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Introduction

Legal philosophers have been wrestling for centuries to define 'property,' but have never advanced much further than the tautology that property is what the law says it is.

This problem has caused practising lawyers very little loss of sleep. Instinctively, if inarticulately, we all know what property is.

The situation is similar with regard to licensing. Although licensing can take a myriad of forms, and is not easily susceptible of definition, most lawyers have a feeling for what it means.

It is simple to suggest that licensing is a right to use property belonging to another, but this remits one to the question of what is 'property' as well as to what is meant by 'use.'

These definitional problems are not entirely academic, as among the issues with which the courts are increasingly dealing, are the kinds of property which can be licensed, and the extent of the restrictions which can be placed upon a license and yet have it remain a license.

Distinction from Sales or Assignments

A threshold point is that licenses, insofar as they generally presuppose transfer of a grantor's ownership rights, are to be distinguished from sales or assignments.

This distinction has importance in the infrigement area, since in some

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jurisdictions it is only the holder of the underlying property right, *e.g.*, a patentee or his assignee, who has standing to sue for infringement.

For example, in Belgium the right to sue infringers belongs to the patent holder only. If the license is exclusive, the patentee has an obligation to sue, but with a non-exclusive license he does not.[1]

In some countries this problem can be cured by a contractual provision authorizing the licensee to sue, but in Belgium such clauses are void.[2]

In Italy[3] and Germany,[4] exclusive licensees are entitled to sue in their own names for infringement, but non-exclusive licensees may not. Therefore, in these countries, and France and Belgium as well, an obligation on the licensor to proceed against infringers should be specified in the contract.

These illustrations may suggest the generalization that non-exclusive or simple licenses, in the main, have effect only as between the contracting parties, while exclusive licenses can give rights against third parties, at least where the property licensed is of a protected nature such as patents or trademarks.

In the Netherlands, the standing to sue situation is slightly different. Absent a contractual authorization to sue for infringement, a patent licensee cannot sue unless the patentee has been notified of the infringement and failed for two months to take action. A trademark licensee has no right to sue, so a contractual procedure for taking action against infringers should be provided.[5]

As assignee or purchaser has no problem with standing to sue in countries where it is a problem for the licensee, so long as he has met the transfer-of-registration requirements, since an assignee or purchaser is deemed to stand as an owner.

Tax Aspects of the Distinction

The distinction between assignment and license also has importance in the tax field. In some jurisdictions, the consideration for transfer of underlying industrial property rights is taxed to the transferor in a different way from royalty receipts.

For example, in the United States, if one transfers all substantial rights

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[1]Belgian Law of May 24, 1854, as most recently modified by the Law of June 1, 1964 (*Moniteur Belge*, June 19, 1964), art. 4.

[2]*Répertoire Practique du Droit Belge*, BREVETS D'INVENTION, No. 301 (1949).

[3]Oriani, *Licensing in Italy*, in Pollzien & Bronfen, eds., INTERNATIONAL LICENSING AGREEMENTS (N.Y. 1965), p. 175.

[4]Reimer, *Patentgesetz und Gebrauchsmustergesetz* § 9, Anm. 84, 63, 7, 71 (3d ed., Cologne 1968).

[5]Netherlands Patent Act (Octrooiwet), 1912 *as amended*, art. 43, para. 5.

to make, use and sell under a patent within a specified territory, the transaction is deemed a transfer of a capital asset.[6] The consideration is taxed to the transferor at the capital gain rate, which is considerably less than the rate applicable to ordinary royalty income.

This favorable treatment can be obtained even if the payment of the consideration is made periodically and calculated according to the productivity or use of the property involved, in a fashion similar to the normal royalty.[7]

The other side of the coin is that such capital payments are normally not deductible in arriving at taxable income for the purchaser of the patent, whereas royalty payments on a license would be. However, this may not make too much difference as the purchaser's cost of the patent can be amortized.[8]

In international situations, it is sometimes possible to manage things so that the payment is deductible as a royalty for the transferee, say in Belgium, and still qualifies as a capital payment to the transferor in the United States.

As these consequences are important, and result from legal notions of whether a document comports a license or a sale, a significant burden falls upon the draftsman to make clear both exactly what has been transferred and the nature of the consideration.

Even careful drafting may not be dispositive, as on occasion the courts will require substance to govern form. For example, in France, the courts have held purported exclusive trademark licenses, drawn to endure for the life of the mark, to be *de facto* sales for both property and tax purposes.[9]

Why Licensing?

There are several reasons why an enterprise might choose to license its products.

First and foremost, licensing is the cheapest way of penetrating a foreign market. No investment and no labor force is required, as would be the case if one went into business directly in the foreign country.

Secondly, the risks are minimal. A licensor has little exposure to the

[6]U.S. INT. REV. CODE of 1954, § 1235. *See* Waterman v. Mackenzie, 138 U.S. 252 (1891); Vincent A. Marco, 25 T.C. 544 (1955), Comm. acq. 1958-2 CUM. BUL. 6.

[7]As to tax effect of field-of-use restrictions, *compare* United States v. Carruthers, 219 F.2d 21 (9th Cir. 1955); First National Bank of Princeton v. United States, 136 F. Supp. 818 (D. N.J. 1956); *Milton P. Laurent,* 34 T.C. 385 (1960); and Wm. S. Rouverol, 42 T.C. 186 (1964), with Fawick v. Commissioner, 436 F.2d 655 (66th Cir. 1971). As to know-how sales, *see* Stalker Corp. v. United States, 209 F. Supp. 30 (E.D. Mich. 1962); Heil Company, 38 T.C. 989 (1962), Comm. acq. 1963-1 CUM. BUL. 4.

[8]*See* MERTENS, LAW OF FEDERAL INCOME TAXATION, §§ 23.72–76 (Mundelein, Illinois, 1972).

[9]*See* Nouel, *Licensing in France,* in Pollzien and Bronfen, eds., INTERNATIONAL LICENSING AGREEMENTS (N.Y. 1965), p. 129.

pitfalls which can arise in doing business abroad, ranging from the dangers of expropriation to making a mis-step due to ignorance of foreign labor or investment laws.

Moreover, licensing is probably the easiest method of getting started and giving one's products exposure in a foreign country. Especially for an enterprise which has little experience abroad, licensing is often a far better way of entering a foreign market than starting from scratch.

Although there is a certain danger that a foreign licensee may become a competitor of the licensor after the license terminates, this is usually outweighed by the likelihood that the parties will become more closely associated and enter into partnership, or the licensor take over the operations of the licensee as a going concern.

Licensing also has certain tax advantages. Under most of the double tax relief conventions of recent years, licensing royalties may be paid out of one country to a foreign licensor with little or no withholding tax, and certainly less tax than would be payable on profits and dividends if one chose the alternative of doing business through a foreign subsidiary.[10]

In most cases, the royalty withholding rates between the United States,[11] England[12] and EEC countries are nil. Lump-sum payments in lieu of royalties also generally escape withholding.

[10]Indeed, the OECD draft model double taxation convention, which has been the basis of most recent double taxation treaties between developed countries, provides for no withholding on royalties paid to a foreign resident if the royalty recipient has no permanent establishment in the country from which payments are made. *See* REPORT OF THE OECD FISCAL COMMITTEE, DRAFT DOUBLE TAXATION CONVENTION ON INCOME AND CAPITAL (Paris 1963).

[11]National income tax withholding rates on patent royalties paid to non-resident U.S. enterprises from EEC countries:

	Normal Rate	*Treaty Rate*
Belgium	20%	Nil
France	19.2% (effective rate)	5%
Germany	25.75% (effective rate	Nil
Italy	28.125% (on ⅔ of gross)	Nil
Luxembourg	12%	Nil
Netherlands	Nil	Nil

[12]National income tax withholding rates on patent royalties paid to non-resident U.K. enterprises from EEC countries:

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Belgium	20%	Nil
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Germany	25.75% (effective rate)	Nil
Italy	28.125% (on ⅔ of gross)	Nil
Luxembourg	12.0%	5%
Netherlands	Nil	Nil

Royalties, as well as lump-sum payments, are subject to value added tax on the Continent, but the burden falls on the licensee, and is not really a burden, since he can recover it by way of credit against the V.A.T. he must pay. Still, for safety, an international licensor is advised to include a provision in his license agreement that royalties will be paid net of V.A.T.

On the negative side, it must be admitted that licensing has the disadvantage of minimizing the amount of control which the licensor can exercise over production and distribution. Also, while it reduces the economic risks to the licensor, licensing normally can be expected to produce a lower long-term profit return than would a successful direct manufacturing and sales system.

Weighing these pros and cons, it would seem that licensing is most appropriate either for small companies, when a substantial investment is not possible, or in cases in which the market to be licensed will require relatively limited quantities of goods and mass production is not required.

It makes little sense for a large company to license a product for mass production when it could be the primary producer and probably realize a greater profit. Although there are exceptions, the American approach to direct investment versus licensing in Europe has tended to follow this view.

American business with Japan, on the other hand, has inclined more to the licensing system, but this is because of the heavy restrictions on foreign ownership participations in Japan.

A Licensing Glossary

A vocabulary or jargon has grown up in the licensing field. In many cases the terms are of English or American origin and are used on the Continent in default of good translations.

A prime example is the ubiquitous term *know-how*. Except for the occasional and usually inadequate definition in a tax statute,[13] this term is in most instances, not defined in municipal law. Of course, it refers generally to the information and techniques necessary to carry out or apply business processes.

In many respects, know-how licenses are a breed apart and some of their peculiar facets are discussed hereunder.

The term *parallel licensing*, or *multiple parallel licensing*, classically refers to grant of similar exclusive licenses for the same industrial property to two or more parties in different territories. In the European context, the term also is used to refer to grants given to two or more parties of the

[13] *E.g.*, English Income and Corporation Taxes Act, 1970, § 386(7). *Compare* U.S. REV. PROC. 69-19, I.R.B. 1969-39, 12.

patent or mark, for the same product taken out in different countries. For example, a grant of the French patent for a product to one party, and of the German patent to another party.

When a party purchases goods in one country and imports them into a second country in which there exists a licensee who is marketing the same products, the first party is said to be a *parallel importer,* and considerable litigation has centered around the right of the second party to prevent *parallel imports* by means of various devices, including industrial property licenses.

The traditional companion of *parallel licensing* in Europe, especially when the licensed property, itself, does not guarantee territorial exclusivity, has been *export prohibition clauses.* These are clauses which prohibit a licensee from exporting outside his territory and from selling to customers who intend to export and usually oblige the licensor to require other *parallel licensees* also to refrain from exporting or selling for export.

