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**Digital Exhaustion: Furthering Social Justice  
in a Streaming-Dominated Copyright Ecosystem**

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*Extended Abstract (WORK-IN-PROGRESS)*

***ON BALANCE***

The role of copyright law in furthering social justice is blurred. On the one hand (and primarily), copyright law aims to guarantee a more or less exclusive protection for the benefit of creators and other contributors to the creative process (e.g. publishers, producers). On the other hand, copyright law also intends to strike a fair balance between the interests of various stakeholders, both for the benefit of individuals and the society as a whole. Such balancing tools include e.g. various limitations and exceptions (including the fair use doctrine in the US), the limited term of protection, procedural and fundamental rights based safeguards. Most often, however, these balancing tools remain “objective” in nature, and apply to all members of a given class of stakeholders (e.g. rightholders, licensed or free users, consumers etc.). Copyright norms (and, occasionally, the lack of exclusive rights) often further socially desirable goals, e.g. strengthening the access to and preservation or dissemination of cultural goods; supporting creative re-uses of contents etc. These norms nevertheless lack “social justice” perspectives.

In my presentation, I am going to focus on one of the exclusive rights granted to rights holders, namely, the *distribution right*; and one of the specific limitations to that right, namely, the *first sale or exhaustion doctrine*.

***ON THE POLICY CONSIDERATIONS OF THE DOCTRINE OF EXHAUSTION***

The doctrine of exhaustion is based upon three primary policy objectives: the superiority of property rights over copyrights, the reward theory, and the restraint of rights holders over market control.<sup>1</sup>

It is now generally accepted that property rights of lawful acquirers take precedence over copyrights, if it comes to the tangible copies of protected subject matter.<sup>2</sup> As the US House of Representatives stated, after the enactment of the US Copyright Act of 1976, “the copyright owner’s exclusive right of public distribution would have no effect upon anyone who owns ‘a particular copy or phonorecord lawfully made under this title’ and who wishes to transfer it to someone else or to destroy it.”<sup>3</sup>

The superiority of property rights gained further reinforcement with the reward theory. According to the reward theory, the rights holder is able to freely set the initial purchase

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<sup>1</sup> See Puig (2013) 162–170 regarding these three policy considerations and their erosion.

<sup>2</sup> *Paul Edmond Dowling v. United States*, 473 US 207 (1985) 216–217; Schricker (2006) 33–43; Loughlan (2007) 402; Reh binder (2008) 2; Wenzel and Burkhardt (2009) 22–23; Fagundes (2010) 652–705.

<sup>3</sup> H.R. Rep. (1976) 79.

price of copies of their work, as fair reward for the transfer of ownership, although the rights holder is not entitled to any further reward related to subsequent acts of distribution.<sup>4</sup> The reward theory has been extended by the ECJ to include the digital domain. In *UsedSoft*, the court noted that exhaustion might apply “if the first sale of the copy of work concerned enabled the above stated rightholder to acquire a just reward.”<sup>5</sup>

Both of the aforementioned policy considerations closely relate to the third, namely, that the copyright holder does not have and, in the sense of competition law, should not have the chance to fully control the secondary market.<sup>6</sup> Exhaustion inevitably guarantees that rights holders cannot control all forms of distribution and thus excludes the emergence of absolute monopolies. This anticompetition policy argument can be effectively traced in the EU, where the acceptance of the doctrine of exhaustion shares a causal relationship with the intention of strengthening the internal market and protecting the free movement of goods.<sup>7</sup>

These primary policy considerations are further supplemented by a number of secondary, or indirect, considerations.<sup>8</sup> Commentators unanimously agree that the mere existence of the doctrine of exhaustion makes it easier to acquire copies, due to their affordability (as it results in the decrease of retail prices) and their availability (as it maintains access to works being permanently or temporarily withdrawn from the primary channels of the market). In addition, exhaustion supports the preservation of cultural heritage.<sup>9</sup> Without the doctrine of exhaustion, culturally important contents could have potentially been lost from society forever, after the initial distribution is terminated by the rights holders.

