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The Limits Placed by EEC Law on Territorial Protection in Patent Licensing: A Case Study in Community Law-Making

*Donald L. Holley*

In this article, Mr. Holley examines the ways in which the EEC Commission's interpretations of the EEC Treaty, European Court decisions, and suggestions made by Member States and industry influence the development of EEC law. By focusing on the Commission's draft patent licensing regulation, the author identifies existing conflicts between preserving patent rights and the EEC objectives of protecting competition and the free flow of goods among the Member States.

INTRODUCTION

For the past ten years, the Community bodies which make EEC law, legal commentators, and organizations which influence the law's development have been engaged in the intricate exercise of working out the relationship between the provisions of the Treaty of Rome which concern the free flow of goods and the protection of competition, and those that guarantee industrial property rights. The relationship between these provisions will most likely be firmly established in the next few years, but at the moment there is no clear set of rules. Thus, while a definitive review of the territorial protection afforded licensors and licensees under Community law cannot be made at this time, the cur-
rent legal situation does offer an interesting case study in EEC law-making.

A major focal point of this study is the manner in which the various bodies and other forces that shape EEC law operate to influence both one another and the law's development. A second point of concentration involves the process of finding the point at which certain basic objectives of the Treaty—in particular market integration—give way to another objective: preserving property rights such as patents. The patent licensor now faces the problem of attempting to discern this point when he wants to afford himself territorial protection against sales by a licensee, or to protect a licensee's territory against sales by others. The resulting conflict between the parties' expectations and the Community objectives presents a focal point from which to examine the protection granted to competition and consumers by Articles 85 and 86 of the Treaty, the free flow of goods among the Member States by Article 30, and patent rights by Article 36.

Decisions by the Commission and the European Court over the last decade have developed the issues relevant to this subject to a certain extent. Recently, the Commission sharpened its focus on these issues when it proposed an important measure of Community legislation: its draft patent licensing regulation. When issued in final form, that measure will give a block exemption to certain exclusive grants and

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1 No attempt will be made here to discuss similar questions which may arise regarding other forms of industrial and intellectual property rights. It may simply be observed that the legal answer will usually differ depending on what is deemed to be the "specific subject matter" of the property right in question.

2 Article 85(1), prohibiting agreements or concerted practices that may affect trade between Member States and that have as their object the prevention, restriction, or distortion of competition within the Community, is likely to raise issues in any patent license and will certainly do so when territorial protection is involved. Article 86, concerning abuses of dominant positions, can also be relevant in enforcing industrial property rights, but the provisions of this Article are usually not of importance in regard to the present question. In any event, it should be noted that as a matter of Community law, the monopoly given by a patent will not in itself give rise to a dominant position within the meaning of Article 86.

3 Article 30 can be applied in this context to prohibit a national court of a Member State from deciding that importation involves patent infringement when such a decision would produce an effect equivalent to an import quota. See the review of Article 30 case law in van Themaat & Gormley, Prohibiting Restrictions of Free Trade within the Community: Articles 30-36 of the EEC Treaty, 3 NW. J. INT'L L. & BUS. 577 (1981).

4 Article 36 may be applied to prevent the application of Article 30 to protect the specific subject matter of the patent right. For a review of the case law regarding Article 36, see id. at 601-07.

5 The draft regulation was published at 22 O.J. EUR. COMM. (No. C 58) 12-18 (1979). The proposal has evoked extensive comment on both sides of the Atlantic. For a comparison between the proposed EEC rules and existing U.S. rules, see Handler & Blechman, An American View of the Common Market's Proposed Group Exemption for Patent Licenses, 14 INT'L LAW. 403 (1980).
other clauses in patent licenses. The proposal may never result in a final regulation, but it seems likely that a regulation will eventually be adopted in a form not fundamentally different from that now proposed. As a step in Community rule-making, the publication of the draft regulation must itself be seen as an event of major importance in Community law. While the draft appears to be largely an expression of the Commission’s own views, it also seems to reflect significant input of Member States and industry. The draft proposes norms on issues that have not been treated in decisions, and those proposed norms now cannot be safely ignored by parties to a patent license. For purposes of the present study, the draft regulation defines and illustrates the problems as well as certain options for their solutions.

