

European Patent for the Common Market

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I. THE EUROPEAN PATENT

Historical Background

International cooperation first took shape in the 1883 Paris Convention for the protection of Industrial Property¹ which contains very general provisions including equal protection to the nationals of a contracting state and nationals of other contracting states. It also introduced the principle of priority right. This convention provides for the existence of special agreements. Both the Convention on the Grant of European Patents, signed on 5 October 1973 ("Munich Convention")² and the Convention for the European Patent for the Common Market, signed on 15 December 1975 ("Luxembourg Convention")³ constitute such special agreements. It should be noted that the Paris Convention is currently being reviewed in Geneva.

Once the Munich and Luxembourg Conventions have been ratified and come into force, probably in 1979, the work commenced 20 years previously will have been brought to a successful conclusion.

In 1959 the six member states of the communities, under the chairmanship of the commission, established a Working Party, under the chairmanship of Dr. Haertal, which published a first preliminary draft containing most of what is now in the two conventions.

Between 1964 and 1968 work was discontinued because of political differences between the governments in particular with reference to the aim of the draft and the related question of the accession of nonmember states. Furthermore the draft was thought to be too perfectionist and too ambitious and thus unlikely to succeed. It was certainly in advance of its time; for example it contained economic clauses before the Court of Justice of the European Communities came to deal with this question.

During this period of abeyance other negotiations commenced which resulted in the signing, in Washington in 1970, of the Patent Cooperation Treaty ("P.C.T.")⁴ open to members of the Paris Convention. P.C.T. provides for the possibility of submitting an international patent application, for several countries, which is subject to an international examination for novelty. This convention pro-

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vides for the existence of Regional Patent Treaties such as the Munich and Luxembourg Conventions.

At the end of 1968 it was decided to recommence the work in the form of two legal instruments which with their implementing regulations are now more complex than the 1962 draft.

The Munich Convention introduces a single procedure, common to all the Contracting European States, for the grant of patents. It sets up a European Patent Office to assess patent applications pursuant to the rules of patent law laid down in the Convention. If the application fulfills the requirement and the invention fulfills the criteria laid down, a European patent will be granted which will be valid in the designated states. After grant the unitary law applies no further and the patent is then, with certain exceptions, subject to the law of each state for which it is granted. The convention provides for the existence of special agreements, such as the Luxembourg Convention, having the effect that European patents, granted in respect of all their territory, are unitary in that they are subject to a body of law common to all of them.

Relationship of the Luxembourg Convention with the Treaty establishing the European Economic Community

The Munich Convention is a normal international convention between the Contracting States governed by pure international law. The Luxembourg Convention is also between states, the nine member states of the communities but was intended from the first to create a community patent system inseparable from the attainment of the objectives of the Treaty of Rome and thus linked with the community legal order. This is very clearly illustrated by the Preamble. Furthermore Articles 5, 63 and 73 give jurisdiction to the Court of Justice of the European Communities ("the Court of Justice") and Article 93 declares what all member states already accept namely that the provisions of the EEC Treaty have precedence over the provisions of the convention.

Article 68 of the Luxembourg Convention provides that, unless otherwise specified, the convention on jurisdiction and enforcement of judgments in civil and commercial matters ("Brussels Convention")⁵ applies to patent actions. Article 85 provides that the Brussels Convention shall not have effect in any state where it has not entered into force. Negotiations are far advanced on an instrument which will bring the Brussels Convention into force in the three new member states of the European Communities.

II. THE ECONOMIC CLAUSES

Background

There had long been general acceptance of the necessity for provisions to prohibit the partitioning of the Common

Market by means of the Community Patent or of national patents. Member states were ready to accept the principle that the marketing in one member state of goods protected by a community or national patent exhausts the rights resulting from that patent. This principle was expressed in "the Economic Clauses" submitted as draft Articles 32 and 78 to the Luxembourg Conference. However a protocol was also submitted which provided for the economic clauses to come into force only after a transitional period.