Commentators noted that exhaustion ensures the proper functioning of consumer protection law: e.g. by the transparency of transactions,<sup>10</sup> respecting the privacy of consumers,<sup>11</sup> or guaranteeing that the consumer expectations (based on the language of an agreement) are met.<sup>12</sup> Furthermore, the competition generated by secondary markets triggers more innovation by rights holders. Indeed, any overprotection of copyrights and significant restrictions on secondary markets can chill innovation by users and

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<sup>4</sup> The UrhG that codified exhaustion for the first time in Germany designated the reward theory as the leading policy consideration of the principle. Compare to Walter and von Lewinski (2010) 135, note 226. On the *Belohnungstheorie*, see further Reimer (1972) 225–226; Röttinger (1993) 94; Puig (2013) 162.

<sup>5</sup> *UsedSoft v. Oracle* (2012) para. 63.

<sup>6</sup> Schack (2005) 180; Targosz (2010) 343.

<sup>7</sup> In *Théberge*, the Supreme Court of Canada took a similar stance against absolute control by rights holders. Compare to *Théberge v. Galerie d'Art du Petit Champlain Inc., et al.*, [2002] 2 S.C.R. 336, 2002 SCC 34, para. 37. On the decision, see de Beer and Tomkowicz (2009) 12–13; Ghosh (2013) 38–39; Crowne (2015) 802.

<sup>8</sup> On these secondary or indirect policy considerations, see Reese (2003) 585–610; Perzanowski and Schultz (2011) 894–901; Serra (2013) 1774–1781; Puig (2013) 160–162; Shinall (2014) 376; Reis (2015) 189–194; Katz (2015) 109–117; Rub (2015) 773–795; Kerber (2016) 153–156. These considerations were discussed by Advocate General Szpunar in his Opinion in the *Tom Kabinet* case. See: Case C-263/18, *Nederlands Uitgeversverbond and Groep Algemene Uitgevers v. Tom Kabinet Internet BV and Others*, Opinion of Advocate General Szpunar, 10 September 2019, EU:C:2019:697, para. 80–96.

<sup>9</sup> Compare to e.g. Mulligan and Schultz (2002) 472; Kaufman (2009); Katz (2015) 110.

<sup>10</sup> Hess (2013) 1971–1978; Trampuž (2016) 175–177.

<sup>11</sup> Kerber (2016) 165.

<sup>12</sup> Oprysk and Klein (2020).

competitors of rights holders.<sup>13</sup> The doctrine also effectively mitigates against the effects of technological “lock-in,” by allowing for a more relaxed enjoyment of works. This is done through decreasing the reliance on the unique formats and channels of access applied by manufacturers, distributors, and aggregators.<sup>14</sup> Exhaustion can ultimately facilitate competition among digital platforms and other service providers.<sup>15</sup> This seems to be plausible in the digital domain but seemed to be a valid claim in the pre-Internet era, too.<sup>16</sup>

### ***ON THE DIGITAL***

The problems associated with the doctrine of exhaustion have grown concurrently with the emergence of digital technologies, in particular with the development of the Internet. Many commentators foresaw the current dilemma confronting digital exhaustion, as to whether the doctrine of exhaustion is applicable to contents (digital files) that were originally sold over the Internet.<sup>17</sup> Indeed, the emergence of “digital exhaustion” was triggered by digital marketplaces (especially iTunes almost two decades ago) gaining commanding ground in the dissemination of copyright protected contents. The dilemma posed by the tectonic changes in the consumption of cultural goods challenges the preexisting set of economic rights, the freedom to provide services, the free movement of goods, as well as the traditional business models of the copyright industry.