THE BACKGROUND OF TRADITIONAL LICENSING LAW

When a patent license is granted on patents in one Member State, the basic rights the licensee receives are limited to the jurisdiction for which the license is granted. If the licensee sells the licensed product in another Member State in which a parallel patent exists, the patentee, and sometimes even an exclusive licensee for that territory, may sue for patent infringement in a court of that other Member State. Similarly, the first licensee in question can be assured that others selling into

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6 While the Commission has been authorized by Council Regulation 19/65 to adopt the regulation without the consent of the Member States, a certain degree of opposition by Member States may cause the Commission to refrain from adopting the regulation.

7 The regulation would perhaps already have been adopted had it not been thought by the Commission that a 1978 decision of the Commission, subsequently brought before the European Court for review, might resolve the issue of whether an exclusive grant of industrial property rights and related territorial protection violates article 85(1). That case, Breeders' Rights—Maize Seed, will probably be decided in 1982. The Commission decision was published in 21 O.J. EUR. COMM. (No. L 286) 23 (1978).

8 A number of Commission officials and authoritative academic writers who have carefully examined the legal questions underlying the present study have taken firm positions as to how the law should develop. No attempt will be made here to give a comprehensive bibliography, but in regard to expressions of views by officials we may in particular note H. Johannes, Industrial Property and Copyright in European Community Law (1976). With regard to studies by academic writers, a recent and detailed study can be found in P. Demaret, Patents, Territorial Restrictions, and EEC Law (1978). See also Waelbroeck, The Effect of the Rome Treaty on the Exercise of National Industrial Property Rights, 21 Antitrust Bull. 99 (1976). This article does not attempt to predict the outcome of the important issues yet to be decided by Community authorities, nor does it suggest which outcome seems desirable as a matter of policy. Rather, this article focuses on the way the debate and interaction of these various forces have brought the law to its present state of development.

9 In certain Member States, including Germany, the United Kingdom, France, and Italy, an exclusive licensee is entitled to bring an action for patent infringement.
his territory without having a license to do so will be subject to suits for patent infringement.

On the basis of their experience throughout the world, many licensors and licensees have come to believe that territorial protection is not only common practice and commercially useful but also evidence of one of the fundamental rights attached to a patent. In particular, such protection enhances the value of the patent because it allows the patentee to convince a licensee obtaining territorial protection to take a license and to pay an enhanced royalty of a certain amount. The licensee is thus assured of being the exclusive party using the patent in a particular area.

IMPLICATIONS OF COMMUNITY LAW

Following the founding of the European Economic Community in 1957, two patent law issues arose concerning these questions, which are not immediately apparent. The first issue was the extent to which the natural separation of the national markets within the Community resulting from national patent rights can, in the light of Article 85, legitimately be strengthened through contractual provisions. The question, initially within the domain of decision by the Commission, cannot, however, be usefully examined today without reference to how the European Court will decide the extent to which the right to sue for patent infringement has been limited by Article 30 of the Treaty of Rome.

It was only after a number of years that legal writers began seriously to consider the possibility that infringement suits might be prevented by the Treaty. To the surprise of many close observers of EEC law, in 1971 the European Court took a big step toward unifying the market which then consisted of six Member States, at a certain expense to industrial and intellectual property rights, when it decided the Deutsche Grammophon case. Although Deutsche Grammophon did not involve a patent, the European Court's holding on the rights protecting recordings clearly suggested that in patent cases, the European Court would hold that once a patented product had been sold or “put on the market” in one Member State with the consent of the owner, importation of the product into another Member State could not be


prevented by a patent infringement suit based on a parallel patent of common origin. The rule was further clarified a little over two years later when the European Court decided Sterling Drug, a case which expressly involved patents. By that time the European Court's position was clear: relief in a patent infringement suit would in certain circumstances be deemed an effect equivalent to an import quota prohibited by Article 30 of the Treaty of Rome and not protected by the saving clause of Article 36.

Despite the uncertainties produced by Articles 30 and 36 in other situations, the general rule established by these European Court decisions indicates that, for example, a parallel importer having bought a patented product from a U.K. patent licensee who has made the product under license in the United Kingdom can be assured upon exporting it to the Netherlands that neither the patentee who licensed the U.K. company nor a Dutch licensee can rely on a parallel Dutch patent to prevent the import into the Netherlands.

