

# THE TEN COMMANDMENTS OF PARALLEL TRADE

## LOS DIEZ MANDAMIENTOS SOBRE EL COMERCIO PARALELO

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**Abstract:** Parallel trade is not a new issue, but the problems caused by this phenomenon are current. Parallel importations take place specially related to some products, such as medicines or cosmetics. One of the reasons is because there is a price difference for the same products across Europe. In the present article we will study through ten questions what parallel trade is, why it arises and the legal problems it causes regarding mainly three disciplines such as industrial property, competition law and unfair competition.

**Keywords:** parallel trade, trade mark, exhaustion, pharmaceutical products, free rider.

**Resumen:** El comercio paralelo no es un tema nuevo, sin embargo, los problemas que este crea sí que lo son. Las importaciones paralelas están especialmente vinculadas con determinados productos como los medicamentos y los cosméticos. Una de las razones que lo explican es la diferencia de precio para el mismo producto en atención al país de la Unión en el que nos encontremos. En el presente artículo a través de la formulación de diez preguntas estudiaremos qué es el comercio paralelo, por qué surge y los problemas que origina en relación a tres disciplinas como son la propiedad industrial, el derecho de la competencia y el derecho de la competencia desleal.

**Palabras clave:** comercio paralelo, marca, agotamiento, productos farmacéuticos, distribuidor independiente.

**Sumario:** I. Introduction. II. What is Parallel trade?. III. Why does parallel trade take place?. IV. Who benefits from it?. V. How does parallel trade arise?. VI. What is the legal bases of parallel trade?. 1. General Approach. 2. Free movement of goods. 3. Exhaustion of trade mark rights. VII. Are there any limits to the exhaustion. 1. Introduction. 2. Re-packing. VIII. What happens with luxury products? IX. How to protect the official network and the brand from unfair competition. 1. Unfair competition illicit against free riders. 2. Proof and the relationship between unfair competition and infringements of trade mark rights. X. What are the usual practices to restrict parallel trade?. XI. What about the parallel trade of pharmaceutical Products in EU?. 1. Introduction. 2. Problems. A) Shortages. B) Supply quota and dual price by pharmaceutical companies. a) Introduction. b) Supply quota. c) Dual pricing.

### I. Introduction

1. The main goal of this article is to study the parallel trade and its implications for Brands, distribution and European Competition Law<sup>1</sup>. Parallel trade is not a new issue; the first cases about parallel trade took place more than forty years ago, starting as soon as the European Union was born.

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<sup>1</sup> Part of this text was presented in the “Sixth Max Planck PostDoc Conference on European Private Law” which took place at the Max Planck Institute for Comparative and International Private Law in Hamburg, Germany, from 18 to 19 April 2016. I would like to thank the Directors of the Max Planck Institute the opportunity to have been there and the organizing team for all the attentions.

Although parallel trade is not a recent phenomenon, it does not mean it is not a current legal problem. To prove that, we only have to look at some cases that are pending in some European jurisdictions like the Spanish one, where the judges have to decide how to solve some of the problems parallel trade causes regarding, *ad ex.*, the Schweppes case<sup>2</sup>.

2. The present study is going to be divided in ten questions. These questions let us deal with the main problems parallel trade causes in the different markets across European Union.

## II. What is Parallel trade?

3. Parallel trade refers to the sale of products outside the official distribution network. It happens when a genuine product, branded goods, are imported and sold in a market without the consent of the owner of that trade mark<sup>3</sup>. The important thing is that the sale in the importing country is made by

<sup>2</sup> Among others, *ad ex.*, *Juzgado de lo mercantil* of Santander of 21 March 2016, AC\2016\604. This case is pending in many courts in Spain, thousand of bottles of tonic have been removed the market since 2014. The reason is that tonic was made in United Kingdom (hereinafter UK) and was sold in Spain by parallel traders. These parallel traders were non authorized distributors by the owner of the brand Schweppes for Spain. To understand better this case is necessary to know its background: the tonic sold in Spain under the brand *Schweppes* belongs to *Orangina Schweppes company*, this company at the same time belongs to *Suntory group*, an important Japanese group of beverage. However, the brand Schweppes for tonic made in England belongs to *Coca Cola Group*. Therefore, two trade marks (*Schweppes*) have two owners inside UE. *Coca Cola* is the manufacturer and the official distributor for the tonic Schweppes for UK, Ireland and Greek. While *Orangina Schweppes company* is the manufacturer and official seller to all countries in the European Union (also Spain), with the exception of UK, Ireland and Greek. Spanish drinks distributors cost less money to import English tonic than to buy to official Spanish distributor in Spain. However, this situation doesn't like *Orangina Schweppes*. This company doesn't want that another company sells tonic *Schweppes* manufactured abroad in Spain. Therefore in base of its trade mark right has tried to stop the parallel trade of British Schweppes tonic in Spain. The legal arguments used by *Orangina* to hold its position were basically: parallel trade damage the trade mark because its existence hinder the trade mark to fulfill its essential task in the market what is indicate the origin of the product. The sale of the same products (tonic) with the same brand (*Schweppes*) but manufactured by two different companies can confuse the consumer. He will not be able to know the features of the product he is buying. Each company manufactures the tonic according to its criteria, and that do not necessarily match between the two. The brand fulfill an essential task in the market, the consumer chooses a product for its features, if these are not continuous, the quality change, the consumer can stop buying that brand. Definitely, the legal reasoning follows for the majority Spanish courts has been similar to the decision of the European Court of Justice in *Ideal Standard Case* in 1994 (ECJ of 22 June 1994, *Ideal Standard*, C-9/93, *Rep.* 1994, p. I-02789) In that case, the Court understood that it is possible to isolate the markets when there are two owners of different trade marks for two Member States as long as these proprietor companies are not economically linked. This is because the essential function of the brand mark is adversely affected because it is not possible to guarantee that all goods bearing the same brand have been manufactured under the control of a single undertaking which is accountable for their quality. Which weighs more? , freedom of importation or trade mark rights? To date the balance is tipped in favor of the trade mark right.

<sup>3</sup> Regarding parallel trade *vid.* I. ANTÓN JUÁREZ, *La distribución y el comercio paralelo en la Unión Europea*, La Ley, Madrid, 2015; E. M<sup>a</sup>. ARES ÁLVAREZ, "Importaciones paralelas", en L. A. VELASCO SAN PEDRO, *Diccionario de Derecho de la competencia*, Iustel, Madrid, 2006, pp. 420 y ss.; E. BONADIO, "Parallel imports in a global market: should a generalised international exhaustion be the next step?", *European Intellectual Property review*, 2011, p. 154; F. CARBAJO CASCÓN, "La marca en los sistemas de distribución selectiva (el problema de las ventas paralelas)", en E. GALÁN CORONA/F. CARBAJO CASCÓN (Coord.), *Marcas y distribución comercial*, Ediciones Universidad de Salamanca, 2011, pp. 165-166; M. FARQUHARSON/V. SMITH, *Parallel Trade in Europe*, Sweet&Maxwell, 1998, p. 68; C. GÓRRIZ LÓPEZ, *Distribución selectiva y comercio paralelo*, Thomson-Civitas, Madrid, 2007, pp. 29-30; N. LEWIN, "The Ten Comandments of Parallel Importation", *Law and Policy in International Business*, I, n<sup>o</sup> 18, 1986, pp. 218-219 ; D.A MALUEG/ M. SCHWARTZ, "Parallel imports, demand dispersion, and international price discrimination", *Journal of International Economics*, Vol. 37, 1994, p. 168; A. J. DE MARTÍN MUÑOZ, *El llamado comercio paralelo en el Derecho mercantil europeo*, Universidad Pontificia Comillas, Madrid, 2001, p. 23; A. F. MUÑOZ PÉREZ, "El conflicto entre la distribución selectiva y el comercio paralelo", en ALONSO UREBA/ L. VELASCO SAN PEDRO/ C. ALONSO LEDESMA/ J. A. ECHEBARRÍA SÁENZ/ A.J. VIERA GONZÁLEZ (dirs.), *Los contratos de distribución*, La ley, Madrid, 2010, p. 691; L. A. NESTER, "Keywords, Trademarks, and the Gray Market: Why the Use is not Fair", *Marquette Intellectual Property Law Review*, Vol. 7, issue 1, 2003, pp. 242-245; C. PRAT, "Comercio paralelo: un flujo de productos y novedades jurídicas que no cesa. La doble perspectiva del derecho marcario y del Derecho antitrust", *Gaceta Jurídica de la Unión Europea y de la Competencia*, n<sup>o</sup> 2230, 2004, pp. 27-28; W. A. ROTHNIE, *Parallel Imports*, Sweet & Maxwell, Londres, 1993, p. 1; C. STOTHERS, *Parallel Trade in Europe: intellectual property, competition and regulatory law*, Hart publishing, 2007, pp. 2-3; X. VAN OVERMIERE/C. SCHILLINGS, *Les importations paralleles dans l'Union européenne*, Anthemis, 2012, pp.17-22; Sobre el comercio paralelo en Estados Unidos *vid.* S. GHOSH, "An Economic Analysis of the Common Control Exception to Gray Market Exclusion", 15, *U. Pa. J. Int'l Bus. L.*, 373, 410, 1994, pp. 373 y ss.; H.C.HANSEN, "Gray Markets Goods: A lighter Shade of Black", *13Brook. J. Int. l*

an agent that is not a member of the official distribution network<sup>4</sup>. This agent is known as *free rider* or *parallel importer*.

The *free rider* buys the goods in a market or economic area (the exporting country) where the prices are lower than in the importing country. The unofficial member sells the goods cheaper in the importing market than the official network does<sup>5</sup>.

### III. Why does parallel trade take place?

4. The main reasons why parallel imports take place could be summarized in three factors<sup>6</sup>: 1) markets where there are restrictions of competition; 2) different prices depending on the sales market; 3) cross-border element.

5. Regarding *markets where there are restrictions of competition* it is necessary to say that these restrictions serve the purpose of establishing limited distribution. In other words, selective distribution or exclusive distribution. These systems don't allow the products to be sold by anyone. In the selective distribution the members are chosen according to qualitative criteria<sup>7</sup>. These criteria should be objective and according to quality aspects related to the store, staff, pre-sale and after-sale services, etc.<sup>8</sup>. These criteria are according to the glamour and standing of the brand. For this reason, this system is usually used for luxury products like cosmetics, perfumes, jewelry, technological products, etc. This is an exception to the prohibition of restrictions of the territory according to art. 4.b.iii *Regulation 330/2010 of 20 April 2010 Regulation (EU) No 330/2010 of 20 April 2010 on the application of Article 101(3) of the*

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L., 249, 1987, pp. 249-265; T.H. HIEBERT, *Parallel Importation in U.S. Trademark Law*, Greenwood Press, 1994; W. SKINNER, "Preventing Gray Markets: Is copyright law the solution?", *Syracuse J. Int'l L. & Com.*, 315, 1998-1999, pp. 315-336; D.R. SUDGEN, *Gray Markets, Prevention, Detection and Litigation*, Oxford, Nueva York, 2009.

<sup>4</sup> According to the European Union Definition, parallel imports are "*products imported into one Member State from another and placed on the market in the destination Member State, outside the manufacturer's or its licensed distributor's formal channels. Parallel imports tend to occur when price levels for similar products between two Member States are significantly different, either as a result of national regulations or of manufacturers' policy. That creates an incentive for traders to buy products in the Member State where they are priced lower and sell them in the Member State where they are priced higher; at a price which allows the trader to make a profit*". *Vid.* Commission Communication on parallel imports of proprietary medicinal products frequently asked questions, Brussels, 19<sup>th</sup> January 2004, available in [http://europa.eu/rapid/press-release\\_MEMO-04-7\\_EN.htm?locale=en](http://europa.eu/rapid/press-release_MEMO-04-7_EN.htm?locale=en).

