INTELLECTUAL PROPERTY AND COMPETITION LAW
A COMPARATIVE APPROACH
EEC AND USA

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RÉSUMÉ

Les monopoles octroyés par les droits de propriété intellectuelle sont-ils en conflit avec les politiques de concurrence qui visent, sinon à éliminer, tout au moins à limiter les monopoles ? Cette question a fait l'objet d'un grand nombre de polémiques et de commentaires. Le débat est en vérité empreint d'une grave confusion: les monopoles découlant des droits de propriété intellectuelle sont des monopoles légaux, et non économiques, qui ne menacent donc pas la liberté de concurrence sur les marchés. De plus, si l'on raisonne à long terme, on ne peut éviter de constater que les droits de propriété intellectuelle visent en fait les mêmes objectifs que les politiques de concurrence, à savoir la protection des marchés contre les actes de concurrence déloyale et le bien-être des consommateurs.

Partant donc du constat que les droits de propriété intellectuelle et les législations relatives aux politiques de concurrence ne sont pas intrinsèquement antinomiques, cette étude tentera de montrer comment l'utilisation inadéquate d'un brevet d'invention, d'une marque de commerce ou de fabrique ou d'un droit d'auteur peut engendrer des conflits d'intérêt avec les objectifs du droit de la concurrence. Les moyens mis en oeuvre par les autorités chargées de faire respecter les législations relatives à la protection de la libre concurrence aux États Unis d'Amérique et dans la Communauté Économique Européenne, en réaction à ces pratiques anti-concurrentielles, feront l'objet d'une analyse comparative.

ABSTRACT

Are the monopolies afforded by intellectual property rights in conflict with competition policies that aim at eliminating, or at least limiting monopolies ? That question has generated much controversy and commentary. Indeed, the debate neglects an important distinction: the monopolies resulting from intellectual property rights are legal ones, not economic monopolies, and therefore they do not jeopardize free market competition. Besides, from a long term view, intellectual property rights tend to achieve the same objectives as those of competition policies, namely the protection of markets against unfair competition and consumers' welfare.

Beginning from the assumption that intellectual property rights and antitrust legislation are not inherently opposed, this study will attempt to establish that an improper utilization of a patent, a trademark, or a copyright may father conflicts of interest with the goals of competition law. The means adopted by the antitrust authorities in United States of America and the Economic European Community in reaction to these restrictive business practices shall be analyzed comparatively.

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To Karine.

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INTRODUCTION

> *Intellectual property... comprises all those things which emanate from the exercise of the human brain, such as ideas, inventions, poems, designs, microcomputers and Mickey Mouse.*[1]

That colloquial definition can be translated in legal terms, and intellectual property would be described as the legal rights that govern and protect products of the human intellect. Those legal rights are patents, trademarks, copyrights, and a bundle of allied rights[2]. Intellectual property rights afford a legal framework for the produce of the mind, not to the products themselves; a patent right protects the inventive process that led to the invention, but not the finished product embodying the process. The rights conferred upon intellectual property rights owners consist of exclusive privileges that allow them to prevent third parties from using, selling, or copying their inventions, names or symbols, or literary, musical, and artistic works. Thus, the owner of intellectual property is protected against encroachment by others by the grant by the state of an exclusionary (and sometimes exclusive) right to the exploitation, for a limited duration, of that which emanates from the intellect. Underlying that absolute or qualified monopoly is the idea that the sole exploitation of the property right is a reward for creating and divulging technological innovation[3]. Since the holder of a monopoly right is able to prevent third

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[1] PHILLIPS & FIRTH, 2d ed. *Introduction to Intellectual Property Law* (1990) at 3.

[2] Such as plant breeders' rights, semi-conductor chips' mask works, and to a certain extent trade secrets and know-how.

[3] The owner of the monopoly so granted can exploit it himself, or sell or license its exploitation by another. Hence, the rights and powers one may enjoy over another's work must also be included in the definition of intellectual property rights.

parties from using his work, he enjoys a genuine property right[4].

The concept of monopoly establishes a link between intellectual property and competition law:

> *It is the primary function of the law of unfair competition to safeguard the competitive community against certain methods of trade and business which are repugnant to and destructive of equal opportunity in honest competition, and to outlaw such practices for the protection of free enterprise*[5].

The purpose of competition policy is to ensure that market rules operate without restrictions, on the basis that the discipline of competition is the most effective mechanism to achieve an efficient allocation of resources. Accordingly, antitrust laws are designed to ensure that market forces are liberated from the distorting effect of trade restraints and practices which might otherwise constrain the operation of normal competition.

It has long been wondered whether intellectual property monopolies constitute a restraint on free competition. For instance, it has been held that there was a significant conflict between patent and antitrust laws, in that patents grant a monopoly whereas competition legislation provides for the elimination of monopolies and exclusionary practices[6]. However, that

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[4] However, it has been held that patents and copyrights were not species of property rights; PALMER, "Intellectual Property: A Non-Posnerian Law and Economics Approach." [1989] 12 Hamline L. Rev. 261. For a criticism of that approach, see MACKAAY, "Economics Incentives in Markets for Information and Innovation." 13 Harvard J. L & Public Policy. 867. Dean Paul Roubier has adopted the view that intellectual rights are property rights, characterized by exclusivity and monopolistic privileges, but are neither rights *in personam* nor rights *in rem*. Unlike the former, intellectual property rights can be enforced against anyone (*erga omnes*), and unlike the latter which are perpetual, they are limited in time; ROUBIER, *Le Droit de la Propriété Industrielle* t.1 (1952) at No.19 and at 86.

[5] CALLMAN, *Trademarks, Unfair Competition and Monopolies* (1984) c.4 at 2

[6] Intellectual property monopolies would close markets and discourage competitive innovation. See "Restrictive Business Practices Relating to Patents and Licences" O.E.C.D Report (1972) at 5. It has been held that incentives to innovation exist naturally in any market, *"without state intervention"*, meaning that the monopolies granted by the state to intellectual property rights owners are not the only way to spur innovation; MACKAAY, supra note 4 at 907.

debate is outdated, and that apparent conflict should not lead to the hasty conclusion that the systems are incompatible. First, intellectual property rights confer upon their owner legal monopolies which do not necessarily generate economic monopolies, or jeopardize free competition[7]. Second, if one analyses intellectual property rights from a long term view, it appears that the goals of intellectual property law are not so remote from those of antitrust policies and laws. The monopoly conferred upon the intellectual property rights owner fulfils two functions that are inter-related. It affords legal protection against infringers and more generally against unfair competition, and consequently it provides incentives for innovation[8]. Technological innovation contributes to economic and social progress, and therefore to consumers' welfare. The limited duration of monopolies as well as the possibility of licensing intellectual property rights promote a widespread dissemination of new technologies.

Thus, both antitrust and intellectual property laws provide means to control unfair competition, and both spur innovation: the former by preventing restrictions on competition; and, the latter by rewarding innovators with an exclusive right of exploitation[9]. Therefore, intellectual property rights in themselves are not in conflict with the objectives of competition policies and laws, but rather tend to participate in the

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[7] See infra note 198 and accompanying text.

[8] Property rights are the keystones of an effective market economy. If innovators were not granted property rights in their works, the latter would be freely counterfeited or plagiarized, and their profitability would be reduced. That would discourage innovation.

[9] A good illustration of the interface between those two areas of law is provided by American constitutional law, where patents constitute an exception to the basic rule of competition embodied in the Sherman Act. That legislation was enacted to combat monopolies, but patentees were granted a legal monopoly on the ground that the purpose of patent rights is *"to promote the progress of science and useful arts, by securing for limited times to authors and inventors the exclusive right to their respective writings and discoveries"* (Article 1, Section 8, Clause 8 of the US Federal Constitution).

accomplishment of those goals, provided they are properly used. The existence of patents, trademarks, copyrights, and the like does not violate antitrust laws, but their exercise may contravene such provisions[10]. That is where the controversy really stands: what constitutes an improper exercise of intellectual property rights ? Patents, trademarks, or copyrights may be used in a way that goes beyond the scope of their legal monopoly, and thus violates antitrust provisions dealing with dominant positions or anti-competitive practices and agreements. Where a patentee attempts to extend the monopoly he owns beyond its legal limits with a view to excluding his competitors, where separately owned national rights in the same trademark are employed for the purpose of excluding imports, allocating markets or imposing different price levels in different markets, or where competition is lessened and trade between several States is affected by means of restriction clauses that intellectual property rights owners include in licensing agreements, antitrust laws are violated.

The United States has the oldest competition law system in the modern world. The foundation on which all US antitrust law has been built is the Sherman Act[11]. The ban of antitrust laws applies to "*restraint of*

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[10] An economic analysis demonstrates that free competition is attained when prices are reduced to marginal costs, thus maximizing yield of society resources. Such a policy seems to be inconsistent with the exclusive rights afforded by intellectual property. Innovation constitutes information whose marginal cost is zero since it can be used at the same time by an indefinite number of persons, and the information is not exhausted by repeated use. A real price can therefore be imposed upon the use of information, and dissemination of innovation may be diminished. See ORDOVER, "Economic Foundations and Considerations in Protecting Industrial and Intellectual Property" [1984] 53 Antitrust L. J. 503; LEHMANN, "Property and Intellectual Property: Property Rights as Restrictions on Competition in Furtherance of Competition" [1989] 20 I.I.C. 1; "Politique de Concurrence et Propriété Intellectuelle" O.E.C.D Report [1989] at 11-14.

[11] That statute was enacted in 1890 as a fundamental charter designed to preserve free competition. The rationale behind that statute is that restriction-free competitive forces shall ensure an effective allocation of resources. Further legislation have been promulgated afterwards to implement an effective policy of protection of free competition: the 1914 Clayton Act and Federal Trade Commission Act, the 1918 Webb-Pomerene Act, the 1936 Robinson-Patman Act, or the 1950 Celler-Kefauver Act.

trade"[12], "*monopolization*"[13], and "*substantial lessening of competition*"[14]. Section 1 of the Sherman Act outlaws any contract or combination effecting a restraint of trade, and section 2 condemns monopolization as such, as well as any attempt to monopolize and combinations or conspiracies to monopolize in interstate commerce[15]. The United States system of competition law was the pioneer which has served as a model for most of the later systems, including that of the Economic European Community (EEC).