A MAJOR UNRESOLVED ISSUE

While the rules formulated by the European Court in these cases were both clear and had major commercial significance, they left undecided the result of one situation which is of essential importance from an industrial point of view: whether to allow suits for patent infringement when the product had not been "put on the market" prior to export to the other EEC countries. In other words, what if the U.K.

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13 Centrafarm BV v. Sterling Drug, [1974] E. Comm. Ct. J. Rep. 1147, [1974] 2 Comm. Mkt. L.R. 480. In this case involving parallel patents, the Court did not deal with the existence of a parallel patent in the Member State where the product had first been put on the market, but only with the product's having been put on the market by the patent holder or with his consent.
14 The variety of situations encountered, the complexity of the analysis and the disparity between the approaches taken by the Commission and the European Court are described by van Themaat & Gormley, Prohibiting Restrictions of Free Trade within the Community: Articles 30-36 of the EEC Treaty, 3 Nw. J. Int'l L. & Bus. 577 (1981).
15 Although no case has involved products manufactured by a licensee unrelated to the licensor's group except by the license contract, there seems to be no reason to make a distinction. This point has been examined by Johannes, supra note 8, at 66-67. Questions will, of course, arise in special situations, such as when no patent can be granted in the country of manufacture. See Parke, Davis & Co. v. Probel--Centrafarm, [1968] E. Comm. Ct. J. Rep. 55, [1968] Comm. Mkt. L.R. 47. See also, Merck & Co., Inc. v. Stephar BV, 23 O.J. EUR. COMM. (No. C 260) 4 (1980). Another example is when the patent has expired in the country in which the goods are produced. See Dymo Industries, Inc., v. Etiketten Service Arnhem BV, 23 O.J. EUR. COMM. (No. C 17) 10-11 (1980). This case has now been withdrawn. A further question involves goods produced under a compulsory license. See Pharmon BV v. Hoechst AG, 23 O.J. EUR. COMM. (No. C 347) 28 (1980).
licensee had exported directly to the Netherlands?\textsuperscript{16} Middlemen are not employed in the export of certain raw materials and many capital goods. Thus market integration would not be achieved by the rules as so far developed without the possibility of direct sales by a licensee. Even when middlemen are used, the licensee is often in a better position to make export sales than middlemen—for various reasons—which include better familiarity with the product, price advantage, and ability to predict and control product quantities available for export. According to the prevailing view, in such instances, the product is not considered to have been “put on the market,” as the European Court has consistently phrased the rule in its holdings thus far.\textsuperscript{17}

Under EEC law, the remaining question is not one to be resolved by the Commission, because its decision-making power in these matters extends only to Articles 85 and 86. Rather, the European Court must decide the issue when a Member State court refers the matter to the European Court for an interpretation of Articles 30 and 36. The European Court will almost certainly have the occasion to examine the question in due course, but it is not clear how the Court will approach the question, or how it will decide it. It appears that the Court will probably approach the issue by recognizing that giving effect to the patent right in an infringement suit brought under these circumstances would be essentially equivalent to an import quota within the meaning of Article 30 that must be prohibited unless, within the meaning of Article 36, permitting the infringement suit is found necessary to protect the specific subject matter of the patent right in the state of import.\textsuperscript{18}

Opinion is divided as to whether the European Court should find territorial protection necessary to protect the specific subject matter of the patent right,\textsuperscript{19} but at least all interested parties will have the oppor-

\textsuperscript{16} For purposes of the issues in question, sale by an independent U.K. licensee to a company in the United Kingdom belonging to its own group which then exported to the Netherlands would presumably be deemed a direct export.

\textsuperscript{17} It has been argued that the patentee’s granting a license, perhaps combined with production by the licensee, is itself a “putting onto the market.” This position was expressed by Johannes in the 1979 hearings organized by the Commission in connection with the draft patent licensing regulation. Johannes bases his view principally on the concept that the “specific subject matter” to be protected is not the various national patents but rather the invention. The European Court’s phrasing of its ruling in \textit{Sterling Drug}, lends some support to this view. See Centrafarm v. \textit{Sterling Drug}, [1974] E. Comm. Ct. J. Rep. 1147, [1974] 2 Comm. Mkt. L.R. 480.

