

Intellectual Property Rights, EEC Policy

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Conflicts between intellectual property rights and community law to continue in 1986, but ground rules are emerging.

The conflict between the concerns of EEC competition policy and those of intellectual property holders and parties to licensing relationships has been a characteristic feature of the first three decades of the European Community. The quest of absolute territorial protection conferred upon intellectual property holders and then loosened by national law presents certain difficulties in a Community attempting to shape 12 member states into a single integrated market. The fact that intellectual property protection is crucial to develop and disseminate technology throughout the Community is recognized, but it is not considered sufficiently important by Community law at this stage to compensate for the risk that exclusive licensing arrangements might hinder the existing tendencies of national markets to resist integration.

From a Community perspective we are in a transitional stage, a period in which there is an absence of Community standardization or full harmonization of intellectual property law. In this transitional stage, as the European Court of Justice has recognized, the determination of the conditions and procedures under which the protection of intellectual property rights is granted is still a matter for national laws (*Maruyama v. Nissey Kasei Gohs* [1982]).

Nevertheless, there are three sources of authority in the Treaty that ensure that this determination is only an initial decision, subject to the ultimate power of Community law to decide when intellectual property rights have been improperly

exercised.

The first of these sources is Article 55 of the Treaty of Rome, which applies to licensing agreements and acts which obligations and restraints in such agreements are caught by Article 85(1) because they have either the intention or the effect of preventing, restricting or distorting competition.

The second source is Article 86, under which holders of patent, copyright, and other forms of intellectual property rights may be viewed as holding dominant market positions, capable of abuse if conduct in the exercise of these rights, which amounts to a violation of Article 86.

Articles 85 and 86 are viewed as a system of competition law, applicable to private undertakings. They have the common aim of maintaining effective competition within the Common Market albeit on different levels.¹ The third source, Articles 20-26, the provisions on the free movement of goods and services, also results in the Court placing limits on intellectual property rights with the aim of avoiding partitioning of the market. Insofar as Articles 20-26 apply to intellectual property rights, they do not bear directly upon private undertakings but upon the application of national intellectual property rights legislation to member states and in particular the enforcement of infringement proceedings in the courts of member states.² These provisions pose the question, when will the very enforcement of intellectual property rights constitute a violation of the Treaty because it amounts to an unjustified inter-

ference with the free movement of goods between the member states?

In all three instances, assuming that the conduct or agreements of some dimension affect trade between the member states, national law may make an initial definition of the scope of the property right, but the Treaty requires that the ultimate power to determine when that intellectual property right has been improperly exercised is reserved to Community law. Let us look at the way this conflict has been resolved in each of these situations.

ARTICLE 85 AND INTELLECTUAL PROPERTY RIGHTS

Licensing agreements can appear quite benign in the competition policy implications of a single state like the U.K. They add to inter-brand competition by bringing, or visa competition onto the market and help to spread the technology throughout the country. Moreover, they have relatively few disadvantages since they can be viewed by national authorities as little more than an alternative to the patentee, himself, exploiting the right. From an EEC competition law perspective, however, licensing agreements are more complex phenomena. They may offer the prospect of a more rapid diffusion of technology throughout the common market and the potential to enhance inter-brand competition. However, they have the less attractive quality of carving out member states as exclusive territories. This is often necessary for the purpose of encouraging businesses to invest in the capital equipment essential to manufacture the licensed product. Never-

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1. See, e.g., *Agge v. AG, Hellenic Gulf v. Hellenic*, 124 ECR 2749.

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olicies, it is thought to endorse existing tendencies in member states to relate integration into a common market.

The task for the European Commission and the Court of Justice in respect of technology licensing has been to decide how the Treaty applies to determine the priorities between these two aspects of technology licensing, and the answer has not always been the same from both quarters.

The Commission has long been prepared to recognize that exclusive territorial protection might be indispensable for patent and know-how licenses and that without adequate territorial restrictions, licensees would not be prepared to invest in the process.