Prior to the advent of the competition rules of the Rome Treaty, the combination of *parallel licensing* and *export prohibition clauses* was frequently used to carve up the European market into national units which were the truly exclusive preserve of each national licensee. This has come to be known as *absolute territorial protection.* The recent legal development, examined *hereunder,* has made this technique extremely dangerous from the competition law standpoint, as it inhibits the primary purposes of the Treaty of having one unified European market.

The term *tied license* or *tying arrangements* refers to contractual arrangements requiring the licensee to purchase from a particular source any articles other than the licensed article, or to refrain from purchasing or using items not supplied from a particular source. These arrangements are prohibited by national law in many cases, *e.g.,* Section 57 of the English Patents Act which provides that the penalty for inclusion of these arrangements is nullification of the patent in question.[14] They also create severe EEC competition law problems.

One can unwittingly fall into a tied license situation when the licensor is intended to be a supplier of raw materials to his licensee. Supply, of course, is permissible, but it is advisable never to make it a condition of a license agreement.

The term *package licensing* refers to a situation in which several patents, either related or unrelated, are licensed as a group to one licensee. It has a pejorative connotation when the licensor is in a position to force the

[14]Curiously, there seems to be no counterpart of Sec. 57 in English trademarks legislation, a loophole which would seem to want correction.

licensee to take licenses he does not want in order to get the one or two licenses he does need.

It can happen that a party has a patent which he cannot exploit because another party holds a patent for another part of the end product or process and, indeed, the second party may be blocked by the patent of the first party. This situation can be alleviated by reciprocal grant of licenses, and this is known as *cross licensing*.

Another way of solving this problem, and also facilitating grant of sublicenses for combined patents, is for the holders to place the patents either by license or assignment with a common holder and take licenses in return, or license third parties, if need be. This is called *patent pooling*.

Defined field licensing is still another approach. Rather than granting a license under specified patents, a general license to operate in a defined field may be appropriate. This is especially true when the technology is complex so that know-how, rather than patents, is of primary importance. Such licenses are usually non-exclusive and frequently are limited to a specific commercial plant.

Licensee estoppel refers either to judicial doctrine or contractual provisions (sometimes called *non-aggression* or *non-attack clauses*), preventing a licensee from attacking the validity of his licensor's patent or mark. [Even though it had been a time-honoured doctrine,] licensee estoppel has been invalided in American licensing by the 1969 United States Supreme Court decision in *Lear, Inc. v. Adkins*.[15] Contractual provisions of this nature may also be invalid in Holland, but they appear to be valid in France and Belgium and, to a limited extent, in Germany.[16] English law also recognizes the estoppel principle.

The term *field-of-use restrictions* refers to limitations in a license to specific technical or commercial fields and no others, the other fields of exploitation being reserved to the licensor.

Another important term is *grant-backs*. This relates to the improvements which a licensee may make on a licensed product when using it. The licensor may desire to reserve a right to such improvements in the future and will normally require that details of such improvements be communicated to him. As to future improvement patents, the licensor may require that licenses, even exclusive licenses, be given to him, or that such patents be assigned back to him.

Grant-back clauses of this nature can give rise to charges of patent mis-use, for the reason that they can be used by the larger industrial

[15]395 U.S. 653 (1969).

[16]German Cartel Office (Bundeskartellamt) *Tätigkeitsbericht* 1965, p. 64; 1966, p. 73; 1969, p. 98; 1961, p. 58; 1967, p. 88; 1968, p. 88; 1965, p. 53.

corporations as a way of perpetuating their domination of a field beyond the term of the original patent. For instance, if a patent is granted for seventeen years, but during the course of that term the state of the art advances and the patentee has reserved rights to all future patents, his monopoly can be considerably extended. For this reason, the United States Department of Justice has signaled its intention to attack *exclusive grant-back clauses* as illegal *per se*.[17]

The Legal Context of Licensing

The kinds of property which may be subject to a license are as broad as the definition of property itself. In the field of industrial property, the most common subjects are patents, trademarks, tradenames, copyrights, designs, know-how and trade secrets. A rather vague and new area is computer programs.[18]

These industrial property rights arise and are governed by municipal law. They vary considerably from country to country. For example, in Italy at present,[19] and until 1960 in France, pharmaceutical products could not be patented.

Patents for medicines in France are now subject to considerations of public welfare, and if the patentee does not sufficiently exploit the product by producing sufficient quantity at reasonable prices, the patent can be limited or withdrawn or official licenses given.[20]

Thus, a necessary first step in any licensing of industrial property is to examine in detail the scope of the subject property and the restrictions placed upon it by local law.

By and large, national patent laws give patentees the right to exclusivity within the country of issuance, at least until the first sale of the product. This has usually been construed to include the right to bar parallel importations of the product from abroad. The latter feature of the national industrial property laws seems to be in conflict with the notion of one unified Common Market, and is a source of considerable controversy in the EEC.

In licensing in the international context, one must also consider the various treaties which overlay national law. Among the most important are

[17]Address of Assistant Attorney General McLaren to the PTC Research Institute of George Washington University, Washington, D.C., June 5, 1969, reprinted in CCH TRADE REG. REP., para. 50,246 (1969).

[18]As to computer programs, *cf.* Address of P. T. Mitches to the Canadian Computer Conference, Toronto, September 15-17, 1971, reprinted in 7 LES NOUVELLES 29. (LES NOUVELLES is the journal of the Licensing Executives Society.)

[19]Italian Royal Decree No. 1127, June 29, 1939, Article 14. *See* Italian Civil Code, arts. 2584-91.

[20]French Law No. 68-1, January 2, 1968, arts. 37-38.

the Paris Convention (1883) on industrial property (and the subsequent development toward a European patent), the Berne Copyright Union (1886) and Universal Copyright Convention (1952) in the field of copyright, and the Arrangement of Madrid (1891), as well as the Benelux Uniform Trade Mark Law (1969), in the trademark area.[21]

Heed in license drafting must also be given to the omnipresent threats of domestic restrictive practices legislation, EEC competition law and American anti-trust law, all of which on occasion can have extra-territorial effect.[22]

Generally, those types of industrial property which can be licensed are also freely alienable, subject in certain instances to changes of registration. They are also transferable by will and capable of being pledged.

In Italy, trademarks are not transferable unless the business using the mark is also transferred.[23] The same was true in Belgium until the Benelux Uniform Trademark Law went into effect last year. Under the Benelux law, assignments of trademarks must be for all of the Benelux countries as a bloc, but licenses can be more restrictive as to territory.

The rights of a licensee are generally not assignable without the consent of the licensor. In Italy and France, for example, the courts have refused to recognize attempted assignments by licensees, on the theory that it makes a difference to the licensor who practices an invention or trademark.

This doctrine probably does not apply in the case of a merger or takeover of the licensee, and therefore rights of termination in the event of a major change of ownership of one of the parties to the license should be provided in the license contract. The pattern of business consolidation is such today that if one omits to cover this problem, licensees or licensors may find themselves embarrassingly "in bed" with a major competitor after the latter merges with, or takes over, the other party to the license.

Know-How and Trade Secrets

Know-how and trade secrets are a special case in industrial property. Essentially, know-how licenses are contractual arrangements *inter se*, for disclosing information not generally available. There is no guaranteed exclusivity and anyone else is free to use the information, if he can discover

[21]Texts (except Benelux law) in English available in the UNESCO looseleaf publication, DESIGN LAWS AND TREATIES OF THE WORLD (Leyden 1966).

[22]*See* Wallace, *Multinational Patent and Know-how Arrangements*, 39 ANTITRUST L.J. 791 (1970). EEC competition law and German cartel law can also have extra-territorial effect; *see* Deringer, *A Practitioner Looks at the German and EEC Rules*, in the ABA booklet CURRENT LEGAL ASPECTS OF DOING BUSINESS IN EUROPE (Theberge, ed., Chicago, 1971).

[23]Italian Decree No. 929, June 21, 1942.

and apply it. Accordingly, secrecy obligations on both parties—and not only the parties, but also their employees—are the most important features of know-how licenses. Their strength lies solely with the rules and remedies of municipal contract law.

A licensee of know-how can be placed in an awkward position if the know-how—*e.g.* a manufacturing process—is discovered and used by a third party. The licensee may find himself paying royalties, while his competitor is marketing the products without any royalty burden, and thus can sell them more cheaply with the same profit. There appears to be no principle of law which intervenes here to relieve the licensee, and, theoretically, an obligation to pay royalties can continue in perpetuity.[24]

For this reason, it is essential in know-how contracts, to provide for a reduction or abatement of royalties if a third party acquires and uses the know-how. For instance, a clause can be included to the effect that if, during the period of the agreement, the know-how is published or falls into the public domain otherwise than through the fault of the licensee, the amounts of royalties payable shall be reduced in amounts proportional to the lessened value of the know-how to the licensee as a result of such publication.

A similar clause should be provided in the event that a third party obtains a patent on the know-how. Such a clause may force the parties into a dispute or arbitration as to what the lessened value is, but even that is better than continuing to pay royalties at the original rate.

It is also essential in know-how contracts to provide that the licensee may continue to use the know-how after termination of the license. Otherwise, a licensee of know-how whose license has been terminated, can find himself with a sizeable plant based on his former license and no right to use it.

Furthermore, one must keep careful records of the use and disposition of licensed know-how. If the know-how is allowed to become mixed and jumbled with the licensee's own technology, he can be confronted with an impossible job of "unscrambling the omelette," when the license terminates

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[24]However, German law may require that know-how agreements become unenforceable after such time as the know-how becomes generally known. See *Explanatory Notes to Articles 20 and 21 of the German Act Against Restraints on Competition* in the looseleaf OECD GUIDE TO LEGISLATION ON RESTRICTIVE BUSINESS PRACTICES (Paris, 1966). Moreover, at least one American writer seems to have suggested that a logical result of Lear, Inc. v. Adkins is that know-how royalty arrangements might be required to terminate once the know-how becomes public. *See* Adelman, *An Antitrust Decision: Lear v. Adkins,* 58 A.B.A.J. 45 (1972). In Mr. Adelman's words: "*Lear,* when properly viewed as an antitrust case, dealt with the question of whether it constitutes an unreasonable restraint of trade to collect royalties on a previously secret invention once it has been disclosed to the public." (At p. 46).

if, as is commonly provided, he must "return" the know-how, or documents relating to it, to his licensor.