The issues regarding the Economic clauses which were finally settled at Luxembourg were:

(a) should the Economic Clauses come into force only after a transitional period?

(b) should the principle of exhaustion of rights apply where the patentee puts the goods on the market for the first time in a member state where there is no patent for those goods?

The issue regarding the protocol providing for a transitional period

In favor of the protocol it was suggested that economic integration in the Common Market was not developed enough to justify the immediate application of the economic clauses and that industry would need a transitional period to adjust to what was claimed to be a new situation.

The effect of the protocol would have been to permit, during the transitional period, the patentee to control the marketing of his goods within the Common Market, within national partitions, by means of infringement actions to prevent the import from one member state to another of goods which he or his licensee had put on the market of the exporting member state, and he could have maintained different prices in different member states.

In paragraph 13 of its Opinion N. 74/209/EEC⁶ the Commission declared:

A Protocol of this sort would therefore set out to amend the Treaty (EEC). An amendment, however whose effect would be to restrict freedom of movement of goods as laid down at present by Community Law could not be carried out by a Convention by Member States outside the procedures expressly laid down by the Treaty (Article 236).

The commission's arguments based on *Deutsche Grammophon v. Metro*⁷ were subsequently further justified by *Centrafarm v. Sterling Drug*⁸.

The protocol was abandoned.

The issue regarding exhaustion of patent rights in respect of goods first marketed in a member state where there is no patent for those goods

Certain member states maintained that it was contrary to the general principles of patent law to apply the exhaustion principle to goods which a person or company directly or indirectly marketed in a member state where they were not covered by a patent so that they could freely enter another member state where that person or company owned a patent covering them. In such circumstances the patentee could not benefit from his monopoly. A third party, without having to incur an inventor's development costs, could, in a member state where they were not patentable produce cheaply goods similar to those of a patentee in another member state. If that patentee wished to export his goods to the member state where he had been unable to obtain protection he would have to reduce his price to compete with the third party. If the exhaustion

principle applied to his exported goods they could freely circulate back to compete with the patentee's goods in the protected member state undermining the higher prices he charged there to recover his development costs. Hitherto it has been rare for industry to apply for patents in all nine member states so that the situation outlined above could frequently arise where proprietors of patents in some member states exported to other member states where they had been unable or unwilling to obtain patent protection. In such circumstances these patentees would not export and, so the argument ran, free circulation of goods would in fact be prevented. The partisans of this argument proposed to limit the economic clauses so that they only applied where goods had been marketed in a member state where they were protected by a national patent or the community patent. Thus these clauses would not apply in a patent free area where, for example a national patent had lapsed or where the community had been enlarged by the accession of a new member state.

The commission in its Opinion 75/597/EEC⁹ admitted that in certain cases a patentee may be forced to sell his products more cheaply in a country where he has no patent if a third party is able to market the product, the subject of the invention, in that country at a lower price. The commission opposed the proposal, making inter alia, the following points.

It is not the purpose of the law of patents to guarantee to the patentee a higher profit than that which can be derived from the market price. A patentee is only granted, for a certain period, the exclusive right to forbid anyone else to make and market the subject of his invention. This exclusive right is the counterpart of the fact that an application for a patent makes the invention accessible to the public.

The proposal was incompatible with the EEC Treaty as it envisaged free movement of patented goods only in the rare event that parallel patents existed in all member states. Thus it would, in the ordinary course of events, lead to a partitioning of the market as regards products put on the market by the patentee or by a third party with his consent in a part of the community where those products were not protected.

A patentee with sufficient productive capacity to cover the needs of the common market as a whole and with no serious competition in member states where he had no patent cover would have been able to benefit from the proposal, maintain different price levels in the protected and unprotected areas and use infringement actions to preserve his position.