Indeed, in the early 1960s in the *Christiansen Message*,¹ it was prepared to concede that certain restrictive clauses, relating for example to the exploitation of the invention in manufacture, use or sale, resale-of-use limitations, quantity and quality standards and non-competition improvement notification obligations fell outside Article 85(1) altogether. The basis of the Commission's thinking was that these clauses entailed "only the partial maintenance of the right of prohibition contained in the patentors' exclusive right in relation to the licensee who in other respects is authorized to exploit the invention."² As far as restrictions that ensured protection of the grant of exclusivity in the licensee were concerned, however, the Commission was more monumental. It stated, "Leaving out of account the conventional question of whether such exclusive undertaking has the object or effect of restricting competition, they (sic) are not likely to affect trade between Member States as things stand in the Community at present."³

By the 1970s, however, the Commission's view had sharply altered. The views expressed in the *Christiansen message* were explicitly clar-

ified and the Commission made it plain that in its view an exclusive patent licensee was caught by Article 85(1) and required justification under Article 85(3).⁴ Since then, it has remained unwilling to accept the view that such clauses might actually mitigate competition and therefore not be caught by Article 85(1) in the first place. Nor has it been persuaded by the argument that an exclusive licensee is only an alternative to the legitimate possibility that would have been enjoyed by the patentee should he have exploited the patent himself in that territory.

■ Patent Licenses ■

It was only a question of time before the Commission's view led to the need for a patent licensing block exemption since too many patent licenses were caught by Article 85(1) to be able to be exempted individually.

While preparing the final draft of the patent licensing block exemption, the European Court of Justice's decision in *Maire* (1982) was handed down indicating that the Court took a rather different view of Article 85. In *Maire* the Court made the point that not all forms of territorial exclusivity were caught by Article 85(1) and had to be justified under 85(3). It held that the licensee could give an exclusive license to the licensee without automatically falling within Article 85(1), as long as the license was "open," that is allowing parallel imports by other licensees and parallel importers.

What was offensive in that case was the absolute territorial protection granted to the licensee — in the form of obligations placed on fellow licensees as well as the licensee to prevent the export of relevant goods into the licensed territory. This obligation together with the licensee's exclusive right meant that the licensee was "closed"; parallel imports were not possible.

Consequently, the agreement not only fell within 85(1), it could also not be justified under 85(3). But in *Maire* (and the Court made it clear that as long as a license was open, i.e. permitting parallel imports by

licensees, it could include a means of exclusive territorial protection for licensees and not be caught by Article 85(1) in the first place.

Nevertheless, the Commission continued to work, as the assumption that most if not all patent licenses were caught by Article 85(1) and required exemption. Its major concern in the substance of the arguments for the need for greater incentives for licensing in the form of exclusive-territorial protection was to build a reasonably minimal of protection into the block exemption itself, i.e., for example, by allowing a five-year restriction on passive sales and a restriction on active sales for the life of the patent in licensee licensee and licensee. (Regulation No. 209/84). For this method presupposes that Article 85(1) applies in the first place.

While preparing the final draft of the patent licensing block exemption in 1984 it became clear that know-how licensing would also eventually have to be block exempted. The patented licensing regulation was inapplicable to mixed patent/know-how licenses in which the know-how dominated, as well as to pure know-how licenses. Moreover, it offered no protection to licensing in territories where the patent protection was nonexistent, whether owing to expiry, non-granting, or unavailability of patent protection.

The know-how block exemption (Regulation No. 208/84), which was adopted in November 1983 and came into force on April 1, 1985, represents a move to a more licensing friendly legal regime.

Mixed patent/know-how licenses that fall outside the 1984 regulations as well as pure know-how licenses are accommodated in the know-how regulation.

Know-how is given recognition as an intellectual property right, with secrecy as part of its specific subject matter even without a formal status in national law. Know-how licenses can offer 10 years' exclusive-territorial protection for the know-how consisting of a ban on active sales, and this period can be extended for the life of a patent in a mixed agreement in territories

1. *Notion Patent Licensing Agreements*, 10 December 1962.