Article 85 of the EEC Treaty (also known as the Rome Treaty) prohibits agreements or concerted practices which may affect trade between Member States, or distort competition within the common market. Article 86 condemns the abuse of dominant market position[16]. Besides, articles 30 to 36 of the Treaty, although not included in the competition provisions, may have an impact on intellectual property since they deal with the free movement of goods within the Community, and specifically describe industrial and commercial rights as potential exceptions to the principle.

When comparing US and EEC competition laws, it must be borne in mind that the development of the two systems has been influenced by the historic conditions of the USA and Europe, which differ considerably.

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[12] Sections 1 and 3 of the Sherman Act.

[13] Section 2 of the Sherman Act.

[14] Sections 2, 3 and 7 of the Clayton Act.

[15] US antitrust prohibitions confer enormous discretion upon judges in deciding what specific practices are prohibited, since neither section 1 nor section 2 of the Sherman Act contains specific guidance as to what is prohibited or permitted.

[16] Both provisions contain a non-exhaustive list of specific practices that are prohibited, and article 85 has certain agreements or conducts fall outside the scope of the prohibition by means of an exemption procedure.

Whereas the Sherman Act was enacted by the American Congress in response to abuses in certain sectors of American industry, the competition rules of the EEC were to supplement the general objectives of the Rome Treaty which sought to establish a common market. Further, when respective antitrust legislation was drafted, the USA and Europe were at different industrial levels. Industrial development was far more advanced at the time the competition provisions of the EEC Treaty were introduced than it had been in the USA when the Sherman Act was promulgated. And the development of European and American industries before the creation of their respective competition statutes were entirely different[17]. There are other factors which complicate a comparison. Competitive conditions are not so homogeneous in Europe as in the United States, given that EEC Member States pursue different national policies. Therefore, simple situations under US law may become very complicated under EEC law. In terms of procedure, "treble damages" are unknown to the European authorities[18], and exemption procedures do not exist under US antitrust laws[19]. The US antitrust laws are enforced by the government in both civil and criminal court proceedings and by administrative action. Those laws may also be enforced in civil proceedings by individuals, and there are two federal agencies in charge of the antitrust legislation enforcement: the Antitrust Division of the Department of Justice (DOJ) and the Federal

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17 See BORK, "Legislative Intent and the Policy of the Sherman Act" [1966] 9 J. L Econ. 7 at 15; DILLARD, "Economic Development of the North Atlantic Community" (1967) at 406; and generally VAUGHN, *The United States Patent System: Legal and Economic Conflicts in American Patent History* (1956).

18 US procedure permits any damages to be trebled, meaning that the violator can be imposed a fine without need for criminal proceedings.

19 See further at p.71

Trade Commission (FTC). Within the EEC, national authorities do not use their powers to enforce the legislation of the Community, but have to complain to the Commission of the European Communities, Directorate General IV, who will take civil actions. On the other hand, several factors may be advanced in favour of a comparison. *"Both the USA and the EEC rest on a common and fundamental interest in and respect for the maintenance of a free, fair and competitive market system"*[20]. And both systems agree on the fact that free market may be threatened by arrangements and conduct adopted by private undertakings[21].

How those differences and common points affect the way EEC and US systems treat intellectual property in the context of competition law is the subject of this thesis. No doubt another interesting and useful thesis could be written about the policy implications of emphasizing intellectual property rights rather than free market competition, but this study focuses upon a comparison of the legal regimes on those subject-matters now in force in the USA and the EEC. It is a difficult matter to decide how to balance the amount of protection that needs to be afforded to innovators to encourage them in their endeavours, against the desirability of maintaining an open and competitive market and protecting individual competitors. We will compare how American and European authorities balance those interests, and observe that although they start from different standpoints, EEC and US antitrust systems often agree on the pro-competitive or anti-competitive effects of an intellectual property rights owner's conduct. We

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[20] FEJO, *Monopoly Law and Market* (1990) c.1 at 12.

[21] See generally FULGATE, "The Common Market and the United States Antitrust Laws" [1963] 38 N.Y.U.L.Rev. 458; EWING, "Antitrust Enforcement and the Patent System: Similarities in the European and American Approaches" [1980] 11 I.I.C. 279.

shall divide this study in two parts, considering first the unilateral use of intellectual property rights, and its effect on provisions relating to free circulation of goods or services and dominant positions or monopolies. We will then examine how contractual exercise of patents, trademarks or copyrights, by means of licensing agreements, may affect trade or distort competition.

PART ONE : RELIANCE ON INTELLECTUAL PROPERTY RIGHTS IN EXTRA-CONTRACTUAL RELATIONSHIP

Ownership of intellectual property rights are tools which, when placed in the hands of one person or undertaking, may be harmful for free competition. By virtue of the patent, trademark, or copyright he owns, that person is entitled to enforce his rights and oppose infringers. Further, thanks to the legal monopoly intellectual property rights afford to their owner, the latter may attempt to strengthen his position in a market. Such behaviour is not in itself illegal. Nevertheless, European and American competition authorities watch carefully to ensure that such reliance on intellectual property rights does not father antitrust violations. In this respect, two areas appear to be especially sensitive to unilateral conduct. Parallel importations of patented, trademarked, or copyrighted products may be hindered by intellectual property rights owners claiming their rights are infringed. Furthermore, relying on the monopolistic or dominant position they have acquired, intellectual property rights holders may engage in abusive behaviour to extend their monopoly or exclude competitors. We shall therefore compare the respective attitudes of American and European legislators to the question of parallel imports, and toward monopolization or abuse of dominant position.

CHAPTER I : THE QUESTION OF PARALLEL IMPORTS

Parallel imports, or "gray goods" are genuine patented, trademarked or copyrighted products, originally produced in State A, and either exported or authorized to be produced in State B, that are re-imported from B to A[22]. It is important to emphasise that gray goods are not counterfeit products, but genuine articles: the patentee or the trademark holder may have consented to the production of these goods in a foreign country by means of a licence of rights, and the parallel importation is performed by either the licensee or a third party who purchased the goods from the licensee[23].

The questions that European and American antitrust authorities have to answer are whether parallel imports are lawful, and especially whether they can be prevented by the original intellectual property rights owner. The positions adopted by the EEC and the USA, although they may have certain common points, are rather different, the former being much stricter than the latter. Indeed, the whole issue is based on a common notion: the exhaustion of rights. We shall first appraise the origins and areas of application of this principle, then we will review its exceptions.

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22 *"Generally, gray goods are genuinely produced and trademarked goods that are sold outside of their authorized distribution channels"*; Mc Carthy, 2d ed. *Trademarks and Unfair Competition* 1984 at No 30.[35].

23 See generally HAHN, "Gray Market Goods: Has a Resolution Been Found ?" [1991] 81 Tdmk Rep. 58; PALLADINO, "Gray Market Goods: The US Trademark Owners' View" [1989] 79 Tdmk Rep. 158; TAKAMATSU, "Parallel Importation of Trademarked Goods: A Comparative Summary" [1982] 57 Wash. L. Rev. 433.

Section 1 : Exhaustion of Rights

The doctrine of exhaustion provides an answer to the following questions: can an intellectual property rights owner who manufactured goods in a Member State A, then marketed them in a Member State B, prevent the goods marketed in B from being imported into A ? Can an intellectual property rights owner who manufactured and marketed goods in A, but also enjoys legal protection regarding those goods in B, rely on his rights to prevent the marketing of his products in B ? Can the holder of intellectual property rights protecting the goods he manufactured and marketed in A, prevent the importation of similar goods manufactured and marketed (but not covered by any intellectual property right) in B ?[24] In substance, the exhaustion principle prevents a patent, trademark or copyright holder from relying on his rights to prosecute alleged infringers. This may occur after the intellectual property rights owner has sold his products or consented to the exploitation of his rights by another.

> *Sale of it [an article embodying the patented invention]* ***exhausts*** *the monopoly in that article and the patentee may not by virtue of his patent, control the use or disposition of the article*[25].(Emphasis added)

Thus, the first sale of a patented article exhausts the monopoly vested in the patentee, and prevents the latter from exercising his exclusive rights over subsequent users of the article.

This basic definition is common to both US and EEC systems. The European Court of Justice has emphasised that principle in the course of

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[24] See SCHATZ, "The Exhaustion of Patent Rights in the Common Market" [1971] 2 I.I.C. 1.

[25] *US v. Univis Lens* 316 US, 241 [1942].

defining the specific subject-matter of patent rights:

> *The exclusive right to use an invention with a view to manufacturing industrial products and putting them into circulation **for the first time***[26].(Emphasis added)

However, the way the doctrine is applied in the EEC is different from the way it is perceived in the US. It bears emphasis that the origins, as well as the areas and conditions of application of the principle, differ significantly.

A/ Origins of the Principle

The exhaustion of rights doctrine was introduced in the United States in 1873, in *Adams v. Burke*. Burke, an undertaker, purchased patented coffin lids from manufacturers who had been authorized by assignments to make and sell such lids in Boston, and use them outside of Boston. Adams, who had acquired similar rights in all territories outside of Boston, filed suit for infringement against Burke for alleged unauthorized use of coffin lids in Adams' territory. The Supreme Court denied relief to Adams, and set out the following principle with respect to the licensed products:

> *... When they are once lawfully made and sold, there is no restriction on their use to be implied for the benefit of the patentee or his assignees or licensees.*[27]

It was further held in *Keeler v. Standard Folding Bed* that while a patentee may restrict the territory of sale by his licensee to one part of

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[26] *Centrafarm BV v. Sterling Drug* [1974] E.C.R. 1183.

[27] *Adams v. Burke* 84 US, 453 [1873]; see also *Hobbie v. Smith* 2 F. 656 [NDNY 1886]; *Hobbie v. Jennison* 149 US, 365 [1893]; *Edison Electric Light Co. v. Goelet* 65 F. 613 [1894].

the United States, he cannot restrict the territory of resale of the article[28]. It is thus clear that *"the first authorized sale of a patented article in the United States frees the article territorially from the scope of the patent grant, and affords the purchaser the right to use or sell the article anywhere in the United States"*[29].