\textsuperscript{18} This is the approach adopted by Johannes, \textit{supra} note 15, at 70-75.

\textsuperscript{19} Johannes seems to recognize that a patentee’s protection against sales by a licensee may in some cases be necessary to preserve the existence of the patent licensor’s rights, \textit{id.} at 73, but nevertheless finds such protection incompatible with a unified market. Johannes finally concludes that the protection should not be deemed a part of the existence of the patent right, or, in other words, of the specific subject matter. \textit{id.} at 74.
tunity to present their views. The Member States have considered the matter at various times and at one point left the impression that they would like the Court to permit such protection when they adopted Article 43(2) of the Community Patent Convention.\textsuperscript{20} Despite the fact that the Member States are being consulted by the Commission regarding the patent licensing regulation, the Member States acting individually, will have the opportunity to reiterate their views by arguing as interested parties when the issue arises before the European Court.

Because no prediction can confidently be made regarding the Court's decision of this issue, licensors and licensees for the time being are left to speculate. Some licensors may be in no hurry to have an answer because they believe that licensees, faced with such uncertainties, will exercise restraint. Licensor may also fear that the final answer of the European Court will be one they do not want to hear. Even the Commission itself may not have determined what position it will take in its own arguments before the Court.\textsuperscript{21} Another factor that may tend to restrain either a licensor or licensee from suing for infringement is that upon learning of the suit, the Commission may charge that the licensing grants on which the suit is based infringe the competition rules of Article 85, and perhaps Article 86. This other legal aspect, to a great extent under the control of the Commission, is closely related to the Article 30 question, yet at the same time is quite distinct from it.

**The Impact of Article 85**

The other half of the problem involving the competition rules based on Articles 85 and 86 is primarily within the domain of the Commission. Even though the European Court will make the final ruling on any appeal from a Commission decision, the Commission initiates policy formation and makes decisions that are binding unless overturned on appeal. In practice, this often means that for a substantial period of time an entire area of law will be regulated solely by the

\textsuperscript{20} The official title of the Convention, which is not yet in force, is the Convention for the European Patent for the Common Market. The provision in question states: "The rights conferred by the Community patent may be invoked against a licensee who contravenes any restriction in his license which is covered by paragraph 1." Paragraph 1 recognizes that a license can be granted for a part of the Community.

\textsuperscript{21} As indicated at note 19 supra, Johannes, who at present heads the Industrial Property Rights section of the Commission's Competition Directorate-General, took the position in his 1976 book that infringement relief could not be granted in the country of import. He was speaking in his personal capacity, of course, and it remains to be seen what position the Commission will take in arguments before the European Court. It may be noted, however, that in discussions with the Member States on the Community Patent Convention, the Commission opposed Article 43(2). See note 20 supra.
Commission. So far, this has been the case for patent licensing, where the Commission's 1962 Notice governed the field until the series of Commission cases began in 1971. Further, none of the issues treated in the Notice or in the Commission cases has yet been decided by the European Court.

Obviously harmony between the two sets of rules is highly desirable. In order to avoid confusion, any final legal solution must take into account both the set of rules based on Articles 30 and 36 and those based on Article 85 so that the scope of one set of rules is not basically incompatible with the other. Before examining the joint solution proposed by the Commission in its draft patent licensing regulation, we shall review briefly the Commission's treatment of the basic antitrust issues involved.

As interpreted by the European Court, Article 85(1)\(^\text{22}\) prohibits restrictive agreements or concerted practices that have or may have an appreciable effect on competition within one or more of the Member States. Applicability of Article 85(1), however, depends on whether the normal flow of trade between two or more Member States may be affected, directly or indirectly, to an appreciable extent. From the text alone, the Article appears to be concerned exclusively with the furtherance of competition. In practice, however, the analysis of competitive effect is often given secondary importance by the Community authorities when they focus on their determination to further the integration of the market. Under this approach, it seems inevitable that the infringement of Article 85(1) which will provoke the surest condemnation (and often substantial fines) is a prohibition, hindrance, or disincentive relating to exports or imports from another part of the Community. An agreement or concerted practice with such a purpose or effect is not only a per se violation unless it escapes under the de minimis exception (of truly minimal interest to most parties);\(^\text{23}\) an agreement having that effect has always appeared to have little chance of being exempted under Article 85(3).\(^\text{24}\)

\(^{22}\) See note 2 supra.