The policy arguments introduced above have their roots in the analog world, prior to the invention of digital technologies and, crucially, the Internet. The drastically altered landscape we face today has prompted certain commentators to reason that the doctrine of exhaustion shall only apply if several supplementary requirements are met. These are as follows: that the copies sold by the rights holder and resold by the acquirers shall not compete (rivalrousness and *Rivalität*), the acquirer of the original copy shall not maintain exclusive control over the copy of the work (excludability and *Exklusivität*), and the quality of the copies shall deteriorate over time (consumability and *Abnutzbarkeit*).<sup>18</sup> It is doubtful whether these requirements can easily be met in the digital age. In light of this, jurisprudence and academia, in several countries, have been reluctant to apply exhaustion to digital content. 21<sup>st</sup> century copyright laws (as well as rightholders and courts) seem to be, however, less ready to embrace a “digital exhaustion doctrine”. I argue and seek to demonstrate that the doctrine *should* be expanded to the digital environment. I believe that the policy basis and the goals of the

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<sup>13</sup> Wolfgang Kerber noted that “permitting too far-reaching restrictions in regard to the resale and use of digital copies might stifle and block too much further valuable innovation activities, because then the users/innovators might need too often the consent of the copyright owners.” See Kerber (2016) 164.

<sup>14</sup> Region codes used on DVDs are such classic access control DRMs that lead to the “lock-in” of lawful acquirers of the original DVDs. See further Yu (2012) 187–264.

<sup>15</sup> Kerber (2016) 164.

<sup>16</sup> Aaron Perzanowski and Jason Schultz have shown that several years prior to, and following, the codification of the first-sale doctrine in 1909, US courts allowed for the creative reinterpretation or transformation of the purchased copies as well as the creation of new material objects (e.g., rebinding lawfully sold copies of works). See Perzanowski and Schultz (2011) 912–922.

<sup>17</sup> See Koehler (2000); Gaubiac (2002) 10; Cook (2010) 118–120. See further the European Commission’s analysis in COM(96) 568, 17–19; and Advocate General Kokott’s Opinion in *Football Association Premier League Ltd and Others v. QC Leisure and Others*, Joined Cases C-403/08 and C-429/08, ECLI:EU:C:2011:43, paras. 184–188.

<sup>18</sup> Capobianco (2013) 409–413; Zech (2013) 376–377.

doctrine remain valid in a digital 21<sup>st</sup> century, too. Control over lawfully accessed copies of protectable expressions by their acquirers is desirable.

Denying the existence of a digital first sale doctrine might be dogmatically easy. The dominance of streaming services over the market of tangible copies also tends to speak against such a doctrine. Indeed, any argument in favor of the digital avatar of the exhaustion doctrine requires verbal gymnastics. The spread of streaming services and the denial of a digital first sale doctrine nevertheless tend to replace one of the most historic and fundamental right of humans, namely, ownership interests with licenses. Such changes are socially undesirable. This presentation aims to highlight the goals and policy arguments in favor of a digital first sale doctrine. The application of the doctrine in the digital domain might guarantee social justice for the class of “lawful users” to preserve their rights to effectively control the fate of copies “purchased” in a digital format.

### ***SPEAKING TO THE WALL***

In the first edition of my book “Copyright Exhaustion”, I argued that the digital exhaustion conundrum might be solved by the introduction of some normative changes to the international framework/backbone of the exhaustion doctrine; and by the consequent use of some technological measures.<sup>19</sup> As of now, currently working on the second edition of that monograph, I argue that the solution lies mainly in reconsidering the policy grounds and – especially – putting greater emphasis on the doctrine’s social (rather than normative) role.

In the *Tom Kabinet* case, the ECJ concluded that the resale of lawfully acquired e-book by an online marketplace runs afoul of the existing norms of copyright law. Likewise, the Second Circuit has confirmed the trial court’s denial of ReDigi’s business model for the resale of lawfully acquired iTunes tracks, even if the model was supported by (an almost perfect) forward-and-delete technology.<sup>20</sup> Furthermore, following a long and windy legislation process, the European Parliament and of the Council has voted against introducing a “hybrid online sales” contract within the frames of the Directive 2019/770.<sup>21</sup> And the list might be continued by other examples. This, almost full, disregard of the policy considerations of exhaustion makes me, on the one hand, feel that it is like talking to the walls, when it is about the “balance” in the digital age, and, on the other hand, that the solution to the said conundrum shall lie elsewhere (than in pure normative changes and technological measures).