2. *Ibid.*

3. *First Report on Competition Policy of the Commission* (1962) and, e.g. *Verordening (1973) (E.O.R. 1973) (Commission Report, 1973) C.M.R. 1001*.

where a patent is in issue. (Article 1). They can also provide for licenses a five-year ban on parallel imports by other licensees as well as by third parties. (Articles 1, 3(a), 1, 3). In both cases, the period begins from the date of the first license in the EEC for the technology.

← Acceptance of Ban →

There is acceptance of the post-*Merck* test as a necessary accompaniment to the transfer of know-how (Article 2(3), 3(1), Recod 14) and royalties can be spread over the full license period (Article 2.1(f); 3(4), 17 Recod 15). Both clauses are verbodend.

Yet the Commission continues to be more concerned with the horizontal dimension of know-how licensing relationships—i.e. the potential competition between licensees and licensees than to promote the relationship as two different vertical stages of the technology transfer process. Thus, non-challenge clauses (Article 3(a)) quantity restrictions (Article 3(f)) and non-competition clauses (Article 3(f)) are all included in the *Merck* list.

Moreover, the Commission has once again opted for a "hands-on" method of regulating the licensing process. Know-how must not only be secret and substantial, it may also be identified, i.e. described sufficiently to verify that it meets the requirements of novelty and substantiality. Improvements can only extend the 30-year period of exclusivity if they are made into a formal second licensing agreement. Know-how licenses are viewed as all being caught by Article 85(1) and requiring exemption under Article 85(3) in order to avoid being void under Article 85(2).

Yet the Court's decision in *Mane Sae*¹ has not stopped. Indeed, cases such as *Colief II* (1982), *Perceptis* (1984), and *Elmer Jersey* (1985) have given it renewed vigor. In *Perceptis*, for example, the EC indicated that where certain restrictions are indispensable or ancillary to franchise agreements, such as non-competition clauses of a territorial scope, and provisions that maintain the identity and reputation of the franchisor's network,

they may not be caught by Article 85(1). However, since the Court in *Perceptis* held that territorial exclusivity for franchisees could be caught by Article 85(1), it was necessary to limit a block exemption for franchise agreements (see Regulation No. 4087/88). Nevertheless, the approach of the Court to Article 85(1) indicates a continued divergence of view between Commission and Court.

There has been some speculation about the reasons for the change in the Commission's position.² One possible explanation is that the Commission was initially misled by experts with experience of a single country's competition policy and took a wide-to-narrow policy with a Community dimension. Moreover, it cited an escape route that the new approach serves to ensure that the Commission can maintain a laissez-faire central over developments in the field.

Why is it that the Court has taken a different view of Article 85(1)? One answer is that the Court approaches the article from the vantage point of judges interpreting the language of the Treaty rather than an administration or economists hoping to shape a common market by the exercise of their discretion. The Court's mode of interpretation is not purely textual as in the U.K. courts, but the "purposeful" or even "contextual" interpretation given by the Court do mean with and work through the language of the Treaty. Article 85(1) provides that only "agreements, decisions or concerted practices which— prevent, restrict, or distort competition within the Common market are prohibited" and if an agreement adds a competitive to competition, it can hardly be said to be preventing or distorting it. Moreover, the interpretation given to 85(1) in respect of intellectual property licensing must be in line with the interpretation given to Article 85(2) by the Court in a wide range of com-

petition cases, including joint ventures and distribution agreements.³

What are some of the implications of this divergence of view? One implication is that there may be more for intellectual licensees to attempt an analysis of their licenses to see whether they are caught by Article 85(1) in the first place, for those appear to be something of a new technology exception to the scope of Article 85(1). The novelty of the technology, combined with the need to establish it on the market, might together convince the Court that certain restrictions may be necessary to provide an incentive to a licensing arrangement that it will not be caught by 85(1) at all. Its net effect is to improve competition by bringing another competitor onto the market rather than restricting or destroying it.⁴ Certain licensees will inevitably want to play a safe and attempt to fit into a block exemption. Nevertheless, it remains to be made in this context a revised implication is that there may be a fall-back position to the effect that the clause or agreement is not caught at all by Article 85(1).