\(^{23}\) Under the Commission's Notice on Agreements of Minor Importance, 20 O.J. EUR. COMM. (No. C 313) 3-4 (1977), in principle, a restriction will not be deemed to have an appreciable effect on competition if two criteria are met: if it affects not more than 5 percent of the product market in a substantial part of the Common Market, and the worldwide turnover in all product lines of the groups which are parties to the agreement does not exceed 50 million ECU (currently about U.S. $52 million).

\(^{24}\) The Commission has normally considered that an export prohibition can be refused an exemption on the basis of any one of the first three of the four criteria of Article 85(3):

(i) contribution to improving the production or distribution of goods or promoting technical or economic progress, while
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3:561(1981)

In the area of distribution, EEC law on clauses affecting exports to other parts of the Community is relatively clear.\(^{25}\) Whether an export prohibition should be treated the same way when included in a patent license however, has been questioned. Export to a country outside the territory would not be feasible if patent infringement results in the country of import and if there were no Treaty or other obstacle to an infringement suit. It may be argued that such an export prohibition would not be an appreciable restriction of competition because an infringement suit could be brought against the exporter.\(^{26}\) In such circumstances, the contractual export prohibition might be seen as giving the licensor only an alternative remedy. In some cases, of course, restrictive effects could still be discerned from any export prohibition. The patent might be too weak to withstand challenge in the country of importation, or it might be easier for the licensor to sue on contract or go to arbitration for violation of a license clause than to sue for infringement. As a matter of law, however, it seems that the restraint might well be appreciable in some circumstances, particularly, for example, when the patent is weak. Thus, even if the licensor were later assured that Article 36 would be interpreted in a way favorable to him so as to allow an infringement suit, he could not be assured of immunity from prosecution by the Commission which has opposed such clauses, nor could the licensor be certain of succeeding in a national court if he were to sue on contract.

(ii) allowing consumers a fair share of the resulting benefit, and
(iii) not imposing restrictions which are not indispensable to the attainment of these objectives; and
(iv) not affording the possibility of eliminating competition in respect of a substantial part of the products in question.

No export prohibition has yet been exempted. Certain restrictions which limit the ability to export have, however, been granted a block exemption by Commission Regulation 67/67, relating to exclusive distribution. In *Distillers Company Ltd v. Commission*, [1980] E. Comm. Ct. J. Rep. 2229, [1980] 3 Comm. Mkt. L.R. 121, one of the issues before the European Court was the possibility of an exemption for a pricing policy that impeded exports in order to protect exclusive distributors; however, the case was decided on another issue.

25 One minor but certainly interesting exception is that raised in the *Distillers* case, note 24 *supra*. Official policy is so strongly against clauses adversely affecting exports or imports within the Community that once such a restriction has been found, the parties imposing it will be in serious danger of a substantial fine unless covered by a notification or by the block exemption of Commission Regulation 67/67. The remaining doubt concerns not the principle of law but the interpretation of circumstances that will be deemed to constitute a disincentive to exports.

26 Jaume, then a director in the Commission's Competition Directorate-General, took this position in *Accords de licences et règles de concurrence*, 15 *REVUE DU MARCHÉ COMMUN* 674 (1972).
The Approach of the Draft Regulation

The Commission began establishing its precedents concerning the relevance of Article 85 to patent licensing late in 1971 when it exempted exclusive patent manufacturing licenses covering a part of the Community on condition that the licensee was granted no exclusive sales rights within the Community and obtained non-exclusive sales rights for all the Community. By imposing such a condition, the Commission avoided giving the licensor or another licensee the opportunity of suing for infringement when the licensee exported elsewhere in the Community. It was not until late 1975 that the Commission even referred to the possibility of there being circumstances in which it might be willing to exempt an export prohibition imposed on the licensee.