### ***SIX NOTES/RECOMMENDATIONS TO REBALANCE EXHAUSTION IN THE DIGITAL AGE***

#### **#1**

AG Szpunar echoed a recurring argument in his Opinion to the *Tom Kabinet* case, when he declared exhaustion obsolete in the age of streaming and online subscriptions.<sup>22</sup> There is no doubt that online consumption of copyright-protected contents tend to be

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<sup>19</sup> Mezei (2018) 158-165.

<sup>20</sup> Capitol Records, LLC v. ReDigi Inc., 910 F.3d 649.

<sup>21</sup> Directive (EU) 2019/770 of the European Parliament and of the Council of 20 May 2019 on certain aspects concerning contracts for the supply of digital content and digital services.

<sup>22</sup> Case C-263/18 (AG Opinion), para. 95.

more access-based rather than “ownership-based”. Nevertheless, a significant amount of contents is still available for download and purchase; and that is true for almost all sectors of the copyright industry. Consequently, the need to address the resale of lawfully acquired copies of protected subject matter cannot be ignored yet.

#2

In light of the rulings mentioned above, the doctrine of exhaustion can practically lose its relevance in the online environment. Is such castration of the doctrine really in the interests of the society?<sup>23</sup> Would it not be wiser to force/keep competition between the rights holders and newcomers in order to guarantee the best available services for the benefit of the whole society?<sup>24</sup>

#3

Yves Gaubiac noted as early as in 2000 that the dematerialization of works and the advancement of online uses made it necessary to appropriately categorize the supply of digital contents via the Internet. The importance of such categorization is great, as it can directly affect the fate of the doctrine of exhaustion.<sup>25</sup> The same opinion was expressed by Advocate General Kokott in *FAPL*.<sup>26</sup> The CJEU seemed to be unable to sidestep the service versus goods dichotomy in *Tom Kabinet*. Admittedly, as indicated above, the existing norms do not allow for a “hybrid model” of online contracts. A consumer/end-user oriented approach, which provides “copyright benefits” (in this case, the mere exclusion of the loss of the doctrine of exhaustion) in case they conclude an online contract for the provision of digital contents representing protectable subject matter, would be the most reasonable and balanced solution to the stalemate of the service versus goods dichotomy.

#4

In *Tom Kabinet*, AG Szpunar concluded that “although there are strong reasons for recognising the rule of exhaustion of the right of distribution in the case of downloading, other reasons, however, at least as strong, are opposed to such recognition. Thus, the weighing up of the various interests involved does not cause the balance to come down in a different way from that which follows from the letter of the provisions in force”.<sup>27</sup> No doubt, balancing various interests is a troublesome and challenging task – and therefore a subjective one as well. With full respect to AG Szpunar’s detailed analysis of the policy considerations, I disagree with such a conclusion. Indeed, if we compare the pros and cons of digital exhaustion, much more relevant arguments speak in favour of generalized application of the doctrine of exhaustion. E.g. the three-step test (especially its third prong, related to the economic effects of any subsequent uses) does not apply to exhaustion; the fact that downstream commerce is cheaper allows for easier access to culture and for the reinvestment of the remaining resources in the economy as a whole;

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<sup>23</sup> Ohly (2020) 186–187; Homar (2020) 29.

<sup>24</sup> Advocate General Szpunar expressly noted that the position in the *VOB* case (the acceptance of e-lending, partially based on a *de facto* acceptance of digital exhaustion) would lose its significance if the CJEU voted against digital exhaustion. Compare to Case C-263/18 (AG Opinion) paras. 71–72. In *Tom Kabinet*, the CJEU was not frightened by such a consequence.

<sup>25</sup> Gaubiac (2002) 10.

<sup>26</sup> Joined Cases C-403/08 and C-429/08, *Football Association Premier League Ltd and Others v. QC Leisure and Others, and Karen Murphy v. Media Protection Services Ltd.*, Opinion of AG Kokott, 3 February 2011, EU:C:2011:43, paras. 184–188.