These cases merely introduced or provided definitions of the exhaustion of rights principle. More important is *Jackson v. Vaughn*, where the theoretical foundation of the doctrine was clearly described[30]. It must be emphasised that in all previous cases, the beneficiaries of the exhaustion of rights were purchasers of the goods, not licensees. This key point should be borne in mind since it will be of crucial importance when we compare US and EEC laws. In *Jackson v. Vaughn*, the facts were similar to those in Adams v. Burke. Jackson, the owner of patents for horse hayforks, licensed Myers & Bros of Ohio exclusively to manufacture and sell the patented articles east of the Rocky Mountains. In return, the licensee agreed it would not permit the goods to be sold west of the Rocky Mountains. A third party, Vaughn, indirectly purchased horse hayforks from Myers & Bros and sold them in San Fransisco. Jackson brought suit against Vaughn, contending that, due to Myers' limited license, Vaughn had acquired no right to sell the patented articles west of the Rocky Mountains. The Court dismissed the suit:

> *The license to Myers & Bros provided that they should not permit the patented hayforks to be sold, directly or indirectly, west of the Rocky Mountains; but Vaughn was*

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28 157 US, 659 [1895].

29 NORDHAUS, *Patent - Antitrust Law* (1972) at 395

30 73 F. 837 [1896].

> *not a party to this licence. He was a perfect stranger to any contractual relation that existed between the patentee and his licensees. It was not binding on him, or on any other purchaser not a party to the contract. It is a rule of the law of contracts, so elementary that it need hardly to be stated, that one not a party to a contract is not bound by it.*[31]

Hence, the exhaustion of rights in US law is justified by the fact that a restriction included in a licence agreement may not be so extended as to impose restrictions upon a third party. We shall see, however, that this rule is subject to many exceptions, especially with respect to trademark rights. Regardless of the territorial limit utilized, it is ineffective to prevent the purchaser of a patented article, acquired from a valid licensee, from using or reselling the article elsewhere. Such a secondary territorial restraint may involve antitrust violations[32].

The exhaustion of rights principle was introduced by the European Court of Justice in 1971[33]. The justifications for it are to be found in one of the major goals of the European Economic Community: the free movement of goods. The EEC faces the task of establishing a common market between

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31 *Ibid* at 843; that reasoning was followed in *US v. General Electric Co.* 272 US, 476 [1926]: *"It is only when he [the patentee]... seeks to control and restrain those to whom he has sold his patented article in their subsequent disposition of what is theirs, that he comes within the operation of the Antitrust Act"*; see also *US v. Standard Sanitary Mfg Co.* 226 US, 20 [1912]; *US v. Motion Picture Patent Co.* 225 F. 800 [DC.PA. 1915]; *Russel v. Tilgham* 275 F. 235 [1921]; *US v. Arnold Schwinn* 338 US, 365 [1967]; *C.A Norgren v. US* 268 F.Supp. 816 [1967].

32 See generally SPIRES, *Doing Business in The United States* (1990) c.10 at 10.07{7}-{c}; and LIPNER, "The Legality of Parallel Imports: Trademarks, Antitrust and Equity" [1984] 19 Tex. Int'l. L. J. 553.

33 In *Deutsche Gramophon v. Metro-SB Grossmarkte* [1971] E.C.R. 487. The sources of that doctrine can be traced to *Consten & Grunding v. Commission* [1966] E.C.R. 229, where the Court drew a distinction between a normal trademark agreement which does not fall within the prohibition set out in article 85-1, and an agreement which amounts to an improper use of intellectual property rights. In *Parke Davis v. Probel* [1968] C.M.L.R. 47, the Court intimated that some similar distinction between the existence and the exercise of rights might be applied to agreements which fell within article 30, and those which fell under article 36. Interestingly, the same reasoning was adopted in the American decision Automatic *Radio v. Hazeltine* 339 US, 827 [1950]. The Supreme Court stated that the mere acquisition of patents was not *per se* illegal, but an improper use of the right might be caught by the antitrust laws. See also *US v. Singer Mfg Co.* 374 US, 174 [1963].

Member States reproducing the conditions of one national market on a community-wide scale. But intellectual property rights are substantially governed by the laws of each Member State[34]. Hence, the owner of an intellectual right in one State may prevent the importation of products lawfully marketed in another Member State by suing for infringement of his right under national law, thereby obstructing the free movement of goods across frontiers. Articles 30 and 34 of the EEC Treaty prohibit measures having effects equivalent to quantitative restrictions on imports and exports between Member States, but their application is limited by article 222 of the Treaty which states "*This treaty shall in no way prejudice the rules of Member States governing systems of property ownership*", and by the first part of article 36 which designates "*...the protection of industrial and commercial property*" as an exception to the application of articles 30 to 34 (it has also been pointed out that articles 30/34 were addressed to States, and were not directly applicable). However, the European Court of Justice has overcome this apparent inviolability of national intellectual property systems, relying in particular on the provision contained in the second part of article 36 which states that the use of intellectual property rights "*shall not, however, constitute a means of arbitrary discrimination or a disguised restriction on trade between Member States*". The Court has introduced fundamental changes in law through the development of the

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[34] There is no real harmonization on a Community-wide scale with respect to intellectual property rights. The existing European Patent Convention facilitates the application procedure by establishing a central European Patent Office (located in Munich). Thus, an applicant is thereby given the possibility to apply for his patent in several Member States, by means of a single application to the European Patent Office. However, if his application succeeds, he will be granted a bundle of national rights. A single patent enforceable throughout the twelve Member States is provided by the Community Patent Convention. However that treaty is not yet, in force for very few States have ratified it. An equivalent convention establishing a single European trademark is presently in the process of being negotiated.

"doctrine of exhaustion", so designed as to prevent intellectual property rights owners from relying on their exclusive rights with a view to impeding the free movement of goods within the common market. The leading case is *Deutsche Gramophon v. Metro-SB Grossmarkte*[35]. Deutsche Gramophon was producing and selling records in Germany under the label "Polydor". Metro, a German supermarket, obtained much cheaper supplies of the same records in France where they were sold by a subsidiary of Deutsche Gramophon. When Metro attempted to import the goods to Germany, Deutsche Gramophon claimed it was an infringement of its rights under the German Copyright Act. The Court held that the derogation from the free movement of goods afforded to industrial and commercial property by article 36 was limited. In particular, it said that article 36 permitted restrictions on the rules provided in articles 30/34 only:

> *"... to the extent to which they are justified for the purpose of safeguarding rights which constitutes the* ***specific subject-matter*** *of such property"*(Emphasis added)

Thus, where restrictions go beyond that limit, they may constitute an exercise of intellectual property rights which is inconsistent with the Treaty. Article 36 protects the existence of such rights, not their exercise. Since Deutsche Gramophon had **consented** to the marketing of its copyrighted products in France, it could no longer rely upon its rights under German law to prevent their importation: by permitting the records to be sold in another Member States, it exhausted its rights[36].

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[35] [1971] E.C.R. 487; See generally ALEXANDER, "Observations sous Deutsche Gramophon v. Metro Grossmarkte" [1971] Cah. Dr. Eur. 594.

[36] The position of copyrights is more complex than any other intellectual property rights because the various laws regarding them in Member States differ significantly in their nature and scope. So the Court has refrained from defining the specific subject-matter of copyrights, but continues to apply the exhaustion principle in copyright cases. See e.g.,

The distinction between the existence and the exercise of intellectual property rights does not exist as such in US law, but the patent misuse theory resembles it closely. It is generally recognized in American law that a valid patent creates a monopoly, and no one should be prevented from obtaining a patent or protecting it by litigation. If, however, it can be shown that the application was made with a view to creating an illegal monopoly or to restraining trade, then such an action can be enjoined[37]. Underlying the patent misuse doctrine, is a policy designed "*to prevent a patentee from projecting the economic effects of his admittedly valid grant beyond the limits of his legal monopoly*"[38]. If the misuse of a patent is an unfair method of competition, the Federal Trade Commission can issue a cease and desist order under sections 5{a} and 6 of the Federal Trade Commission Act. It was established in *Coca-Cola Co. v. Howard Johnson Co.* that the same reasoning, whether founded on a violation of antitrust or other law, could be raised in trademark matters[39].

Therefore, although the definition of the exhaustion doctrine is identical under US and EEC laws, one must not be misled by that

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Musik-Vertrieb v. GEMA [1981] E.C.R. 147; *Dansk Supermarked v. Imerco* [1981] E.C.R. 181; *EMI v. Patricia.IM Export* [1989] E.C.R. 79.

37 See generally *Clinton Engineers Corp. v. Briggs & Sratton Corp.* 175 F.Supp. 390 [1959]; It must be emphasised, however, that misuse of a patent does not necessarily constitute a violation of the antitrust laws. The Supreme Court held in *Walker Process Equipment Inc. v. Food Machinery & Chemical Corp.* 382 US, 172 [1965], that a patent monopoly and a Sherman Act monopolization were different in nature . A particular patent may be so weak that, economically speaking, there is no monopolistic market position. Often, a patent will only give the patentee very limited market power and it will by no means create a monopoly in an economic sense. The patent may have to compete on a market with many other inventions which serve the same purpose, and a monopoly cannot be said to exist. See generally LAVEY, "Patents, Copyrights and Trademarks as Sources of Market Power in Antitrust Cases" [1982] 27 Antitrust Bull. 433; and FEJO, *Monopoly Law and Market* (1990) c.10 at 312.

38 Callman, *Trademarks, Unfair Competition and Monopolies* (1984) c.4 at 60. See also *Panther Pumps & Equipment Co. v. Hydrocraft Co.* 468 F.2d, 225 [CA 7th. 1972].

39 386 F.Supp. 330 [DCND 1974].

similarity. Since the objectives of the systems are different, it is not surprising to witness a great divergence in the way the principle is applied.

