

# Compensating for Innovations

*Employer's rights to take over an employee's invention is greatly limited in Sweden; a change is considered*

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I will give a brief description of the existing situation, and then discuss the proposal for a new law that has been made, and finally I will relate a few compensation cases which have been dealt with by the State Arbitration Board.

## PRESENT SWEDISH LAW

The present Swedish law in this field dates back to 1949. It is optional except in some respects, primarily in that a so-called reasonable compensation cannot be eliminated by negotiation prior to the conception of an invention.

The most characteristic feature of the law is that the right of an employer, according to Paragraph 3, to take over the inventions of an employee is more limited than what can be found in the corresponding law of any other country. Thus, the employer has an unconditional right to take over all rights to the invention of his employee only if:

- a. Research or inventive activity is the main task of the employee.
- b. The invention has been conceived essentially as a result of such activity.
- c. The invention falls within the sphere of activity of the employer.
- d. The invention comprises a specified assignment placed before the employee in the line of duty and falls within the sphere of activity of the employer.

If it should be a question of an invention, the exploitation of which falls within the field of activity of the employer but which has been conceived in some other association with the employment than what is stated above, the employer has an unconditional right only to a nonexclusive license.

This paragraph has caused several problems, particularly because it has been interpreted very narrowly by the State Arbitration Board. Thus, as inventions falling under points a - c, only those inventions have been included where it has been possible to prove that the employee has in fact devoted more than 50% of his time to research or inventive activity. This has led to a situation in which, for example, a manager of a laboratory has been able to maintain that he did not

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belong to this category since he devoted more than 50% of his time to administrative work, however qualified his inventive activity in other respects may have been.

Of interest in the present situation is also the fact that, according to Paragraph 6, the employee is entitled to a reasonable compensation for the right to the invention that the employer takes over if the invention proves to be patentable in Sweden.

Further, according to Paragraph 5, there is also a requirement on the employer to notify, within four months from the date when he becomes aware of the invention, whether he wishes to take over any right to the invention. However, during the time up to the takeover, the employee himself is entitled to apply for a patent on the invention, but in that case he must notify the employer as soon as possible.

## PRESENT COLLECTIVE AGREEMENT

As I mentioned, this law is optional and can thus be replaced by a voluntary agreement. This has also been done between the Swedish Employers' Confederation (SAF) on the one hand and the Swedish Association of Graduate Engineers (CF) and the Swedish Industrial Salaried Employees' Association (SIF)—salaried employees in the private sector—on the other hand. The agreement contains a considerably more extensive right for the employer to inventions made in his service.

The inventions are divided into three categories, A, B and C. An A invention is an invention which falls within the duty or special assignment of the employee. By this is meant that the invention shall have been made in the course of the work undertaken by the employee and for which the salary is intended to be a compensation. It is of no consequence whether the work that has resulted in the invention constitutes the main duty of the employee.

A B invention is an invention the exploitation of which falls within the field of activity of the employer but which is nevertheless not an A invention. A C invention is an invention which is neither an A invention nor a B invention.

An A invention belongs to the employer with right of ownership, and the employer may also take over all rights to a B invention.

This extended right on the part of the employer, in relation to the law, has been compensated by a standard compensation system. This means that on average, the employee today receives compensation amounting to a few thousand Swedish Kronor for an invention which results in a patent in Sweden.

In those cases where the invention becomes a great economic success, a higher compensation may be paid.

The agreement contains some specified terms—primarily one of eight months within which the employer shall notify whether he wishes to take over a B invention.

In both the law and the agreement provisions are made for the case that disputes between the parties arise. In such cases the parties may turn to a board of arbitration, which in the case of the law is only advisory. For the Industrial Arbitration Board, however, the Arbitration Act applies, which means that the decision of the Board is without appeal. It can be observed that the law, which is thus applied in a number of government authorities and state-owned companies, has led to a number of disputes in the State Arbitration Board, whereas the Industrial Arbitration Board has not had a single case since it was formed in 1969.

In spite of this, dissatisfaction has been expressed not only concerning the law but also concerning the agreement which, in the opinion of the employee organizations, has led to too small compensations. Therefore, a commission was appointed in 1977 to investigate this matter, and it has now presented its proposal for a new law.

## PROPOSAL FOR NEW LAW

The proposed bill differs considerably from the present law in several respects and is a compromise between the experts taking part in the investigation, almost all of which on one or several points have made reservations to the proposal by submitting special observations.

The controversial issues have been essentially the following:

### 1. *The Right of Disposal*

The proposal would lead to an extension of the unconditional right of the employer to take over an invention, as compared with the Act of 1949, however not to a sufficient extent since, compared with the present agreement, it would only give the employer the right to so-called A inventions.