An interesting sidelight was cast on know-how by the case of *Lear, Inc. v. Adkins*,[25] which raised the issue of whether know-how could be licensed at all. The argument of Justice Black in a separate opinion, ran that the American federal government has specifically accorded certain protection to ideas by the patent law, and the patent law should be exclusive because it pre-empts the field. Any other protection of ideas, such as the secrecy provisions of a know-how agreement, should be deemed in derogation of free-competition and the notion that ideas should be freely accessible to all. One lower court subsequently so held—that is, said know-how licensing is completely invalid—but to the great relief of the patent bar, this decision was reversed on appeal.[26]

Mr. Justice Black's position in the *Lear* case, was anticipated by two decisions he authored in 1964, the *Sears*[27] and *Compco*[28] cases, which held that a State unfair competition law could not be used to prevent a third party from making and selling identical 'Chinese' copies of unpatentable designs. In these cases, the designs were certain kinds of lighting fixtures. Again, the reasoning was that the patent law is the only form of protection available; absent a patent, anyone can copy the idea.[29]

The position in Europe seems universally to be that know-how can be licensed, and that royalty and secrecy provisions in respect of it are enforceable. Certainly, this is the better view, as know-how is a most important kind of property and licensing promotes its dissemination. Under the view of Justice Black, the only way a person could exploit his know-how, would be by keeping it in his bosom and using it himself.

Elements of a Licensing Contract

It is difficult to generalize about drafting license contracts in any useful way, as most of the problems are *sui generis* for each kind of property and country, but it could be helpful to mention some provisions which a typical agreement might contain. Reference may also usefully be made to a checklist of the kind set out in the Appendix.

The one universal generalization which can be made is that licensing on

[25]395 U.S. 653, *supra*, note 15.

[26]Painton v. Bourns, 309 F. Supp. 271 (S.D.N.Y. 1970), *rev'd*, 442 F.2d 216 (2d Cir. 1971).

[27]Sears, Roebuck v. Stiffel Co., 376 U.S. 225 (1964).

[28]Compco Corp. v. Day-Brite Lighting Inc., 376 U.S. 234 (1964).

[29]*Cf.* Lahr, *The Federal Preemption Doctrine: Protection of Industrial Property and Its Relation to the Sherman Act*, 39 ANTITRUST L.J. 812 (1970).

the Continent is a matter of contract. No special form of agreement is required in any country, and even oral licenses can be valid.

This means that in drafting a license agreement for Europe, one can feel relatively free to use his usual form of agreement, at least as a beginning draft. Indeed, the author starts from the premise that 'contract is contract' the world over; if one can draft something which is intelligible, it does not matter what form is used.

It is standard English practice to divide licensing agreements into two parts, one being the contractual provisions and the other the formal license. This is done for English registration purposes, so that the terms of the contract other than the specific grant, *e.g.* royalties, do not appear of public record. While this is not usual on the Continent, it seems unobjectionable as a matter of form, so long as the two pieces of paper, the contract and the license, are clearly integrated.

Registration is generally optional for a license agreement in Europe, but it is often advantageous for the licensee to register. For example, in the Netherlands, registration puts third parties on notice of the license, and will help protect the licensee if the patentee should grant licenses or assignments to others. Also, the patent office is notified by registration of the license and will inform the licensee if the patent is not kept in force by payment of annual fees.[30]

Likewise, in France, a licensee who has not registered might lose his rights in case the licensor grants another license or sells his rights to a third party. However, apparently relatively few license agreements are registered in practice.[31]

A typical agreement would begin with a preamble describing the subject matter of the license, perhaps referring to a schedule for the details, patent claims and numbers, etc.

Next would come the granting clause, defining the scope of the license and whether it is exclusive or not.

When a licensor grants an unlimited exclusive license, normally he is precluded from practising the invention himself and from granting licenses to others.[32] In France, however, and possibly elsewhere, the licensor retains the right to make personal use of the invention unless contractually waived.[33]

Of course, in a non-exclusive license, the licensor may properly exercise

[30]*Cf.* Netherlands Patent Act, 1912, *as amended,* art. 34.

[31]*See* Nouel, *supra* note 9.

[32]*See* Cutter Laboratories, Inc. v. Lyophile-Cryochem Corp., 84 U.S.P.Q. 54, 65 (9th Cir. 1949); Rollman v. Commissioner, 113 U.S.P.Q. 356, 361 (4th Cir. 1957).

[33]Nouel, *supra* note 9.

rights under the invention himself, and may authorize others to use it.

It is also possible to have various hybrid arrangements by which the rights licensed are partially exclusive. For example, the license may be exclusive except as to the licensor himself or a prior non-exclusive licensee.[34]

A patent right is normally for the manufacture, use and sale of the patented item, but these facets are divisible for licensing purposes. For example, the grant might be to make and use, but not sell, the licensed device.[35]

In most countries, a license may be properly granted under a patent application, as well as under a patent. In this case, an additional provision for cut-off of the obligation to pay royalties should be incorporated to cover the contingency of denial or limitation of the application by the patent office.

A patent licensee ordinarily has an implied right to have others make licensed devices for it, but as implied rights are always open to question one should be explicit about whether this is to be allowed.[36]

The scope of the license may be subject to restrictions of many kinds. For example, a patent may contain two sets of claims, one directed to a process, the other to an apparatus, and the license may grant the right to use one or the other, but not both. Similarly, various 'field-of-use' restrictions of the kind mentioned earlier, such as only to sell in the non-commercial field, as well as quantity or territorial restrictions may be imposed.

Ordinarily, a licensee does not have an implied right to grant sublicenses.[37] Therefore, this should be bargained for and covered by an express provision. The parties should indicate the terms and conditions to be embodied in any sublicense, and whether or not the sublicense may have a duration independent of the primary license. Also, the licensee should be obliged to furnish the licensor with copies of any sublicenses.[38]

The next provision of interest is the consideration. This can be either a fixed sum or royalties. A fixed sum might be appropriate if, for example,

[34]Mechanical Ice Tray Corp. v. General Motors Corp., 62 U.S.P.Q. 397, 402 (2d Cir. 1944).

[35]Adams v. Burke, 84 U.S. 453, 456 (1973); United States v. General Electric Co., 272 U.S. 476, 490 (1926).

[36]*Compare* Harshberger v. Tarrson, 83 U.S.P.Q. 179, 181 (N.D. Ill. 1949) with Reynolds Spring Co. v. L.A. Industries, Inc., 40 U.S.P.Q. 515, 518 (6th Cir. 1939).

[37]*See* Mathely and Plaisant, *Juris-Classeur Commercial*, BREVETS D'INVENTION, Fasc. XXIV, No.'s 43, 72-74 (Paris); *compare* Heywood-Wakefield Co. v. Small, 37 U.S.P.Q. 363, 369 (1st Cir. 1938).

[38]*Cf.* National Pigments & Chemical Co. v. K. C. Williams & Co., 94 F.2d 792, 796 (8th Cir. 1938).

many small items were involved, and the parties wished to avoid detailed record-keeping which percentage royalties on each item sold might entail.

Royalties can be calculated in various ways, but are usually determined on the basis of sales or output. Of course, timing of when the payment is due, means payment and rights of audit need to be covered.

A recent United States Supreme Court case has found it patent mis-use to insist on a royalty calculated on the basis of a percentage of a licensee's total sales when the patented product is not used at all by the licensee.[39] So the royalty should bear some reasonable relationship to use, unless both parties agree on some other formula for their mutual convenience.[40]

To guarantee that the licensor will receive some compensation, provision may be made for the payment of minimum royalties for a specified term. Failing this, the parties might provide that upon the licensee's failure to make minimum performance, the license will be converted from exclusive to non-exclusive or be subject to cancellation.

Payment of royalties or technical assistance fees to foreigners is subject to prior governmental approval in France, and the authorities on occasion have frowned upon minimum royalty provisions on the theory that they might be a way of "dodging" the French exchange control rules.

In representing a non-exclusive licensee, one can ask for a "most favored licensee" clause. This type of clause provides that if the licensor grants any other license on more favorable terms, such terms shall apply to the immediate licensee. The clause may embrace all terms of the license or be confined to royalties.[41]

What happens in the case of patent invalidity should also be covered with regard to royalties. The decision in *Lear, Inc. v. Adkins*[42] seems to say that a licensee can avoid paying royalties altogether on an invalid patent which he is attacking. The rationale is that, as licensee estoppel is no longer permitted, the licensee must be able to avoid paying royalties or else the licensor will drag out the patent litigation interminably. Whether a licensee has a right to refund of royalties already paid was not decided, but it is implied by the reasoning of the court that he does if the patent is found to be invalid.[43]

[39]Zenith Radio Corporation v. Hazeltine Research, Inc., 395 U.S. 100 at 133-140 (1969).

[40]*Cf.* Glen v. Perfect Fit Industries, 5 CCH TRADE REG. REP. para. 72,750.

[41]*Cf.* Hazeltine Corp. v. Zenith Radio Corp., 100 F.2d 10 (7th Cir. 1938).

[42]395 U.S. 653, *supra* note 15.

[43]Troxel Manufacturing Co. v. Schwinn Bycicle Co., 172 U.S.P.Q. (W.D. Tenn. 1971), applying *Lear,* held on a motion for summary judgment, that the licensee was entitled to refund of all royalties paid, plus interest, under a license agreement for a patent which was found invalid by another court. This decision may be appealed and was severely criticized in 7 LES NOUVELLES 40 (1972).

Next, one would deal with other obligations of the licensee, and these can include grant-back clauses and licensee estoppel clauses where permitted, and an obligation to work the license. How far one can go with these restrictions is not clear in Europe, but certainly export prohibitions imposed on a licensee, or arrangements carving up territories on a basis of absolute exclusivity, are among the most dangerous from the standpoint of competition law.

A licensor will frequently desire to require the licensee to mark licensed devices with the number of the licensed patent. This can be important because it has been held that if patented devices sold by the licensee are not properly marked, there can be no recovery against third parties for infringement occuring prior to actual notice.[44]

If a device is to be sold by a licensee under the licensor's trademark, the requirements of a conventional trademark license should also be considered.

The subject of warranties is a touchy one in patent licensing. Few, if any, warranties are implied in licenses, so this is always a subject for the contract.[45]

In representing a licensee, reasonable warranties to ask for, include:

- —Ownership of the patent by the Licensor;
- —No third-party claims;
- —The patent will be kept in effect as a formal matter;
- —The patent will not be restricted;
- —The patent is independent of other previous patents of the same patentee; and
- —No compulsory licenses will be issued.