Commission and Court decisions had clearly developed the issues arising under Articles 30 and 36 and Article 85 when the Commission completed another in a series of drafts of its patent licensing regulations which it was prepared to publish as the definitive draft in March of 1979.

In its draft, the Commission proposed to treat an export prohibition directed at another part of the Community no more severely than an exclusive sales right granted with regard to an EEC patent. The draft demonstrates what had become fairly evident from preceding cases: the Commission has decided to give priority to integration of the Community market, except for temporary protection of relatively small parties, regardless of the protection that may or may not eventually be held by the European Court to be available against direct exports by licensees outside their territories.

In preparing its draft, the Commission faced at least two major uncertainties. The first is whether the European Court will eventually hold that the grant of an exclusive sales right in a patent license is not in itself a violation of Article 85(1) because such a grant is "within the scope" of the patent. A number of industry circles have strongly urged this view upon the Commission. This approach excludes whatever is within the "scope" of the patent from the reach of Article 85(1); it is not necessarily inconsistent with the now-accepted approach of defining the reach of the Treaty prohibitions by referring to the "subject matter" or the "existence" of the patent, as opposed to the exercise of the patent.

Nevertheless, using the test of the patent's "scope" tends to extend the domain that was in principle immune from attack under Article 85(1).

Regardless of which test is used, if the Court were to hold that an exclusive patent license is not subject to attack under Article 85(1) merely because of its exclusivity, the Commission would be obliged to make a fundamental change in its approach in the patent licensing regulation.

The second question is whether the Court will eventually hold that a patent infringement suit cannot be used to stop imports from direct sales by licensees in other parts of the Community. In view of the relationship of the two issues, it is questionable whether the Court would be likely to hold exclusive sales grants in patent licenses immune from attack under Article 85(1) and at the same time hold that infringement suits cannot be brought because of the prohibition of Article 30. In preparing the patent licensing regulation, the Commission obviously could not afford to base its draft on one assumption to the exclusion of the other. The Commission sought market unity and had to cover every possibility, even if it resulted in certain undesirable side effects.

Thus, if the regulation is adopted without change in this respect and the Court does not hold exclusive sales grants immune from attack under Article 85(1), the Commission will obtain a result which an eventual holding of the Court permitting infringement suits by virtue of Article 36 would not change with regard to the majority of licensing situations since exclusive sales grants would not be permitted. On the other hand, if the Court were to hold that as a result of the prohibition of Article 30 and the lack of protection of Article 36, the licensee can, freely export to other parts of the Community, even in the absence of a grant of sales rights under parallel patents in those countries, the Com-

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29 Article 1(2) of the draft regulation as published in March 1979 provides in relevant part:
Exclusivity of sales and analogous prohibitions of the sale of patented products outside the licensed territory shall be exempted . . . only:
(a) Where the total annual turnover of the licensor or licensee whose market is to be protected by an export ban imposed on the other party or on another licensee does not exceed 100 million units of account; [the exemption] . . . shall remain applicable notwithstanding that this turnover is exceeded by up to 10% in two consecutive financial years; in calculating total turnover, sales of goods and services recorded in the last financial year by the undertaking concerned and all undertakings having economic connections with it shall be taken into account; and
(b) if the exclusivity of sales and export bans have been agreed at most for the duration of the most recent patent existing at the time when the agreement was entered into; this period may not be extended in respect of such obligations by licensing agreements in respect of patents for new applications or improvements; and
(c) if the patented product or product manufactured by the patented process may be sold throughout the Community by commercial undertakings which have no economic connections with the licensor or licensees; and
(d) if the licensee either manufactures the licensed products himself, or has them manufactured by an undertaking that has economic connections with him.
mission’s restrictions in its patent licensing regulation on grants of exclusive sales rights would not have been necessary to have achieved a market unity and would have significant broader implications for the parties to a license. The system contemplated by the proposed block exemption regulation limits the possibility for a licensor to assume the obligation not to ship into the territory of the licensee, whether or not that licensor was producing within the Community. In most cases, the system also prevents the licensee from being able to sue for infringement upon the introduction into his territory of goods produced under a parallel patent outside the Community since he would not be an “exclusive” licensee.30