B/ Areas and Conditions of Application

Shortly after the *Deutsche Gramophon* decision, the question arose whether the doctrine of exhaustion was limited to copyrights. In subsequent cases, the European Court of Justice extended the application of the principle to other intellectual property rights. In *Centrafarm BV v. Sterling Drug*, Centrafarm had purchased a drug ("Negram") in the United Kingdom and exported it to the Netherlands[40]. Sterling Drug, which held patent rights for the drug in both countries, brought an action against Centrafarm to prevent it from selling the product in the Netherlands. The Court repeated the view expressed in *Deutsche Gramophon*, namely that article 36 permitted derogations from the free movement of goods provisions only to the extent that it was necessary to protect the specific subject-matter of the right which, in the case of a patent, was:

> *The exclusive right to use an invention with a view to manufacturing industrial products and putting them into circulation* ***for the first time,*** *either directly or by the grant of licences to third parties, as well as the right to oppose infringements.* (Emphasis added)

The Court went on to say that it might be legitimate to invoke a patent right to prevent imports of a product from a Member State where it was not patentable, and had been produced by a third party without the patentee's consent. In 1968, three years before the Court articulated the exhaustion principle, it held in *Parke Davis v. Probel* that the owner of a

40 [1974] E.C.R. 1183.

patent in one country within the EEC may enforce its national patent right so as to prevent the import to that country of goods manufactured by a third party in another Member State where patent protection is not available[41]. However, a derogation from the free movement of goods provisions is not justified where the product has been put onto the market in a legal manner by the patentee or with his consent, in the Member State from which it has been imported. Therefore, Sterling Drug could not rely on its Dutch patent because the drug had been marketed in the United Kingdom with its consent by its licensee[42]. Thus, the Court laid down a Community notion of exhaustion of patent rights. The patentee is entitled to try to earn a monopoly profit at the point at which goods were first put onto the market, but after having done so he loses any right to control their further movement[43]. In *Centrafarm BV v. Winthrop*, the facts were similar to those in *Centrafarm v. Sterling Drug*, and the Court adopted the same reasoning it followed in its *Deutsche Gramophon* judgment. In that case, the Court defined the specific subject-matter of a trademark as:

> *The guarantee that the owner of the trademark has the exclusive right to use it, for the purpose of putting products protected by the mark into circulation for the first time.*[44]

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[41] [1968] E.C.R. 47.

[42] See generally on this case DEMARET, "Le Brevet Communautaire après Centrafarm: un Instrument Dépassé ou Inachevé?" [1977] R.T.D.E. 1; and WEGNER & MULLER, "Negram: the Common Market - Wide Exhaustion of Patent Rights Through Territorial Licences" [1975] 57 J.P.O.S. 46.

[43] See also *Allen & Hanbury v. Generics* [1988] E.C.R. 1245; and more generally JOLIET, "Patented Articles and the Free Movement of Goods Within the EEC" [1975] 28 Current Legal Problems. 15.

[44] [1974] 2 C.M.L.R. 480; *Sterling Drug* and *Winthrop* differ materially on their facts from *Deutsche Gramophon* in only two respects. First, the product in question was here manufactured in a Member State other than that in which the opposition to its importation arose, and secondly its importation into that second State was in fact opposed by a subsidiary of the manufacturer rather than by the manufacturer itself.

Thus, Winthrop could not exercise its rights under its Dutch trademark to prevent the import of drugs from the United Kingdom which had been marketed there by another company belonging to the same group. In transferring the power to market the product to a subsidiary, the right has been exhausted.

In *Hoffman-La-Roche & Co.AG v. Centrafarm BV*, Centrafarm purchased drugs from La-Roche Britain (a subsidiary of the Swiss parent Hoffman-La-Roche), re-packaged the drugs in the Netherlands (to comply with German packaging legal requirements), and sold them to its subsidiary in Germany[45]. However, Centrafarm left the brand "La-Roche" on the new packages, as well as its own mark and the words "Marketed by Centrafarm GmbH". La-Roche Germany brought an action with a view to preventing Centrafarm Gmbh from marketing the drugs in Germany. Thus, the Court had to answer the question whether the rights which constitute the specific subject-matter of a trademark included the right to prevent a trademark from being affixed to products by a third party. The Court broadened the scope of trademarks' specific subject-matter, which is now not only the right to be the first to place a product on the market bearing a specific mark and the right to restrain third parties from affixing that mark without authorization, but also the right to prevent any use of a trademark by a third party which may undermine the guarantee of origin provided by a mark. From that standpoint, the issue before the Court became whether the exercise of a trademark owner's right amounted to a disguised restriction on trade between Member States. Indeed, such a restriction might arise if the trademark owner were to enforce his rights

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[45] [1978] E.C.R. 1139.

to prevent re-packaging by a third party, even if the operation was carried out in such way that it could neither affect the original condition of the product nor its identity of origin. The Court concluded that, in the present case, those characters were not affected since it was stated on the new packages by whom the re-packaging had been done. Therefore the reliance on a trademark right would artificially partition the market[46].

From those decisions it can be concluded that the exhaustion doctrine, as applied in the EEC, rests on two important principles: on the one hand, it is based on the consent of the owner of intellectual property rights to have his rights manufactured or marketed by someone else, in which case they are exhausted. On the other hand, since a distinction is made between the existence and the exercise of the rights, it is grounded on the specific subject-matter of each of these rights. Any exercise of intellectual property rights that would undermine that subject-matter is generally considered to be a violation of the free movement of goods provisions of the EEC Treaty. With respect to the question of whether the patentee or trademark owner has consented to have his rights exploited by another, US law is in accord with European authorities. Thus, in *Hogue & Berrien County Package v. Wise*, it was said that "*the purchaser of patented articles from one* ***authorized*** *to sell becomes possessed of an absolute property in such articles, unrestricted in time or place*" (emphasis added)[47]. As to the specific subject-matter of intellectual property rights,

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[46] See also *Centrafarm v. American Home Products* [1978] E.C.R. 1823.

[47] *Hogue & Berrien County Package v. Wise* 35 U.S.P.Q. 72 [1933]; see also *Sheila's Shine Prod. v. Shiela Shine Inc.* 486 F.2d, 114 [5th Cir. 1973], where the acquiescence of the trademark owner in the defendant's use of the mark constituted a defense to an infringement action; and NORDHAUS, supra note 29 at 395: "*The first* ***authorized*** *sale of a patented article in the United States frees the article territorially from the scope of the patent grant...*"

it seems that US courts do not apply this test with the same stringency. Nevertheless, as stated earlier, they condemn disproportionate exercise or misuse of rights.

> *Under the patent law the patentee is given by statute a monopoly of making, using and selling the patented article... As long as he makes no effort to fasten upon ownership of the article he sells no control of the prices at which his purchasers shall sell, it makes no difference how widespread his monopoly. It is only when he adopts a combination with others, by which he steps out of the scope of his patent right and seeks to control and restrain those to whom he has sold his patented articles in their subsequent use of what is theirs, that he comes within the operation of the Antitrust Act.*[48]

Thus, the privileges afforded to a patentee are limited by the statutory definition of the patent monopoly.

However, the scope of application of the exhaustion principle is much broader in EEC law than in the USA. The foundation of US exhaustion doctrine is that a contract does not bind third parties. Thus, it is only the latter who may benefit from the exhaustion of rights.

> *The purchaser of the patented article, having acquired it in either cases legally, acquires also with the purchase the privilege of using it or reselling it again in all parts of the United States. The argument that in the enforcement of this doctrine the inventor in a case like this may lose the exclusive benefit conferred upon him under the patent laws is answered by the fact that he may protect himself by special contract limiting the use of the patented article to those to whom he sells or grant territorial rights.*[49]

Under US antitrust law, a territorial restriction clause imposed on a licensee by a licensor is generally valid, as we shall see further. In other

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48 *US v. General Electric Co.* 272 US, 476 [1926].

49 *Russel v. Tilgham* 275 F. 235 [1921].

words, a licensor can lawfully restrict the activities of his licensee as to the use or sale of the licensed products. The licensee may not invoke the exhaustion of his licensor's rights and then import gray goods from one state into another. Thus, in *Security Materials Co. v. Mixermobile Co.*, the exclusive licensee for Southern California under a patent covering a mobile cement mixer (Mixermobile) brought an infringement suit against the defendants who were licensed to sell the patented machine throughout the United States, except Southern California, for using and selling Mixermobile in that state. The defendants replied that they were entitled to do so because the machines *"had passed without the limits of the patent monopoly"* after the first sale. The Court disagreed:

> *If defendants... should sell a Mixermobile free of restrictions to an ordinary purchaser in the territory covered by the licence, the machine would pass "without the limit of the monopoly". But that is not the kind of sale involved... Both defendants procured the machines in question as licensees under their licence. In their hands then, the machines remain subject to the patent monopoly, hence to the licensing agreement thereunder... Any sale or use in this territory by another licensee constitutes an infringement of that portion of the patent monopoly...*[50]

Acting as licensees, the defendants could not rely on an exhaustion of rights. Only purchasers are entitled to do so.

Under EEC law restriction clauses are *per se* unlawful and anti-competitive, although many exemptions have been granted by the Commission of the European Communities[51]. It is thus sometimes possible for a licensee, under certain circumstances, to invoke the exhaustion of

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[50] 72 F.Supp. 450 [SD Cal. 1947].

[51] See Part II, c.2.

rights principle[52]. Moreover, a licence clause which, directly or indirectly, prevents parallel imports between Member States is void and unenforceable[53].

Thus, a major difference in the scope of application of the exhaustion principle between the United States and the European Community is that it is only subsequent purchasers of a patented, trademarked or copyrighted article who may rely on this doctrine under US law. Both third parties and licensees may invoke it under EEC law. Further, unlike the European Court of Justice which applies the exhaustion principle to patents, trademarks and copyrights equally, US courts are less severe with certain intellectual property rights than others. For instance, the principle enunciated in *Jackson v. Vaughn*, according to which a restriction between a licensor and a licensee does not bind a third party, has been overruled in certain trademark cases. In *Jur-Amsco Co. v. Janrus Camera Inc.*, an exclusive American distributor for the German made GRUNDIG dictating and transcribing machines had created a domestic market for improved German trademarked machines. The distributor sought a temporary injunction against a third party who was selling inferior but genuine GRUNDIG machines. The Court granted the injunction *"on the basis of interference with the plaintiff's property rights"*, and further held that a contract:

> *... not only binds the parties to it by the obligation entered into, but also imposes on all the world the duty of respecting that contractual*

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[52] See *Centrafarm v. Sterling Drug* [1974] E.C.R. 1183 and *Centrafarm v. Winthrop* [1974] 2 C.M.L.R. 480.

[53] See EC Commission's Regulation 2349/84 on Patent Licences, or Regulation 1983/83 on Exclusive Distribution Agreements, see infra note 181.

obligation.[54]

Such a position is justified by the fact that, under US law, trademarks carry no monopoly, or more precisely do not monopolize the product itself. *"The patent is a monopoly, the trademark is not"*[55]. Therefore, US exhaustion doctrine is not absolute in its application. Under EEC law too, the principle allows certain exceptions.

