

# Few Restrictions on Licensing in Canada

*Compulsory licensing aspects, other features explored in review of law; amendments proposed*

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By way of comparison with many countries, there are relatively few legislative restrictions on the licensing of technology under Canadian patent laws. The major feature of the Canadian patent system, as it relates to the transfer of technology, is the compulsory licensing scheme, which has as its purpose the encouragement of the working of a patented invention in Canada.

It must be remembered that a license agreement is a contract. A license is a permission given by the owner of a right in property, such as a patent, to another to invade the right free from legal recourse. The permission may be oral or written. The permission may be a mere dispensation that is revocable. It may alternatively be found in a contract that defines the respective rights and obligations of the licensor and the licensee. A license does not set up rights as between the licensee and the public, but only permits the licensee to do acts that the licensee would otherwise be prohibited from doing. It does not create a property right in the licensed property.

Because the license agreement is a contract, it is subject to the same general rules that relate to contracts in general. A license agreement is construed under its applicable law. Parties may choose an applicable law or may be governed by the principles of private international law.

By entering into a license agreement, both the patentee and a licensee create mutual rights and obligations which are independent and distinct from the patent. Therefore, these rights can subsist whether the patent subsists or not. I will not say any more with respect to "voluntary," as opposed to "compulsory," licenses, except to mention several statutes pertaining to the transfer of technology. The discussion will then proceed to the compulsory-licensing provisions.

## *Canadian Government Controls*

The Export and Import Permit Act places certain restrictions on the export of certain technical devices and technical documentation to certain designated nations. Permits are required to ship such devices or documentation. The list of countries and types of devices and documentation is extensive and beyond the scope of this paper.

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In practice, documents pertaining to the filing of foreign patent applications are not included within the scope of the restrictions. However, the legislation is broad enough to cover such applications. The Patent and Trademark Institute of Canada is lobbying to have patent applications expressly exempted from the scope of the legislation. A clause should be inserted in any license to make the license conditional on obtaining a permit, if necessary.

## *Reporting Requirements*

The Corporations and Labour Unions Returns Act, known as "CALURA," applies to all corporations that carry on business in Canada, unless specifically exempted, which have together with all affiliated corporations, as defined, gross revenues for the reporting period, exceeding \$15 million or assets exceeding \$10 million. Such corporations must file detailed corporate and financial information annually. In certain circumstances, information relating to transactions involving the transfer of technology must also be filed. Annual returns concerning the amounts of royalties paid to persons outside Canada for patents, copyrights, industrial designs, trademarks and tradename rights must be filed. New provisions require additional information relating to transfers of technology from abroad.

## *Tax Considerations*

Under the Canadian Income Tax Act, there is a 25% withholding tax on amounts paid or credited by a resident of Canada to a nonresident as a rent, royalty or similar payment, including any payment for the use of or the right to use in Canada any property, invention, patent, design or model, plan, secret formula, process or other thing whatever. This withholding tax may be reduced or eliminated under one of Canada's international tax conventions. For example, under the Canada-U.S. Income Tax Convention, the rate of withholding tax on royalties, as defined in the Convention, is generally reduced to 10%.

## *Competition Law*

In assessing the validity and enforceability of patent licensing agreements, consideration must be given to those sections of the Patent Act and the Competition Act that are intended to guard against the abuse of exclusive rights under patents. The insertion of any restrictive term in a patent license agreement, even if it constitutes an abuse of exclusive rights, does not avail the defendant as a defense in an action for infringement of the patent concerned. Such abuse can only be established and remedied by the compulsory licensing procedure provided by the Patent Act or by invoking

the powers of the Competition Act.

### *Recordal*

Every grant of any exclusive right to make and use and to grant to others the right to make and use a patented invention, within and throughout Canada or any part thereof, must be registered in the Patent Office. While it is only necessary to register an exclusive license, it is advisable to record even a nonexclusive license. However, because a license often contains terms, such as royalties, which the parties wish to keep confidential, a short-form license agreement should be registered.

The Canadian Government has recently revealed its plans to make amendments to the Canadian Patent Act. One aspect of the proposal relates to voluntary licenses. Although assignments of patents will still have to be recorded, the proposed legislation removes the requirement that exclusive licenses be recorded in the Patent office. However, within a prescribed period, a patentee will have to provide to the Commissioner prescribed information concerning licenses granted after the amendments are enacted. At present, it is not known what information will be required.