ARTICLE 86 AND INTELLECTUAL PROPERTY RIGHTS

In the past year, Article 86 has been applied to intellectual property cases in far greater numbers than earlier years. It has long been clear that possession of a property right can amount to a dominant position, particularly where the geographic market is at least a member state market. It has also long been plain that while the mere existence of such a right, e.g. the ownership of the patent itself, was not an abuse, the exercise or utilization of the property right could amount to an improper exploitation of the product under Article 86.⁵ What was not entirely clear, however, was whether prop-

¹ *See*, e.g., *Case* 155/80 *Merck* [1981] ECR II-4073. The role of patent analysis in Article 85(1) was suggested as a primary test in *Case* 15/74 *Roche* [1976] ECR II-489 and *Case* 10/77 *Parsons* [1977] ECR II-1029. See also *Case* 10/78 *Parsons* [1978] ECR II-1029.

² *See*, e.g., *Case* 10/78 *Parsons* [1978] ECR II-1029. The role of novelty and Article 85(1), 1987 Oxford Yearbook on Competition Law, November 1988, 10-124. *See* also *The Role of Novelty*, 1988 *COMP* 44.

³ *See*, e.g., discussion in *Case* 44/84 *Comptoir* [1984] ECR II-2173 at pp. 2184.

⁴ *See*, e.g., *Case* 10/78 *Parsons* [1978] ECR II-1029 and *Case* 10/77 *Parsons* [1977] ECR II-1029. *See* also *The Role of Novelty*, 1988 *COMP* 44.

only holders as a consequence of abusive conduct prohibited by Article 86—could be forced to provide a licensee to supply to a third party. The DSM settlement cast a long shadow. In two recent cases, however, *Hilti v. Hilti* (1988) and *Reform* (1988) the European Court has indicated that it is prepared to go to some length to recognize the legitimacy of traditional property rights. In both cases the Court reiterated its earlier observations in *Centropet v. Nancy-Rhône Lignite* (1982) to the effect that, with respect to the protection of designs and models and in the absence of Community standardization or harmonization of laws, national legislation may determine not only the conditions and procedures for protection but also which products are to benefit from protection, even where they form a part of a unit that is already protected as such.

In *Valvo v. Veng*, *Valvo* had brought proceedings against *Veng* for infringement of registered design rights in respect of *Valvo* car wings. *Veng's* defense was that the refusal by *Valvo* to grant a license was in breach of Article 86. The European Court's judgment emphasized that the right of the proprietor of a protected design to prevent third parties from manufacturing and selling or importing products incorporating the design without his consent constitutes the very substance of his exclusive right, and that, therefore, to require the proprietor of a protected design to grant a license for the supply of products incorporating the design to third parties, even in return for a reasonable royalty, would amount to depriving the proprietor of the substance of his exclusive right. It held that a refusal to grant such a license contract, in itself, constitutes an abuse of a dominant position. Something more was required in the exercise of an exclusive right by the proprietor of a registered design in order to make it abusive conduct prohibited by Article 86.

The Court gave three examples of abusive conduct:

1. The arbitrary refusal to supply spare parts to independent operators.
2. The fixing of prices for spare

parts at an unfair level.

3. A decision no longer to produce spare parts for a particular model, even though many cars of that model are still in circulation.

In *Reform* another spare parts case, the European Court made substantially the same points.

The clear guidance that appears to be emerging from these new cases is that as long as effective competition is maintained, i.e., as long as the products in question are available and remain so on terms that are not abusive then a refusal to license an intellectual property right will not be automatically abusive. Moreover, if a licensee to manufacture or market them is available and remains so on terms that are not abusive, then a refusal to supply that product may not in fact be abusive conduct.¹³ Where, however, the intellectual property holder refuses both to supply and to license, this possibly could amount to abusive conduct by an intellectual property holder enjoying a dominant position. The recent case of *Magill v. BBC, ITV and RTV* (1988) provides an illustration. In *Magill*, the three T.V. companies produced individual weekly guides and brought a copyright infringement action against *Magill* for bringing out a comprehensive weekly guide. The Commission first decided that the TV broadcasting organizations occupied a dominant position in the market for weekly guides in virtue of their factual monopoly over production and the publication of their weekly listings, as well as their copyright protection. It then found that the companies refused to supply advance weekly listings, combined with their listing of licensees to publishers only of individual weekly guides, was abusive conduct because this prevented the meeting of a substantial potential demand for comprehensive weekly TV guides. The Commission went on to order the companies to end their infringement of limiting their licensing policies, to supply each other and third parties on request and on a number

of reasonable conditions, and if licensees were granted, to grant them for a reasonable royalty.