Section 2 : Exceptions to the Exhaustion Doctrine

A/ Lack of Consent

An important factor in determining the application of the exhaustion principle is the consent of the intellectual property rights owner to have his rights exploited or his products marketed by another. Therefore, if it is established that he did not consent, he should not suffer an exhaustion of his rights. For instance, the US Trade and Competitiveness Act of 1988, amending the patent laws, provides that the owner of a process patent has the right to exclude other firms from using or selling throughout the United States or from importing products made by that process. Anyone who sells or uses in the USA, or **without authority** imports into the USA, a product made by a US patented process is liable as an infringer[56]. According to Wilbur Fulgate, those provisions initially designed to keep out imports of products made abroad also encompasses the sale or use of

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[54] 155 NYS 2d, 123 [1956]; see also *Metropolitan Opera Ass'n Inc. v. Wagner Nichols Recorder Corp.* 101 NYS.2d, 483 [1950]; *Revlon Inc. v. Crest Distributors Inc.* 190 NYS 2d, 745 [1959]; *Second Nat.Bank v. Samual & Son Inc.* 12 F2d, 963 [1926].

[55] CALLMAN supra note 5, part 1, c.4 at 9; see also FULGATE, 4th ed. *Foreign Commerce and the Antitrust Laws*" (1989) at 99. See infra note 186.

[56] 35 USC. 271 (1988).

products made in the United States[57].

Another relevant situation is where a **compulsory licence** is granted. It would hardly make sense to say that the patentee has agreed to the license. Compulsory licences are awarded where a patentee is not using or exploiting his right during a certain time. In exchange for the monopoly he is given, the inventor is expected to work his patent to make it available to the public. If non-use of the right is not justified, a compulsory licence may be granted to a third party, in exchange for a fair royalty. However, under US law, patentees are not obliged to exploit their inventions. Where US courts grant compulsory licences, they do not rely on a statutory obligation, but rather on equity. For instance, compulsory patent licenses are a long recognized penalty for patent antitrust violations[58]. In *Pharmon v. Hoechst*, the European Court of Justice emphasized that compulsory licences constituted exceptions to the application of the doctrine of exhaustion[59].

There is another kind of situation in which the exhaustion doctrine cannot apply. That is where two or more undertakings own an intellectual property right which, at an earlier date, belonged to a single enterprise. To prevent intellectual property from being exercised in such ways as to impede parallel imports, the European Court of Justice set out a **doctrine of "common origin"**. By definition, a "common origin" situation arises where

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[57] FULGATE, supra note 55 at No 8.10.

[58] See *Besser Co. v. US* 343 US, 444 [1952]; *Henry v. A.B Dick Co.* 224 US, 1 [1911]. On the question of compulsory licenses, see generally CANTOR, "Evolution Toward Compulsory Licensing ?" [1953] 35 J.P.O.S. 372; CHAVANNE & BURST, *Droit de la Propriété Industrielle* (1990) at 246-249. Under US law, compulsory licensing may also be decreed when a patent concerning atomic energy is intentionally used to violate antitrust laws (Atomic Energy Act 42 USC, s.2183 [1954]).

[59] [1985] E.C.R. 2281; In US law see *US. v. Gypsum Co.* 340 US, 76 [1950]; *American Cyanamid Co. v. Fed. Trade Comm.* 363 US, 757 [CA 6th. 1966].

an owner of intellectual property has voluntarily assigned a partial interest in his original rights or where there is some form of forced divestiture of a part of such right (e.g expropriation). Here again it will be easier to understand the theory by referring to the case in which it was announced. It is important to underline that the common origin doctrine was created for the specific purpose of the *HAG case No 1*, and that the Court abandoned that position in the *HAG case No 2.*

In *HAG No 1* HAG AG was a German coffee producing company which owned the trademark "HAG" in Germany, Luxembourg, and Belgium[60]. In 1927, it created a subsidiary in Belgium, Café HAG S.A (HAG Belgium), and transferred its "HAG" trademarks in Belgium and Luxembourg to that subsidiary. After World War II, the shares in HAG Belgium were sequestrated as enemy property and sold to the VAN OEVELEN family. In 1971, HAG Belgium transferred its trademark in Belgium and Luxembourg to another company, VAN ZUYLEN FRERES. In 1972, the original German company, HAG AG, which shortly after the war had registered its trademark in Belgium and Luxembourg, began delivering its coffees to Luxembourg retailers under the German trademark "HAG". Van Zuylen Frères instituted an action before a Luxembourg tribunal (which referred it to the European Court of Justice under article 177 proceedings) for trademark infringement and for cancellation of the Belgian and Luxembourg registrations made by HAG AG. The question for the Court was whether Van Zuylen (HAG Belgium) could prevent HAG AG from importing coffee to Luxembourg or Belgium without Van Zuylen's authorization. It held:

> *It cannot be accepted that the exclusiveness of*

60 *Van Zuylen Frères v. HAG AG* [1974] E.C.R. 731.

> *the trademark right, which can be the consequence of the territorial limits of the national laws, should be relied on by the holder of a trademark with a view to prohibiting trading, in one Member State, of goods lawfully produced in another Member State under identical mark which has the same origin.*[61]

Thus, it seems to be immaterial whether the division of intellectual property ownership resulted from voluntary assignment or forced divestiture. The material consideration is that intellectual property owned by two undertakings was, at some earlier stage, held by a single undertaking and therefore may be traced back to a common origin. This condition is sufficient to prevent a trademark holder from relying on his rights to stop direct imports from another Member State, notwithstanding his lack of consent. Indeed, the notion of consent is irrelevant in the common origin principle, and the *HAG* case has been criticized on this latter point[62].

It has also been observed that, when considering possible confusion with respect to coffee products in consumers' minds which could result from its decision, the Court concluded that consumers could be informed of the origin of trademarked products by other means such as labelling, but it neglected the fact that consumers might be misled as to the origin of two products bearing the same mark but manufactured by independent companies. An example would be the case of telephoned orders[63].

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61 *Ibid* at 735.

62 MANN, "Industrial Property and the EEC Treaty" [1975] 24 I.C.L.Q. 31. This author was so outraged by the judgment that he advised national courts to stop referring questions on intellectual property to the European Court of Justice.

63 See D.GUY & G.LEIGH, *The EEC and Intellectual Property* (1981) at 223. The Court hinted that if the indication of origin of a trademarked product is useful, consumers may be informed by means other than those which affect the free movement of goods. But the indication of origin given by a trademark is primarily concerned with identifying the party responsible for the product. HAG has been criticized on the ground that it might result in

After the HAG case, the question arose whether the common origin doctrine was likely to be applied to other intellectual property rights. It was held that trademarks were distinguishable from other intellectual property in that the length of protection afforded is indefinite and, as such, trademarks can have much more serious and lasting effects in dividing national markets. In consequence, trademarks are entitled to less protection than other intellectual property rights[64]. For those reasons the common origin doctrine should not apply to all intellectual rights. That view was sustained in the *Coditel* case, where the defendants raised the argument that the performing rights involved had a common origin[65]. The Court rejected that claim, relying on the specific purpose of such rights - namely the right of the owner to require fees for each performance of a film - precisely because he receives royalties based on performances rather than royalties based on initial sales of tangible objects, and held that the assignment of performing rights was governed by articles 59/60 rather than 30/36. The common origin principle was unlikely to apply to such assignments[66].

One must also take into account the fact that the doctrine was not

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a purchaser being faced with a choice between identical packages carrying identical characteristics and that it will be difficult to prevent the "trespasser" from getting a free-ride on the goodwill of the lawful trademark owner in the country concerned. See HAWK, 2d ed. *United States, Common Market, and International Antitrust: A Comparative Guide*" (1986 and suppl.) at 589; and DAVIS, "The EEC and Transfer of Technology" [1977] 59 J. Pat. Off. 424.

64 See BEHRINGER & SCAGNELLI, "Global Competition: The Role of Intellectual Property" [1989] 79 Trademark Reporter 78.

65 See infra note 74 and accompanying text.

66 The Court's decision in *EMI Records Ltd v. CBS Records Ltd* [1976] E.C.R. 811 is relevant in this context too, since the doctrine of common origin is only to be applied as between Member States and shall not be invoked as between a Member State and a non Member State.

to apply where there was no common origin at all. In *Terrapin Ltd v. Terranova Industries*[67], a German company, Terranova, which manufactured and marketed prepared plaster for facades, owned the "TERRA", "TERRANOVA", and "TERRAFABRIKATE" trademarks in Germany. Terrapin Ltd, an English manufacturer, attempted to sell prefabricated houses (which it already marketed in the United Kingdom) in Germany, and sought to register its trademark "TERRAPIN" in the German Registrar. Because of opposition proceedings instituted by Terranova, the application failed. But Terrapin started to market its products under its mark in Germany, notwithstanding its failure to obtain registration of "TERRAPIN" in that country. Much litigation between the two companies followed, until the Court ruled that :

> *It is compatible with the provisions relating to the free movement of goods that an undertaking established in a Member State A, by using its...trademark rights existing there, prevent the import of similar goods from an undertaking established in a Member State B, if these goods have been lawfully given a distinguishing name which may be confused with the trademark which is protected in State A for the undertaking established there, if their national trademark rights arose autonomously and independently of one another...*[68]

Hence, the common origin doctrine does not apply where similar marks were created separately.

Interestingly, in *Terrapin v. Terranova* as well as in the *HAG* case, the issue of similarity of trademarks, and the consequent risk of confusion for the consumer was raised, but not sustained by the Court. In the *HAG case No 2*, where the Court reversed its previous jurisprudence and gave

67 [1976] 2 C.M.L.R. 482.

68 *Ibid* at 484.

up the common origin doctrine, it considered the question of misleading consumers as relevant.

In the *HAG case No 2* the parties involved were still HAG AG (Germany) and HAG Belgium, but Van Zuylen Frères had been purchased in 1979 by a Swiss company, Jacob Suchard S.A, which consequently acquired the Belgian "HAG" trademark[69]. The fact were also similar to those litigated in 1974 (HAG No 1), but in a reverse order. Sucal began to supply the German market with decaffeinated coffee under its trademark. HAG Germany applied to its national courts to prevent the importation of goods which would infringe its trademark. Sucal raised the defence of common origin, relying on the first *HAG* case, but HAG AG presented a further argument: "KAFFE HAG" had acquired the status of a famous brand in Germany, and the German coffee was superior in quality to the Belgian one thanks to a new manufacturing process. Hence, a similarity of trademarks would confuse consumers as to the quality of the product. In article 177 proceedings, the Court took that risk into account and reversed the judgment it rendered in *HAG No 1*:

> *Where the mark originally had one owner, but where that single ownership ended as a result of an expropriation, each of the owners of the trademark right must be able to prevent the importation and marketing, in the Member State where the mark belongs to him, of products originating from the other owner, if they are similar products bearing an identical mark which may cause confusion.*[70]

Such behaviour would not be inconsistent with the free movement of goods provisions as set out in the Treaty. It took sixteen years for the Court to

69 *S.A CNL-Sucal v. HAG AG* [1990] 3 C.M.L.R. 571.