The result of the proposal is incompatible with one of the fundamental aims of the EEC Treaty, namely the creation of conditions with regard to the free movement of goods within the community which are identical to those which exist in a domestic market.

The commission drew attention to its earlier written Opinion relying on *Deutsche Grammophon* and then referred to *Sterling Drug* in which the Court of Justice declared:

In fact, if a patentee could prevent the import of protected products marketed by him or with his consent in another member state, he would be able to partition off national markets and thereby restrict trade between member states, in a situation where no such restriction was necessary to guarantee the essence of the exclusive right flowing from the parallel patents.

The question referred should therefore be answered to the effect that the exercise, by a patentee, of the right which he enjoys under the legislation of a member state to prohibit the sale, in that State, of a product protected by the patent which has been marketed in another member state by the patentee or with his consent is incompatible with the rules of the EEC Treaty concerning the free movement of goods within the Common Market.

This decision, like the *Deutsche Grammophon* decision (a case in which no parallel exclusive right existed) is based solely on the fact that the marketing of the goods took place in another member state independently of the existence or absence of parallel protection. Thus the proposal could not be defended on the ground that Sterling Drug was concerned only with products imported from a member state where a parallel patent existed.

The court also took the view that the patentee may by means of an infringement action oppose importation of a product coming from a member state where it is not patentable and has been manufactured by third parties without the consent of the patentee.

It follows that the patentee cannot forbid importation of the product from a member state in which it cannot be patented but where it has been put on the market by a third party with his consent. This is also the case if the patentee himself puts the product on the market in that member state.

The same considerations apply where goods covered by a community patent are marketed in a member state, where the patent has no effect, by the patentee or by a third party with the patentee's consent.

During the conference it was submitted that, whilst the legal arguments of the commission could well be solidly based, the Court of Justice had not yet had an opportunity to rule on a question involving importation of products from a member state where they had no patent cover. As a result of the discussions Article 32 and 81 of the Luxembourg Convention were drafted in their present form. They confirm the principle of exhaustion of rights of community and national patents unless there are grounds which, under Community law, would justify the extension of the patent rights.

Added Emphasis

Before considering the principles enshrined in these articles it is again worth emphasizing that nothing in them affects the right of a patentee to bring an action against any third party who imports into a member state where the patentee owns the relevant patent goods which have been manufactured and marketed by a third party without the patentee's consent in a member state where no relevant patent exists.

Community and national patent rights, as a general rule, are exhausted as soon as the product has been marketed in any member state whether patent protection exists in that member state or not. Thus reasons for the nonexistence of patent protection (e.g. non-patentability of the product, existence of an opposing prior national patent, failure to apply for a patent or lapse of the patent) are irrelevant.

The marketing must have been by the patentee or by a third party with the express consent of the patentee.

There is an exception to this general rule where there are grounds which under community law would justify the

deferment of exhaustion. Community law would justify the deferment of exhaustion. Community law certainly includes the provisions of the EEC Treaty and its subordinate legislation, and the jurisprudence of the Court of Justice. Justification might also be possible on the grounds of principles which are common to the national law of all the member states and which are not contrary to community law. Until there are references to the Court of Justice it is difficult to envisage what can qualify for this exception.

However from *Sterling Drug* it seems clear that the exception cannot successfully be invoked by the proprietor of parallel patents to prevent the import of a product which has been marketed in another member state, where he has patent protection, by the patentee himself or with his consent.

It will be recalled that Sterling Drug claimed:

— that the existence of price differences resulting from government measures and substantial changes in exchange rates were grounds which would justify the prevention of imports. The court ignored the exchange rate argument and dismissed the price differences as of no significance.

— control of the distribution of the product with a view to protecting the public against defects therein was also a ground of justification. The court rejected this argument on the grounds that the necessary measures must be such as may properly be adopted in the field of health control and must not constitute a misuse of the rules concerning industrial and commercial property.