Magill has been appealed to the Court of Justice and its outcome is not entirely clear. Nevertheless, as *Valvo* and *Reform* the Court has already provided some general rules for licensees whose refusal to supply or license do not cut off all routes to a market with a substantial demand.

ARTICLES 30 AND INTELLECTUAL PROPERTY RIGHTS

Under Article 30 of the Treaty the protection of intellectual property rights is viewed as an exception to the basic principle of free movement of goods. It is allowed as long as it does not amount to either a means of arbitrary discrimination or a disguised restriction on trade between member states. The European Court of Justice, prodded by the Commission, has given a narrow reading to the exception provided in Article 36, preferring to give a greater priority to the needs of the Community. Its progress toward an integrated market,¹⁴ it has repeatedly stressed that the capacity of national law to determine the existence and scope of intellectual property rights recognized by Article 36, is subject to, and limited by, the determination by Community law of the "specific subject matter of such rights."¹⁵

As the Court put it in *Centropet v. Sterling Drug Inc.* (1978):

"In a trademark procedure except for one of the fundamental principles of the Common Market, Article 36 may not only affect the degree from the free movement of goods where such designation constitutes the purpose, subject-matter, rights which constitute the specific subject matter of this property.

In respect of patents, for ex-

13. The exception to Article 22 that the Treaty shall in no way prejudice the laws in Member States governing the ownership of property... has been held to govern only the "existence" of intellectual property rights, not the conditions of their exercise. The exercise may be limited, by the patent owner, to give effect to the prohibition under Article 86: "By Article 22, however, the proprietor of a right enjoys only a personal right, and it is possible to transfer the conditions of its exercise to a licensee and thereby to E.C. Commission (1984).

14. This analysis is suggested by Paul Craig in a recent (1987) column in the *Competition Policy, Recent Developments*, April 1987.

ample,¹² the ECJ has held that the specific subject matter of a patent is "the exclusive right to use an invention with a view to manufacturing industrial products and putting them into circulation for the first time either directly or by the grant of licenses to third parties, as well as the right to impose infringements." The patentee can't try to earn a monopoly profit by exploiting the patent himself, but must be put to the goods on the market himself, or by another party with his consent, or he has exhausted his right to control their further movement. *Convidem v. Sandoz Drug Inc.* (1979).

Within the space created by the doctrine of exhaustion, national law can define the scope of the intellectual property right. For example, when goods have been brought into circulation without the owner's consent, owing to a conspiracy, because the patentee retains his rights to prevent imports under national law (*Stamm v. Handt* (1985)).

Moreover, where national legislation provides for statutory licenses of rights, this effectively restricts the specific subject matter of the patent right to include no more than a right to a fair royalty for the use made of the invention under a license of right. *Allen & Meubon v. Litman* (1986). Similarly, where the member state provides a particular concept of relative novelty — as in section 50(1) of the U.K. Patents Act 1949, its definition will be accepted unless it operates as a disguised restriction on trade or as arbitrary discrimination. *Thurler v. Fausto* (1984). In *Thurler* the infringing goods, consisting of portable radios, had been manufactured in Italy and imported into the U.K., the argument of the importer that the patents were void because the invention was not novel under the more usual test in other member states was rejected because Article 10 did not preclude a member state defining the conditions for the grant of patents so long as they did not amount to a form of arbitrary discrimination or a disguised restriction on trade. The test of arbitrary discrimination was reasonably straightforward.

12. Another example of justice is offered by the Court's decision in the *Alcatel* case that first origin is applied to trademarks.