The draft regulation indicates a clear choice by the Commission in favor of market integration. Apart from exceptional cases that might be found entitled to an individual exemption, patent rights are to be used to protect a licensee within the Community from sales from other Community countries only when the licensee is small enough to be deemed in need of protection. Under the draft as published by the Commission, weakness is defined only in terms of group turnover.31 In discussions with industry circles, however, the Commission has indicated that a more developed criterion is desirable, if one could be found that was subject to precise application. Thus, the final criterion may be more complex and closer to the market realities.32

30 The Commission would, of course, take the position that the prohibition against exclusive licenses, whether or not they relate to market unity, comes from Article 85(1), as shown by a number of Commission decisions. According to the Commission, the block exemption regulation is meant to liberalize that rather strict rule by putting into effect an automatic “rule of reason” permitting exclusive manufacturing licenses regardless of the size of the parties, and also exclusive sales rights when accompanied by manufacturing rights in instances when the protected party is relatively small. Nevertheless, it should be recognized that in working out any system, the considerable incursion of EEC law on what had always been deemed a proper exercise of patent rights can be explained primarily by the imperatives of market unity within the Community. The system contemplated by the block exemption regulation, when read in conjunction with the Commission’s interpretation of Article 85(1), denies a licensor the right to give an exclusive license by which the licensee can achieve some degree of protection even when market unity is not involved. This result, of course, offers certain advantages from the point of view of increased competition, but it has nothing to do with Community market integration. It is by no means clear that the Commission would have required such limitations on a licensee’s rights to protection in the absence of the over-riding consideration of market unity.

31 See note 29 supra.

32 Article 1(2) of the draft regulation exempts a grant of sales exclusivity to a licensee only if the annual worldwide turnover of the licensee’s group did not exceed 100 million ECU. In the October 1979 hearing, the Commission gave interested parties the opportunity to express their opinions concerning the draft regulation. A great deal of attention was focused on the turnover criterion, which a number of parties criticized as being arbitrary. While the Commission did not indicate at that time any decision to abandon the turnover criterion set forth in the draft regulation, it has shown an interest in pursuing an alternative criterion that would take into account
While insisting upon market integration for the larger parties, the
draft regulation presents at the same time a noteworthy and almost sur-
prising concession to the needs of licensing parties by permitting the
use of export prohibitions to protect small- and medium-sized busi-
nesses through a block exemption. This development is noteworthy be-
cause, as observed earlier, export prohibitions within the Community
have not been permitted in any EEC case except in the rare *de minimis*
situations.\(^33\)

The regulation as presently proposed would not permit an export
prohibition to be used to protect a market within the Community
where no valid patent exists.\(^34\) Thus, if a licensor granted rights in a
patent license under both patents and related know-how, and in one
Member State no patent had been obtained and no patent application
was pending, the regulation would not permit protection of that market
regardless of the weakness of the party to be protected on that
market.\(^35\)

**The Present**

Major undecided issues and important unadopted regulations
leave licensing parties uncertain about the effects of their contractual
arrangements. First, the situation described above obviously presents a
dilemma of considerable proportions for licensors and licensees who
think they need to obtain or give some territorial protection within the
Community. For the time being, in many situations they can proceed
to grant exclusive licenses for both manufacture and sale without con-
cern that the Commission will consider such grants an intentional or
negligent violation that would result in fines.\(^36\) However, the parties
will not know what effect their agreements will have in the courts, even

\(^33\) See note 23 and accompanying text *supra.*

\(^34\) See Article 3(13) of the draft regulation, note 5 *supra.*

\(^35\) While the proposed rule represents a policy decision by the Commission, the result is also
perhaps suggested by the more technical consideration that to allow a protection of a territory
where no patent exists would not be within the scope of a patent licensing regulation. Such pro-
tection could presumably be given in a regulation granting a block exemption in regard to know-
how agreements.

