even the copyright owner manage to make it, it may be costly to enforce it.

Similar example could be found in some developing countries’ parallel importation regulation. Several developing nations have laws permitting only one national distributor for products imported under the copyright¹⁷³. Some scholars worry that it can be used efficiently to ban the parallel imports.¹⁷⁴ The only one national distributor has difficulty to enforce his contract obligations to each potential consumer.

Therefore, more and more multinational firms are active to acquire their distributors or establish their own distribution markets, rather than work with independent wholesalers.¹⁷⁵

7.3 Exhaustion in Cyber Environment

With the rapid development of information technology, the cyber environment becomes an area should not be ignored. The digital technology has, at least, two significant meaning to the copyright exhaustion issue.

¹⁷¹ Maskus *Supra* note 169

¹⁷² Posner *Supra* note 39, P 43

¹⁷³ Maskus *Supra* note 169, p. 1273

¹⁷⁴ *Ibid*

¹⁷⁵ Raff, Horst and Nicolas Schmitt, ‘Endogenous Vertical Restraints in International Trade’, 49: *European Economic Review* (2005), pp. 1877-1889; Raff, Horst, and Nicolas Schmitt, ‘Why Parallel Trade May Raise Producers’ Profits’, *Journal of International Economics* (2007)

Firstly, the huge amount of workload to produce an advanced digital program is far beyond single person's knowledge ability, in other words others' contribution to a piece of work is essential. Referring to a country, without the updating knowledge or lack of effective distribution of related knowledge could delay its improvement of certain industry in related area. Secondly, the internet and the nature of digital work including the computer program enable the distribution cross the national boundary much easier. It reduces large amount of implementation of international exhaustion.

In the TRIPS agreement, the computer program is eligible for the protection of copyright¹⁷⁶. In the cyber environment, the digital product such as computer program may be examined with regards to criterion that if the product is present in the form of material object. If it just purely relies on the online service, according to that, digital product that could be divided into three groups, offline use in material works with material medium; online use in material works with material medium and online use in material works without material medium.

As a form of copyrighted work, it is not easy to answer how to establish the exhaustion rule on the digital product especially when it involves with the internet. It is suggested that the rule of the exhaustion should apply on internet with a condition that author would have a monopoly for the installation of his work on the Internet but could not thereafter prohibit unauthorized uses over the network.¹⁷⁷ On the ground of that, once an author has authorized the installation of his work on the network, he loses control over its exploitation given the possibility available to users of copying it and of transferring it to other serves.¹⁷⁸

The computer program in the material form, typically in the form of CD-ROMS, is subject to copyright law much similar the traditional copyrighted work. The traditional exhaustion is subject to the distribution right by the reason that in civil-law countries, the right over things enjoys the priority, when the ownership of material object conflicts with the distribution right. So the distribution right exhausts after its first sale. Therefore, in the cyber law exhaustion doctrine could be applied after the sale of digital copies that provide the offline multimedia service, because the principle of exhaustion is tied to an actual sale, which means the right holder must definitely lose any possibility to dispose of that particular copy.

Whereas, the right holder of online service is not loss any possibility to dispose the copy, there are offer of service rather than sales of material objects¹⁷⁹. There is no exhaustion, not even when the bits lawfully are

¹⁷⁶ "Computer programs, whether in source or object code, shall be protected as literary works under the Berne Convention (1971)." Article 10 paragraph 1 of TRIPS

¹⁷⁷ Jerome Passa, 'The Protection of Copyright on the Internet', 5 *Perspectives on Intellectual Property*

¹⁷⁸ *Ibid*

¹⁷⁹ See Loewenheim and Schricker, quoted by Michael Lehmann, 'Digitization and Copyright Agreements', 8 *Perspectives on IP*, p. 202

copied to the receiver's hard drive, or when the user lawfully makes a material copy.¹⁸⁰ If there is no first sale, obviously the exhaustion should not applied.

Under the EU Law, the principle of the free movement of goods only applies to material copies, and it could not extend to on-line transmissions that involved no material medium. Para. 19 of the Preamble of the proposed E.U. Directive of December 10,1997 clearly states: the question of exhaustion does not arise in the case ofon-line service ...every on-line service is in fact an act which will have to be subject to authorization where the copyright or related right so provides. With regards to online database, European Directive 96/9 (33) states that:

“Whereas the question of exhaustion of the right of distribution does not arise in the case of on-line databases, which come within the field of provision of services; whereas this also applies with regard to a material copy of such a database made by the user of such a service with the consent of the rightholder; whereas, unlike CD-ROM or CD-I, where the intellectual property is incorporated in a material medium, namely an item of goods, every on-line service is in fact an act which will have to be subject to authorization where the copyright so provides.”

For the online-service the author could decide further distribution of his article¹⁸¹, as long as there is no first sale of material works without material medium.