70 *Ibid* at 576.

recognize that the reasoning it adopted in *HAG No 1* amounted to ignoring the distinction between the existence and the exercise of intellectual property rights. As emphasised in the *Deutsche Gramophon* case, that basic distinction is a fundamental element of analysis when deciding whether an intellectual right owner is overcoming his legitimate privileges, and thus infringes articles 30/36 by hindering parallel imports. Nevertheless, the common origin principle has only been applied in one case, and it seems that as far as the relationship between an intellectual property rights holder and third parties having effects on the free movement of goods policy of the Community is concerned, the matter is to be settled by the exhaustion principle[71].

Whereas under EEC law exceptions to the principle are limited, the US exhaustion doctrine admits so many exceptions that it is no longer a principle, but rather an exception itself. We saw in *De-Jur Amsco Co. v. Janrus Camera* that courts do not hesitate to set aside the exhaustion theory to afford greater protection to intellectual property rights holders and even to consumers. A parallel may be drawn between *HAG No 2* and *De-Jur Amsco*: in both cases, it was thought that effective protection of trademark rights would directly afford greater protection to consumers, by avoiding potential misleading or confusion in public's mind[72].

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[71] For an illustration of the difficulties encountered in the USA when dealing with trademarks in divestiture situations, see *Philip Morris Inc v. Imperial Tobacco Co.* 401 F.2d, 179 [4th Cir. 1968].

[72] See *Independent Baking Powder Co. v. Borman* 130 F. 726 [1904]:"*... by granting such protection, the law enables the public to exercise a free choice between two products, and dictates that competing products be sold without deception as to their source of production and manufacture*". See also *California Packing Corp. v. Sun Maid Raisin Growers of California* 273 F.2d, 282 [CA 9th. 1959].

B/ Performing Rights

European law is not as flexible as American law, and is very cautious as to the exemptions it provides because the exhaustion of rights is an effective means to achieve the Common Market. Nevertheless, the European Court of Justice is aware of the fact that intellectual property rights need protection, and that this protection may sometimes be inconsistent with the logic of the exhaustion principle. Such is the case with performing rights. They can be defined as rights to perform, display, transmit or otherwise communicate a work in which a copyright is vested (literary, dramatic, musical, or artistic works). Performance includes speeches, plays, and any mode of visual or acoustic presentation including presentation by means of a sound recording, film, broadcast or cable programme[73]. The European Court of Justice recognized in *Coditel v. Ciné Vog Films* that there was a factual difference between performing rights as an element of copyrights, and copyrights in literary and artistic works such as books or records[74]. Ciné Vog was the exclusive licensee in Belgium of the copyright vested in a French movie. It brought an action to prevent a cable company, which picked up a transmission of the film in Germany, from showing it in Belgium. According to the doctrine of exhaustion, the right could be said to be exhausted since the film had been broadcasted in Germany with the copyright owner's consent. But the Court held that the broadcasting of a film by television involved the provision of a service, and was therefore covered by articles 59 and 60 of the Treaty rather than articles 30 to 36.

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[73] See generally CORNISH, *Intellectual Property: Patents, Trademarks, Copyrights and Allied Rights* (1989); BROWN, *Copyrights, Unfair Competition and other Topics Bearing on the Protection of Literary, Musical and Artistic Works* (1970).

[74] [1982] E.C.R. 3381.

The exhaustion principle therefore could not apply to such broadcasting, having regard to the particular way in which a movie is made available to the public, namely by performance. It had also been thought for some time that industrial designs were beyond the scope of the exhaustion of rights, but the Court included them in *Keurkoop v. Nancy Kean Gifts*[75].

C/ Foreign Countries

Further, it must be borne in mind that the exhaustion doctrine is intended to implement articles 30 to 36 of the Treaty, which prohibit only quantitative restrictions or measures having equivalent effect between Member States. Therefore, a situation involving at least one non Member State is *prima facie* not subject to an exhaustion of rights. In *EMI Records Ltd v. CBS United Kingdom Ltd*, the "Columbia" trademark in the USA was owned by CBS Inc., while the "Columbia" trademarks in all EEC Member States were held by members of the EMI group[76]. EMI Records Ltd manufactured records in the United Kingdom under the label "Columbia", and other "Columbia" marked records were manufactured by other EMI subsidiaries in most of the EEC Member States. CBS manufactured records in the USA and elsewhere under the "Columbia" trademark, and a proportion of these records were sold within the EEC, the brand "Columbia" being obliterated or concealed. EMI Records Ltd instituted parallel proceedings against the English, German and Danish subsidiaries of CBS Inc. The Court was asked whether the free movement of goods provisions prevented EMI from exercising its trademark rights under

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75 [1982] E.C.R. 2853; However, for the same reason as with copyrights (see supra note 36), the Court refrained for a long time from defining the specific subject-matter of these intellectual property rights. It eventually did in the recent *Renault* and *Volvo* cases. See infra note 131 and accompanying text.

76 [1976] E.C.R. 811.

national laws in the relevant Member States so as to prevent CBS from selling in those Member States goods bearing the mark "Columbia". The Court replied categorically that EMI could enforce its rights against foreign imports. Thus, a trademark owner is entitled to exercise its intellectual property rights in such a manner as to restrain either the importation of products under the same mark from outside the Community, or the manufacture and marketing of products with the same mark in the EEC by a proprietor of the mark outside the Common Market[77].

There is a similar principle in the United States, although it is subject to much more controversy. Section 42 of the Trademark Act of 1946 (The Lanham Act) bars entry to US customs of foreign imported merchandise *"which shall copy or simulate"* the name or registered trademark of a domestic manufacturer or trader[78]. The application of that provision to spurious or counterfeit marks raises no legal issues. However, there is a long history and controversy with regard to the application of section 42 of the Lanham Act, together with sections 526 and 337 of the Tariff Act of 1930, in keeping out "genuine" merchandise[79].

Apollinaris Co.Ltd v. Scherer, a 1886 lower court decision which dealt with the importation of gray goods from abroad, was an influential decision for over four decades. That case involved an exclusive distributorship

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[77] See ALEXANDER, "Observations sous EMI Records Ltd v. CBS UK Ltd" [1976] Cah. Dr. Eur. 116; and HAY & OLDEKOP, "EMI/CBS and The Rest of The World: Trademark Rights and The European Communities" [1977] 25 Am. J. Comp. L. 120.

[78] 15 USC. 1124.

[79] On this topic, see HAWK, *United States, Common Market and International Antitrust : A Comparative Guide* (1986 and 1991 Suppl.) at 423; FULGATE, *Foreign Commerce and the Antitrust Laws* (1989) c.8 at 19, 35, 109; DAM, "Droit Antitrust et Distribution de Produits de Marques" in *Brevets et Marques au Regard du Droit de la Concurrence en Europe et aux États-Unis* (1968) at 189.

system of mineral water in the US. The defendant purchased genuine water in Germany, imported it into the United States, and sold it under the same trademark at prices lower than those of the plaintiff. The latter sought a preliminary injunction to prevent the defendant's importation or sale of the water, based on a trademark infringement action. The Court held: *"The defendant is selling the genuine water, and therefore the trademark is not infringed... the law of trademark cannot be invoked"*.[80]

Bourjois & Co. v. Katzel presented a similar situation that evoked a special solution both by the courts and Congress[81]. The plaintiff, a US company, purchased the US business of a French cosmetic manufacturer, including the trademarks "BOURJOIS" and "JAVA" used on its face powder. The US company continued to import the same powder and to sell it in boxes substantially similar to those used by the French manufacturer. The plaintiff brought an action for an injunction to restrain the defendant from infringing its marks by importing the same genuine product from the French manufacturer and selling it in the USA in boxes resembling plaintiff's. The District Court held for plaintiff, emphasising that the plaintiff could have sold any other powder under its trademark and that the public regarded the product as coming from the US company, not the French company. The Court of Appeal reversed, reasoning that the defendant did not copy or simulate the plaintiff's goods, and that *"if the goods sold are the genuine goods covered by the trademark, the rights of the owner of the trademark are not infringed"*[82]. The Supreme Court

[80] 27 F. 18 [1886].

[81] 260 US, 689 [1923].

[82] 275 F. 239 [2nd Cir. 1921].

agreed with the District Court, stating that the trademark indicated *"that the goods came from the plaintiff although not made by it... It stakes the reputation of the plaintiff upon the character of the goods"*[83].

Between the Court of Appeal's and the Supreme Court's *Bourjois v. Katzel* decisions, Congress enacted what is now section 526 of the Tariff Act of 1930, which provides that it shall be unlawful to import into the United States merchandise of foreign manufacture bearing a trademark owned by a US citizen, association, or corporation if the trademark is properly registered in the Patent Office and with the Secretary of Treasury, in the absence of a written consent to such importation by the trademark owner. Section 526 was intended to protect US trademark owners from fraud against them by foreign assignors of a business, but it has been used as a tool to protect foreign manufacturers in maintaining an exclusive US distribution system and a higher price for their goods in the US market[84].

The next significant American case involving parallel imports was *US v. Guerlain*[85]. The government instituted civil actions against three corporations contending that their use of section 526 to prevent importation of genuine perfume bearing their registered trademark had excluded potential competitors from dealing in these goods and violated

83 260 US, 692 [1923]; In *Bourjois v. Aldridge* 263 US, 675 [1923], the Supreme Court held, that on the authority of *Katzel*, the Collector of Customs was required to stop at customs the genuine face powder bearing the infringing trademarks.

84 See generally FULGATE, supra note 55 at 111; see also *Original Applachian Artworks Inc. v. Granada Elec. Inc.* SDNY.640 F.Supp. 928 [1986]; *W.Goebel Porzellanfabrik v. Action Industries* SDNY. 589 F.Supp. 763 [1984].