<sup>5</sup> *Vid. ad ex.*, ECJ 6 January 2004, *Bayer*, Cases C-2/01 P y C-3/01 P, p. I-64. The Case Bayer is a clear example of what parallel trade is, the Bayer Group is one of the most important pharmaceutical companies in the worldwide. It is present in all Member States through its subsidiaries, being a leader in the chemical and pharmaceutical sector. Bayer sells, among many other drugs, a product known under the name Adalat and Adalat. As it is known, governments set prices of medicines in many Member States. The prices for this medicine were lower in France and Spain than in the UK, between 1989 and 1993. This situation led to wholesalers to buy more quantities of the drug in Spain and France in order to resell in the UK at a higher price. Due to the existing parallel trade on the product, Bayer suffered significant losses in the UK because their sales were down by almost half. *Vid.* About this case and the parallel trade in pharmaceutical products, A. GARCÍA VIDAL, "El comercio paralelo de medicamentos", *CDT*, octubre 2013, vol. 5, n° 2, pp. 317 y ss.

<sup>6</sup> We have defended this idea in a previous article, *vid.* I. ANTÓN JUÁREZ, "Los derechos de copyright fuera de juego como vía para combatir las importaciones paralelas en Estados Unidos", *CDT*, vol. 7, n° 2, octubre 2015, pp. 24-44.

<sup>7</sup> About the criteria to select members in the selective distribution network, *vid.* F. CARBAJO CASCÓN, "El contrato de distribución selectiva", en A. BERCOVITZ RODRÍGUEZ-CANO/ M<sup>a</sup>. A CALZADA CONDE (Dirs.), *Contratos Mercantiles*, 5<sup>a</sup> ed., Madrid, Thomson-Aranzadi, 2013, pp. 792-799; C. GÓRRIZ LÓPEZ, *Distribución selectiva y comercio paralelo*, Thomson-Civitas, Madrid, 2007, p. 35, this author remarks an important aspect what distinguish selective distribution from other ways of distribution, "*la característica esencial de la figura no es la selección de los distribuidores, presente en todas las formas de comercialización de bienes y servicios, sino que se impone esa selección a todos los miembros del sistema. Es decir, tanto el fabricante como los empresarios que hayan contratado con él podrán suministrar los productos exclusivamente a los comerciantes que reúnan los requisitos exigidos por el fabricante y estén dispuestos a realizar las prestaciones exigidas —o bien a los consumidores finales—*". In the judgments of ECJ, *vid. ad ex.*, ECJ 25 October 1977, *Metro I*, case 26/76, *Rep.* 1977, p. 1877, par. 20; ECJ of 11 December 1980, *L'Oréal*, case 31/80, *Rep.* 1980, p. 3776, par. 16; ECJ of 19 July 1980, *Lancôme*, case 99/1979, *Rep.* 1989, p. 2511, par. 20; ECJ of 16 June 1981, *Salonia*, case 126/80, *Rep.* 1981, p. 1565, par. 24; ECJ of 11 October 1983, *Demo-Studio Schmidt*, case 210/81, *Rep.* 1983, p. 3046, par. 2; ECJ 25 October 1983, *Telefunken*, C-107/82, *Rep.* 1983, p. 3155, par. 35; ECJ of 3 July 1985, *Binon*, case 243/83, *Rep.* 1985, p. 2034, par. 31; ECJ of 22 October 1986, *Metro II*, case 75/84, *Rep.* 1986, p. 3076, par. 37.

<sup>8</sup> *Guidelines on Vertical Restraints* (OJ C-130/1, 19.05.2010), par. 175.

*Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices* (hereinafter R. 330/2010)<sup>9</sup>. Therefore if a distributor does not fulfill the qualitative criteria, it can be excluded by the proprietor of the network<sup>10</sup>. But *a contrario sensu* if the distributor fulfills the objective criteria, it cannot be excluded; this could be an antitrust illicit on grounds of art. 101.1 TFEU<sup>11</sup>.

Regarding exclusive distribution, the chain is formed based on quantitative criteria. The qualitative criteria are not as important as the number of distributors per area<sup>12</sup>.

To sum up, both systems limit the access to the network. Not everyone can sell the products, only authorized members.

In contrast with limited distribution, we can find open distribution. In this kind of distribution system, there are not restrictions to be a member, anyone can be one. The products which are sold under open distribution are not subject to parallel trade. The reason is that the price is the same in all the markets where the product is sold.

6. This allows us to move to the second factor or consideration, *the different price for the same goods depending on the sales market*. This price difference is due to three reasons:

- 1) *Standard of living*. There are countries where the rent per capita is higher than in others. This situation means that in these countries the citizens have more money to spend. Brands, or rather companies after these brands- manufactures, suppliers, distributors- are aware of that and they try to make as much profits as possible. Increasing the price in luxury products without a reason has become a usual practice.
- 2) *Cost of the distribution network*. Directly related to the above, the price difference among countries is due to the cost of the distribution network. There are countries where establishing a distribution system is more expensive than in others. The cause could be the cost of the Staff's salaries, the presale and after sale services or the publicity fees, because they are different among countries. Naturally these costs have an effect on the price of the products.
- 3) *Currency fluctuations*. The change in the value of money is another factor that explains why the goods do not have the same price in all the countries where they are sold<sup>13</sup>.

7. Finally, the last factor would be the *cross-border element*. Parallel trade is difficult to understand without this foreign element, buying in one country to sell in another. The business works if the margin of profit is enough to cover the cost of the importation, transportation, etc.

#### IV. Who benefits from it?

1. Regarding this question there have been different opinions, depending on who you ask about it. According to *free riders*, parallel trade is positive for the consumers and the markets<sup>14</sup>. They think parallel imports are an alternative in the supply. It implies more competence for the market because the

<sup>9</sup> OJ L 102/1, 23.4.2010.

<sup>10</sup> ECJ 25 October 1977, *Metro I*, case 26/76, *Rep.* 1977, p. 1877, par. 20.

<sup>11</sup> ECJ 25 October 1983, *Telefunken*, C-107/82, *Rep.* 1983, p. 00767, par. 37. *Vid.* against this opinion, P. GONZÁLEZ DE ZÁRATE CATÓN/J. MARCOS RAMOS, "La negativa de suministro por parte del fabricante en los sistemas de distribución selectiva: ¿acuerdo entre empresas o conducta unilateral?", *Rcd*, n° 16, 2015, pp. 5 y ss, these authors have hold that it is not possible to understand the refusal by the manufacture to be a member when a distributor fulfill all the objective requirements is an unlawful practice contrary to art. 101.1 TFEU. From their opinion, such a practice cannot be an agreement among manufacturer and all the official distributors, this refusal is an unilateral conduct and this should be exempt from prohibition.

<sup>12</sup> Regarding the exclusive distribution *vid., ad ex.*, R. ALONSO SOTO, "Tipología de los contratos de distribución comercial", en ALONSO UREBA/ L. VELASCO SAN PEDRO/ C. ALONSO LEDESMA/ J. A. ECHEBARRÍA SÁENZ/ A.J. VIERA GONZÁLEZ (dirs.), *Los contratos de distribución*, La ley, Madrid, 2010, pp. 63-68; J.L. DÍAZ ECHEGARAY, "El contrato de distribución exclusiva o de concesión", en A. BERCOVITZ RODRÍGUEZ-CANO/ M<sup>a</sup>.A. CALZADA CONDE, *Contratos mercantiles*, 5<sup>a</sup> ed, Vol. I, Thomson Reuters Aranzadi, Navarra, 2013, pp. 727-779.

<sup>13</sup> Commission Decision of 8 May 2001, *Glaxo Wellcome*, OJ L 302, 17.11.2001, pars.30-32.

<sup>14</sup> *Vid.* I. ANTÓN JUÁREZ, *La distribución y el comercio paralelo en la Unión Europea*, La Ley, Madrid, 2015, p. 127.

official distribution network loses the exclusivity to be the only one selling products in that market. According to them, parallel trade keeps the prices in check.

In line with this vision, the European Commission has showed his position regarding parallel trade in several decisions<sup>15</sup>.

2. However, this opinion about who are the beneficiaries of parallel trade is not shared by manufactures and official members of a distribution network. According to them, free riders are parasites whose business consists in taking advantage of the official network services and the brand image<sup>16</sup>. They think parallel trade doesn't offer positive aspects for either market or consumers, besides, in the case of pharmaceutical products, its existence discourages the investment in research and development<sup>17</sup>.

3. From our point of view, we consider that the beneficiaries of this kind of trade could be: the parallel agent or independent distributor, the single market and the consumers.

The independent distributors can develop a way to make business. Parallel trade allows them to be present in a market as competitive as this one. These agents could be the most beneficial ones, because they can take advantage of the different prices of the product and the good reputation of a brand. However, they are not the only ones. The single market is more real, the competence is more effective with the existence of parallel trade. There are fewer barriers between Member States. One of the reasons is because the official distribution network is not alone in the market; parallel traders compete with the official distribution network reducing practices which try to divide the European market<sup>18</sup>. The consumer can benefit from parallel trade in two ways. Indirectly, the more agents in a market, the more competence there is. Therefore, under these conditions we can presume that the prices of the products are usually lower when there is no monopoly. Directly, because the consumers can buy branded products, genuine products more low-priced than if they buy the products from official distributors.

## V. How does parallel trade arise?

4. The most common reason is usually the disloyalty of the official members of the network. The official members are the ones who sell the products to independent resellers, agents that do not belong to the official distribution network. These acts are usually prohibited by the agreement between the owner of the network and the official distributor. Selective distribution contracts can include clauses to prevent

<sup>15</sup> Commission Decision 8 May 2001, *Glaxo Wellcome*, OJ L 302, 11.11.2001; Commission Decision of 13 July 1987, *Sandoz*, OJ L 222 de 10.8.1987.

<sup>16</sup> Using the reputation of another person to take advantage of his prestige could be an illegal act according to unfair competition regulation. In fact, this kind of acts could be in conflict with art. 12 Ley de Competencia Desleal española. *Vid.* C. GÓRRIZ LÓPEZ, *Distribución selectiva y comercio paralelo*, Thomson-Civitas, Madrid, 2007, pp. 358-360; F. CARBAJO CASCÓN, "La marca en los sistemas de distribución selectiva (el problema de las ventas paralelas)", en E. GALÁN CORONA/F. CARBAJO CASCÓN (Coord.), *Marcas y distribución comercial*, Ediciones Universidad de Salamanca, 2011, pp. 174-175; J. MASSAGUER FUENTES, "La protección de los sistemas de distribución selectiva ante las ventas grises" en Homenaje a H. BAYLOS, *Estudios sobre derecho industrial*, Grupo español de la AIPPI, Barcelona, 1992, pp. 463 y ss; A. F. MUÑOZ PÉREZ, "El conflicto entre la distribución selectiva y el comercio paralelo", en ALONSO UREBA/ L. VELASCO SAN PEDRO/ C. ALONSO LEDESMA/ J. A. ECHEBARRÍA SÁENZ/ A.J. VIERA GONZÁLEZ (dirs.), *Los contratos de distribución*, La ley, Madrid, 2010, p. 730.

<sup>17</sup> CFI of 27 September 2006, *GlaxoSmithKline*, T-168/01, *Rep.* 2006, p. II-02969, pars 146 y 258.

<sup>18</sup> *Vid.* CFI of 9 July 2009, *Peugeot*, Case T- 450/05, *Rep.* 2009, p. II-02533, where Peugeot Nederland, a wholly-owned subsidiary of Peugeot S.A., organizes and runs the Peugeot products and services distribution network in the Netherlands. Peugeot S.A. in association with Peugeot Nederland had applied measures (known as remuneration system) designed to restrict parallel exports from the Netherlands to other Member States. These measures aimed to the exclusion of export sales from a bonus system. Bonus official car dealers to sell in Netherlands, but this bonus disappeared when the cars were going to be exported. It clearly manifests the will to treat export sales less favourably than national sales and thus leads to a partitioning of the market in question. The Court held that these measures were contrary to Article 81(1) EC, current 101.1 TFEU, because it was an indirect way to restrict parallel trade and to partition the market among member states.

resales to third parties who are not members of the official network<sup>19</sup>. The reasons for this disloyalty by an official distributor may be varied; from the need to get rid of stock of products from past seasons to the temptation to earn more money with a single sale. This failure causes a “shortfall” in the official distribution network.

On other occasions, the shortfall in the distribution network is due to the owner of the distribution network selling goods to third parties (non-official members) to resell them outside European Economic Area (EEA). The problems come up when the third party breaches the agreement and ends up selling the products in the area or country where it is specifically forbidden to resell the products, *ad ex.*, in some of the European Union countries<sup>20</sup>. This is another way parallel trade appears.