III. ASSIGNMENT AND LICENSES

Assignment

Article 81 (2) provides that where two or more proprietors of different national patents for the same invention have economic connections with each other the principle of exhaustion applies. Thus, for example, a parent company in one member state cannot, by means of an infringement action, prohibit the import from another member state of goods manufactured and sold by its legally independent subsidiary company in that other member state when each company owns a parallel national patent covering those goods. The question of exhaustion of rights in this example should not be confused with the question of competition law and the commission's decision 69/195/EEC *Re Christiani & Nielsen N.V.*¹⁰ to the effect that where a subsidiary is wholly owned by its parent company and it is found as a matter of fact that the subsidiary is not able to engage in economic action which is autonomous of its parent company, then in spite of their separate legal identities the two companies will be regarded as one for the purposes of community competition law.

The article however, does not deal with the situation where the proprietor of two or more parallel national patents assigns one of them to a third party with whom he has no economic connections. So far there has been no ruling by the Court of Justice in such a situation.

Article 85 of the EEC Treaty applies only to restrictions on competition which are either the object, the means of the consequence of an agreement or a concerted practice or a decision of an association of enterprises. It is not unknown for an assignment of industrial property to be an element of a market sharing agreement or concerted

practice. However in many cases the applicability of Article 85 to restrictions on trade between member states involving the assignment of patents may not be important because Articles 30 to 37 of the EEC Treaty may in any case prevent national patent rights from being used to divide up the Common Market.

It will be recalled that in *Centrafarm* the Court of Justice declared that Article 36 of the EEC Treaty allows derogations from the principle of free circulation of goods in cases where there exist patents the original proprietors of which are legally and economically independent.

Original proprietors here, it is submitted, means persons who have made an invention independently of each other and who have each obtained a patent for that invention. An assignee is not an original proprietor but the holder of a derived right. There is no justification for treating such a holder more favorably than the holder of a derived right under an exclusive license, which commercially may be very close to an assignment. If he were to be treated more favorably assignments might well replace exclusive licenses as a means for attempting to partition off national markets.

It seems unlikely therefore that the assignment to third parties of a patent, or of an invention for which the third party can subsequently apply for a patent, will provide an escape from the application of the exhaustion principle "unless there are grounds which, under community law, would justify the extension of the rights conferred by the patent."

Licenses

Under Article 43 (1) of the Luxembourg Convention a license contract may be exclusive or nonexclusive. One should distinguish between a license to manufacture and a license to sell. Under Article 93 of the convention the EEC Treaty, and in particular in this context Article 85 thereof, has precedence. Thus in entering into a license whether written or otherwise, where this is possible, it is essential to see whether or not it contravenes Article 85 (1) and, if it does, to see if an exemption under Article 85 (3) is possible.

Several decisions of the commission with regard to exclusivity are worth studying:

- Re the Contract of Burroughs AG and Geha Werke GmbH¹²
- Re the Agreement of Burroughs AG and Etablissements L. Delplanque et Fils¹¹
- Re the Agreements of the Davidson Rubber Company¹³
- Re the Agreement of A. Raymond & Co/Nagoya¹⁴
- Re Kabelmetal-Luchaire¹⁵
- Re Bronbemaling/Heidemaatschappij¹⁶
- Re AOIP/Beyrard¹⁷

These decisions overrule the relevant parts of the Commission's Notice on patent licensing agreements of 24 December 1962 ("The Christmas message")¹⁸. From these decisions it is clear that an exclusive license may restrict competition because, for the duration of the license, the licensor loses the possibility of granting a license to other firms in the licensed territory. An undertaking by a patentee thus to restrict his freedom is not of the essence of his rights as a patentee even where the licensee has gone to the trouble and expense of improving the invention. Pursuant to Article 85 (3) the commission may declare Arti-

cle 85 (1) inapplicable to the granting of exclusive rights where this results in promoting economic progress by making possible the licensing agreement in question or where, the exclusivity provides a stimulus for the licensee to penetrate a territorial or product market which has not yet been exploited by the licensor.