Most patent lawyers are extremely reluctant ever to give warranties of patent validity, or that the patent does not infringe any patents of third parties. One reason for this in the American context is that an astonishing 70 percent of the patents in litigation are currently held invalid, there being a definite difference of opinion between the patent office and the courts as to what is patentable.[46]

One can feel fairly comfortable warranting that the device works, or is fit for the purpose intended, but a warranty that it has commercial utility is dangerous because rather open ended. Of course, vagueness in warranties inevitably leads to problems.

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[44]Gordon v. Easy Washing Machine Corp., 39 F. Supp. 202 (N.D. N.Y. 1941).

[45]Applicance Corp. of America v. Speed Queen Corp., 89 U.S.P.Q. 1 (7th Cir. 1951); M. Nirenberg Sons, Inc. v. Trubenizing Process Corp., 49 U.S.P.Q. 464 (N.Y. Sup. Ct. 1941).

[46]*See* Sease, *The Inventor's Dilemma: Whose Fault?*, 58 A.B.A.J. 267 (1972), citing Gausewitz, *Brief in Support of Proposed Amendments to Section 103, Title 35, Patents, U.S. Code*, 51 J. PAT. OFF. SOC'Y 290, 298-299 (1969).

On the question of governing law, the contract should usually provide which national law governs the license. Most jurisdictions will accept the parties' choice of law so long as it bears a reasonable relationship to the contract. Absent a choice-of-law clause, the law of the country of issuance of the patent or mark, or the law of the forum state, is usually applied.

Specification of a law other than the law of the country of issuance will not, of course, govern the validity of the patent or trademark, which is always a matter of the law of the country where registered. Neither will it avoid the public policy mandates of the state in which litigation occurs.

It is most common in patent licenses to select the law of the state in which the patent was granted. As an infringement suit will normally arise in that state, this avoids the problems of proving foreign law. It also has the advantage that both the patent and contract matters will be governed by the same country's law. However, it may be to one's advantage to specify the law of the licensor's jurisdiction as if, for example, in licensing know-how in Italy, one felt the English law protecting know-how secrecy was more clear than the Italian law on the subject. Normally, a reference to Italian law in this kind of situation would be accepted by the Italian courts.[47]

Arbitration is not too common in patent licensing, but it can have utility, particularly in deciding royalty disputes, as the courts generally dislike patent cases, and they take considerable time in deciding them. Generally, a determination of patent validity must be remitted to the civil courts.

Other provisions which should be included are the method for proceeding against infringers and who bears the costs, duration of the contract, termination and events of default, but here one can easily adapt from standard forms.

American Anti-Trust Law

A word about the American experience may be relevant, not only because it could serve as a model for Europe, but also because in practicing internationally one can feel fairly safe in saying that if a restriction is permissible under United States law, it will probably be permissible in most foreign countries. This is not universally true, of course, but it is a good rule of thumb.

Applying this rule of thumb may not be easy as, after more than eight years of anti-trust legislation on the books, the American anti-trust law of licensing is still unsettled, and *Lear, Inc. v. Adkins*[48] has not clarified matters. At least, however, a few problem areas can be indicated.

[47]See Introductory Provisions, Italian Civil Code, art. 24.
[48]395 U.S. 653, *supra* note 15.

The starting point is that while it is of the essence of patent law that it confers a monopoly, a public policy bias for free competition requires the monopoly to be construed restrictively. Thus, any attempt to exceed the legal monopoly enters the anti-trust field. As a result, tied licenses and agreements not to deal in goods which compete with products covered by licensed patents have long been subject to attack under the anti-trust laws.

More recently, the Department of Justice has announced a two-fold test for licensing provisions:

> (I) Is the provision justifiable as necessary to exploit the patent monopoly? and
> (II) Are less restrictive alternatives available which are more likely to foster competition?[49]

Even if a provision satisfies the first test, it must still meet the second.

Under these tests, the following are subject to attack:[50]

1. Grant-back clauses, especially if exclusive.[51]
2. Field of use restrictions, especially if they divide such fields among licensees who would otherwise be competitors.[52]
3. Restrictions on the *manner* in which a licensee who has purchased products from his licensor can resell them. For example, in the pharmaceutical field, a restriction on a licensee requiring him to resell in dosage form rather than in bulk.[53]
4. Restrictions which give licensees the right of prior approval of grant of other licenses. The thought is that a veto of this nature imports elements of collusion, and licensors should be free to license all whom they wish.[54]
5. Restrictions which give the licensor power to fix prices of the licensee. This practice was originally upheld in the 1926 *General Electric* case,[55]

[49]Address of Assistant Attorney General McLaren, *supra* note 17.

[50]For an excellent review of the Justice Department policy announcements and recently-filed cases, *see* Kittler, *Current State of Patent and Know-how Licensing*, 27 BUSINESS LAWYER 691 (1972).

[51]*Compare* Transparent-Wrap Mach. Corp. v. Stokes & Smith Co., 329 U.S. 637 (1947); Stokes & Smith Corp. v. Transparent-Wrap Corp., 161 F.2d 565 (2d Cir. 1947), *cert. denied*, 322 U.S. 787 (1947), *with* United States v. General Electric Co., 115 F. Supp. 835, 847 (D. N.J. 1953); United States v. Wisconsin Alumni Research Foundation (D. Wis. Dec. 30, 1969 – Consent decree).

[52]*Compare* General Talking Pictures Corp. v. Western Electric Co., 305 U.S. 124 (1938), *with* the comments in ANTITRUST DEVELOPMENTS 1955-1968: A SUPPLEMENT TO THE REPORT OF THE ATTORNEY GENERAL'S NATIONAL COMMITTEE TO STUDY THE ANTI-TRUST LAWS, at 72 (Washington, D.C., 1968); United States v. Fisons, Ltd., Civil Action No. 69-C, N.D. Ill. filed July 23, 1969.

[53]*See* United States v. Glaxo Group Ltd., 302 F. Supp. 1 (D.C. 1969), 328 F. Supp. 709 (D.C. 1971); United States v. Birdsboro Steel Co., 139 F. Supp. 224 (W.D. Pa. 1956).

[54]*Compare* United States v. Besser Manufacturing Co., 96 F. Supp. 304 (E.D. Mich. 1951), *aff'd*, 343 U.S. 444 (1952), *with* United States v. Krasnov, 335 U.S. 5 (1957), *affirming per curiam* 143 F. Supp. 184 (E.D. Pa. 1956). *Cf.* McCullough v. Wells Surveys, 343 F.2d 381 (10th Cir. 1965).

[55]United States v. General Electric Co., 272 U.S. 476 (1926).

but the holding has been whittled away, especially when collusion between two or more dominant companies in an industry may be involved.[56]

6. Package licensing, especially when the licensee, in order to get the license he wants, is forced to take other licenses in another area.[57]
7. Use of discriminatory royalty rates for ulterior purposes.[58]
8. Licensee estoppel clauses.[59]
9. Operation under an invalid patent. The Justice department has indicated it will attack the validity of patents in certain instances, as it is certainly an abuse of the patent laws to claim the monopoly when it is not justified.[60]

In addition to criminal and civil sanctions, remedies available for patent misuse in the United States include compulsory licensing, declaration of patent invalidity, and a general injunction because of the misuse.[61]

Although the American law contains a number of things which are illegal *per se*, a "rule of reason" is more generally applied which judges the economic effect of restrictions.

The Justice Department has recently promulgated some guidelines for licensing in the international area, which may be commended to all practitioners concerned with the international scope of the American anti-trust laws.[62] A number of detailed hypothetical cases of international licenses of

[56] *See* United States v. Line Materials Co., 333 U.S. 287 (1948); United States v. Huck Manufacturing Co., 382 U.S. 197 (1965), *affg per curiam* 227 F. Supp. 781 (E.D. Mich. 1964); Ethyl Gasoline Corp. v. United States, 309 U.S. 436 (1940), United States v. United States Gypsum Co., 333 U.S. (1948); Barber Colman Co. v. National Tool Co., 136 F.2d 339 (6th Cir. 1943).

[57] Zenith Radio Corp. v. Hazeltine Research, Inc., 395 U.S. 100 (1969); American Security Co. v. Shatterproof Glass Corp., 268 F.2d 769 (3d Cir. 1959); McCullough v. Wells Surveys, 343 F.2d 381 (10th Cir. 1965).

[58] La Peyre v. F.T.C., 366 F.2d 117 (5th Cir. 1966); Laitram v. King Crab, 244 F. Supp. 9, new trial denied, 245 F. Supp. 1019 (D. Alaska 1965); Peelers Co. v. Weindt, 260 F. Supp. 193 (W.D. Wash. 1966). As to discrimination in granting licenses among competitors, *compare* Allied Research Products, Inc. v. Heatbath Corp., 300 F. Supp. 656 (N.D. Ill. 1969), questioned in Bela Seating Co. v. Poloron Products, Inc., 438 F.2d 733, 738 (7th Cir. 1971), *with* Hartford Empire Co. v. United States, 323 U.S. 386 (1945).

[59] *See* Bendix Corp. v. Balax, 421 F.2d 809 (7th Cir. 1970); United States v. Ciba Corp., Civil Action No.'s 791-69 and 792-69 (D. N.J., filed July 9, 1969). United States v. Fisons Ltd., Civil Action No. 69C 1530 (N.D. Ill., filed July 23, 1969).

[60] *See* United States v. Glaxo Group Ltd., 302 F. Supp. 1 (D.C. Cir. 1969); Stern, *Antitrust Implications of Lear v. Adkins*, XV THE ANTITRUST BULLETIN 663 (1970). (Mr. Stern is Chief, Patent Unit, Department of Justice, Antitrust Division); Day, *Relation of Patent Validity to Antitrust*, 39 ANTITRUST L.J. 801 (1970). As to the situation of fraudulent representation to the Patent Office as a basis for antitrust violation, *see* Beckman Instruments, Inc. v. Chemtronics, Inc., 328 F. Supp. 1132 (W.D. Tex. 1971); Cataphote Corp. v. De Soto Chemical Coatings, Inc., ___ F.2d ___ 171 U.S.P.Q. 736 (9th Cir. 1971); SCM Corp. v. Radio Corporation of America, 318 F. Supp. 433 (S.D. N.Y. 1970).