5. Parallel imports can also take place in a market due to the configuration of the official distribution network. In other words, when a product is sold in many countries, one of the ways is to use an indirect distribution channel as selective distribution system. But often establishing a selective distribution system in all the markets where the products are marketed is impossible. Either because it is expensive, or because there are no agents that meet the requirements that the network requires. For that reason, the network owner chooses other options to sell the products in that market. For example, exclusive distribution. Furthermore, the official network could market the products in some countries through selective distribution and in other through exclusive distribution. This organization makes the existence of parallel trade possible “the prohibition to sell products to non-official members” can only be required to official distributors in the territories in which the network operates through that system. Therefore, in the countries where the products are sold through other distribution system such as the exclusive one, it is not legal, at least from the European competition law, such prohibition. Consequently, official members who sell through selective distribution in a European country can find products sold by independent agents in their market. This is possible because these free riders can get the goods from official members who market the products through an exclusive distribution system<sup>21</sup>.

## VI. What is the legal basis of parallel trade?

### 1. General Approach

6. Parallel importations are not specifically regulated in a European text. Although there are no references to parallel trade in Regulations like the TFEU or secondary European legislation, the Euro-

<sup>19</sup> The effect of these clauses in selective distribution agreements have been very studied under European Competition Law. These clauses are legal as long as they are implemented in territories where is established a selective distribution network. *Vid. C. GÓRRIZ LÓPEZ, Distribución Selectiva y ...., op. cit., pp. 205-206.*

<sup>20</sup> ECJ of 28 April 1998, *Javico*, C-306/96, *Rep.* 1998, p. 173, pars. 10-28. *Yves Sant Laurent* agreed with *Javico*, German distributor, that *Javico* would sell cosmetics under the trade mark *Yves Sant Laurent* in Russia, Slovenia and Ukraine. The destination of the goods was precise: outside of EEA. Moreover, the agreement contained a prohibition of reimporting and marketing those products in European Union. *Javico* was in breach of its contractual obligations and end up marketing the products in England, Netherlands and Belgium. This behavior of *Javico* made possible *Yves Sant Laurent* products were marketed in those European countries outside of the official distribution network. The ECJ answers regarding if this kind of clauses were contrary to art. 101.1 TFEU (ex. art. 85.1) was: “Article 85(1) of the Treaty precludes a supplier established in a Member State of the Community from imposing on a distributor established in another Member State to which the supplier entrusts the distribution of his products in a territory outside the Community a prohibition of making any sales in any territory other than the contractual territory, including the territory of the Community, either by direct marketing or by re-exportation from the contractual territory, if that prohibition has the effect of preventing, restricting or distorting competition within the Community and is liable to affect the pattern of trade between Member States. This might be the case where the Community market in the products in question is characterised by an oligopolistic structure or by an appreciable difference between the prices charged for the contractual product within the Community and those charged outside the Community and where, in view of the position occupied by the supplier of the products at issue and the extent of the supplier’s production and sales in the Member States, the prohibition entails a risk that it might have an appreciable effect on the pattern of trade between Member States such as to undermine attainment of the objectives of the common market”(par. 28).

<sup>21</sup> For a further detail about this problem *vid. I. ANTÓN JUÁREZ, La distribución y ...., op. cit., pp. 296-298.*

pean Institutions have encouraged parallel importations in the internal market<sup>22</sup>. This position could be based on the principle of the free movement of goods. They have understood that parallel trade is an alternative to the official distribution network. It implies more competence in the market because it increases the agents. The single market becomes more real with the existence of parallel trade.

7. But at the same time, the proprietor of a trade mark has the right to protect its mark and its network. To avoid the restriction of free circulation of goods inside EU, the proprietor of a trade mark has limited exercise of his exclusive rights regarding the first commercialization in the EU of the goods bearing that trade mark. This is established in community regulations which regulate the European exhaustion of trade mark right<sup>23</sup>.

8. The purpose of the exhaustion of trade mark right is to avoid the proprietor's opposition to the subsequent commercialization in EU. The exhaustion constitutes a restriction on the exclusive rights of the owner of the trade mark stemming from the first commercialization of the goods.

Therefore, according to these principles, parallel trade is totally legal. This could be a general rule. The trade mark rights cannot be used to restrict parallel trade. In fact, we will see how many practices to avoid parallel trade are prohibited under European Competition Law. For example, the restriction of the exportation among Member States. Nevertheless, the owner of a distribution network can protect his system of free riders according to some rules of European Competition Law, for instance, art. 4.b.iii R.330/2010.

9. For those reasons we can affirm that parallel trade navigates between free circulation of goods and Intellectual Property Protection.

## 2. Free movement of goods

10. The free movement of goods is the framework of trading between Member States<sup>24</sup>. This principle makes possible the free selling and buying of European goods inside the internal market<sup>25</sup>. The Customs Union (art. 28 TFEU) were necessary to manage this as well as the elimination of any quantitative restrictions on imports/exports and all measures having equivalent effect within the single market (art. 34 y 35 TFEU)<sup>26</sup>.

Since the beginning of the Union and due to the importance of this notion, the Court of Justice was concerned about what "measures having equivalent effect" should mean; that concept has been developed by ECJ in numerous resolutions<sup>27</sup>. In the first case, *Dassonville*, the ECJ hold "*All trading*

<sup>22</sup> ECJ of 6 April 2006, *General Motors y Opel Nederland*, C-551/03 P, *Rep.* 2006, p. I-03173, pars. 66-67; Commission Decision of 8 October 2003, *Nintendo distribution*, OJ L 255, 8.10.2003; JECJ of 10 February 2011, *Activision Blizzard Germany/Comision*, C-260/09 P, *Rep.* 2011, pars. 70-87.

<sup>23</sup> Directive (EU) 2015/2436 of the European Parliament and of the Council of 16 December 2015 to approximate the laws of the Member States relating to trade marks (OJ L 336, 23.12.2015); Regulation (EU) 2015/2424 of the European Parliament and of the council of 16 December 2015 amending Council Regulation (EC) N° 207/2009 on the Community trade mark and Commission Regulation (EC) No 2868/95 implementing Council Regulation (EC) N° 40/94 on the Community trade mark, and repealing Commission Regulation (EC) No 2869/95 on the fees payable to the Office for Harmonization in the Internal Market (Trade Marks and Designs) [OJ 341/21 24.12.2015]

<sup>24</sup> European Commission, *Free Movement of Goods: Guide to the application of Treaty provisions governing free movement of goods*, 2013, Ref. Ares (2013)3759436, p. 8.

<sup>25</sup> *Vid. A. MATTERA, El mercado único europeo. Sus reglas, su funcionamiento.* Civitas, Madrid, 1998, pp. 55-56.

<sup>26</sup> For a further detail about this articles *vid. C. BERNARD, The substantive law of the EU: the four freedoms*, Oxford University Press, 4<sup>th</sup> ed., 2013, pp. 71-118.

<sup>27</sup> *Vid. ad ex.*, about the concept of "measures having equivalent effects", ECJ of 11 July 1974, *Dassonville*, case 8/74, *Rep.* 1974, p. 837, par. 5; ECJ of 20 February 1979, *Rewe-Zentral AG/Bundesmonopolverwaltung für Branntwein (Cassis de Dijon)*, case 120/78, *Rep.* 1979, p. 649, par 15; ECJ of 14 December 1979, *Regina/ Henn & Darby*, case 34/79, *Rep.* 1979, p. 3795, pars. 11-13; ECJ of 24 November 1982, *Commission/Ireland*, case 249/81, *Rep.* 1982, p. 4005, par. 20; ECJ of 7 May 1985,

*enacted by member states which are capable of hindering, directly or indirectly, actually or potentially, intra-comunitary trade are to be considered as measures having an effect equivalent to quantitative restrictions*”<sup>28</sup>. Therefore, this broad interpretation shows the position of the European Union authorities regarding this issue, participating on the European market is a right for everybody, and they can participate on the market on whatever terms they choose.

**11.** The single market is one of the most important goals of the Union, free movement of goods is one of the ways to achieve it, the way to understand this principle conditions how to understand the rest of European liberties and other matters such as *Competition Law* and *Industrial and Intellectual property Law*. Therefore, we can affirm that legality of parallel trade is inherent to the understanding of the single market and the principle of the free movement of goods, because, parallel trade is nothing more than an “image” of the free circulation of goods.

### 3. Exhaustion of trade mark rights

**12.** The exhaustion of industrial and intellectual property rights is a restriction in the prerogatives stating that the proprietor has to be the owner of a trade mark, a patent or a copyright or another right. Therefore, based on the doctrine of exhaustion, once the product bearing a mark has been placed in the EEA by their proprietor or by a third party with their consent, the proprietor cannot oppose to the subsequent commercialization of the product<sup>29</sup>. The extent of the exhaustion varies from system to system; it can be national, regional or international<sup>30</sup>. But, anyway, the Member States do not have a choice<sup>31</sup>. All the States Member in order to achieve the interior market and respect the principle of free movement of goods had the obligation to reform its national laws and adopt the regional one, well-known as community exhaustion<sup>32</sup>. This election in favour of community exhaustion by European authorities has been criticized, especially by parallel traders. They consider the community exhaustion lets the trade mark holders abuse their rights to stop parallel trade. In fact, they claim that one of the reasons why products in Europe such

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*Commission/Francia*, as. 18/84, *Rep.* 1985, p. 1339, par. 13; ECJ of 12 July 1990, *Comisión/Italia*, C- 128/89, *Rep.* 1990, p. I- 3697, par. 22; ECJ of 18 May 1989, *The Queen/Royal Pharmaceutical Society of Great Britain- ex parte Association of Pharmaceutical Importers*, cases 266 y 267/87, *Rep.* 1989, p. 1295, pars.15-16; ECJ of 25 July 1991, *Aragonesa de Publicidad Exterior y Publivia*, C-1/90 y C- 176/90, *Rep.* 1991, p. I- 4151, pars. 8-14; ECJ of 21 March 1991, *Monteil y Samanni*, C-60/89, *Rep.* 1991, p. I- 1547, pars. 37-39; ECJ of 24 November 1993, *Keck y Mithouard*, C-267/91 and C-268/91, *Rep.* 1993, p. I-6097, pars. 11-12; ECJ of 26 June 1997, *Familiapress*, C368/95, *Rep.* 1997, p. I3689, par. 8; ECJ of 11 December 2003, *Deutscher Apothekerverband*, C322/01, *Rep.* p. I14887, pars. 67; ECJ of 30 April 2009, *LIBRO*, C-531/07, *Rep.* 2009, p. I-03717, par. 15; ECJ 10 of February 2009, *Commission/Italy*, C-110/05, *Rep.* 2009, I-509, par. 33; ECJ 9 of December 2010, *Humanplasma*, C-421/09, *Rep.* 2010, p. I-0000, par. 26; ECJ 7 of April 2011, *Francesco Guarnieri & Cie contra Vandevelde Eddy VOF*, C-291/09, *Rep.* 2011, p. 02685, par. 15.

<sup>28</sup> ECJ of 11 July 1974, *Dassonville*, case 8/74, *Rep.* 1974, p. 837, par. 5.

<sup>29</sup> ECJ 16 July 1998, *Silhouette*, C-355/96, *Rep.* 1998, p. I- 04799, par. 18.

<sup>30</sup> Regarding national exhaustion, this kind of exhaustion takes places once the goods bearing a mark are commercialized by the holder or by an authorized party in a national market. At the opposite end we can find the international exhaustion. The right is exhausted with the sale of the product in any market in the world. In the middle it would be the regional exhaustion. The holders of these rights may oppose the resale or importation of their products when the goods bearing a mark have not been marketed within the EEA.

<sup>31</sup> ECJ of 20 November 2001, *Zino Davidoff*, Cases C-414/99 to C-416/99, *Rep.* 2000, p. I-08691, par. 32.