Article 43 (2) permits the licensor to invoke his rights against a licensee who contravenes any restriction in the license, but only if the license is one to which Article 85 (1) is not applicable. It seems likely that a restriction on manufacture and use can be enforced as can a restriction as to sales territory which requires the licensee by analogy with Commission Regulation 67/67 (19) to refrain, outside the territory covered by the license, from seeking customers for the products to which the license relates, from establishing any branch or from maintaining any distribution depot. However it should be noted that in the AOIP Beyrard Decision the commission said:

The protection of one licensee or assignee against the competition of another licensee or assignee constitutes a restriction of competition within the meaning of Article 85 (1), when such protection results from a contractual prohibition on exports or imports.

and

An exemption can also be granted in an appropriate case for a prohibition on exports applicable to the first sale only and of limited duration, the object of which is the mutual protection of the parties or of other licensees.

A number of arguments have been raised in favor of prohibiting direct imports into the territories of licensees and the patentee.

— The court has only ruled in the situation where the patented goods have been put on the market with the consent of the patentee. If the licensee markets the goods outside the territory allocated to him, such marketing is not with the consent of the patentee. There is no point in permitting a territorial limitation if the licensee can ignore it. In answer to this it is suggested that, pending a ruling of the Court of Justice, the territorial limitation covers the place of manufacture and use and the active seeking of customers.

— The purpose of the patent system is to make new technical knowledge available to the public as quickly as possible in order to promote innovation. The patentee can choose to exploit his invention himself or by transferring his exclusive right to a licensee or he can do both. If he must face competition from his licensee he will have less incentive to grant licenses. Thus industrial development will suffer. If he does grant licenses he will to cover his risks, ask higher royalties thus limiting the competitive power of licensees and reducing the number of candidates. The answer to this lies in Article 85 (3) in appropriate cases.

— Large enterprises can easily circumvent direct competition by establishing their own factories and distribution systems to the detriment of small and medium enterprises which, through lack of resources, have to exploit their patents through licensees. Should such circumvention by a large enterprise result in any abuse of a dominant position Article 86 of the EEC Treaty will provide the answer. The small and medium enterprises may in appropriate cases be able to invoke Article 85 (3).

From the foregoing it seems possible to deduce that where a community patent has been licensed for part of

the territories in which it is effective the licensor and his licensees may be able to enforce restrictions on actively seeking customers, establishing branches or depots for the purpose of selling patented goods in each others territories but that they will not otherwise be able to prohibit direct imports, unless in each case they obtain exemption under Article 85 (3).

According to the Ninth General Report on the Activities of the European Communities (page XLII) by the end of 1976 the commission will be submitting to the council a proposal for a block exemption regulation in respect of certain patent licensing agreements, to benefit mainly the small and medium firms.

By 1979, when the Luxembourg Convention is in force, most doubts as to the interpretation of Article 43 should have been removed.

Compulsory Licensing

The relevant Articles apart from those in Part II Chapter V (Articles 46 to 48 — Community Patents) are Articles 81 and 82 (national patents) and 89 (Community, European and national patents). The governments of the member states also decided in a Resolution to commence work on common rules on the granting of compulsory licenses in respect of community patents.

Article 46 (1) confirms that Article 32, regarding exhaustion of the rights conferred by the community patent, does not apply to compulsory licenses. Article 81 confirms that exhaustion of the rights conferred by a national patent also does not apply to compulsory licenses. It perhaps seems difficult to justify, under community law, different treatment for products marketed under a compulsory license and products marketed under a contractual license. However, until common rules for compulsory licensing exist throughout the community, the different national rules may, it is claimed, if the exhaustion principle is applied, create additional distortion of competition.

The convention leaves it to the national authorities to apply their own, at present, very different rules on the grant of compulsory licenses of which the extent and effect is restricted to the territory of the member state concerned.