85 SDNY 155 F.Supp. 77 [1957]; see also *Ercona Camera Corp. v. Bromwell* 246 F.2d, 675 [1957].

section 2 of the Sherman Act. The court held that each US defendant was *"part of a single international business enterprise with a foreign company"* and therefore each was prohibited from utilizing section 526, which was limited to independent US trademark owners. The court also found that unlike the trademark in *Katzel*, which had truly indicated the domestic origin of the goods, the trademark under consideration indicated that the goods originated in France *"inasmuch as the whole burden of defendant's advertising was to emphasise French origin."*[86] Thus, a US owner of a US trademark can license an independent foreign company to use it and keep out foreign imports with such a trademark under section 526.

The US trademark holder may also invoke section 337 of the Tariff Act of 1930, as amended in 1988[87]. Section 337 declares to be unlawful unfair methods of competition and unfair acts in the importation of products in the United States or their sale, which would *"destroy or substantially injure"* a US industry, or prevent its establishment, or *"restrain or monopolize trade and commerce in the US"*[88]. In the *Duracell* case, it was decided that section 337 was violated by imports and distributors who bought foreign-manufactured Duracell batteries on the

86 See also *K-Mart v. Cartier* 486 US, 281 [1988]; *NEC Electronics v. Cal.Circuit ABCO* 810 F.2d, 1506 [9th Cir. 1987]; *Vivitar Corp. v. US* 761 F.2d, 1552 [Fed.Cir. 1985]; *Olympus Corp. v. US* 792 F.2d, 315 [2nd Cir. 1986].

87 19 USC. 1337 (1988).

88 Prior to the 1988 amendments, the statute specified that an American industry had to be *"efficiently and economically operated"*. This is no longer required. As amended, section 337 has particular provisions dealing with intellectual property; the importation and sale within the US of articles that infringe a US patent or copyright, articles that are made under a process patented in the US, articles that infringe a registered trademark, or a semiconductor chip product that infringes a registered mask work are unlawful if an industry relating to the article exists.

European market and imported them into the USA[89].

Hence, both EEC and US law allows parallel imports from non-Member States and foreign countries to be prevented, either by recourse to national intellectual property laws, or customs regulations. But as far as parallel importation between EEC Member States or American States is concerned, policies diverge. Within the EEC, a strict application of the exhaustion doctrine ensures that parallel imports are not prevented. There are nevertheless few exceptions that allow intellectual property rights owners to rely on their rights to prosecute infringers, even if that may slightly affect the free movement of goods within the Community. Such exemptions to article 36 of the EEC Treaty are justified by the need to afford sufficient protection to innovators. There is no equivalent to articles 30 and 36 in US law. The exhaustion of rights principle is therefore not applied with the same stringency. Although the case law seems to be respectful of the principle with respect to patent rights[90], the doctrine of exhaustion has become an exception with regard to other intellectual property rights. But it does not mean that a patentee, or a trademark or copyright owner is free to rely on his rights and affect or

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[89] *In Re Certain Alkaline Batteries* [US ITC, 1984] 1 Int'l. Trade Rep. No 9 at 239. President Reagan, exercising his veto power, disapproved of that decision. According to HAWK, supra note 63 at No 452-2, the *Duracell* decision is noteworthy because the views expressed by the majority and the minority of the commissioners only diverged on the interests to be protected - those of the trademark owners and those of the consuming public. But it was unanimously recognized that section 337 had been violated. See generally on this topic BRUNSWOLD, "Section 337 of US Tariff Act: A Revised Weapon Against Foreign Patent Infringement" [1979] 10 I.I.C. 52.

[90] See *US v. National Lead Co.* SDNY 63 F.Supp. 513 [1945]. However, the exhaustion of rights is not applied to field of use restrictions which follows the patented article into the hands of a purchaser who knew of the license restriction and chose nevertheless to use the article outside the licensed field. See *General Talking Pictures Co. v. Western Elec.Co.* 304 US, 175 [1938]; also *De Forest Radio Tel.& Tel.Co. v. US* 273 US, 236 [1927]; *Chemagro Corp. v. Universal Chemical Co.* 244 F.Supp. 486 [DCED Tex. 1965]. Reasons for such disparate ends are not very clear: courts have founded their decisions on a test whether the license restriction falls reasonably within the reward the patentee is entitled to secure. See e.g., *Eversharp Inc. v. Fisher Pen Co.* 204 F.Supp. 649 [DCND Ill. 1961].

distort trade within the USA. There may not be a similar free movement of goods policy in the US and in the EEC, but both systems can put into play antitrust provisions when dealing with the situation where intellectual property rights are owned by one undertaking, which faces third parties beyond the scope of contractual relationships. Particularly relevant in such situation are the provisions governing dominant positions (article 86 of the EEC Treaty) or monopolization (section 2 of the Sherman Act).

CHAPTER II : ABUSE OF DOMINANT POSITION AND ATTEMPTS TO MONOPOLIZE

Antitrust laws are designed to maintain competitive order and provide the means of keeping competition free. Freedom to compete presupposes freedom to enter a market, freedom to develop and grow in that market, and freedom from monopoly pressure. This latter goal is ensured in the EEC by article 86 of the Rome Treaty which prohibits abuse of dominant position, and in the United States by section 2 of the Sherman Act which condemns monopolization, as such, as well as any attempt to monopolize, and combinations or conspiracies to monopolize, in interstate commerce.

"Dominant position" is the analogue of "monopoly power" under the monopolization offense of section 2 of the Sherman Act. Thus, both provisions require a showing of significant market power. The language of neither provision, however, defines or offers much guidance as to what constitutes market power, or as to the requisite degree of market power necessary for a violation. We shall first compare the general principles underlying article 86 of the EEC Treaty and section 2 of the Sherman Act, with respect to the definitions of dominant position and monopoly power. We will then review how EEC and US case law determine an abuse of dominant position and a violation of section 2 of the Sherman Act.

Section 1 : Dominant Position under Article 86 of the EEC Treaty and Monopoly under Section 2 of the Sherman Act

A/ Extent of the Respective Prohibitions

There is a fundamental difference in the approaches adopted in the EEC and the USA with respect to monopolies. Under EEC law, a dominant position *per se* is lawful. Article 86 only prohibits an abuse of dominant position. The Court has made it clear that mere ownership of intellectual property cannot be attacked under article 86[91]. However, if it is established that an improper exercise of intellectual property rights is committed by an undertaking which enjoys a dominant position, and if it follows that this behaviour is likely to affect trade between Member States, then the exercise of the rights is caught by article 86.

Under US law, monopoly itself is presumed to have anti-competitive effects[92]. If we compare the wordings of the respective definitions of the subject-matter, the contrast is striking. The Commission of the European Communities has provided the following definition of a dominant position:

> *Undertakings are in a dominant position when they have the power to behave independently*

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[91] See *Parke Davis v. Probel* [1968] E.C.R. 55, where the Court said that ownership of a patent is not an abuse itself, although *"the utilisation of the patent could degenerate into an improper exploitation of the protection."*

[92] Such a view is ideologically justified by CALLMAN, supra note 5, c.4 at 3: *"Socially, sociologically, and politically, the oppression of an individual's economic freedom by any power, economic or political, is anathema to a democratic economic, and this concept has clearly directed our approach"*

> *without taking into account, to any substantial extent, their competitors, purchasers and suppliers.*[93]

The generally accepted definition of monopoly power under section 2 of the Sherman Act is the power to control prices or exclude competitors. That negative approach is emphasised by the fact that monopolization requires the possession of market control in a relevant market, and wilful acquisition or maintenance of that power, as opposed to growth or development as a consequence of superior product, business acumen, or historic accident[94]. Thus, section 2 contains an element of intent or purpose to acquire a monopoly[95]. The test is therefore twofold: the existence of market power; and, an intent to exercise it[96]. The test is also twofold under EEC law, except that whereas the first step - the existence of the dominant position - is similar, the second one differs in that the Commission do not look for an intent to exercise a dominant position, but rather a will to improperly exercise - to abuse - that dominant position. Moreover, as a prerequisite for article 86 to be invoked, it is necessary to show that the abuse in issue may affect trade between EEC Member States.

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93 *United Brands v. Commission* [1978] 1 C.M.L.R. 429.

94 See *US v. Grinnel Corp.* 384 US, 563 [1966]; *Aspen Skiing Corp. v. Aspen Highlands Skiing Corp.* 472 US, 585 [1985]; *Standard Oil Co. of New Jersey v. US* 222 US, 1 [1911].

95 Mere possession of market power is not sufficient to constitute an offense of monopolization. *"Monopoly in the concrete is not prohibited... The Act using the word "monopolize" prohibits conduct rather than status"*; *US v. Reading Co.* 253 US, 26 [1920]. Monopoly power which is attributable to "*commercial realities*" or to the limited size of a market has been excused; *Woods Exploration & Producing Co. v. Aluminium Co. of America* 284 F.Supp. 582 [DCSD Tex. 1969]; *Union Leader Corp. v. Newspapers of New England* 180 F.Supp. 125 [DC Mass. 1959]. *"But becoming a monopoly simply to make more money is not a legitimate business justification for monopolizing."*; CALLMAN, supra note 5, c.4 at 119; see also *Poster Exchange Inc. v. National Screen Service Corp.* 431 F.2d, 334 [CA 5th, 1970]). Actual exercise of control over prices or actual exclusion of competitors is direct evidence of monopoly power; see *American Tobacco v. US* 328 US, 781 [1946]; *MCI Communications Co. v. American Tel.& Tel. Co.* 708 F.2d, 1081 [7th Cir. 1983].

96 See *International Salt v. US* 332 US, 392 [1947]; *United Banana Co. v. United Fruit Co.* 245 F.Supp. 161 [DCD Conn. 1965].

There is no need to prove that trade has actually been affected, provided that there is a possibility of that happening[97]. Intent, purpose, and effect are the elements that determine the illegality of conduct under US antitrust laws, and a *"reasonable probability"* to restrain competition is sufficient to put section 2 of the Sherman Act into play[98].

B/ Operation of One Entity

There are other common features to article 86 and section 2 of the Sherman Act. Both can be violated by a single economic unit, without the necessity of any contract, combination, or conspiracy. Article 86 uses the word "undertaking", which the EC Commission has defined as any legal or natural person engaged in a form of commercial activity[99]. In economic terms, an undertaking is also defined as an independent entity which can compete on a market, and is able to choose its own behaviour[100]. However, a problem arose with respect to groups of companies, as parent and subsidiaries networks. The question was whether such groups constituted a single unit or two different entities. The crucial test is the extent to which the parent company exercises effective control over the activities of the subsidiary. In *Metro-SB Grossmarkte v. Saba*, a refusal to supply was held to be an abuse of dominant position. Indeed, the defendant, Saba, was a subsidiary of Thomson, which was in a dominant position. But since Thomson exercised no control over Saba, they were separate companies and

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97 See *Instituto Chemioterapico Italiano & Commercial Solvents Co. v. Commission* [1973] C.M.L.R. D.50; *Bodson v. Pompes Funèbres des Régions Libérées S.A* [1988] E.C.R. 2479.