<sup>32</sup> Regarding community exhaustion *vid.* A. BERCOVITZ RODRÍGUEZ CANO, *Comentario a la ley de marcas*, Navarra, Aranzadi, 2008; M. BOTANA AGRA, «El derecho de marca en la jurisprudencia del Tribunal de la CE: de un derecho descafeinado a un derecho con cafeína», *Cuadernos de Jurisprudencia sobre propiedad industrial*, n.º 9, 1992, pp. 41 y ss.; A. CASADO CERVIÑO y C. BORREGO, «Agotamiento del derecho de marca», en *Comentarios a la Ley y al Reglamento de marcas* (C. GONZÁLEZ BUENO coord.), Madrid, Civitas, 2003, p. 364; T. DE LAS HERAS, *El agotamiento del derecho de marca*, Montecorvo, Madrid, 1994; C. FERNÁNDEZ NOVOA, *Tratado sobre Derecho de marcas*, Marcial Pons, MADRID, 2001, pp.371-391; A. GARCÍA VIDAL, “El alcance territorial del derecho de marca en la reciente jurisprudencia del TJCE”, *ADI*, 20, 1999; M. LOBATO GARCÍA MIJÁN, *Comentario a la Ley 17/2001, de Marcas*, Civitas, 2002, pp. 561 y ss.; P. MARTÍN ARESTI, “Art. 36, agotamiento del derecho de marca”, en A. BERCOVITZ CANO (Dir.)/ J.A. GARCÍA CRUCES GONZÁLEZ (Dir. adjunto), *Comentarios a la Ley de Marcas*, Tomo I, Aranzadi, 2008; C. PRAT, “Comercio paralelo: un flujo de productos y novedades jurídicas que no cesa. La doble perspectiva del derecho marcario y del Derecho antitrust”, *Gaceta Jurídica de la Unión Europea y de la Competencia*, n.º 230, 2004, pp. 27- 44.



as cosmetics are more expensive than in USA is due to the community exhaustion. They think international exhaustion in all Member States could avoid this problem<sup>33</sup>.

13. Nowadays the community exhaustion is regulated in art. 15 of the current Directive (Directive 2015/2436). Although international exhaustion is the broadest and the best for the existence of parallel importations, this does not mean the community exhaustion does not let parallel trade takes place. In fact, according to community exhaustion, once the product is marketed in any State Member under the proprietor consent, they cannot oppose the resale of his product. This principle makes legal parallel trade inside European Union.

14. Therefore, three requisites are necessary for community exhaustion: 1) releasing goods in a market; 2) with the consent of the proprietor; 3) this market must be the EEA market.

## VII. Are there any limits to the exhaustion?

### 1. Introduction

15. Once a product bearing a trade mark has been released in an EEA market by the proprietor or with their consent, the proprietor of the trade mark rights loses the possibility to stop the subsequent resales of the products bearing such trade mark. This is the general rule that makes parallel trade legal. However, every general rules has exceptions. Thus, according to 15.2 Directive 2015/2436 about marks, the owner of a trade mark can recover their exclusive right, they can avoid the resale of his product when the free rider damages some of the functions the trade mark fulfills, *ad ex.*, identifying the origin of the product or damaging the quality or the reputation of the trade mark. In those cases, the proprietor of a trade mark can stop parallel trade.

The art. 15.2 Directive 2015/2436 as well as previous regulation art. 7.2 First Directive mentions “legitimate reasons”, but there is not a closed list of reasons which legitimate the proprietor to oppose the sale of their product once it has been put on the market<sup>34</sup>. According to the topic of the present work, we are going to remark one specific situation: Could the re-label or the re-pack of a product made by a free rider be understood as a legitimate reason according to art. 15.2 Directive?

### 2. Re-packing

16. Manufactures often decide to sell their products with different packets, labels or even brands depending on the country where the products are going to be marketed. The reasons after these politics can be quite different, from adjusting the consumer preferences in a specific market to following the law or even a way to restrict parallel imports.

17. Regardless of the reasons for the change, the purpose of this section is to study what possibilities the free rider has to make changes in packaging, labels, etc. without involving an infringement of trade mark rights. In many cases, free riders have little choice if they want to market the product; modifying the package or the label or even the prospectus in the case of pharmaceuticals, is the only alternative.

<sup>33</sup> Regarding the opinion of European Commission about this problem *vid. Commission Staff Working Paper Possible abuses of trade mark rights within the EU in the context of Community exhaustion*, Brussels, 21.5.2003, SEC(2003) 575. The European Commission understood that the best regime of exhaustion is the community one. In the case parallel trade was restricted by right holders, the way to fight against this situation is through European Competition Law, not changing the extension of exhaustion of industrial and intellectual property rights.

<sup>34</sup> ECJ of 11 July 1976, *Bristol-Myers Squibb*, C-427/93, C-429/93 y C-436/93, *Rep.* 1996, p. I-3457. pars. 26 and 39.

18. It has been considered a modification of the product when free riders change the package of a product and therefore an exception to exhaustion of a trade mark<sup>35</sup>. This is mostly a general rule. The holder of a trade mark may oppose the change of the container or package of his product. However, this rule has been modulated in favor of parallel trade. The proprietor will not be able to oppose the re-labeling or re-packaging in the following situations: a) that the opposition of the trade mark owner contributed to the artificial partitioning of the markets between member states<sup>36</sup>; b) that the original condition of the product remained unaffected by its repackaging<sup>37</sup>; c) that the identity of both the original manufacturer and the repackager was clear following the repackaging<sup>38</sup>; d) that the presentation of the re-packaged product did not, or was not likely to, damage the reputation of the trade mark or its owner<sup>39</sup>; e) that the repackager gave notice of his intention to the trade mark owner before the repackaged product entered the market, and provided a sample on request<sup>40</sup>.

19. Therefore, opposition to re-labeling or re-packaging would not be possible for the right holder when the parallel importer is able to fulfil those criteria. Thus, the general rule is that the burden of proof is on the parallel importer<sup>41</sup>. Parallel importer must give the owner of the trade mark enough information; this information will help the proprietor with the decision of whether such repackaging is necessary in order to the product for being marketed in the Member State of importation.

However, there are aspects that are quite difficult to prove from the position of the parallel trader, *ad ex.*, the re-labeling or re-packaging does not harm the image or reputation of the brand. Thus, in these cases the ECJ has considered sufficient that the parallel importer submit sufficient evidence to presume that such a requirement would be met, falling the obligation to prove otherwise on the holder<sup>42</sup>.

<sup>35</sup> ECJ of 23 May 1978, *Hoffmann-La Roche*, case 102/77, *Rep.* 1978, p. I-1139; ECJ of 10 October 1978, *Centrafarm*, case 3/78, *Rep.* 1978; ECJ 3 December 1981, *Eurim-Pharm*, case 1/81, *Rep.* 1981, p. I-2913; ECJ 11 July 1996, *Bristol Myers Squibb/Paranova*, C-427/93, C-429/93 y C-436/93, *Rep.* 1996, p. I-3514.

<sup>36</sup> ECJ 11 July 1996, *Bristol Myers Squibb/Paranova*, C-427/93, C-429/93 y C-436/93, *Rep.* 1996, p. I-3514, pars. 42-47.

<sup>37</sup> ECJ 11 July 1996, *Bristol Myers Squibb/Paranova*, C-427/93, C-429/93 y C-436/93, *Rep.* 1996, p. I-3514, pars. 48-57.

<sup>38</sup> ECJ of 28 July 2011, *Orifarm y Paranova Danmark/Merck*, C-400/09 and C-207/10, *Rep.* 2011, p. I-0000, par. 36, in this judgment the Court hold that “*It follows from all the foregoing that Article 7(2) of Directive 89/104 must be interpreted as not allowing the proprietor of a trade mark relating to a pharmaceutical product which is the subject of parallel imports to oppose the further marketing of that product in repackaged form on the sole ground that the new packaging indicates as the repackager not the undertaking which, on instructions, actually repackaged the product and holds an authorisation to do so, but the undertaking which holds the marketing authorisation for the product, on whose instructions the repackaging was carried out, and which assumes liability for the repackaging*”. About the necessity to indicate the new packaging’s author, *vid. F. FORNI*, “*Il Farmaco di importazione parallela ha trovato l’autore del suo riconfezionamento*”, *Diritto comunitario e degli scambi internazionali*, LII, n° 1-2, 2013, pp. 113-118.

<sup>39</sup> In the case of pharmaceutical products should be kept special care with how to present the product. Therefore a faulty packaging, poor quality or untidy can not inspire confidence in the consumer and, in this type of products is crucial because being closely related to health, the public is demanding. Thus, these aspects must be taken into account by the parallel importer when modifying the package (ECJ of 11 July 1996, *Bristol Myers Squibb/Paranova*, C-427/93, C-429/93 y C-436/93, *Rep.* 1996, p. I-3457, par. 66. The ECJ distinguished to what extent should take care of the container depending on whether the drug was intended for hospitals or sold directly to consumers. In the first case, the presentation is not as important, because the drug is provided to the patient by professionals so that the consumer does not see the package. However, in the second case, the condition of the packaging itself becomes important, since the consumer can directly see the packaging of the drug. Although it has been prescribed by a professional and this will inspire confidence, a container little care can cause suspicion in the consumer about the quality of the product. Likewise, the holder may also oppose the changes in cases where the new tags or packaging affect the brand image and damaging its seriousness, quality and consumer confidence (ECJ of 26 April 2007, *Boehringer II*, C-348/04, *Rep.* 2007, p. I-3430, par. 43; ECJ of 4 November 1997, *Parfums Christian Dior*, C- 337/95, *Rep.* 1997, p. I- 6034, par. 45). In addition, acts of the parallel importer as not to include the mark on the outer packaging, put their own logo or style, or the adhesion of an additional label that hides totally or partially one of the brands of the holder and print their name in capital letters may allow opposition by the proprietor for harming the reputation of the brand (ECJ of 26 April 2007, *Boehringer II*, C-348/04, *Rep.* 2007, p. I-3430, pars. 45-47).

<sup>40</sup> ECJ 11 July 1996, *Bristol Myers Squibb/Paranova*, C-427/93, C-429/93 y C-436/93, *Rep.* 1996, p. I-3514, par. 69.

<sup>41</sup> ECJ of 26 April 2007, *Boehringer II*, C-348/04, *Rep.* 2007, p. I-3430, par. 48.

<sup>42</sup> ECJ of 26 April 2007, *Boehringer II*, C-348/04, *Rep.* 2007, p. I-3430, pars. 48-54.

### VIII. What happens with luxury products?

20. In luxury products, such as cosmetics, perfumes, watches, etc. the quality of the product is not just result of their material characteristics, but also of the allure and prestigious image which bestows them an aura of luxury. This aura of luxury emanating from them is essential because it enables consumers to distinguish them from similar goods. Therefore, an impairment of that aura of luxury is likely to affect the actual quality of those goods<sup>43</sup>.

21. This scenario takes place when branded goods, in fact, luxury products, are sold outside the distribution network. This resale is totally legal as long as the trade mark rights are exhausted, once the goods have been put on the market of the EEE by the proprietor or with their consent. The trade mark shall not entitle the proprietor to prohibit its use on grounds of its exclusive right. The question that we want to point out is whether luxury goods resold outside distribution network can imply an exception of exhaustion of trade mark rights. Once the product is marketed under a selective distribution system, could the damage in the reputation of a trade mark be understood as a “legitimate reason” according to art. 15.2 Directive?

22. A balance must be struck between free movement of goods and trade mark exclusive rights. The Court of Justice has provided that it is necessary to study each case individually, so as to determine whether the sale outside the network or sale without the requirements of the selective distribution system impair the distinctive function and brand reputation as the holder *ius prohibendi* comes back. As seen in the ECJ judgment *Copad/Dior Couture*, sales outside the network can impair the quality of branded products, but for “the possibility of harm” to become a real damage to the reputation of the brand it is necessary to take into account aspects such as who the recipients of the products are and the conditions of that particular selective distribution system<sup>44</sup>.

23. In line with the vision hold by the Court of Justice on several occasions, the national court is the one who must check whether the specific circumstances allow this. In other words, national courts have the best position to decide if there is a legitimate reason to except the exhaustion. Spanish courts have provided in various decisions that the marketing of branded products by dealers outside the official network is a legitimate reason to except the exhaustion according to art. 36.2 Ley 17/2001, de 7 de diciembre, de Marcas, because it undermines the prestige of the brand<sup>45</sup>. However, this recognition does not always mean that a sale outside of the selective distribution systems constitutes per se a legitimate reason to prohibit the subsequent commercialization of branded products once this right is exhausted. The circumstances of each case –sales target, volume, nature of the product, the trajectory of the parallel importer in the market, ad ex., its prestige, its modus operandi, the kind of store where the product is sold, if pre and post sales service are used – can determine if the proprietor has a legitimate reason to invoke the trade mark rights according to art. 15.2 Directive<sup>46</sup>.