Most computer software is too big to finish by one programmer, the cooperation to finish and the modification to the program need to access to the source code of the program. The source code is the code in human language, which through the compiler translates into executable code by computer in order to direct computer to perform particular tasks. Open source program refers to the program in which the source code is open to access by anyone who is interested in observation and modification. There is a prerequisite to adopt the open source into the program (so called open source software) is a license approval, in which the software should be free to access and distribute. To some extent, the open source license exhausts the distribution right of computer program that based on open source. Since the distribution in the internet has beyond the boundary of territory, the open source license exhaustion is the international exhaustion.

¹⁸⁰ *Ibid*

¹⁸¹ *Ibid*

8 Conclusion

No one will doubt that the value brought by the books and any other forms of copyrighted work to the accumulation and enhancement of knowledge to all human-being. Neither doubt one the crucial role the copyright law plays. The role tries to maximize the completely social value results from each signal piece of art.

For example, the U.S. Constitution grants Congress the power to enact copyright laws in order to “promote the progress of science and useful art.”¹⁸² The rewards designed to encourage the creator is used to exchange for allowing the public access to the creative but protected work. According to Justice Stevens’s comments in *Sony Corp. of America v. Universal City Studios, Inc.*, “the monopoly privileges that Congress may authorize are neither unlimited nor primarily designed to provide a special private benefit. Rather, the limited grant is a means by which an important public purpose may be achieved.”¹⁸³ Moreover, Justice Stewart described the basic purpose of the Copyright Act as follows¹⁸⁴:

“Creative work is to be encouraged and rewarded, but private motivation must ultimately serve the cause of promoting broad public availability of literature, music, and the other arts. The immediate effect of our copyright law is to secure a fair return to an “author’s” creative labour. However, the ultimate aim is, by this incentive, to stimulate artistic creativity for the general public good.”

With regard to copyright law, even those countries with civil tradition, so called the law of author, the protection granted to the authors is the method for providing the incentive to disclose the creative work to the public, but not the method to guarantee the “ultimate aim” for the “general public good”. To reach the effective and sufficient dissemination of the creative work to public, the mechanism of distribution in copyright law is irreplaceable.

The distribution beyond the physical boundary to another territory, as the reason to charge more to the legitimate copyrighted work, obviously can not be “effective” in term of knowledge dissemination; the limitation of distribution to certain geographical location neither fail to be “sufficient” dissemination. The national exhaustion’s setback to knowledge dissemination is increasingly evident in the globalised era.

The information revolution facilitates the possibility of effective and sufficient dissemination in the international context, from the both technical

¹⁸² Hughes, *Supra* note 8, p. 390

¹⁸³ *Sony Corp. of America v. Universal City Studios, Inc.*, 464 U.S. 417, 429 (1984)

¹⁸⁴ *Twentieth Century Music Corp. v. Aiken*, 422 U.S. 151, 156 (1975) ; also see *Mazer v. Stein*, 347 U.S. 201, 219 (1954)

and implemental perspective¹⁸⁵. Moreover, the international instruments enable the freedom of member to choose the international exhaustion in national legislation.

Those who in favour of status quo argue that things work well as they are, either are the publishers who are trying their best to reap the maximum benefit from each market, or are the local distributors those who are worried the open market will bring the competition. Due to the lack of statistic research, and various situations from the country to country, no one has the capability to decide the universal rule to solve all problems related to exhaustion rule in copyright, maybe that's the reason why the TRIPS leave this free to interpret.

However, it is not implied that status quo actually works well in all countries, where have national exhaustion rule in their copyright legislation, both developing countries and developed countries. The tailor-made survey and analysis need to be done in each country that pay number of money on import copyrighted works, in order to provide evidence that is more adequate to policy makers. While in the common law countries, the judge can depend on the case law tradition to influence the exhaustion regulation, after all they are person who are supposed to the "ultimate aim" better.

The article is not aiming at whether copyright protection, as a whole system is desirable or not, but how to adjust this system such as exhaustion rule to full fill the needs of the original intention of copyright system. The country should re-examine the national copyright industry to see if implantation of national exhaustion may really to reach the "ultimate aim" for the "general public good", even although that purpose might be suffered frustration from other aspects of legislation. Such as in the contract law, the contract could be used to control the vertical dissemination between the copyright owner and local distributor, furthermore, in some cases, the limitation to dissemination of knowledge is beyond the IP law. For example, in China "the Chinese General Administration of Broadcasts, Films and Televisions issued on April 1 a new regulation requiring that all the videos communicated or shared on any website be licensed by the authority, irrespective of whether a website has acquired the copyright license."¹⁸⁶

Since the Berne Convention as early as 1886, internationalisation of copyright law is progressively realization, and this tendency is going on. The international exhaustion rule functions the "ultimate aim" for the "general public good", in other words, the distribution of knowledge and improve the human well-being, it cannot be the exception as well.

¹⁸⁵ See the Chapter 7.3 in this article.

¹⁸⁶ A2knetwork, the 2009 IP-Watch Report. <<http://a2knetwork.org/sites/default/files/ip-watchlist09.pdf>>, visited on May 3 2009

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