[61] *Cf.* Ansul Co. v. Uniroyal, Inc., 306 F. Supp. 541 (S.D. N.Y. 1969), *aff'd*, 5 CCH TRADE REG. REP. para. 73,568 (2d Cir. 1971); *cf.* Vitamin Technologists v. Wisconsin Alumni Research Foundation, 146 F.2d 941 (9th Cir. 1945), *cert. denied*, 325 U.S. 876 (1945).

[62] Memorandum of the Department of Justice Concerning Antitrust and Foreign Commerce, 5 CCH TRADE REG. REP. para. 50, 129 (1972).

patents and know-how are discussed. The guidelines give an impression of surprising latitude in present Government anti-trust thinking, if not entirely pellucid reasoning.

Common Market Competition Law

The competition law of the European Community is based mainly on Articles 85 and 86 of the Rome Treaty.

Article 85(1) generally prohibits agreements or concerted practices which affect trade between member states and are liable to prevent, distort or restrict competition, specifically including price-fixing, marketing sharing, price discrimination, etc. A possibility of exemption is provided by Article 85(3) for agreements which contribute to improvements of production, distribution, technology or economic progress.

Article 86 interdicts abuse of a dominant market position by any enterprise, including *inter alia* imposition of unfair or unequal prices or trading conditions, limitation of production, tying arrangements and the like.

The implications of these Treaty provisions for licensing have been elaborated in three principal sources: (1) An announcement of the EEC Commission of December 24, 1962 relating to patent licensing agreements, known for its date of issue as the "Christmas Message";[63] (2) Commission Regulation 67/67 of March 22, 1967;[64] and (3) the case law of the European Court of Justice and the Commission.

Of these, the case law is by far the most important. In several respects, the case law has overridden the "Christmas Message," so reliance on that Message must be cautious.

The Conflict Between EEC and Member-State Industrial Property Law

Before attempting a distillation of the rules which have evolved for licensing, it is necessary to consider the complex problem of the place of national industrial property laws in the Common Market setting.

One starts from the premise that a primary purpose of the Rome Treaty is to achieve unification of the European market in terms of free movement of goods and services between member countries.[65]

[63]JOURNAL OFFICIEL DES COMMUNAUTÉ EUROPÉENES *(J.O.)* Dec. 24, 1962, 1 CCH COMMON MARKET REP. para. 2698.

[64]J.O. March 22, 1967, 1 CCH COMMON MARKET REP. para. 2,727. This regulation expires by its terms Dec. 31, 1972, but the Commission has announced that it intends to renew the regulation, without other changes, for an additional ten years, *i.e.* until the end of 1982 (J.O. July 20, 1972 C. 79/3).

[65]*Treaty Establishing the European Economic Community,* arts. 2-3, 9-11.

National industrial property laws are natural barriers to achievement of unification of the European market, to the extent that industrial property rights conferred by any one country of the Community can be used to bar importation from other Community countries, thus insulating the country where protection exists from competition from other member states.[66]

Indeed, the traditional marketing pattern in Europe has been on the basis of national units in which distributors or licensees have been accorded strict exclusivity which was enforced by various devices including industrial property licenses and export prohibitions.

Reconciliation of this fundamental conflict between the national industrial property laws and the market unification purpose of the Community requires the greatest care lest the structure of the important protections accorded by such laws be pulled down and nothing left in its place.

Modes of Resolution of the Conflict:

1. Law Reform

The Community authorities have attacked this problem on two fronts. The first is proposed reform of national industrial property laws to conform to the purposes of the Common Market. This reform is still in a very preliminary stage.

Illustrative of current thinking, the draft proposals for the Common Market Patent Convention envision that if a patented product has been put on the market in one of the member states by a patentee or his licensee, the patentee of persons 'economically connected' with him and holding parallel patents for the same product in other member states may not object to its sale in such other states on patent grounds. In other words, the first marketing in a member state by a holder of parallel patents, will exhaust the patent protection in all member countries.[67]

2. Development of Competition Law

The second and more fruitful attack to date has been on the front of

[66]Alexander, *Brevets d'Invention et Règles de Concurrence du Traité CEE*, § 92, p. 180 (Brussels 1971) confirms that the right of patentees to bar importations of the patented article from other countries is a common feature of the national patent legislation of the EEC countries. The same right has generally been claimed to exist, although the legal basis for it is less clear, for trade mark holders under national trademark laws. The recent trend in trademark law thinking has been to emphasize the role of the mark as identifying the source of the product. See the cases discussed in Beier, *La Territorialité du Droit des Marques et les Échanges Internationaux*, 98 JOURNAL DU DROIT INTERNATIONAL 5 (1971).

[67]*See* Alexander, *Industrial Property and the Common Market*, 9 COMMON MARKET LAW REVIEW 35, 45-51 (1972); Deringer, *Towards European and EEC Patents*, XVI THE ANTITRUST BULLETIN 151, 158-162 (1971).

competition law. The *Grundig-Consten* case[68] affords a good illustration of competition law in action.

The German manufacturer, Grundig, had placed an export prohibition clause upon Consten, its distributor of electronic appliances for France, and had also allowed Consten to register the French trademark "GINT," which was affixed to all licensed products manufactured by Grundig, as a means of keeping Grundig products not supplied to Consten by Grundig out of France. Thus, Consten was intended to have the French market to himself; he could not sell outside it, but neither could other parties sell within it. Similar arrangements were in force with distributors of Grundig in other member states.

When other importers bought Grundig products bearing the "GINT" mark into France and offered them for resale, Consten sued alleging interference with the exclusive distributorship as well as trademark infringement. While these suits were pending, the Commission ruled that the exclusive dealing arrangement and trademark license were in contravention of Article 85. Both Grundig and Consten brought actions for annulment of the Commission's ruling.

The European Court of Justice held the suits could not be maintained as both the export prohibition arrangement, and the attempt to reserve the French market through the trademark license contravened Article 85. The Court did not invalidate the "GINT" mark, itself, but only its *exercise* through the license agreement intended to reserve the French market to the licensee.[69]

The same principle was applied in the more recent *Sirena* decision,[70] in which the Court refused, under Article 85, to allow the owner of an Italian trademark for cosmetic products to use his mark to preclude import of the same product from Germany by a lawful user of the mark in that country. In *Sirena,* both the German and Italian parties had acquired rights to the mark in their respective countries from the same party, but the Italian holder had purchased his outright in 1937, incidental to the purchase of the entire Italian business relating to manufacture and sale of the marked product.

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[68]Grundig-Verkaufs, GmbH and Éstablissements Consten S.A. v. EEC Commission, Court of Justice Cases No.'s 56/64 and 58/64, Recueil XII-4, 429 (1966), CCH COMMON MARKET REP. para. 8046 (Transfer Binder 1961-1966).

[69]In the author's view this distinction between the *exercise* and the *existence* of industrial property rights is untenable in practice; how one can enjoy or profit from existence of a right without being able to enforce it is not clear. Nonetheless, it is obvious the Court feels itself impelled to this distinction by Articles 36 and 222, mentioned *infra.*

[70]Sirena S.R.L. v. Eda S.R.L., Court of Justice Case No. 40/70, Recueil XVII, 1971, 69 (1971), 2 CCH COMMON MARKET REP. para. 8101.

The major difference between *Sirena* and *Grundig-Consten* under Article 85, is that the Court, in *Sirena,* was not averse to *stretching* to find the 'agreement' necessary to bring an exercise of marks which seeks to establish absolute territorial protection within the ambit of Article 85. It can be expected in the future that the Court might stretch even further, and would be willing to imply an agreement where none exists on paper.

In *Sirena,* the Court also said that a trademark holder does not have a dominant position under Article 86, merely because he can prohibit third parties from marketing products within the protected state. He must be able to prevent effective competition in the relevant market as well. A higher price for the marked product can be an abuse of a dominant position, if it cannot be justified by objective evidence (*e.g.*, higher costs in the protected state).

Sirena left open the possible loophole that national unfair-competition law could be used by an exclusive distributor to block third parties' imports into his territory. This was put to rest by the *Beguelin* case[71] in which the Court held French unfair competition law could not be used in combination with an exclusive distribution contract to bar the importation, at least where the only unfair act was parallel importation.

In the very fundamental *Deutsche Grammophon* case,[72] the Court dealt with the special German protection, akin to copyright, which accords sound-recording manufacturers exclusive rights of sale in Germany of records made in that country. The record manufacturer supplied the records in question to its French subsidiary, from whom they were purchased, reimported by a circuitous route into Germany, and offered for sale at a reduced price below that at which Deutsche Grammophon permitted them to be sold. Deutsche Grammophon attempted to obtain an injunction against import, but this was deemed incompatible with the principle of free movement of goods. In the Court's words,

> It conflicts with the provisions regarding the free movement of goods in the Common Market if a manufacturer of recordings so exercises the exclusive right granted to him by the legislation of a member-State to market the

[71] Beguelin Import Co. v. G.L. Import Export S.A. Court of Justice Case No. 22/71 (Nov. 25, 1971), 2 CCH COMM. MKT. REP. para. 8,149, (1971) Comm. Mkt. L.R. 81. N.b.: The *Beguelin* case was concerned with the special French unfair competition doctrine of *opposabilité aux tiers;* this is quite different from Anglo-American unfair competition theories of "passing off," and the latter in the author's judgment remains to be tested under EEC competition law as a means of preventing parallel imports as well as for other purposes. Considering that a major aspect of trademark legislation is to protect consumers so they know what they are buying (see *Sirena*), a passing-off argument could have substance.

[72] Deutsche Grammophon Gesellschaft mbH v. Metro-SB-Grossmarkte GmbH & Co. K.g., Court of Justice Case No. 78/70 (June 8, 1971), 2 CCH COMM. MKT. REP. para. 8,106, (1971) Common Market Rep. 631.

> protected articles as to prohibit the marketing in that member-state of products that have been sold by him himself or with his consent in another member-state, solely because this marketing has not occurred in the territory of the first member-state.[73]

The Court in *Deutsche Grammophon,* following *Sierna,* also said that holding of the German industrial property right, by itself, was not a dominant position within the meaning of Article 86. Only if exercise of the right enables the holder to prevent competition in a considerable part of the market will Article 86 apply. Offer of the goods in question by the party seeking protection at a higher price than the importer, if not explainable on objective grounds, can be conclusive proof of abuse of dominant position.

In the patent field, the only European Court decision thus far is *Parke-Davis,*[74] which antedated *Sirena* and *Deutsche Grammophon.* There, the Court was confronted with a suit by a patent holder in the Netherlands to bar importation of a drug from Italy, where patent protection for drugs is not permitted under national patent law. (In this respect the case is similar to *Deutsche Grammophon,* for the German protection for record manufacturers was not available under French law). In *Parke-Davis,* the Court went the opposite way from *Deutsche Grammophon* and upheld the patentee's claim. The Court said the invocation of patent rights to bar importation was not in violation of either Article 85 or 86.