<sup>27</sup> Case C-263/18 (AG Opinion) para. 97.

a digital exhaustion doctrine is in full compliance with the logic of the reward theory; voluntary remuneration systems (like the one Tom Kabinet or ReDigi imagined) might further ease tensions. *De facto* or *de jure* monopolies are not supported by copyright (and competition) law, and therefore the preservation of the *status quo* by the hindering of external innovations is truly undesirable. History also demonstrated that downstream commerce did not quash ‘original’ markets – indeed, rights holders modernized their business models in the wake of new technological or social challenges.<sup>28</sup> I believe that the fear of technological superiority of digital files over analogue ones (which is not an absolute truth, however), the negative commercial consequences or the complicated control of file exchanges do not trump the arguments listed above.

#### #5

The legal distinction between the online supply of software and other subject matter necessarily leads to tensions with other legal norms, especially consumer protection law. As we have seen above, the European Union’s directive on consumer protection treats the online supply of contents equally – irrespective of the copyright status of the works. Consumers can have a valid claim to have their purchases treated on an equal footing – and for the doctrine of exhaustion to apply to lawfully acquired copies of subject matter other than software, too. This argument has been accepted by a recent trial court ruling in France. In *Union Fédérale des Consommateurs*, an association representing consumers’ interests successfully claimed that a leading computer games producer’s strict limitations on the resale of lawfully acquired computer games ran against French consumer protection laws. The French court also held that such computer games (in compliance with the CJEU’s *Nintendo* ruling), as mixed works, fell under the scope of the InfoSoc Directive, rather than the Software Directive. Consequently, consumers/end-users should be allowed to dispose of the copies they downloaded against payment from the software corporation’s website under the doctrine of exhaustion.<sup>29</sup> If this ruling is confirmed by the court of appeals, it will be able to serve as solid grounds for a ‘consumer-law-based doctrine of exhaustion’ on a European level, too.

#### #6

The CJEU’s treatment of e-books as a service rather than goods in *EC v. France*, and the reliance on the making available to the public rather than on the distribution right in *Tom Kabinet* does not only lead to the exclusion of e-books (and almost all other subject matters) from the scope of exhaustion, but also narrows down the limitations and exceptions available to end-users (lawful acquirers) under the InfoSoc Directive. As Member States have implemented this Directive with notable differences, it is possible that nationals of various EU countries face significantly different treatment with regard to limitations and exceptions.

### **CONCLUSION**

In sum, I would urge – from legislators to judges – to take into consideration more arguments benefitting the “class of consumers”, people who are practically curtailed of some privileges that – on the other end of the spectrum – used to limit the exclusive

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<sup>28</sup> See in detail: Mezei (2018) 148–154.

<sup>29</sup> *Union Fédérale des Consommateurs - Que Choisir v. S.A.R.L. Valve*, Tribunal de Grande Instance de Paris, N° RG 16/01008.

rights of various rights holders. To be more certain at this stage, I argue for the followings. Let's recall that I stated that the doctrine of exhaustion is based upon three primary policy objectives: the superiority of property rights over copyrights, the reward theory, and the restraint of rights holders over market control. These objectives are further supplemented with various "secondary", but not less relevant considerations. Suppose that we are devoted to keep balance between social classes. If so, in an online environment, where the first primary policy objective (namely, the superiority of property rights over copyrights) might be at stake (in the lack of a clear and general acceptance of "virtual ownership"), the two remaining primary policy consideration shall come into the foreground to counterbalance the growing powers of rights holders. The reward theory and restraint of rights holders over market control shall dominate the discourse. An even more balanced solution might be reached, if we keep our eyes on the secondary goals of exhaustion, mainly those related to the role of the doctrine in preserving access to cultural goods through downstream commerce.

The second edition of my "Copyright Exhaustion", expected to be out in 2021 at Cambridge University Press, I am going to develop these arguments into a more concise opinion.