This would not give the employer the right to so-called experience inventions, which in the opinion of the industry is not a satisfactory situation. Because of the flow of information that exists within the companies, it is not unusual that an invention is conceived as a result of an employee, in the course of his employment, acquiring knowledge about a certain technical field and the current problems associated with this technical field in other sections of the company.

The employers therefore consider it reasonable that they are given a possibility of acquiring the invention, which has been conceived essentially by exploitation of experience gained in their business. The employees, on the other hand, see a more limited right of taking over as a strong argument in a negotiation when it comes to obtaining a larger compensation for an inventor. This would give the employees a possibility to threaten to sell the invention to another party. In reality this extreme step would never be taken, according to the employees.

### 2. *Obligation to Apply for a Swedish Patent*

If the employer takes over the right to an invention,

he is obligated to apply for a Swedish patent no later than six months after the takeover. The alternative is to keep the invention secret, but in that case the employer has to accept that the invention is patentable in Sweden with the ensuing obligation to pay compensation.

In view of the proposed high minimum compensation, the industry finds the alternative difficult to understand. Many examples can be given that the patentability of an invention is hardly any guarantee for its economic value.

### 3. *The Size of the Minimum Compensation*

The proposal introduces a system involving a compulsory minimum compensation. It is the duty of the employer to see to it that the question of compensation is solved by offering the employee a compensation, within certain time limits, which must not be below a specified index-tied amount. This amount is at present approximately 16,000 Swedish Kronor plus social expenses, approximately 30%. If the patent costs are included, this will result in a minimum cost of at least 30,000 Kronor, or US \$6,000, to take over the entire right to an invention in Sweden.

For the majority of inventions which never result in anything, this is far too high an amount to pay in compensation, and there is a risk that the introduction of this law would have an effect which is exactly opposite to its purported purpose—namely, a decline in the technique development.

### 4. *Deadlines and Administration*

The proposal contains a plurality of deadlines which must be observed, above all by the employer. If he is not observant, he may lose the right to the invention completely, be fined for damages, or be obliged to pay considerable compensations for inventions that are really not patentable. Thus, within six months from the allowance of the patent application by the Patent Office, the employee shall be offered a final compensation. Furthermore, according to Paragraph 14, the employer is obligated to pay out the offered nonrecurrent amount immediately, despite the fact that the employee may object that the compensation offered is too small. Such a paragraph may easily lead to the employer regularly offering much too little, which will result in lengthy and expensive negotiations.

An additional problem is that the investigators are of the opinion that Paragraphs 35-37 in the co-determination law (MBL) shall be applied in the matter of so-called preferential right of interpretation. If a dispute arises concerning the size of the compensation, the trade union is thus considered to have a preferential right to decide on the compensation. If the employer does not bring an action before a court or request the opinion of the State Arbitration Board within 10 days from the termination of the negotiations, the interpretation of the trade union shall apply if this is not unreasonable.

Thus, it has not been possible to reach a broad agreement on a new proposal for a law, and this is reflected in the comments which have now arrived from the various quarters to which the proposal has been referred for consideration. The majority of the employers seem to reject the proposal entirely—apart from the

representatives of the state of which at least some are prepared to accept it with certain minor alterations.

Generally speaking, therefore, it is hard to believe that the proposal will lead to a new legislation, although one cannot be sure.

### STATE ARBITRATION BOARD

When it comes to the compensation which at present are recommended by the State Arbitration Board, I have certain problems because the decisions are secret if the parties do not admit publication. However, some cases have been published, and the principles governing the determination of the compensation are of course not secret.

One case which has been discussed a great deal refers to two inventions which are employed in the bakery production of buns and cakes. One of the inventions related to a dough scissors, the other to a device for spreading, for example, almond paste onto a layer of dough. The dough scissors device involved an automatization of a previously manually-used dough scissors.

During the discussion about the size of the compensation, the employer stated that the patent related to devices and not to methods. The saving, if any, that the employment of the invention has entailed cannot therefore be made the basis for determining the compensation. The only factual ground is the value of the machines. The purchase price (including profit for the machine manufacturer) amounts to 4,100 Kronor each for the dough scissors and the spreader. A realistic market price is probably 5,000-7,000 Kronor for the spreader and 15,000 Kronor for the dough scissors.

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If these prices should be applied to the total installation cost of the employer, this would amount to a sum of approximately 400,000 Kronor. Two percent on this net sales price, about 8,000 Kronor, could be considered a reasonable compensation.

The inventor, on the other hand, maintained that the market price must be fixed against the background of the savings that an installation of the device would involve. The inventor was of the opinion that he should be entitled to 25% of these savings in compensation plus 300,000 Kronor for having been prevented, through the acquisition by the employer, from selling the invention to other bakeries in Sweden. He also claimed he had been prevented from applying for patents abroad by the employer having delayed the case.