\(^36\) In a notice accompanying the publication of the draft regulation, *supra* note 5, at 12, the
Commission indicated that parties conducting their affairs in accordance with the Commission's
1962 Notice on Patent Licensing Agreements would not be fined. With respect to grants of sales
exclusivity, the 1962 Notice sets forth the Commission's view that an agreement by a licensor with
a licensee not to authorize anyone else to exploit the invention and not to exploit the invention
in the near future; both the exclusive manufacturing and sales rights may be found void because they violate Article 85(1). The parties can decide to resort to exclusive manufacturing rights alone with the assurance that they will eventually be covered by the block exemption when the patent licensing regulation is adopted. However, the licensor will often want to give more market protection than the exclusive manufacturing rights alone would carry. Some products can easily be transported throughout the Community with little or no obstruction from transport costs or other factors. The need for protection in addition to exclusive manufacturing rights becomes of even greater importance as the Community becomes more fully unified due to the lack of technical and other barriers to selling throughout the ten-Member State area.

One alternative is for the parties to enter into an agreement granting full territorial protection through exclusive manufacturing and sales rights and export bans, and then to notify the Commission of the license agreement in a request for an exemption under Article 85(3). Many parties hesitate to notify the Commission of the license agreement, however, because of the real or imagined difficulties created by requests for an exemption. The parties have to assume that the Commission probably will grant an exemption for complete territorial protection only if the circumstances are either somewhat like those of the draft regulation, i.e., the clause protects a party presumably needing protection, or if some exceptional circumstances can be shown. It is by no means clear what types of exceptional circumstances the Commission will consider convincing.

Another possibility is for the licensor to impose no export prohibition but simply to grant the licensee no sales rights outside the territory. The licensor will hope to be able to sue for infringement if the licensee sells outside his territory. The licensee would, however, have to assume that the person pursued for infringement of a patent of a Member State would be likely to raise the issue of Article 30 before the national court as a defense to the infringement suit and that the case would be referred to the European Court.

THE FUTURE

For most prospective contracting parties, the most significant and immediate question is whether there will be a block exemption regulation for patent licenses and what form it will take. It seems likely that a regulation will be adopted in due course and that its provisions in re-
gard to the questions considered here will not be fundamentally different from those in the published draft.\textsuperscript{37}

Despite the undisputed importance of the patent licensing regulation, it appears that adoption of the regulation will not affect the more economically important licenses, except to settle the issue of exclusive manufacturing grants and whatever territorial protection may result from them. Most exclusive sales grants or export prohibitions included in such patent licenses are designed to protect relatively important companies. Under the regulation as proposed, the permissibility of exclusive sales grants or export prohibitions under Article 85(1) will continue to depend on the possibility of a specific exemption under Article 85(3) based on the facts of the individual case.

In most cases, a licensee cannot legally be given an exclusive sales grant without an exemption under present Commission decisions. However, at least until the European Court decides otherwise, a patentee can protect a non-exclusive licensee against another licensee who makes direct sales into the first licensee's territory without having a right under the patent to sell into that territory by suing for infringement. To prevent such infringement suits, the Commission would have to hold that a licensor violates Article 85(1) by failing to grant all licensees non-exclusive sales rights throughout the Community. At present, there seems to be no indication that the Commission will do so. Rather, it appears that regardless of the final wording of the patent licensing regulation, Articles 30 and 36 will retain their importance in the majority of the economically important cases. The final solution to this problem will thus depend to a very large extent on the European Court.

**Conclusion**

The final shape of the legal rules apparently will be determined as a matter of Community policy rather than as a reflection of the strictly juridical point of view. The central question for both the European Court and the Commission will be whether the Community goal of furthering market unity among the ten Member States will override the important economic interests that parties think justifiably attach to patents. Important questions are yet to be settled by the Commission, in cases that are not yet in progress. These cases must be decided in the light of the European Court's decisions in cases either before it or yet to

\textsuperscript{37} The European Court's decision in the pending *Breeders' Rights-Maize Seed* case could, of course, require fundamental changes in the regulation's approach to these questions. See 21 O.J. EUR. COMM. (No. L 286) 23 (1978) for the Commission decision.
be filed. Meanwhile, both industry circles and Member States continue to press their views upon the Commission. The dialogue between the various bodies which affect EEC law and the Community authorities is not fully open to public view, but we may hope that the authorities will determine only after due deliberation this important point of equilibrium between market unity and patent rights.