24. One aspect to take into consideration is that infringements of trade mark rights can only be legally claimed by the trade mark holder or an exclusive licensee authorized to do so (art. 40 LM). This is interesting because the other integrated distributors will not be able to take action against the free rider regarding the infringement of a trade mark. The only way the official distributors affected by parallel trade fight it would be an action by unfair competition.

<sup>43</sup> ECJ of 23 April 2009, *Copad/Dior Couture*, C-59/08, Rep. 2009, p. I-03421, pars. 25-26.

<sup>44</sup> ECJ of 23 April 2009, *Copad/Dior Couture*, C-59/08, Rep. 2009, p. I-03421, par.58.

<sup>45</sup> Judgment of *Audiencia Provincial* of Zaragoza (Sect. 4<sup>a</sup>) of 20 October 2003, *Clarins Paris/Supermercados Sabeco*, num. 558/2003, (AC 2003/1693), par. 5; Judgment of *Audiencia provincial* of Madrid (Sect. 28<sup>a</sup>) of 5 October 2006, *Bulgari y Hevige Distribución S.L/Makro Autoservicio Mayorista S.A.*, num. 140/2006, (JUR 2007\54756), par 3; Judgment *Audiencia Provincial* of Alicante (sect. 8<sup>a</sup>), *L'oreal y otros/Univexva S.L*, num. 352/2008 of 14 October 2008 (JUR 2009\26671), par. 8.

<sup>46</sup> *Vid.* F. CARBAJO CASCÓN, *La distribución selectiva...*, p. 188.

25. Without prejudice to any action regarding the infringement of his mark the owner of the trade mark, may also take action, not only against the free rider, but also against the authorized distributor because they infringed the clause prohibiting the resale to non-members of the official distribution network. Nevertheless, from our point of view, such action against the official distributor will not be as effective in cases where parallel imports take place because the network is not sufficiently shielded. In other words, the manufacturer may have closed their distribution networks differently in the various countries in which they operate. So, maybe in some countries, the manufacturer has opted for selective distribution and in others for a more permissive distribution. This detail is relevant to the official distributor who resells the products to third parties. If there is no such clause prohibiting the resale to third parties, the official distributor would not have breached the contract and it would be more difficult for the holder of a trade mark to defend themselves against parallel trade.

## IX. How to protect the official network and the brand from unfair competition

### 1. Unfair competition illicit against free riders

26. The trade mark holder and / or owner of the official distribution network as well as members of the official distribution network can take action against the independent reseller on the grounds that their actions violate the Spanish Unfair Competition Law (Ley 3/1991, de 10 de enero, de Competencia Desleal)<sup>47</sup>. However, it is not easy to fit within some of the activities of parallel imports as illicit established by Spanish Unfair Competition Law<sup>48</sup>. Despite the circumstances in each case playing an important role, we have to remark five unfair competition acts which could be used against the free rider. These are:

27. *Deceptive acts.* The art. 5.1 LCD provides that a behavior is unfair for being misleading when it involves the use or dissemination of false or incorrect information or omission of true, and brings to mislead the recipients of such information who may alter their economic behavior in relation to aspects such as the nature, characteristics, method of manufacture or distribution of goods or services, the existence or not of after-sales service, among others<sup>49</sup>.

A parallel importer reselling products outside the official network may mislead buyers by making them believe that they belongs to the official network, and therefore can offer pre-sale and after-sale services<sup>50</sup>. However, when the customer is aware that he is not buying the product from an official distributor and after-sales services are not going to be provided, there is no disloyalty in the free rider's behavior because there is no deception. Thus, if the independent distributor reported his condition to consumers or if a reasonably informed consumer can easily deduce from the way a product is sold (no advertising, no customer care or the features of the shop) that who is selling it is not an official distributor, these acts will not be illegal under the Spanish Unfair Competition Law<sup>51</sup>. In the Spanish Unfair Competition Law, there is an act of deception according to art. 5 when the free rider's acts are not only

<sup>47</sup> Official Journal number 10, of 11 January 1991. It was modified by Law 29/2009, of 30 December (Official Journal number 315, of 31 December 2009).

<sup>48</sup> Vid. E. BARRERO RODRÍGUEZ, "La posible configuración de las actividades de comercio paralelo como actos desleales de confusión o de engaño en el marco de la distribución selectiva", *Rcd*, nº 18, 2016, p. 4.

<sup>49</sup> Regarding art. 5 of the Spanish Unfair Competition, vid. Law J.A GARCÍA-CRUCES GONZÁLEZ, "Art. 5 LCD. Actos de engaño", in A. BERCOVITZ RODRÍGUEZ-CANO (Dir.), *Comentarios a la Ley de Competencia desleal*, Aranzadi Thomson-Reuters, 2011, pp. 118-142; C. LEMA DEVESA, "Los actos de engaño en la Ley de Competencia Desleal", in J.A GÓMEZ SEGADE/ A. GARCÍA VIDAL (Dir.), *Derecho Mercantil en el umbral del siglo XXI. Libro Homenaje al Prof. Dr. Carlos Fernández-Novoa en su octogésimo cumpleaños*, Marcial Pons, Madrid, 2010, p. 355 *et seq*; A. TATO PLAZA/ P. FERNÁNDEZ CARBALLO-CALERO/ C. HERRERA PETRUS, *La Reforma de la Ley de Competencia desleal*, La Ley, Madrid, 2010; A. ZURIMENDI ISLA, "Actos de engaño", en F. MARTÍNEZ SANZ (Dir.), *Comentario práctico a la Ley de Competencia Desleal*, Tecnos, Madrid, 2009, p. 95 *et seq*.

<sup>50</sup> Vid. F. CARBAJO CASCÓN, "La marca en los sistemas de distribución selectiva (el problema de las ventas paralelas)", en E. GALÁN CORONA/F. CARBAJO CASCÓN (Coord.), *Marcas y distribución comercial*, Ediciones Universidad de Salamanca, 2011, p. 174.

<sup>51</sup> Vid. F. CARBAJO CASCÓN, "La marca en....", p. 174.

misleading but also the conduct of the parallel importer alters the economic behavior of customers<sup>52</sup>. That is, the client, as a result of false or truthful information, decides to purchase the products from a free rider and not from the official distributor.

**28. Likelihood of association.** The art. 6.2 Spanish Unfair Competition Law includes the likelihood of association, which is closely related to acts of deception since the recipient is misled in both of them. The difference between the two types is that in the case of the association, error refers to the identity of the offeror. The illegal act is making the consumer incorrectly associate the origin of the provision<sup>53</sup>. In connection with parallel trade, the free rider can commit this act of unfair competition when they sell products which contain this legend on the reverse “the products can only be sold by authorized dealers”<sup>54</sup>. This can lead to a wrong assumption about the origin of the products. The problem arises when this association makes the consumer think that the free rider is going to provide presales or aftersales services<sup>55</sup>. However, a well-informed consumer could easily detect that he is acquiring the product of an unofficial reseller by the simple presentation of the products or the service received. If you know that you are buying the product to an unofficial distributor there is no risk of association.

**29. Use of another's reputation.** The art. 12 LCD provides that it is unfair to take advantage of another's reputation<sup>56</sup>. This behavior happens when someone takes advantage of the professional reputation of another in a market. It usually has to do with the use of distinctive signs of other traders. This is what happens with parallel trade of branded products. The free rider takes advantage of the prestige of the brand and its advertising as a business strategy. In this sense it can be said that such use is practically unavoidable, since both aspects go hand in hand<sup>57</sup>. From our point of view, once the trade mark right is exhausted, the resale of the product is free, and being a branded product, the reputation the trade mark is, almost always, going to give an advantage to the free rider. Thus, the more prestigious the mark, more advantage the free rider will get and the less likely this kind of illegal claim of unfair competition prospers.

**30. Inducing a breach of contract and using it.** On the one hand, art. 14.1 Spanish Unfair Competition Law points out illegal the act of inducing another to breach basic duties of a contract. We can find a clear example when an independent distributor induces an authorized member to not respect the clause prohibiting resale to third parties not authorized by the official network. On the other hand, the art. 14.2 Unfair Competition Law states that it is unfair induction to provoke the termination of a contract or the use of a foreign contractual infringement when it is intentionally accompanied by circumstances such as deception, the aim of eliminating a competitor or similar<sup>58</sup>. With respect to parallel

<sup>52</sup> Vid. J. A. GARCÍA-CRUCES GONZÁLEZ, “Comentario al art. 5 LCD...”, pp. 128 y 131.

<sup>53</sup> Regarding art. 6 of the Spanish Unfair Competition, *vid.* M<sup>a</sup>. M. CURTO POLO, “Artículo 6. Actos...”, pp. 143-153; V. MAMBRILLA RIVERA, “Prácticas comerciales y competencia desleal. Estudio del Derecho comunitario, europeo y español. La incorporación de la Directiva 2005/29/CE a nuestro Derecho interno (Incidencia en los presupuestos generales y en la cláusula general prohibitiva del ilícito desleal)(Y tercera parte)”, *Rcd*, núm. 6, 2010, p. 75 *et seq.*; J. MASSAGUER, *Comentario a la Ley de Competencia Desleal*, Civitas, Madrid, 1999; M. MONTIAGUDO, “El riesgo de confusión en el Derecho de marcas y en el Derecho contra la Competencia Desleal”, *ADI*, 1993, p. 73 *et seq.*; J. VIERA GONZÁLEZ, “Los actos de confusión e imitación en el Proyecto de Ley por el que se modifica el régimen legal de la competencia desleal”, *Rcd*, núm. 6, 2010, p. 153 *et seq.*

<sup>54</sup> Vid. F. CARBAJO CASCÓN, “La marca en...”, p. 173.

<sup>55</sup> Vid. E. BARRERO RODRÍGUEZ, “La posible configuración...”, pp. 10-11; A. F., MUÑOZ PÉREZ, “El conflicto entre...”, p. 729.

<sup>56</sup> Regarding art. 12 of the Spanish Unfair Competition, *vid.* A. ARROYO APARICIO, “Artículo 12. Explotación de la reputación ajena”, A. BERCOVITZ RODRÍGUEZ-CANO (dir.), *Comentarios a la Ley de Competencia desleal*, Aranzadi Thomson-Reuters, 2011, pp. 317-350; E. GALÁN CORONA, “Supuestos de competencia desleal por violación de secretos”, en A. BERCOVITZ (Coord.), *La Regulación contra la Competencia desleal en la Ley de 10 de enero 1991*, BOE, 1992, p. 91 y ss; J.I. RUIZ PERIS, “Una reforma consumerista de la Ley de Competencia Desleal o Reforma no siempre significa mejora”, *La Reforma de la Ley de Competencia Desleal*, AA VV, J.I. RUIZ PERIS (Dir.), Tirant Lo Blanch, Valencia, 2010, p. 13 *et seq.*

<sup>57</sup> Vid. C. GÓRRIZ LÓPEZ, *Distribución selectiva y...*, p. 359.

<sup>58</sup> Regarding art. 14 of the Spanish Unfair Competition, *vid.* E. M<sup>a</sup> DOMÍNGUEZ PÉREZ, “Artículo 14. Inducción a la infracción contractual”, A. BERCOVITZ RODRÍGUEZ-CANO (dir.), *Comentarios a la Ley de Competencia desleal*, Aranzadi Thomson-Reuters, 2011, pp. 379-403; J.A. GÓMEZ SEGADÉ/A. GARCÍA VIDAL (Dir.), *Derecho Mercantil en el umbral del siglo XXI. Libro Homenaje al Prof. Dr. Carlos Fernández-Novoa en su octogésimo cumpleaños*, Marcial Pons, Madrid, 2010; A. TATO PLAZA/P. FERNÁNDEZ CARBALLO-CALERO/ C. HERRERA PETRUS, *La Reforma de la Ley de Competencia desleal*, La Ley, Madrid, 2010.

trade the first violation of art. 14.2 LCD would not be relevant, since a parallel trader does not seek the completion of an agreement but the breach of it by the official distributor in order to access to goods<sup>59</sup>. In addition, induction to the termination of a contract is entirely lawful within the proper functioning of the market. It is natural to look for customers or production factors of competition. Illicit only takes place when the circumstances which accompany the induction are contrary to << the objective good faith >>. In other words, deceit or bad practices are used for the termination of the contractual relationship<sup>60</sup>. The illicit art. 14.1 exists with induction mere breach of contract. It is not necessary that the inductor achieve its objective. The biggest problem for infringement claims of this type is the evidence. Although no conclusive evidence is required, as it can be obtained - from a particular data as a set of circumstances surrounding a particular action, prove that there has been such influence to breach the contract can be difficult, especially when lacking documents substantiating such induction<sup>61</sup>.