The Case Law in Perspective

Reconciliation of *Grundig-Consten, Sirena, Beguelin* and *Deutsche Grammophon,* on one hand, with *Parke-Davis* and the traditional view of the protections accorded by industrial property law, on the other, is very difficult, but five points should be noted about the cases:

1. The holding of *Deutsche Grammophon* on exhaustion of the German record-manufacturer's protection against imports was made independently of Article 85 or 86, and is best understood as an industrial property law decision, based on the principle of free movement of goods.

2. As regards Article 85, in *Sirena* the Court was relying on an agreement, albeit a very antecedent one, for application of Article 85. The situation is the same in *Beguelin* and *Grundig-Consten,* where the agreements were much stronger factors. If there had been no agreement whatsoever in *Sirena,* and the German importer had acquired its right to the

[73] *Id.,* (1971) Common Market Law Rep. 631 at 659.

[74] Parke-Davis & Co. v. Probel, Reese, Beintema-Interpharm & Centrafarm Co's., Court of Justice Case No. 24/67, Recueil XIV-2, 81 (1968), CCH Comm. Mkt. Rep. para. 8054 (Transfer Binder 1967-1970).

mark independently, or trademark protection could not be obtained for the mark in Germany, *Sirena* would probably have come down the other way under Article 85.

3. As regards Article 86, in each of *Deutsche Grammophon, Sirena* and *Parke-Davis,* the Court was confronted with a substantial price differential between the plaintiff's prices and the defendant-importer's prices. The Court became progressively more emphatic in each case about the effect of a price differential under Article 86, to the point that in *Deutsche Grammophon,* which is the most recent of the three, it said a price differential, if not explainable on objective grounds, can be *conclusive* evidence of an Article 86 abuse. This "toughening" of the formula may pressage increased attention on Article 86 in cases of this nature, but to date Article 86 has been much less of a threat to use of industrial property rights than Article 85.

Moreover, in all these cases, the Court was careful to point out that holding of an industrial property right in a member state, the national law of which gives the holder the right to exclude importations is not, by itself, an abuse of a dominant position. The holder must also be able to prevent effective competition in the market. Presumably, in order to determine the effect on competition, market analysis and the position of other manufacturers and sellers must be considered. This means that Article 86 will only apply in certain cases where a substantial anti-competitive effect on the market can be shown. Thus, it is unlikely that Article 86 could ever be used as a general solution to the problem of using industrial property rights to bar importations into one member state from other member states.

4. In *Parke-Davis,* the products were originally marketed in Italy by a third party and were not patentable. If the Court had allowed them to be resold in Holland, Parke-Davis' Dutch patent would have been rendered worthless. Thus, absence of patent protection in the state of the first sale was a key factor in *Parke-Davis.*

If Parke-Davis, itself, had first marketed the products in Italy, the case would have been more difficult, but the same reasoning applies: Since patent protection was not available in Italy, to allow free import to Holland by third parties would have deprived Parke-Davis of much of the value of its Dutch patent. If the *Deutsche Grammophon* reasoning were applied to this situation, Parke-Davis should have had to refrain entirely from selling Italy in order to protect its Dutch patent. This would clearly not have been a good result in the terms of the Community concept of one unified European market.

5. In *Deutsch Grammophon,* and *Sirena* as well, the Court emphasized that the *kinds* of industrial property rights differ from each other, and some

may be entitled to more protection than others. This suggests that patents are more important than trademarks or copyrights; indeed, the Court said as much in *Sirena*. If so, *Parke-Davis* is saved, but it probably should be confined to the situation of absence of patent protection in the state of first sale.

In addition, one must bear in mind, Article 36 of the Treaty, which purports to recognize national industrial property rights so long as they are not used as means of discrimination or restriction on trade between member states. If this is to mean anything, it must mean these rights are valid except as EEC law has overriden them. Article 222 of the Treaty also says that the Treaty shall not prejudice the systems of property ownership in the member states.

Synthesis of the Current Development

The preceeding considerations suggest the following four tentative conclusions, relative to the interplay of EEC law and national industrial property laws, and in particular about the continued viability of national industrial property rights as means of blocking imports into a member country:

I. The problem of parallel industrial property rights held in several Community countries by a common holder or holders acting in agreement is solved on the marketing level after the first sale of the goods by *Deutsche Grammophon*. The first marketing in any protected state will exhaust the protection. Thereafter, the goods can be freely imported into any Community country and the common holder cannot object. Although *Deutsche Grammophon* was not, strictly speaking, a parallel industrial property right case, because the German rights in question did not exist in France, its rationale applies *a fortiori* to parallel situations.

The justification of this result is that the holder has had the benefit of his industrial property protection by first sale, and to let him enjoy a further monopoly by way of barring importations to other member states of the products he has marketed is incompatible with the purposes of the Common Market. *Deutsche Grammophon*, of course, only dealt with a right akin to copyright, but most authorities feel it will be extended to parallel trademarks and patents.

II. In non-parallel situations, if a party with only *trademark* or *copyright* protection in one Community country markets goods subject to the protection in another Community country where no protection exists, likely he cannot bar reimportation following *Deutsche Grammophon*. He has a bet-

ter chance in the case of *patented* goods under *Parke-Davis*. The rationale of the distinction lies with the greater importance of patent rights.[75]

III. The Court has not yet dealt with parallel patent protection at the *manufacturing* level. A common holder may still be able to divide territories and avoid competition at this level by exclusive licenses for protected countries. Indeed, the "Christmas Message" explicitly sanctioned territorial divisions for manufacturing licenses and this was upheld in the *Scott Paper* announcement.[76]

A caveat must be drawn, however, for exclusive manufacturing licenses for products to be marketed in *narrow "oligopolistic" markets* where the manufactured products cannot be transported readily and cheaply from other manufacturing locations. In the recent Commission ruling in the *Burroughs* cases,[77] involving in part two exclusive manufacturing licenses for a special kind of carbon paper under Burroughs' French and German patents respectively, the Commission was careful to point out that exclusive manufacturing licenses limit licensors as well as licensees. Licensors, as a result of exclusivity, lose the faculty of licensing others and the territory of an exclusive marketing license can, thus, effectively be reserved to the licensee.

In these cases, the exclusive manufacturing licenses did not violate Article 85 because the licensees had only small portions of the relevant

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[75]In a paper entitled *A Common Market Overview of the Competition Problem in the Seventies*, published in the American Bar Association's booklet CURRENT LEGAL ASPECTS OF DOING BUSINESS IN EUROPE (Theberge, ed., Chicago, 1971) p. 58 at p. 60, Dr. Herman Schumacher, Director of the Division of General Competition Policy, Directorate-General for Competition, Commission of the European Communities, made the following remarks relative to conclusions I and II (Dr. Schumacher was writing prior to the *Deutsche Grammophon* decision):

> Trademark law and also patent law in particular, are time and again misused to maintain the national frontiers by arranging for absolute territorial protection. Where several firms are parties to such market-sharing, and where there is proof of the existence of agreements or concerted practices for the purposes of market-sharing, I do not doubt that Article 85 is applicable. To avoid misunderstanding however, I must say that, in my opinion, allocation to a patent licensee of a specific area within which to operate is admissible. However, once a product has been legally put into circulation it must be able to move freely within the Common Market. The only exception to this is when the product has been manufactured by a firm without a license to do so in a part of the Common Market where the patent is not protected. If this product were also to move freely, the existence of the patent would be jeopardized.
>
> Trademark law, on the other hand, cannot warrant territorial restrictions as it only relates to the affixing of a distinctive mark. This has been made clear by the *Sirena* judgment.

[76]Scott Paper Co., J.O. Oct. 24, 1968, CCH COMM. MKT. REP. para. 9263 (Transfer Binder April, 1965-Dec. 1969 (out of print)).

[77]Burroughs-Delplanque, J.O. Jan. 17, 1972, 2 CCH COMM. MKT. REP. para. 9485 and Burroughs/Geha Werke, J.O. Jan. 17, 1972, CCH COMM. MKT. REP. para. 9486; see also Davidson Rubber Co., J.O. June 23, 1972, 2 CCH COMM. MKT. REP. para. 9512.

markets, the goods were easily transportable from other manufacturing locations at little cost, and other licensees, as well as Burroughs, itself, could compete at the marketing level. The negative implication, however, of the Commission's stress on these facts is that an Article 85 violation could arise for an exclusive manufacturing license if the situation were opposite.

IV. The case of *purely unilateral exercise* of industrial property right protection by a holder or his licensee to bar imports, where an entirely independent and unrelated party has first marketed them, either with industrial property protection or not in one Community country and another unrelated party is trying to import them into the protected country, does not seem to have been changed. In these situations, the national law protection should remain valid.[78] In other words, if a naked infringer tries to import goods to a protected country, the goods have not been marketed by the holder of the protection or persons related to him, and there is no connection between him and the infringer, the protection should still be available. This is considerably less firm, however, for trademarks than patents, in view of the differences in purpose of the two kinds of rights.

It will be seen that these four conclusions go far to reaching the Common Market Patent Project solution to the parallel import problem, yet still leave much of the protection of national law intact.

Broadly, only if one is involved (a) in a joint action of market restriction within the meaning of Article 85, or (b) in acting unilaterally he has exhausted his protection by marketing in another member state with parallel protection in the case of patents, with or without it in the case of trademarks and copyrights, or (c) is invoking rights in a situation where an abuse under Article 86 can be established, will he be likely not to be able to use industrial property rights in the traditional way.

To be complete, it must be observed that the case law has not yet reached the problem of direct sales by parallel licensees into each other's territory. To illustrate, assume a U.S. licensor has made exclusive manufacturing and sales licenses of parallel patents to licensees in each of France, the Netherlands and the U.K., each license covering the same product and extending only to the national territory of each licensee. Although it is clear from what has been said under Point (I) above that once, for example, the U.K. licensee has sold a product under the license in the U.K., it can then move to France, notwithstanding objections by the French licensee or the licensor, it has not been decided whether the U.K. licensee can sell directly in France in the teeth of the French parallel

[78]*Cf.* Submissions of Advocate General Lamothe in *Sirena, supra* note 70.

licensee. Although prediction of how the law will develop on this problem enters the realm of "pure speculation," it would seem a logical corollary of the free movement of goods principle to allow parallel licensees to sell into each other's territories, particularly in instances where the products are marketed directly by manufacturers to end-users without the intervention of "middlemen." Anything less would resurrect the possibility of "market compartmentalization," which has been the *bête noire* of both the Commission and the European Court to date.