## COMPULSORY LICENSES

A patent is not an unfettered right in Canada. It is subject to the rights of others to have or acquire a license under the patent in certain situations. These situations include use by the government and compulsory licensing in the case of an abuse of the patent rights or in respect of patents for foods and medicines. The right to deal with a patent is also restricted by competition law.

### *Use by Government*

The Canadian Federal Government may, at any time, use any patented invention, although it must pay to the patentee a sum that the Commissioner decides to be reasonable compensation for such use. The preferred position of the government extends only to its servants and agents and not to independent contractors or suppliers. It is unlikely that the Provincial Governments are entitled to this advantage.

### *Compulsory Licenses for Abuse*

There is an old tale that an inventor developed and patented an improved carburetor which enables an automobile to travel 200 kilometres per litre of gasoline and that an oil company purchased the patent to ensure that the invention could never be commercially exploited in Canada. In fact, this could not be done for any length of time because the Patent Act provides that, after three years from the grant of a patent, in the case of certain enumerated "abuses," which include the failure to commercially "work" an invention in Canada, an interested person may apply for a "compulsory license," which is imposed on the patentee by the Commissioner if a license is deemed appropriate in the circumstances.

Patents for new inventions are granted not only to encourage invention, but also, so far as possible to secure that new inventions are worked on a commercial scale in Canada without undue delay. "Work on a commercial scale" means the manufacture of the ar-

ticle, or the carrying out of the process, claimed in the patent in or by means of a definite and substantial establishment or organization and on a scale that is adequate and reasonable under the circumstances.

The exclusive rights under a patent are deemed to be abused in a number of enumerated circumstances. However, these circumstances are not exhaustive and, although unlikely, it may be possible to establish an abuse that does not fall within the enumerated list. In the following discussion of the abuses, wherever reference is made to a "patented article," this term also includes articles made by a patented process.

### *Nonworking*

The exclusive rights in a patent may be abused if the patented invention that is capable of being worked in Canada is not being worked within Canada on a commercial scale, and no satisfactory reason can be given for such nonworking. This is the most common ground of abuse alleged and proved. It is the patented invention as defined by the claims that must be worked. Whether an invention is being worked in Canada may be a difficult question to answer. For example, advance engineering work, the appointment of selling agents or licensing does not constitute working of an invention on a commercial scale. Nor does the separation and packing of bulk product into individual packages. On the other hand, the assembly in Canada of parts made outside of Canada may constitute working in Canada, depending on the nature of the invention.

If working is not carried out in Canada, the onus is on the patentee to give a satisfactory reason why it is not carried on. The absence of domestic demand may be a satisfactory reason. But if there is a demand abroad where the patentee works the invention, the absence of demand in Canada may not be a sufficient reason. That an industry based on the patented invention cannot be pursued as profitable abroad because of labor or material costs is not a satisfactory reason. That the demand for the invention is too limited to warrant domestic manufacture is not sufficient either.

### *Importation*

An abuse exists if the working of the invention within Canada on a commercial scale is being prevented or hindered by the importation from abroad of patented articles. Such importation may be by the patentee or persons claiming under the patentee, by persons directly or indirectly purchasing from the patentee, or by other persons against whom the patentee is not taking any proceedings for infringement. It must be noted that mere importation by itself does not constitute an abuse. It must be shown that the working in Canada of the invention on a commercial scale is being prevented or hindered.

### *Insufficient Supply*

An abuse of the exclusive rights in a patent may exist if the demand for the patented article in Canada is not being met to an adequate extent and on reasonable terms. This may occur if the patentee is restricting the supply to keep prices high.

### *Refusal to License*

The exclusive rights in a patent may be abused if, by

reason of the refusal of the patentee to grant a license upon reasonable terms, the trade or industry of Canada, the trade of any person or class of persons trading in Canada, or the establishment of any new trade or industry in Canada, is prejudiced, and it is in the public interest that a license be granted. In order for this abuse to exist, the patentee must refuse a license entirely or attach unreasonable conditions to it. The mere refusal of a license, though, is not sufficient. It must also be shown that the trade as a whole or the trade of the applicant is being prejudiced. Further, the public interest must be served and the abuse must be curable by the grant of a license.