The board pointed out that both the inventions related to the device. Further, it was of the opinion that the compensation should in principle be determined on the basis of the value of the machine including these devices, compared with other machines for the corresponding purpose available on the market. It is by such a comparison that the commercial value of the invention can be determined. It is another matter that when such a concrete comparison material is not available, it may become necessary to solve the question of compensation with the help of indirect methods of calculation. In the present case there is no information as to the market value of machines which have been manufactured by exploiting the inventions. Therefore, this value must be estimated with the aid of

the investigation that has been submitted regarding the rationalization profits that the use of such machines have entailed.

After some further consideration, the board concludes that in the absence of a further investigation the market price of the spreader device should be fixed at approximately 40,000 Kronor and of the dough scissors at approximately 60,000 Kronor. The board is of the opinion that if the device had been exploited in Sweden, at least some 50 bakeries would have bought them, and then after certain other assumptions it concludes that it should have been possible for the employer to make a gross profit of between 6 and 12 million Kronor. Against this background, the board recommends a compensation of 175,000 Kronor. A minority within the board, including the chairman and the trade union representatives, make reservations against this decision and recommend 750,000 Kronor.

The case is then brought further to arbitration in accordance with Swedish law. During these proceedings the trade union claims that the company has made a bookkeeping profit of 140 million Swedish Kronor for the coming period of 20 years and demand in the first place a compensation of 28 million Kronor and in the second place 2.8 million Kronor. The result is that the board adjudges an amount of 850,000 Kronor.

We have had several similar cases, all of them relating to apparatus the installation of which will lead to certain rationalization profits. For example, a certain improvement of the connection of certain overseas calls has resulted in automation of such calls, with the result that telephone operators have been removed. How should the value of such a saving be assessed!

Personally, I think that one must be extremely careful when making such an assessment.

Normally, the compensation to an employed inventor is often determined against the background of what the employer should have been willing to pay in the form of, for example, royalty for a corresponding invention made by an outside inventor. In this connection, the size of the license fee that can be obtained on a patented product is determined by:

- a. The price of competing products which are not covered by the patent in question.
- b. How great the demand is for the patented product.
- c. How strong the patent is.

If the patent is strong and the price of competing nonpatented products is considerably above the manufacturing cost of the patented product, it is of course possible to take out a high profit/royalty on the latter product.

The scope of protection of the patent is, however, often limited. This means that the possibility of taking out a high price supported by a strong monopoly position is greatly restricted. In accordance with the law concerning the action of the free-market forces, the competitors would otherwise immediately apply all their forces to finding alternative patent-free solutions at more reasonable but still very profitable prices. Also, there is often no reason to doubt the statement of the employer that an alternative solution could be produced. Further, if the employer had been aware of the fact that by exploiting the invention he would be forced to pay a compensation of the order of magnitude

sometimes recommended by the Board, it is not unlikely that he would have investigated alternative possibilities of solving the problem.

In my opinion, it is not economically defensible to regard the situation, which is the basis of the calculations by the employer of the profit generated by the invention, as static. This would presuppose a society without competition. In cases like these, however, it must be considered that a product which, on the basis of a proposed compensation, could be sold on the open market with a profit addition of several hundred per cent, would immediately attract the interest of the competitors. To uphold such a price level would require an extremely strong patent protection. Not even that would help. The prospective profit situation would probably act as a temptation to infringe the patent since, as is well known, the reasonable compensation and the damages adjudged by a Swedish court seldom amount to any deterring figure. On the contrary, they are often fixed at a maximum level of 10% on the net sales value of the patented product.

#### TAXES ON COMPENSATIONS

In closing I would like to point out that at least in

Sweden there are also other problems which do not facilitate a solution to these questions. The taxes. In many cases, the inventor is a well-paid designer which means that he has a rate of taxation of 85% on an increase of his income. If the company pays a nominal compensation of 100,000 Kronor, taking into account the various social costs this would in reality mean that the company would have to pay between 130,000 and 140,000 Kronor, whereas the employee himself would receive 15,000 Kronor—quite a poor efficiency in the opinion of both the employee and the employer. When royalty has been paid, the situation has become even worse because then the employee himself may have to pay the above-mentioned social costs since royalty is considered as income from a business.

Finally, no one has been able to demonstrate that the compensations for inventions made by employees play any major part in influencing the innovative activity. Perhaps this is one of the main reasons why the employers are not very interested in paying unreasonably high compensations. Furthermore, in their opinion the making of inventions has to an increasing extent become a teamwork, and therefore it may be difficult, not to say harmful, for the company to single out a particular person as the inventor.