**31.** However, we can say that it is easier to prove the illicit use by parallel trader, especially when this act is accompanied with deceit. This could be the case when the parallel trader pretends to be an official distributor. The advantage would lie in the access to products without such breach of contract that would have been impossible with an official distributor. There are two key aspects in which the plaintiff should focus: 1) the free rider is aware of the breach of contract by official distributor. When products are identified by code numbers and are accompanied with legends prohibiting resale, it is not very difficult to presume that knowledge<sup>62</sup>; 2) the disloyalty of the official distributor. In this case with the methods normally used in selective distribution systems -codification of goods, restrictions on warranties- the problem of proof may not be such.

## 2. Proof and the relationship between unfair competition and infringements of trade mark rights

**32.** In cases where the holder of a right of industrial property deems its rights violated he should go to court to assert infringement of this with the claim of unfair competition<sup>63</sup>. Given these claims, the Spanish courts used to, after estimating the trade mark infringement, recognize unfair competition illicits. These kinds of lawsuits are common in parallel trade of branded products.

**33.** However, there is now a new case law in which it is considered that when the infringement of an intellectual or industrial property is estimated, analysis of acts of unfair competition are invoked, proof is not necessary<sup>64</sup>. The reason is that with the estimate of the infringement, for example, of a trade mark right, unfair competition acts are recognized as well. Such acts of unfair competition, to be included within the scope of the exclusive right -confusion and association, deception, use of another's reputation... - do not need to be re-analyzed in view of the Unfair Competition Law. A different question arises when the Intellectual/Industrial property Law doesn't give protection, in that case, it is possible to claim on grounds unfair competition. This happens, *ad ex.*, with the induction to the infringement of a

<sup>59</sup> Judgment of *Audiencia Provincial* of Cáceres (Sect. 1<sup>a</sup>) de 22 de enero de 2001, num. 12/2001, AC 2001/542, in this, an independent distributor who sold cosmetics brand *Clarins* was condemned to compensate the owner of the trademark and an official distributor for damages that had caused his unfair behavior.

<sup>60</sup> *Vid.* E. M<sup>a</sup> DOMÍNGUEZ PÉREZ, "Artículo 14...", p. 387.

<sup>61</sup> Judgment Supreme Court of 11 July 2006, num. 746, FJ 7 (RJ 2006\4974).

<sup>62</sup> *Vid.* F. CARBAJO CASCÓN, "La marca en ...", p. 177.

<sup>63</sup> Judgment of *Audiencia Provincial* of Zaragoza (Sect. 4<sup>a</sup>) of 20 October 2003, *Clarins Paris/Supermercados Sabeco*, num. 558/2003, AC 2003/1693, par. 6, in this resolution it was recognized either an infringement of trade mark rights or an illicit of unfair competition by deceptive acts (article 5), confusion (article 6) and use of another's reputation (Art.12 LCD.); Judgment of *Audiencia Provincial* of Madrid (Sect. 28) of 5 October 2006, *Bulgari Spa y Hevige Distribución S.L./Makro Autoservicio Mayorista S.A.*, num. 140/2006, JUR 2007/54756, par. 4 where it is recognized an infringement of trade mark rights but at the same time the independent distributor was condemned by using a *breach of contract* of an official distributor (art. 14.2).Final del formulario

<sup>64</sup> Judgment of *Audiencia Provincial* of Alicante (Sect.8<sup>a</sup>) of 14 October 2008, *L'Oreal S.A. y otros/ Univexva S.L.*, num. 352/2008, JUR 2009/26671, par. 9.

basic contractual duty (art. 14.1 Spanish Competition Unfair Law). There are illicit acts that are not included in trade mark law but, additionally, they can protect the holder's subsidiary. The complementary nature of the law of unfair competition also appears in certain behaviors that don't infringe the exclusive right<sup>65</sup>. Thus, *ad ex.* this could happen when the trade mark rights are exhausted but the behavior of the independent distributor is unfair. Thus, one could say that the estimate of the infringement of trade mark's rights becomes an unnecessary analysis of possible unfair competition acts, unless those free rider's behaviors cannot be included under infringement of the exclusive right<sup>66</sup>.

**34.** This new case law is particularly important as far as the burden of proof is concerned. The probative effort of the trade mark holder decreases when they allege infringement of the distinctive sign when claiming unfair acts. While in the case of infringement of a trade mark, holder must prove misuse of his sign to sue; acts of unfair competition claim has the burden of proving such illicit acts, which, as noted in the previous section, it is not without difficulty<sup>67</sup>.

## X. What are the usual practices to restrict parallel trade?

**35.** Manufacturers, suppliers or official distributors do not like the existence of parallel trade. Therefore they have developed many practices to paralyze it. We can differentiate between "direct restrictions" and "indirect restrictions". Regarding the first, these could be all the provisions of a vertical agreement which has the aim to restrict distributor's actions with its contractual territory and directly preclude the possibility of reselling products to other markets. Those territorial restrictions fall in breach with art. 101 TFEU. It doesn't matter if these restrictions are put into practice by the parties<sup>68</sup>. Hence, if a clause restricts competition by nature, *ad ex.*, clauses prohibiting exports, it is irrelevant if these kinds of clauses have not been implemented by the distributors, its mere existence in an agreement to create a "visual and psychological" effect which contributes to a partitioning of the market<sup>69</sup>.

**36.** Therefore, because the Commission and the ECJ have traditionally considered that such restrictions have the object of restricting competition and are contrary to art. 101 TFEU, manufacturers and suppliers are trying to prohibit parallel trade through implicit contractual clauses and other practices instead of explicitly. Practices like sending circulars to official distributors. It has been studied whether this kind of practices to limit parallel trade can fall within the scope of art. 101 TFEU or whether it was a unilateral decision by the supplier or manufacturer. In this regard, the European competition authorities have created a broad concept of agreement<sup>70</sup>. The implicit measures, contractual or non-contractual, made by suppliers and distributors to restrict parallel importations have been very different. However, a common feature among them is that it has generally been a tendency to consider them contrary to European competition law to be restrictive in accordance with art. 101 TFEU either by object or effect. Therefore we can point out the following: 1) Dual Pricing; 2) refusal to supply; 3) product differentiation; 4) warranty restrictions; 5) codifying goods.

<sup>65</sup> *Vid.* E. BARRERO RODRÍGUEZ, "La posible configuración...", p. 7; F. CARBAJO CASCÓN, "La marca en..." p. 182.

<sup>66</sup> F. CARBAJO CASCÓN, "La marca en..." p. 182.

<sup>67</sup> *Ibidem*, p. 182.

<sup>68</sup> ECJ of 1 February 1978, *Miller*, C-19/77, *Rep.* 1978, par. 7; ECJ 31 of March 1993, *Ahlstroem Osakeyhtioe and others/Comisión (woodlup)*, C-89/85, C-104/85, C-114/85, C-116/85, C-117/85 y C-125/85 a C-129/85, *Rep.* 1993, p. I-1307, par. 176.

<sup>69</sup> CFI of 19 July 1994, *Herlitz*, T-66/92, *Rep.* 1994, II-00531 par. 40.

<sup>70</sup> Regarding the broad concept of agreement, ECJ of 6 April 2006, *General Motors BV/Comisión*, C-551/03 P, *Rep.* 2006, p. I-03173, par. 34; With respect to Commission's decisions in which circulars, letters and guidelines have been sent by manufacturers to distributors in order to stop parallel trade and these have been considered an agreement concerning art. 101.1 TFEU, *vid.* Commission Decision of 23 December 1977, *BMW Belgium*, OJ L 046, 17.2.1978; Commission Decision of 14 December 1984, *John Deere*, OJ L035, 7.2.1985; Commission Decision of 18 December 1987, *Konika*, OJ 23.3.1988; Commission Decision of 28 January 1998, *Volkswagen*, OJ L 124, 28.1.1998; Commission Decision 20 September 2000, *Opel*, OJ L 059, 28.2.2001; Commission of 10 October 2001, *Mercedes Benz*, OJ L 257, 25.9.2002; Commission Decision of 8 October 2003, *Nintendo distribution*, OJ L 255, 8.10.2003

**37. Dual pricing.** This practice consists on the supplier charging higher prices for products intended for export. The distributor is going to pay a higher price for equal products in case he wants to export them. This is a way to restrict parallel trade by the manufacture/supplier; the distributor is going to have more difficulty exporting the products or at least, it is going to be more expensive, these sales are treated less favourably than national ones. These practices can be carried out in several ways, *ad ex.*, the exclusion of the exports from a bonus system or discounts<sup>71</sup>. The art. 101 TFEU is generally applicable to cases where the supplier provides discounts, bonuses and other incentive measures for the distributors in order to restrict parallel trade.

**38. Refusal to supply.** This practice takes place when suppliers restrict the supply or deny it to their distributors because they want to avoid the export or import from one country to another<sup>72</sup>. This practice aims to prevent distributors from having a huge quantity of products. The problem with this practice is that it is unclear whether it can be considered to fall within an agreement or whether it receives unilateral treatment<sup>73</sup>. If the act is part of an agreement, art. 101 TFEU can be applied if such practice eliminates or restricts competition. In the event of being considered a unilateral act and the company carrying it out as market power it could be considered an abuse of a dominant position contrary to art. 102 TFEU. Although these practices are indirect measures the effect is the same than with a direct prohibition exportation<sup>74</sup>.

**39. Product differentiation.** As we studied in a previous part of the article, manufactures can introduce little differences in the product or in its packet depending on the market the products are going to be marketed. At first sight, this practice can be considered legal, because many times it is a way to take into consideration the consumer's tastes. However, the problem arises when the reason after these practices is to difficult the movement of goods among Member States. Such kinds of measures implemented in the vertical agreements have been subject to the assessment of European authorities who consider them restrictive for the competence<sup>75</sup>.

**40. Warranty restrictions.** This practice takes place when the manufacturer denies warranty or after-sales services in their products when they are sold by free riders. One of the direct consequences of this practice is that the manufacturer will accept that the goods sold outside its network have a "lower status" than those that are marketed by the official network. We find consumers truly affected by this practice, since they are the ones who benefit from these services. For this reason, the legality of the limitation of warranties on products to protect the distribution network from unauthorized third parties should be studied with regard not only to the competition rules but also to the consumers 'rules.

Regarding competition law, in the *Zanussi* case, the Commission considered the conditions imposed on the consumer to access the product warranty fall within the scope of art. 101 TFEU<sup>76</sup>. These conditions basically consisted on the warranty being claimed only to the *Zanussi* branch which would originally have sold the appliance, provided that the product had not been used in another country or modified or altered by people not authorized by the manufacturer. Previous to this case, we can remark the *Hasselblad* case, however, in this case, the Commission could not prove irrefutably the discrimination in the warranties among products sold by the official network and the products marketed outside of it<sup>77</sup>.

<sup>71</sup> CFI of 9 July 2009, *Peugeot*, T-450/05, *Rep.* 2009, p. II-02533; ECJ of 6 April 2006, *General Motors BV/Comisión*, C-551/03, *Rep.* 2006, p. I-03173.

<sup>72</sup> Commission Decision of 18 August 1982, *Ford*, OJ L 256, 2.9.1982; Commission Decision 16 November 1983, *Ford*, OJ L 327, 24.11.1983.

<sup>73</sup> ECJ of 6 January 2004, *Bayer*, C-2/01 P and C-3/01 P, *Rep.* 2004, p. I-00023.

<sup>74</sup> Commission Decision of 8 May 2001, *Glaxo Wellcome*, OJ L 302/1, 17.11.2001.

<sup>75</sup> Commission Decision 93/554/EEC *Zera/Montedison*, OJ-L272/28 [1993], pars. 104, 127 and 128; CFI of 7 July 1994, *Dunlop*, T-43/92, *Rep.* 1994, p. II-0044, pars. 131 and 143.

<sup>76</sup> Commission Decision 23 October 1987, *Zanussi*, OJ L 322, 16.11.1978, pars. 12-14.