#### *Onerous Conditions*

The exclusive rights in a patent may be abused if any trade or industry in Canada, or any person or class of persons engaged therein, is unfairly prejudiced by the conditions attached by the patentee to the purchase, hire, license or use of the patented article, or to the using or working of the patented process.

#### *Working of Unpatented Materials*

The exclusive rights in a patent may be abused if a patent for a process involving the use of materials not protected by the patent, or for an invention relating to a substance produced by such a process, has been utilized by the patentee so as to unfairly prejudice in Canada the manufacture, use or sale of any such materials.

#### *Application*

After the expiration of three years from the date of the grant of a patent, the Attorney General of Canada or any interested person may apply to the Commissioner alleging that there has been an abuse of the exclusive rights under that patent and asking for relief from such abuse.

#### *No Order*

If the Commissioner is of the opinion that the objects of the Patent Act will be best attained by making no order, the Commissioner may make an order refusing the application and dispose of any question as to costs of the proceedings as the Commissioner thinks just. The application may be dismissed even if an abuse is established. Unlike the compulsory license provisions for inventions relating to foods and medicines, the grant of relief is entirely discretionary and dependent on furthering the stated aim of the Act. For example, if at the time of filing of an application based on nonworking of the invention or the determination of the proceedings, the patentee is taking active steps to pursue domestic working, a compulsory license may be refused.

#### *Revocation*

If the Commissioner is satisfied that the objects of the Act cannot be attained by the exercise of any grant of a license, the Commissioner can order the patent to be revoked, either immediately or after such reasonable interval as may be specified in the order, unless, in the meantime, such conditions as may be prescribed in the order with a view to attaining the aim of the Act are fulfilled. The Commissioner may, on reasonable cause shown in any case, by subsequent order, extend the specified interval. Revocation is an extreme remedy

and has never been ordered in Canada.

#### *Nonexclusive License*

The most common order made by the Commissioner upon finding that a case of abuse of the exclusive rights under a patent has been established is the grant to the applicant of a license on such terms as the Commissioner thinks appropriate. In settling the terms of such a license, the Commissioner must be guided by several considerations:

1. The Commissioner must, on the one hand, endeavor to secure the widest possible use of the invention in Canada consistent with the patentee deriving a reasonable advantage from the patent rights.

2. The Commissioner must, on the other hand, endeavor to secure to the patentee the maximum advantage consistent with the invention being worked by the licensee at a reasonable profit in Canada.

3. The Commissioner must also endeavor to secure equality of advantage among the several licensees. For this purpose, the Commissioner, on due cause being shown, may reduce the royalties or other payments accruing to the patentee under any license previously granted by the Commissioner. In considering the question of equality of advantage, the Commissioner must take into account any work done or outlay incurred by any previous licensee with a view to testing the commercial value of the invention or to securing its working on a commercial scale in Canada.

Among the terms that may be included in the license is one precluding the licensee from importing into Canada any goods the importation of which, if made by persons other than the patentee or persons claiming under the patentee, would be an infringement of the patent. In such case, the patentee and all licensees are deemed to have mutually covenanted against such importation. The reason for this term should be obvious as the goal of the compulsory license is to encourage working of the invention on a commercial scale in Canada. Any order for the grant of a compulsory license operates as if it were embodied in a deed granting a license executed by the patentee and all other necessary parties.

#### *License for Customers*

If the Commissioner is satisfied that there has been an abuse of the exclusive rights in a patent for a process such that the manufacture, use or sale of materials used in the process is prejudiced, the Commissioner may order the grant of licenses to the applicant and to such of the applicant's customers, and containing such terms, as the Commissioner thinks appropriate.

#### *Exclusive License*

If the Commissioner is satisfied that the invention is not being worked on a commercial scale in Canada, and is such that it cannot be worked on a commercial scale in Canada without the expenditure of capital for the raising of which it will be necessary to rely on the exclusive rights under the patent, unless the patentee or those claiming under the patentee will undertake to find such capital, the Commissioner may order the grant, to the applicant or to another person who is able and willing to provide such capital, of an exclusive license on such terms as the Commissioner may think just. In