Ramifications for Licensing

The practical result of this synthesis for licensing, as far as territorial restrictions are concerned, is that devices such as multiple parallel licenses and cross licenses can no longer be used to ensure absolute territorial protection for licensees.

On the other hand, considerable room is left to enter into exclusive licenses at the marketing as well as manufacturing levels, so long as absolute territorial protection is not attempted for marketing. Indeed, exclusive patent licenses—requiring the licensor not to license third parties and prohibiting him from utilizing the invention himself—were explicitly sanctioned in the "Christmas Message"[79] on the theory that they are not greatly different from assignments of rights and are not likely to affect trade between member states. However, when isolation of a national market is attempted by an exclusive license (or an assignment) of industrial property rights, it is very much open to doubt whether exercise of the industrial property rights is compatible with the Treaty.[80]

Affirmative guidance for *exclusive marketing arrangements* (*i.e.* distributorships) can be obtained from Regulation 67/67, relating to bi-lateral exclusive dealing contracts.[81] These are contracts (not necessarily involving licenses) in which one of the parties undertakes to deliver goods to the other for resale in a specified territory, or one party agrees to purchase products for resale only from the other party. The regulation exempts such agreements from Article 85(1) so long as the only other restraints on the exclusive dealer do not amount to more than: (a) provisions not to manufacture or sell competing products during the life of the contract and for one year thereafter, and (b) obligations not to advertise, establish a branch, or maintain a distribution warehouse outside the contract territory.

It is a fair inference that this exemption extends to *exclusive marketing*

[79]*Supra* note 63.

[80]*Cf.* Remington Rand Italia S.P.A. v. Innovazione Electromarket S.R.L., (1968) COMM. MKT. L. REP. 249, Commission action, 8 *Bulletin of the European Communities* 40 (1969).

[81]*Supra* note 64.

licenses of industrial property rights, so long as the requirements of Article 3 of the Regulation are met. Article 3 states that the exemption of the Regulation will not apply (a) to exclusive cross-licenses by competing parties, or (b) to cases where the parties make it difficult for others to obtain the products in question from other dealers in the Common Market, *especially* where industrial property rights are so used. The reference to industrial property rights, no doubt, is a direct result of the *Grundig-Consten* holding,[82] which came down shortly before Regulation 67/67 was issued.

Certain additional kinds of typical restrictions are specifically allowed by Regulation 67/67, and one can feel free to include them in exclusive marketing licenses. These include:

(a) The obligation to purchase complete lines of products or minimum quantities;
(b) The obligation to sell the products under the trademark or packaging prescribed by the manufacturer;
(c) The obligation to undertake certain sales promotion measures, in particular:
to advertise;
to maintain a sales network or stock;
to assume responsibility for customer service and guarantees;
to employ personnel having specialized or technical training.

Other Kinds of Licensing Provisions under EEC Law

Extrapolating further from the cases and Commission announcements, the following seems to be the current situation on other typical licensing restrictions:

1. *Limitations on the ways a licensed patent may be exploited:* The "Christmas Message" permits division of the 'bundle of rights' conferred by a patent into rights to make, use or sell. The license may be limited to any of the three.

Licenses may also be limited as to *time* (*i.e.* shorter, but not longer, than the patent period), as to *field of use*, and as to *area* (*i.e.* a regional license for a portion of the territory where the patent is granted, or to one specific factory).

The rationale of the exemption of these kinds of provisions from Article 85, is that they all relate to rights conferred by the patent itself, and the patentee is free to deal with them as he would be to sell or assign all or part of his rights.

2. *Sublicenses and assignments:* The Commission's decisions in *Da-*

[82]*Supra* note 68.

vidson Rubber Co.[83] and the two *Burroughs* cases[84] held that explicit or implicit prohibitions on granting sublicenses of patents or know-how were not restraints on competition. The "Christmas Message" also approved restrictions upon grant of sublicenses and non-assignment clauses, *i.e.* limitations of grant of license rights to certain persons.

3. *Minimum royalty:* A minimum royalty provision was upheld in *Burroughs-Deplanque.* In *Raymond-Nagoya*[85] a clause providing that a license was to become non-exclusive rather than exclusive if a certain minimum amount of royalties was not paid was also upheld.

4. *Royalty term—patent license:* The Commission's *Henkel/Colgate*[86] decision made it clear that patent royalties should not exceed the term of a licensed patent.

5. *Royalty term—know-how license:* The term of know-how royalties on licenses to be granted was intended by the contract in *Henkel/Colgate* to be limited to the applicable patent term of the country where such know-how licenses were to be in force, and this was considered not unduly long.[87]

6. *Royalty rates, patented and unpatented products: Burroughs/Geha Werke* approved an arrangement in a combined patent, trademark and know-how license for a 50 percent reduction of royalties when the products were sold without patent protection.

7. *Separate royalties for each patent (package royalties): Henkel/Colgate* cites with approbation that royalties were to be calculated separately for each patent licensed.

8. *Discriminatory royalty rates and rate variation: Henkel/Colgate* indicates that differing royalties for two or more licensees may be used in a manner which will give rise to a market sharing problem under Article 85, so care should be exercised in setting different royalty rates and clearly discriminatory rates should be avoided.

9. *"Most favored licensee" clauses:* A provision ensuring that a licensee would have the most favorable royalty rate given to any other licensee of the same licensor was allowed in *Raymond-Nagoya.*

10. *Quantitative restrictions:* The *Burroughs* cases allowed imposition of requirements on the licensees that they produce quantities sufficient to satisfy demand. The "Christmas Message" seems to allow restrictions on

[83]Davidson Rubber Co., J.O. June 23, 1972 2 CCH COMM. MKT. REP. para. 9512.
[84]*Supra* note 77.
[85]Raymond-Nagoya, J.O. June 23, 1972, 2 CCH COMM. MKT. REP. para. 9513.
[86]Henkel/Colgate, J.O. Jan. 18, 1972, 2 CCH COMM. MKT. REP. para. 9491.
[87]*See also* Davidson Rubber Co., *supra* note 83.

maximum as well as minimum quantities and on the number of times a licensed process is to be used.

11. *Qualitative restrictions and technical criteria:* The "Christmas Message" allowed standards of quality as well as technical production criteria to be imposed on licensees and this was followed both in the *Burroughs* cases and *Raymond-Nagoya.* The rationale of the Commission was that these restrictions had the sole purpose of permitting technically adequate exploitation of the licensed patents.

12. *Tied source of supply:* Requirements that licensees purchase supplies from a certain source insofar as they are unique and indispensable to proper technical exploitation of a licensed patent were sanctioned in the "Christmas Message," but here one should tread cautiously, as the EEC law is certain to receive further development and in many cases these arrangements are prohibited by national law.

13. *Trademark license, obligatory marking of products:* The *Burroughs* cases held that non-exclusive licenses to use the patentee's trademark, and requirements to indicate on the products that they were made under license from Burroughs were not restrictions of competition. The licensees had the right to use other marks as well. The arrangements were deemed to facilitate qualitative and quantitative control by *Burroughs* of the licensed products.

14. *Obligations to affix patent information on the licensed product:* These were approved by the "Christmas Message."

15. *Grant-back clauses:* The "Christmas Message" sanctioned agreements concerning the mutual communication of know-how acquired during the license and the mutual granting of licenses on improvements or new uses. However, this permission is conditional on the requirement that the grant-back clauses be non-exclusive and reciprocal between licensor and licensee. Clauses calling for mutual communication of know-how were also approved in the *Burroughs* cases. In *Raymond-Nagoya,* the Commission required amendment of a grant-back clause to make the grant-back non-exclusive.

16. *Know-how secrecy:* In *Burroughs-Deplanque* the licensee was obliged to keep secret the know-how furnished by Burroughs, during the period of the license and *ten years thereafter,* and to use it only as authorised by the contract. The licensee was also obliged to return all designs, models, etc., embodying know-how to Burroughs ninety days after termination of the contract. The license agreement was for ten years, renewable from year to year thereafter and cancelable on twelve months' notice. A similar secrecy requirement was imposed in *Burroughs/Geha*

Werke, but only for the period of the contract, which was for an intitial term of seventeen years.

The Commission upheld both of these secrecy agreements. In *Burroughs-Deplanque,* it noted that secrecy is an essential element of licensing of unpatented know-how so long as it is not in the public domain. One may infer from this that know-how secrecy provisions will receive liberal treatment in EEC competition law, but to date there has been very little policy or legal development regarding *know-how* contracts.

17. *Licensee estoppel clauses:* In *Burroughs/Geha Werke* the Commission noted with apparent approval, that the parties had revoked a clause in their contract prohibiting the licensee from contesting the patents or patent application of the licensor. One is not certain from the presentation of the case why the parties revoked this clause. The revocation may well have been made for reasons other than EEC law. (It may have been done because German cartel authorities have taken the position that these clauses should be modified in the cases of patents issued by EEC countries;[88] alternatively, it may have been prompted by *Lear, Inc. v. Adkins.*) However, any ambiguity in the Commission's position in *Burroughs/Geha Werke* was clarified in *Davidson Rubber Co.,* in which the Commission clearly insisted upon deletion of non-attach clauses prior to granting exemptions for the licenses in question.

18. *Licensors setting prices for licensees:* There are as yet no firm indications of how the EEC authorities will judge price-fixing provisions in license agreements, but in view of the legal development in this area in France, Germany and America, it seems highly likely such arrangements will be deemed interdicted by Article 85(1).[89]

19. *Patent pools and joint research companies:* The *Henkel/Colgate* decision points out that patent pools are not as free in deciding upon licensing policy as would be single patentees. This is one reason why the Commission in that case required, as a condition of granting exemption from Article 85, that details of all future licenses of the Henkel and Colgate joint research company be notified to it. More generally, *Henkkel/Colgate* also teaches that joint venture agreements, whether for research or other purposes, *between competing companies* always carry the danger of concerted action within the meaning of Article 85(1).

[88]German Cartel Office (Bundeskartelamt) *Tätigkeitsbericht* 1969, p. 98, discussed in Alexander, *supra* note 66, § 126, p. 258.