<sup>77</sup> ECJ of 21 February 1984, *Hasselblad*, case 86/82, *Rep.* 1984, p. 00883, pars. 34-36.



41. *Codes in goods*. “Codes to trace goods” is another practice widely used by the holders of official distribution networks to detect shortfalls<sup>78</sup>. The reasons to codify the goods can be both «legitimate», *ad ex.*, to detect or to identify imitations in food, pharmaceutical or cosmetic products or to help with the removal from the market of products if those were to have a problem, and «illegitimate», *ad ex.*, to combat parallel trade. The Court of Justice has held that parallel traders can protect themselves, according to competence law, from the harm caused by the identification numbers inserted in the goods<sup>79</sup>. Parallel importers will be able to remove the identification numbers when these cause an artificial partitioning of the market between Member States. This is due to the difficulties people involved in parallel trade have for obtaining supplies from official distributors and others for fear of sanctions being imposed by the producers<sup>80</sup>.

However, in the case of selective distribution of branded products, it is only natural that the trade mark holder wants to protect the network and tries to avoid their products marketing by free riders. Thus, the coding and tracking of goods could be justified on such networks. But not for products that are not worthy of such protection. Still, it must be remembered that the brand that deserves protection is always going to find the limit of the free movement of goods and competition rules. For this reason, the inclusion of identification numbers in products sold in different State Members may be less justified from the competition rules when goods are destined to third States<sup>81</sup>. Besides the identification numbers, there are other techniques equally effective for the identification of parallel trade and for retaliation against traitor members and independent resellers. These techniques can vary from recording orders and sales, auditing regular distributors and investigating buyers as happened in the *Volkswagen* case<sup>82</sup> or using statistical methods based on the information that dealers gave the manufacturer like in the *Nintendo* case<sup>83</sup>.

## XI. What about the parallel trade of pharmaceutical Products in EU?

### 1. Introduction

42. The pharmaceutical sector is one of the most controversial areas where parallel trade takes place. Traditionally, parallel trade in medicines has been characterized by the export of these products from countries in the South of Europe (Spain, Greece, and Portugal, among others) to countries in the North of the continent (Germany, Denmark, UK, etc.). Basically, this flow of imports and exports between south-north countries is a consequence of the different prices among countries<sup>84</sup>. Prices in the South of Europe countries are lower than in the North countries. In the case of drugs this price difference is not, (as it happens with luxury goods) because of the commercial policies (pre-sales services, after-sales services, advertising, etc.) that distributors must perform in order to be integrated in the network, but rather because of factors such as the differences in social security systems among Member States<sup>85</sup>.

Many European governments negotiate drug prices with pharmaceutical companies because they have to cover most of the medical expenses of their health systems. These negotiations allow the State to pay a lower price for the medicines. This allows the State to control the price of medicines<sup>86</sup>.

<sup>78</sup> Commission Decision of 21 December 1994, *Tretorn*, OJ L 378, 31.12.1994, pars. 35 and 61.

<sup>79</sup> ECJ of 11 November 1997, *Loendersloot*, C-349/95, *Rep.* 1997, p. I-6227, par. 40.

<sup>80</sup> ECJ of 11 November 1997, *Loendersloot*, C-349/95, *Rep.* 1997, p. I-6227, par. 40.

<sup>81</sup> *Vid.* F. CARBAJO CASCÓN, *La distribución selectiva...*, p. 105 *et seq.*

<sup>82</sup> Commission Decision of 28 January 1998, *Volkswagen*, OJ L 124, 28.1.1998, pars. 130 *et seq.*; CFI of 6 July 2000, *Volkswagen*, T- 62/98, *Rep.* 2000, p. II-2707.

<sup>83</sup> Commission Decision of 8 October 2003, *Nintendo distribution*, OJ L 255, 8.10.2003. This decision was upheld by the Judgment of ECJ of 10 February 2011, *Activision Blizzard Germany/Comisión*, C-260/09 P, *Rep.* 2011, par. 75.

<sup>84</sup> *Vid.* LIBERATORE, Francesco, “UK calls for a ban of parallel trade of prescription medicines- What are the EU competition law implications?”, *European Competition Law Review*, 2013 34 (4), p. 190.

<sup>85</sup> *Vid.* S. VOGLER/J.E.MARTIKAINEN, “Chapter 19. Pharmaceutical Pricing in Europe”, in Zaheer-Ud-Din Barbar (ed), *Pharmaceutical Prices in 21<sup>st</sup> Century*, Adis, 2015, p. 347 *et seq.*

<sup>86</sup> European Commission and ECJ have had to decide on some issues if there was price control on pharmaceutical products and whether it was contrary to the principle of free movement of goods. The Court has held that the national control of drug prices is not an obstacle to the free movement of goods, provided that pricing is not the result of discriminatory practices (ECJ

It also means that many of the drugs can be purchased by citizens at a significantly lower price than if the prices were freely established by the pharmaceutical companies. But not all states have the same concept. Thus, there are states, mainly in Northern Europe where the price of medicines is freely fixed by pharmaceutical companies. This causes a considerable price difference for the same product between the North and the South of Europe<sup>87</sup>.

However, this price difference between States not only lies in the different public health systems. There are other reasons such as the type of drug, how new the product is, the amount of dose delivered, if this product has got a generic counterpart, etc<sup>88</sup>. In order to avoid these price differences or at least reduce them European institutions have introduced policies to standardize the price of medicines between Member States. An example of this can be Directive 89/105 / EEC of 21 December 1988<sup>89</sup>, establishing rules for the control of drug prices or the High Level Group on Innovation and Provision of Medicines (G10 Medicines Group). Measures, ultimately, with little success since Member States are primarily responsible for the policies with regard to the health of its citizens.

## 2. Problems

### A) Shortages

43. One of the major problems that the existence of parallel trade in medicines can provoke is the risk of shortages<sup>90</sup>. Out-of-stock occurrence takes place in markets where drugs are cheaper. So, one might ask whether this shortage would be possible despite the controls that wholesalers are subjected to when exporting goods from one country to another, both among European countries and third countries and European States. Law 29/2006 of Medicament requires the exporter to notify the Spanish Agency of Medicines the medicines subject to exportation<sup>91</sup>. Moreover, this notification procedure should be followed by parallel trader develops in Circular No. 2/2012. This Circular aims to prevent supply problems that might exist in Spain for certain drugs. Moreover, in 2011 was introduced in Law 29/2006 the possibility of sanctioning the distributor for not having minimum stocks of medicines for normal delivery of their activities or services.

44. Another problem comes up when a “new version” of a medicinal product coincides with its “older version” in the same market. The question is whether the existence of the new version causes the prohibition of the importation of the previous version of the medicine, although there is an import authorization still in effect. In the *Ferring* case, both the Commission and the Court of Justice provided that when the holder of a marketing authorization for a drug revokes it for reasons which do not regard public health, the parallel imports of that medicine cannot be prohibited<sup>92</sup>. This situation often happens when a manufacturer sells a new version of a medicine. The reason for that is that the cause of the revocation is simply a formality and does not affect the quality or effectiveness of the product. Therefore, based on the free movement of goods and the principle of proportionality, the parallel importation of

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of 19 March 1991, *Commision/Belgium*, C-249/88, *Rep.* 1991, p. I-01275; ECJ 7 February 1984, *Duphar*, case 238/82, *Rep.* 1984, p. 00175, pars. 21-22).

<sup>87</sup> Concerning Differential Pricing of pharmaceutical products *vid ad. ex.* S. RICHARD, “Differential Pricing of Pharmaceuticals- Lessons from Economic Theory”, en C. GODT, *Differential Pricing of Pharmaceuticals inside Europe: Exploring Compulsory and Exhaustion for Access to Patented Essential Medicines*, Nomos, 2010, pp. 145- 153; with respect to Differential Pricing of Pharmaceuticals inside EEA *vid.* F. FORNI, “Il Farmaco di importazione parallela ha trovato l’autore del suo riconfezionamiento”, *Diritto comunitario e degli scambi internazionali*, LII, n° 1-2, 2013, pp. 96-100.

<sup>88</sup> *Vid.* in this sense, C. DESOGUS, *Competition and Innovation in the EU regulation of pharmaceuticals: the case of parallel trade*, Cambridge, Antwep, Insertia, 2011, p. 42.

<sup>89</sup> OJ L 40, 11.2. 1989

<sup>90</sup> *Vid.* E. ESTEVE SALA, “Desabastecimiento de medicamentos y comercio paralelo”, *Cuadernos de derecho farmacéutico*, n° 18, 2006.

<sup>91</sup> Spanish Official Journal num. 178, 27.07.2006.

<sup>92</sup> ECJ of 20 September 2002, *Ferring*, C-172/00, p. I-06891, par. 20.

drugs from an earlier version cannot be prohibited because of the holder withdrawing the authorization of the medicine in the State of importation for reasons beyond public health.

## B) Supply quota and dual price by pharmaceutical companies

### a) Introduction

45. The pharmaceutical sector is characterized by its lack of transparency. Pharmaceutical companies keep with distrust the data on their industry. However, even with a so particular industry like this, the competition rules can be applied. A justification for this is that there are other sectors, also with singularities where prices are also established by the states that have to follow the competition rules, *ad ex.*, postal services, tobacco industry or banking services<sup>93</sup>. The price regulation does not justify the pharmaceutical sector receiving a different treatment regarding the application of the competition rules<sup>94</sup>.

### b) Supply quota

46. The supply quota has been analyzed by the competition authorities both in art. 101 TFEU and in the art. 102 TFEU. In relation to art. 101 TFEU, the Commission, in the *Bayer case*, considered that measures to restrict the supply imposed by a manufacturer or supplier to his distributors were contrary to art 101.1 TFEU because it meant a prohibition of exports<sup>95</sup>. However, neither the Court of First Instance of the EU nor ECJ reached the same conclusion. There was no agreement regarding art. 101.1 TFEU. The CFI found that the Commission could not prove that an agreement had been struck between Bayer and the wholesalers, because the court understood that the existing business relationship between the parties was not enough<sup>96</sup>. Therefore, Bayer had not imposed an export prohibition to its wholesalers, nor the supplies were subject to such a ban. Moreover, the Court held that the unilateral policy of fixing delivery quotas implemented by *Bayer*, combined with national requirements of complete assortments affecting wholesalers generated the same effect as an export ban; it did not mean it had imposed such a ban nor that there was a collusive agreement between the pharmaceutical company and its wholesalers<sup>97</sup>. Thus, considering the supply quota imposed by Bayer as a unilateral act it could not be prohibited by art. 101 TFEU.

47. As a result of the difficulty of including these behaviors in the art. 101 TFEU, those affected by supply restrictions have tried to use the art. 102 TFEU because they believe that such limitation (supply quota) constitutes an abuse of dominant position.

48. The Court ruled in this regard in *Sot. Lélos Kai Sia (Syfait II)*<sup>98</sup>. The issue was aimed at denouncing the practice conducted by *GlaxoSmithKline* to limit supply to their wholesalers in Greece on three medicines used for the treatment of migraines, epilepsy and asthma products, in order to avoid export to countries like Germany or UK<sup>99</sup>. The question is whether the limitation of the supply by a company with a dominant position is abusive under art. 102 TFEU. And if it is so, whether it is possible that this practice limiting parallel trade in order to protect investment in research by pharmaceuticals are not prohibited.

49. ECJ resolution of this matter was awaited with great interest because of the situation at that time caused by such disparate positions kept by the Advocates General JACOBS and RUIZ-JARABO CO-

<sup>93</sup> *Vid.* C. DESOGUS, *Competition and Innovation in the EU regulation of pharmaceuticals: the case of parallel trade*, Cambridge, Antwerp, Insertia, 2011, p. 222.

<sup>94</sup> In fact the ECJ has hold that the price competition is, until the expiry of the patent, the only form of competition (ECJ of 16 September 2008, *Sot. Lélos kai Sia/ GlaxoSmithKline*, cases from C-468/06 to C-478/06, *Rep.* 2008, p. I-07139, par. 64)

<sup>95</sup> Commission Decision of 10 January 1996, *Bayer*, OJ L 201, 9.8.1996, pars. 189 and 190.

<sup>96</sup> CFI of 26 October 2000, *Bayer/Commission*, T-41/96, *Rep.* 2000, p. II-03383, pars. 73-110.