The U.K. statute was nevertheless inoperative because it applied regardless of the nationality of the applicant or the country of first patent. The test of whether the statute was a disguised restriction was more elaborate. It appeared to require, or at least be satisfied by proof that the purpose of the statute merely concept was to encourage innovation by preventing the "dead hand" of unused or unpublished patent specifications being used to challenge validly granted patents. In other words, Article 10 justified in the extension of the protection provided by national law in this situation.

Furthermore, in *Warner Brothers v. American* (1988), where a Danish video rental firm bought a video in London and imported it to Copenhagen for video rentals, *Warner Brothers* was entitled to bring infringement proceedings under Danish law, which extended copyright protection to video rentals. The fact that *Warner Brothers* had willingly marketed the goods in the U.K. exhausted rights only in respect of sales sales. The Danish statute's recognition of a specific copyright in video rentals could be justified under Article 10 because a specific right of protection in respect of video rentals was essential to insure adequate recompense to authors.

These policy decisions of national law in respect of intellectual property rights all occur, however, within the limits established by the Community law principle of exhaustion.

The purpose of the Community law doctrine of exhaustion of rights is to make it impossible for a patentee to prevent parallel imports once he has licensed to a second member state. The Commission's concern to establish the Community as an integrated continental market is so great that it outweighs the considerations that it might create distortions for farmers wishing to transfer the product to other member states.

CONCLUSIONS

These conflicts between community law and national intellectual property rights will not disappear in the 1990s. Yet, in all these areas

there are legal ground rules evolving that allow licensing to take place. They may not provide the full range of incentives a more productive technology transfer Community policy could provide, but they can be fixed rules.

Broadly, one can envisage two possible prospects for the future. One, a longer term prospect is that of a gradual easing of the constraints of competition policy as the common market under the impetus of 1992 becomes more closely integrated and is intellectual property rights are more fully standardized and harmonized. The Trade Mark Directive¹³ was adopted by the Council on 21 December 1988 and is to be implemented by the member states by 28 December 1991. The Community Patent Convention¹⁴ may possibly be ratified by 1992. These developments will result in further harmonization and standardization. They will also provide a form of a regulation of exhaustion doctrine in the intellectual property laws to all alongside the competition laws. Moreover, the Single European Act and 1992 will further the integration of trade between the member states.

Yet, the timing of this development remains uncertain. There is no assurance of the Community Patent Convention being ratified by 1992. Nor can one be certain when the single European Act will enter in a level of integration that will allow the Commission to relax its grip on licensing agreements.

A second possibility is that the Commission may decide to change its approach and develop a more investor-friendly licensing-friendly competition policy because it more clearly appreciates the point that the transfer of technology within the common market cannot be taken for granted. The Commission appears to proceed under the assumption that the economic and technological energies of the Community are like a potential horse needing to be held on a tight rein. The reality may prove to be that, in the face of fierce competition from

13. 1988 OJ L269 No. 1, 201.

14. OJ L 271, 1988, which provides that patents for a part of the Community that is granted to a state of community patent.

Japan, East Asia and the U.S.A., there is a mood for a much looser rein to ensure that European technology gallops at the desired pace. There are two further arguments that are relevant here. First, the encouragement of transfer of technology itself can have an integrating effect over time. Second, DGIV may decide that its policies should achieve greater consistency with the policies of other divisions of the Commission, designed to encourage the development and

transfer of innovation within the Community. If the Commission can be seen, not by these views it may choose to follow the Court's lead and provide guidelines to licensing agreements which can fall outside Article 85 altogether as well as an easing of the conditions of the Block exemption.

However, even with a more lenient form of regulation under Article 85, the constraints upon the licensing of intellectual property rights provided by Article 86 and

Articles 86-91 will remain in place. Under certain conditions, agreements may initially be exempt under Article 85(1) and nevertheless result in conduct that falls under Article 86. And the parties to licensing agreements and arrangements, which are block exempted under Article 85(1), will be subject to the doctrine of exhaustion under Articles 30-36 and cannot prevent importation once the goods have been put into circulation by licensees in other EEC territories.