[89]*Cf.*, Vereeniging van Cementhandelaren, J.O. Jan. 17, 1972, 2 CCH COMMON MARKET REP. para. 9492; Nederlandse Cement-Handelmaatschappij N.V., J.O. Jan. 26, 1972, 2 CCH COMM. MKT. REP. para. 9493; but compare the Commission's reply to Written Question No. 247/71, J.O. Nov. 13, 1971, 2 CCH COMM. MKT. REP. para. 9471.

20. *"Specialization" agreements:* In *SOPELEM/Langen*[90] among the most recent of several cases of this type, two competing manufacturers of highly technical control equipment for use in hydraulic automation devices each agreed to specialize in different fields of the industry. Each party took an exclusive license to sell in its country, the equipment manufactured by the other (effectively an exclusive reciprocal supply agreement), and each discontinued manufacture of the equipment in the other's special field, and agreed not to develop any new equipment competing with the other's "specialty."

Although this agreement clearly fell within the prohibitions of Article 85(1), the Commission granted it on exemption under Article 85(3). The Commission noted that competition is keen and diffuse in this industry and that the agreement could contribute to increase of production, better distribution and advancement of technology, because it allowed each party to concentrate on the part of the business which it knew best and for which it was best equipped. As the facts of this case certainly pointed to a severe competition law infraction at first blush, the Commission's decision suggests a wide scope for exemption of "specialization agreements" of this kind in the future if a case for production or distribution rationalization can be made.[91]

21. *Arbitration clauses:* These have been accepted in numerous decisions, and seem to pose no competition law problem.

EEC Competition Law in Overview

Viewed as a corpus of law, the European competition decisions can be seen to have two dimensions: Not only are the European authorities concerned with maintaining free competition in the *working* of their market along the lines of the American anti-trust model, they are also, perhaps primarily, concerned in their competition policy with *creation* of the one unified "common" market envisioned by the Rome Treaty.

In the latter field, they have focused their attack on commercial arrangements which maintain the traditional fractionated character of the European market, and derogate from the single unified market ideal. This attack has already had a very significant impact on the traditional uses of industrial property rights, including licensing.

[90]SOPELEM/Langen, J.O. Jan. 17, 1972, 2 CCH COMM. MKT. REP. para. 9488.

[91]*See also:* MAN/SAVIEM, J.O. Feb. 4, 1972, 2 CCH COMM. MKT. REP. para 9494; Wild/Leitz, J.O. Oct. 9, 1971, 2 CCH COMM. MKT. REP. para. 9462. On July 20, 1972, the Commission issued a proposed group exemption on specialization agreements which is likely to become effective by the end of 1972. The proposed regulation is discussed in the author's *Specialization Agreements; Development of a Major Exception to the Competition Rules of the Rome Treaty,* INT'L B.J. (Nov. 1972).

This second ("market creation") dimension of European competition policy is at least partly responsible for the differences in emphasis between competition law in Europe and the United States. While market division on territorial lines has been almost "the whole problem" to date in Europe, it has been much less of a problem in America.[92]

On the side of the "working" of their market, the Europeans have also proclaimed themselves in favour of free competition. If this has not been in a pure "Adam Smith" sense, at least it is in terms of promoting competition between enterprises and avoiding undue private restraints of trade within the spirit of Articles 85 and 86. However, except as the efforts in this area have overlapped with the attack on market dividing arrangements, enforcement has been much less rigorous.[93]

In part this lack of rigor is probably due to the fact that the Europeans are not "deep down" so firmly wedded to pure competition philosophy as the Americans. Certainly the "legislative mandate" is less strong and politically more delicate to apply in Europe than in America. It must also be recognized that achievement of the unified market goal is the more urgent need.

One detects also a "schizophrenia" in European competition policy: Concomitantly with development of a free competition policy under Articles 85 and 86, the Europeans have expressed a desire to promote co-operation, consolidation and fusion between enterprises, to develop large business groupings with sufficient wherewithal to meet "the American challenge." It seems likely that contradictions met in carrying out these cross purposes have debilitated the "pure competition" thrusts.

In the licensing field, one is left with the result that territorial divisions, however attempted, are the most suspect from the competition-law standpoint. Many of the other issues which are "up" for licensing in America remain to be developed in Europe, but it seems inevitable that they will receive attention as the Common Market system consolidates and strengthens.

One is also left with the impression from the European cases, that economic analysis will play an increasing role in European anti-trust development. With the possible exception of the "red flag" of export prohibitions clauses, there has been very little development of *per se* illegality rules. Rather, one is taught by the cases to look at the reasonableness of

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[92]*Cf.* Dam, *Exclusive Distributorships in the United States and the European Economic Community,* XVI THE ANTITRUST BULLETIN 111, 124 (1971).

[93]For a strong critique, see Moss, *The European Community Still Has No Competition Policy,* which originally appeared in French in LE MONDE DE'L'ECONOMIE, Dec. 15, 1970, p. 14, translated and reprinted in XVI THE ANTI-TRUST BULLETIN 443 (1971).

restrictions in their context, and their impact on the relevant market in a manner similar to the American technique.

Use of the economic approach helps to ensure that competition rules will operate only to impede business arrangements in cases of significant economic impact on market conditions. Although this approach makes for less predictability—and therefore makes the legal advisor's job more difficult—the flexibility it affords should be welcomed. *Per se* illegality rules leave little room for adaptation to commercial needs, and are often worse than the maladies they are meant to cure.[94]

Conclusion

Negotiation and preparation of licensing agreements have long been standard fare for lawyers in international practice, but it would be a mistake to regard the lawyer's work in licensing as routine.

The ingredients of a successful license require the utmost care in selection and preparation. Their mixing *en casserole,* to produce an agreement which successfully meets the many problems currently afoot in the licensing field affords considerable scope for the creative lawyer *comma chef de cuisine.*

Sad to say, the delicacy of the soufflé may not be readily appreciated, due to lack of sophistication about the legal aspects of licensing on the part of many of the "consumers" of the lawyer's efforts. This means the lawyer must educate his clients to the importance of obtaining sound legal advice in licensing at an early stage, and following it, a task which is sometimes quite difficult in Europe where many licensing functions are normally performed by laymen.

The consequence of the lawyer's non-participation early in the game is usually, at best, renegotiation of several points when he does come in; at worst, disaster. Indeed, the ground rules for licensing are changing so rapidly, the lawyer, himself, has a substantial task to keep abreast of current developments.

Finally, we must not forget that licensing agreements, for the lawyers, no less than the parties, have the feature that they must be lived with and made to work over a period of time, subject to changing conditions. This means that a major part of a lawyer's job in licensing must be to anticipate *future* developments and problems. In addition to a crystal ball, vigilance and attention to detail are necessary tools of the soothsayer.

[94]This was a major theme of the working sessions of the Section of Antitrust Law of the American Bar Association at the 1971 London Meeting. Proceedings of the sessions have been published in 40 THE ANTITRUST JOURNAL, Issue NO. 4.

APPENDIX

Checklist for Drafting License Agreement

I. *Introduction*
  - A. Parties
  - B. Effective date of agreement
  - C. Place where agreement made
  - D. Licensed subject matter (refer to schedule)
  - E. General rights licensed
  - F. Background of agreement

II. *Grant*
  - A. Exclusive or non-exclusive
  - B. Make, have made, use and/or sell
  - C. Other limitations or restrictions
    - (i) Less than all claims
    - (ii) Territory
    - (iii) Quantity
    - (iv) Style or size
    - (v) Field of use
  - D. Sublicenses
    - (i) Terms and conditions
    - (ii) Duration
    - (iii) Furnishing of copies to licensor

III. *Consideration*
  - A. Lump sum or fixed annual payments
  - B. Royalties
    - (i) Rate
    - (ii) Bases
      - (a) Net sales of patented devices
      - (b) Amount of raw materials
      - (c) Number of articles
      - (d) Total sales
    - (iii) Minimum
      - (a) Full term of agreement
      - (b) Lesser period
      - (c) Upon failure to pay
        - 1. License converted to non-exclusive
        - 2. License subject to cancellation
    - (iv) Maximum
      - (a) In each year
      - (b) In total
    - (v) Most favored licensee
      - (a) Royalties
      - (b) Other terms and conditions
  - C. Tax considerations

The author acknowledges indebtedness to Nordhaus, *Patent License Agreements*, BUSINESS LAWYER, April, 1966, p. 643 at p. 657.

For detailed sample contracts, see MELVILLE, PRECEDENTS ON INTELLECTUAL PROPERTY AND INTERNATIONAL LICENSING (London, 2nd ed. 1972); MASON, STANDARD CLAUSES IN A LICENSING AGREEMENT (London, 1970).

IV. *Royalties Payable*
- A. Time of reports
- B. Time of payments
- C. Audit of books and records
- D. Time limitation on right to examine

V. *Effect of Invalidity of Patent on Royalty Payments*

VI. *Other obligations and Warranties of Licensor*
- A. Improvements developed by licensor
  - (i) Royalties for use
  - (ii) Definition
  - (iii) Period of obligation
- B. Warranties
  - (i) Licensed device works
  - (ii) Commercial utility of licensed invention
  - (iii) Validity of patent
  - (iv) Non-infringement of third party patents
- C. Indemnification for licensee's infringement.

VII. *Other Obligations of Licensee*
- A. Non-attack and acknowledgement of patent validity (Query: *Lear v. Adkins*)
- B. Exploitation
- C. Patent marking
- D. Grant-backs

VIII. *Ancillary Provisions*
- A. Enforcement of patent
  - (i) Severally or jointly by parties
  - (ii) Expenses and recoveries
- B. Foreign patents
- C. Technical assistance and know-how
  - (i) Drawings and specifications
  - (ii) Visitation rights
  - (iii) Personal supervision
  - (iv) Compensation
  - (v) Employment or consulting agreement
  - (vi) Return of, after termination
  - (vii) Right to continue to use after termination
  - (viii) Abatement of royalties clause
- D. Release for past infringement
- E. Patent application
  - (i) Effect of non-allowance of claims or denial of patent
  - (ii) Responsibility and costs of prosecution
- F. Trademark

IX. *Duration*
- A. Effective date
- B. Expiration date
- C. Option to cancel prior to normal expiration

X. *Termination*
- A. Upon breach of agreement
  - (i) Notice of Breach
  - (ii) Period of remedy
  - (iii) Notice of cancellation
- B. Bankruptcy or insolvency of license

XI. *Choice of Law*

XII. *Formal Provisions*

A. Entire agreement

B. Assignment of agreement or rights

C. Notices

(i) Written

(ii) Manner of Service

(iii) When effective

D. Force majeure

E. Arbitration

XIII. *Signature of Parties*