<sup>97</sup> ECJ of 6 January 2004, *Bayer*, C-2/01 P y C-3/01 P, *Rep.* 2004, p. I-00023, par. 88.

<sup>98</sup> ECJ of 16 September 2008, C-3 and 3/01 P, *Sot. Lélos Kai Sia y otros/ GlaxoSmithKline*, *Rep.* 2008, p. I-7139.

<sup>99</sup> ECJ 31 May 2005, *Syfait*, C-53/03, *Rep.* 2005, p. I-04609, pars. 5-11.

LOMER<sup>100</sup>. Advocate General Jacobs considered that a pharmaceutical company is not abusing its dominant position when it refuses to serve the total of orders placed by the wholesalers, although it restricts parallel trade<sup>101</sup>. In fact, the Advocate General questions that parallel trade always generates efficiency in prices, since he considers that most of the benefits generated by parallel trade reverses only to distributors<sup>102</sup>.

Nevertheless, Advocate General RUIZ-JARABO understood that neither the reasons relating to public intervention -limited prices or the obligation to maintain reserves to supply the patients- nor defending the legitimate economic interests justify the conduct of *Glaxo*<sup>103</sup>. Regarding innovation, the conclusions reached by this Attorney General are clear: it is not possible to establish a causal link between the possible damage to investment and parallel trade<sup>104</sup>.

**50.** Given the evident discrepancy in the legal reasoning of the Advocates, the Court opted for a conciliatory position between pharmaceutical and parallel importers. Their reasoning defended that when a company with a dominant position in the market refuses to attend without good cause orders of a previous customer it is carrying out an abuse of its dominant position<sup>105</sup>. Furthermore, with respect to parallel imports, the ECJ also provided that parallel trade has some protection in EU law to the extent that favors the development of trade and strengthens competition<sup>106</sup>.

**51.** However, the ECJ was aware that it was necessary to adopt a favorable attitude to all concerned. Thus, the Court held that the fixing of supply quotas to limit parallel trade could seriously harm consumers if these companies decided to stop marketing certain drugs in countries with lower prices<sup>107</sup>. Thus, the Court modulated its doctrine and held that it could be possible to restrict the supply providing that it is reasonable and proportions causes that justified it<sup>108</sup>. The problem is what aspects national courts will use to determine it<sup>109</sup>. The ECJ considers that a key aspect to justify such restrictions must be the abnormal character of the order<sup>110</sup>. Therefore, it will be the characteristics of the order between the company with a dominant position and its customers the ones that will determine whether such restrictions on the supply quota are an abuse of dominant position.

<sup>100</sup> This case was especially curious because they had come twice to the Court by two different Greek authorities. The wholesalers sued Glaxo before the Greek Antitrust Commission and also the Greek civil jurisdiction. Therefore, they used either the administrative way or civil way. In 2003, the first question comes to the ECJ sent by the Greek Antitrust Authorities. At that time, ECJ did not solve the case because it considered the Greek authority did not have jurisdiction on grounds of c 267 TFEU (ECJ 31 May 2005, *Syfait*, C-53/03, *Rep.* 2005, p. I-04609). Despite that Advocate General JACOBS gave his Opinion (Opinion of Mr. Advocate General Jacobs delivered on 28 October 2004, *Syfait*, C-53/03, *Rep.* 2004, p. I-04609). As the wholesalers also attended the civil proceedings, in 2006 the Court of Appeal of Athens sent another question to the ECJ the same clarifications it had requested by the Greek Antitrust Commission in 2003. The Advocate General RUIZ-JARABO COLOMER's Opinion was related to with the case *Sot. Lélos Kai Sia*, in this case, ECJ went inside the substance of the matter (ECJ of 16 September 2008, C-3 and 3/01 P, *Sot. Lélos Kai Sia y otros/ GlaxoSmithKline*, *Rep.* 2008, p. I-713)

<sup>101</sup> Opinion of Mr. Advocate General Jacobs delivered on 28 October 2004, *Syfait*, C-53/03, *Rep.* 2004, p. I-04609, pars. 77-87, 89, 95-97.

<sup>102</sup> Opinion of Mr. Advocate General Jacobs delivered on 28 October 2004, *Syfait*, C-53/03, *Rep.* 2004, p. I-04609, par. 98.

<sup>103</sup> Opinion of Mr. Advocate General Ruiz-Jarabo Colomer delivered on 1 April 2008, *Sot. Lélos kai Sia*, cases from C-468/06 to C-478/06, *Rep.* 2008, p. I-07139, pars. 86, 90-98 and 106-115.

<sup>104</sup> Opinion of Mr. Advocate General Ruiz-Jarabo Colomer delivered on 1 April 2008, *Sot. Lélos kai Sia*, cases from C-468/06 to C-478/06, *Rep.* 2008, p. I-07139, par. 109.

<sup>105</sup> ECJ of 16 September 2008, C-3 and 3/01 P, *Sot. Lélos Kai Sia y otros/ GlaxoSmithKline*, *Rep.* 2008, p. I-7139, par. 34; ECJ of 14 February 1978, *United Brands*, case 27-76, *Rep.* 1978, p. 67, par. 183.

<sup>106</sup> In the same way, ECJ 16 of January 1992, X, C-373/90, *Rep.* 1992, p. I-131, par. 12.

<sup>107</sup> ECJ of 16 September 2008, C-3 and 3/01 P, *Sot. Lélos Kai Sia y otros/ GlaxoSmithKline*, *Rep.* 2008, p. I-7139, pars. 69-70.

<sup>108</sup> ECJ of 16 September 2008, C-3 and 3/01 P, *Sot. Lélos Kai Sia y otros/ GlaxoSmithKline*, *Rep.* 2008, p. I-7139, par. 71.

<sup>109</sup> A case solved by English Courts was *Chemistree Homecare Ltd v. AbbVie Ltd Case*, n° A3/2013/0559, EWCA Civ. 1338, [7 of November 2013]. Concerning this case *vid.* D. W. HULL, "The application of EU Competition Law in the Pharmaceutical Sector", *Journal of European Competition Law & Practice*, 2015, vol 6, n° 1, pp. 68-69.

<sup>110</sup> It was considered in *United Brands*, that a practice such as cutting supply can not be abusive when orders from distributors are abnormal, although the company occupies a dominant position, it has the right to protect its commercial interests (ECJ of 14 February 1978, *United Brands*, case 27-76, *Rep.* 1978, p. 67, par. 189) *Vid.* B. CONDE GALLEGU, "La política de competencia en el sector farmacéutico: nuevos desafíos para los derechos de propiedad industrial y el derecho de la competencia", *ADI*, núm. 31, 2010-2011, p. 62.

## c) Dual pricing

**52.** Dual pricing is a practice carried out by pharmaceutical and wholesalers although the first one fixes a different price for the product depending on the market<sup>111</sup>. Products for export have a higher price than those intended to be marketed on a domestic market. The result of these agreements is that the export is restricted. The concurrence of wills between pharmaceutical and wholesalers to include such clauses makes the art. 101 TFEU arise. These clauses are contrary to European competition law to be considered collusive because they restore national borders between the markets of Member States. This has been the view of European Institutions<sup>112</sup>.

**53.** However, this statement is currently difficult to sustain after the *GlaxoSmithKline* case. The Court of First Instance, currently the General Court European Union (hereinafter, GCEU) and the ECJ provided in the last judgments that the protection of parallel trade has limits, and therefore practices such as dual pricing can be justified under some circumstances.

**54.** Glaxo Wellcome, a Spanish subsidiary of GlaxoSmithKline which is a well-known pharmaceutical company of British origin, sent new sales conditions concerning eighty two medicines to eighty wholesalers established in Spain. Among the conditions was the imposition of dual pricing for drugs depending on the market they were destined for. Thus, drugs sold in the Spanish market, where the buyer was a pharmacy or hospital, and therefore subject to subsequent reimbursement by the Spanish Social Security, were sold at a price while drugs intended for export were subject to a different price, generally higher.

**55.** These conditions were accepted by most of the Spanish distributors. However, a few of them sued Glaxo Wellcome to the European Commission. The effects of the dual pricing system were considered similar to those that occur with an export ban; therefore, the agreement was restrictive by object according to art. 101.1 TFEU. In addition, the Commission rejected the request for exemption on the grounds that they had not proven the necessary conditions required by art. 101.3 TFEU<sup>113</sup>.

**56.** In the appeal of Glaxo Wellcome, the GCEU ignoring the existing jurisprudential line so far, understood that the protection afforded to parallel trade must be a result of the positive effects on consumers and should not be protected in every case<sup>114</sup>. In view of this Court, a restriction on parallel trade does not automatically mean a restriction of competition by object. Thus, the Court believes that not all restrictions on parallel trade must be contrary to competition law. Thus, the GCEU considered the possibility of granting an exemption from the dual pricing agreement<sup>115</sup>. The GCEU focused on the dual effect of parallel trade. This allows a greater competition in the drug's price. But, on the other hand, this competition makes pharmaceutical revenues lower reducing their ability to invest in R & D. Therefore, the significance of research in the pharmaceutical sector led the Court to consider that the Commission had not properly examined the evidence submitted by Glaxo Wellcome<sup>116</sup>.

<sup>111</sup> Vid. F. LIBERATORE, "UK calls for a ban of parallel trade of prescription medicines- What are the EU competition law implications?", *European Competition Law Review*, 2013 34 (4), p. 193.

<sup>112</sup> ECJ of 28 April 1998, *Javico*, C-306/96, *Rep.* 1998, p. 01983, pars. 13 y 14; ECJ of 6 April 2006, *General Motors BV/ Commission*, C-551/03 P, *Rep.* 2006, p. I-03173, pars. 67-69; ECJ of 16 September 2008, *Sot. Lélos Kai Sia y otros/ GlaxoSmithKline*, C-3 and 3/01, *Rec.* 2008, p. I-7139, par. 65; Commission Decision of 8 May 2001, *Glaxo Wellcome*, OJ L 302/1, 17.11.2001.

<sup>113</sup> Commission Decision of 8 May 2001, *Glaxo Wellcome*, OJ L 302/1, 17.11.2001.

<sup>114</sup> ECF of 27 September 2006, *GlaxoSmithKline*, T-168/01, *Rep.* 2006, p. II-02969, par. 121, where the Court hold: "While it has been accepted since then that parallel trade must be given a certain protection, it is therefore not as such but, as the Court of Justice held, in so far as it favours the development of trade, on the one hand, and the strengthening of competition (...), that is to say, in this second respect, in so far as it gives final consumers the advantages of effective competition in terms of supply or price (...). Consequently, while it is accepted that an agreement intended to limit parallel trade must in principle be considered to have as its object the restriction of competition, that applies in so far as the agreement may be presumed to deprive final consumers of those advantages".

<sup>115</sup> Vid. B. CONDE GALLEGU, "La política de competencia en el sector farmacéutico: nuevos desafíos para los derechos de propiedad industrial y el derecho de la competencia", *ADI*, núm. 31, 2010-2011, p. 58.

<sup>116</sup> ECF of 27 September 2006, *GlaxoSmithKline*, T-168/01, *Rep.* 2006, p. II-02969, pars. 2 and from 299 to 315.

57. Faced with the appeal filed by the parties, the Court confirmed the judgment of the GCEU in some aspects. The Court considers that the Commission erred in its assessment of the criteria which let the exemption of the agreement. Therefore, the exemption of an agreement requires that the restriction is justified and it is consistent with to objective efficiencies related to improving the production or distribution of goods or to promoting technical or economic progress. For this reason, the Court understands that to appreciate these efficiencies evidence provided by the pharmaceutical company must be verified, so that, within those valuations it is not --surprising to appreciate the peculiarities of the sector. Therefore, the Court holding the Commission has taken into account the data provided by Glaxo -- which shows the potential loss of efficiency caused by parallel trade and the effects of restricting investment in innovation<sup>117</sup>. Therefore, the Court agrees with the GC that a free selling price for medicines that are not reimbursed by Social Security Systems State, may involve greater investment in research. Therefore, an exemption to the agreement to establish a double price, although it restricts parallel trade, could be justified if it increases innovation.

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<sup>117</sup> ECJ of 6 October 2009, *GlaxoSmithKline*, Cases C-501/06 P, C-513/06 P, C-515/06 P y C-519/06 P, *Rep.* 2009, p. I-09291, pars. 81-88.