Article 89 permits a member state to make a reserve with regard to compulsory licenses for lack or insufficiency of exploitation of community (Article 47) or national (Article 82) patents during a transitional period of not more than ten to 15 years or until the common rules, envisaged by the resolution have become operative. Thus some member states during the transitional period and all member states after the end of the transitional period, will not, in the interest of a rational division of labor in the Common Market, have the right to grant a compulsory license for nonuse if the patented product has been put on the market of another member state to an extent sufficient to cover the needs of the member state where the compulsory license was applied for.

Linguistic Licenses

Article 88 permits, during what could be an indefinite transitional period, a member state to require the proprietor of a community patent to file, with the European Patent Office, a translation, into the language of that member state, of the specification, within three months of the date of publication (in languages other than the official

language of that member state) of the mention of the grant of the patent. If he does this the patentee is fully protected in that member state.

If the patentee fails to observe this first time limit and if he fails to file his translation within three years and nine months from the publication of the mention of the grant, any third parties in that member state may use the invention without the consent of the patentee but the products cannot circulate into other member states where the community patent has effect. If the patentee files his translation within this second time limit he can:

- claim reasonable compensation from the infringer for the period up to the date of filing and
- enforce his rights to the full from the date of filing.

If the patentee intentionally overruns the second time limit, it is submitted that the use by third parties of his invention was with his consent and the resulting products could thus freely circulate. He still has the possibility of filing the translation but would have to grant licenses on reasonable terms to those who had used or made effective and serious preparations for using the invention up to the time of filing. It has been suggested that such licenses are in effect compulsory licenses and thus there is no exhaustion of rights but this argument is unconvincing because, for example:

- it is a matter of choice for the patentee as to whether or not he files the translation. He may decide not to waste money on a translation because he is able to manufacture the product covered by the patent in another member state at a competitive price in sufficient quantity to satisfy the needs of the member state which had made the reservation. In similar circumstances Article 47 does not permit of compulsory licenses;

- if free circulation of such product were restricted some enterprises might be tempted to use late filing as a device for partitioning the market.

The jurisprudence of the court will in due course settle the dividing line between express and implied consent and the question as to whether linguistic licenses are compulsory or otherwise.

NOTES

1. Official English text published by the World Intellectual Property Organization - Geneva.
2. Text published in three languages by the Government of the Federal Republic of Germany.
3. Official Journal of the European Communities ("O.J.") Nr L 17 of 26 January 1976.
4. English text published by the World Intellectual Property Organization - Geneva.
5. Supplement to Bulletin Nr 2-1969 of the European Communities.
6. O.J. Nr L 109 of 23 April 1974, pages 34 to 36.
7. Case 78/70 (1971), Rec. 4871 (1971) CMLR 631.
8. Case 15/74, ECR 1147.
9. O.J. Nr L 261 of 9 October 1975, pages 26 to 30.
10. O.J. Nr L 165 of 5 July 1969 page 12: (1969) CMLR D36.
11. O.J. Nr L 13 of 17 January 1972 page 30: (1972) CMLR D67.
12. O.J. Nr L 13 of 17 January 1972 page 53: (1972) CMLR D73.
13. O.J. Nr L 143 of 23 June 1972, page 31: (1972) CMLR D52.
14. O.J. Nr L 143 of 23 June 1972, page 39: (1972) CMLR D45.
15. O.J. Nr L 222 of 22 July 1975, page 34.
16. O.J. Nr L 249 of 25 September 1975, page 27.
17. O.J. Nr L 6 of 13 January 1976, page 8.
18. O.J. Nr 139 of 24 December 1962, page 2922.
19. Regulation 67/67 of the Commission of 22 March 1967, on the application of Article 85 (3) of the EEC Treaty to certain categories of exclusive dealing agreements, O.J. Special Edition of November 1972 "1967", page 14.