98 See *International Shoe Co. v. FTC* 29 F.2d, 518 [CA 1st, 1928]; *US v. Bethlehem Steel Co.* 168 F.Supp. 576 [DCSDNY, 1958]; *Anheuser-Busch Inc. v. FTC* 289 F.2d, 835 [CA 7th, 1961].

99 See *AOIP v. Beyrard* [1976] 1 C.M.L.R. D.14.

100 See generally BELLAMY & CHILD, 2d ed. *Common Market Law of Competition* (1978).

the refusal to supply was not an abuse of dominant position since Saba itself enjoyed no such position[101].

C/ Relevant Market

As to the degree of market power necessary to acquire a dominant position or a monopoly, the statutes do not provide any hints. Economics merely offers sophisticated definitions of market power but does not define the point at which market power becomes "monopoly power"[102]. Dominant position and monopoly are therefore "*legal constructs based on policy considerations which suggest where the line should be drawn between acceptable market power and suspect monopoly power*"[103]. It must be borne in mind that the capacity of an undertaking to increase its profits by raising prices and restricting output is subject to consumers' responsiveness, namely the elasticity of demand[104]. Demand elasticity and substitutability must be considered in the wake of a defined market. No

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101 [1986] E.C.R. 150; See also the *Commercial Solvents* case [1973] C.M.L.R. D.50. For a US view, see e.g., *Six Twenty-nine Prod. v. Rollins Telecasting* 365 F.2d, 478 [CA 5th, 1966].

102 Monopoly power is economically defined as the power to reduce output below the level that would otherwise prevail, and the ability to appropriate consumer surplus, causing deadweight losses beyond the transfer of income from buyer to seller. "*Monopoly power is the power to raise prices by restricting output without a significant loss of sales - i.e, the power to fix prices or exclude competition.*"; HAWK, supra note 63 at 788.

103 HAWK, supra note 63 at 789

104 Thus, actual control over prices as well as the power to exclude competitors is an evidence of market power. Where such evidence is lacking, courts and competition authorities have sometimes looked at market shares. The principal dispute between economic and legal literature centres on the role of market share in the measurement of monopoly power or dominant position. See generally LANDES & POSNES, "Market Power in Antitrust Cases" [1981] 94 Harv. L. Rev. 937; BADEN FULLER, "Article 86 EEC: Economic Analysis of the Existence of a Dominant Position" [1979] 4 Eur. L. Rev. 423; KORAH, "Concepts of Dominant Position Within the Meaning of Article 86" [1980] 17 CMLR. 395; CALVANY & SIGFRIED, 2d ed. *Economic Analysis and the Antitrust Law*" (1988). Certain US courts have stated that 90 % of supply "*is enough to constitute a monopoly; it is doubtful whether 60 or 64 % would be enough; and certainly 33 % is not*"; *US v. Aluminium Co. of America* 148 F.2d, 416 [2nd Cir. 1945]. But not all cases are consistent: in *Forro Precision Inc. v. IBM Corp.* 673 F.2d, 1045 [9th Cir. 1982], market shares under 50 % were found to be insufficient to constitute a monopoly power. Other authorities raised the limit at 70 %; *US v. Dupont De Nemours* 351 US, 377 [1956]. The US Supreme Court have warned against an over-reliance on market shares figures on the ground that they are an imprecise tool, sometimes overestimating market power. See *US v. Columbia Steel Co.* 334 US, 495 [1948].

undertaking can be dominant in the abstract, it can only dominate a particular market, *"in any line of commerce"* and *"in any section of the country"*, which is to say in any product or service market and in any geographic market to which the trade may be confined[105].

The relevant market is the area affected by the questioned activity, and it is in that market where the effect upon competition must be assessed. As underlined in *Europemballage Co. & Continental Can Co. v. Commission*, defining the relevant product market is of crucial importance[106]. The product market is one in which products are substantially interchangeable. It includes identical products or products considered by consumers to be similar by reason of their characteristic, price, or use[107]. A similar definition was adopted by the US Supreme Court in the *Cellophane* case, where it held that the relevant market is:

> *... composed of products that have reasonable interchangeability for the purpose for which they are produced - price, use and quality considered... If a slight decrease in the price of cellophane causes a considerable number of customers of other flexible wrappings to switch to cellophane, it would be an indication that a high-cross elasticity of demand exists between them; that the products compete on the same market.*[108]

Further, the important concept of sub-market was introduced by the Supreme Court in *Brown Shoe v. US*[109]. If a particular product line is not

105 Phrases are taken from sections 3 and 7 of the 1914 Clayton Act.

106 [1973] E.C.R. 215; in that case, the Court overturned the Commission's decision on the grounds that the product market had not been correctly defined.

107 See *United Brands v. Comm.* [1978] 1 C.M.L.R. 429; *Hoffman-La-Roche AG v. Comm* [1979] E.C.R. 461; and more generally on this issue BELLAMY & CHILD, supra note 100 at 159-172.

108 *US v. Dupont de Nemours* 351 US, 377 [1956].

109 370 US, 294 [1962].

sufficiently significant to constitute a market, the courts will classify it as a sub-market to determine the effect upon it of a particular transaction. Thus, US courts have defined quite narrow sub-markets which, in turn, have permitted to determine monopoly power and unlawful monopolization under section 2 of the Sherman Act[110].

However, it may happen in particular circumstances that no interchangeability at all is possible. In the *Hugin* case, a Swedish manufacturer of cash registers was held to have a dominant position in the supply of spare-parts for its own machines. The spare-parts constituted a separate market from the cash registers themselves[111].

Moreover, more than one relevant product market may be involved: there may be an adverse effect on competition with respect to different lines of goods. In *US v. Columbia Steel Co.*, the relevant market was differently defined for each of the products affected by a merger[112].

Not only is a dominant position determined by reference to a relevant product market, but it must also be delimited within a geographic market. That geographic area must be a substantial part of the Common Market in which available and acceptable substitutes exist. This substantial part of the Common Market can be constituted by the whole territory of the Community[113], by a single Member State[114], or even by certain regions

[110] See *International Boxing Club v. US* 358 US, 242 [1959]; *US v. Paramount Pictures Inc.* 334 US, 131 [1948]; *US v. Grinnel Corp.* 384 US, 863 [1968].

[111] *Liptons Cash Registers & Business Equipment Ltd v. Hugin Kassaregister AB & Hugin Cash Registers Ltd* [1978] 1 C.M.L.R. D.19; See also *General Motors Continental N.V v. Comm.* [1976] E.C.R. 1367.

[112] 334 US, 495 [1948].

[113] *AKZO Chemie BV v. Comm.*[1986] E.C.R. 1965; *Eurofix Banco v. Hilti* [1989] 4 C.M.L.R. 677.

[114] *General Motors Continental v. Commission.* [1979] E.C.R. 1367.

of one or more Member States. *In Tampa Elec.Co. v. Nashville Coal Co.*, the US Supreme Court defined the geographic market as the area in which suppliers operate and to which purchasers can practically turn for supplies[115]. Local, regional, and national markets have been found[116]. The Ninth Circuit, in *Case-Swayne Co. v. Sunkist Growers Inc.*, enumerated the following geographic market criteria:

> *It seems clear from the decided cases that (1) while the outer limits of the market may be determined by the competition of interchangeable products, (2) there may be a well-defined sub-market which constitutes the relevant market for antitrust purposes, which (3) must correspond to the commercial realities for the industry, (4) is affected by price disadvantages due to transportation costs, (5) is affected by availability of a buyer to supply and existence of economic areas which significantly impede competition, (6) is determined in part with relation to the parties affected in suit, and (7) is a question of facts in the particular case*[117].

Furthermore, the Federal Trade Commission listed the following factors in analysing entry barriers which it considered probative of the geographic market: transportation costs; shipping patterns; price differentials among regions; products differentiation among sales districts; and, the history of entry by firms into new regions[118]. Thus, geographic market definition is related to the importance of barriers to interregional trade[119].

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[115] 365 US, 320 [1961].

[116] See *Lorain Journal Co. v. US* 242 US, 143 [1951]; *US v. Columbia Steel Co.* 334 US, 495 [1948]; *US v. Grinnel Corp.* 384 US, 563 [166].

[117] 369 F.2d, 449 [9th Cir, 1966].

[118] *General Foods Co.* 103 FTC. 204 [1984].

[119] Generally, the absence of imports shows that remote suppliers are not in the same market as local suppliers. Remote sellers have no reason to sell in the local area if local prices are competitive and supply and demand are in equilibrium. In such case, local and remote prices should be on a close level. The presence of imports may be due to the absence of trade barriers, to non-competitiveness of local prices and the like. In such event, a

Hence, the definition of a dominant position or monopoly power is similar under EEC and US laws. But the extent to which article 86 and section 2 of the Sherman Act are violated by such monopolistic positions is radically different. Whereas intentional acquisition or maintenance of a monopoly is unlawful under US law, EEC law only condemns abuses of dominant positions, not the mere existence or acquisition of monopolies. But both systems censure monopolistic behaviour intended to destroy competition.

Section 2 : Abuse of Dominant Position and Monopolization

One of the most difficult question in antitrust cases concerns the criteria needed to determine when conduct engaged in by a firm with significant market power should be prohibited.

The text of article 86 refers to four categories of conduct which may be abusive: imposing unfair prices or unfair trading conditions; limiting production, markets, or technical development; applying dissimilar conditions to equivalent transactions; and, making the conclusion of contracts subject to acceptance by other parties of supplementary obligations (tying-in). The Court's decisions have followed these guidelines[120], and punished some abuses the Treaty writers had not foreseen, such as import or export bans[121], exclusive reservations of

single market including both local and remote can be presumed. The question being what weight should be given to imports into the local markets. See generally on this question HAWK, supra note 63 at 775; ELZINGA & HOGARTY, "The Problem of Geographic Market Delineation in Antimerger Suits" [1974] 18 Antitrust Bull. 45.

120 See for unfair prices, unfair trading conditions and discriminatory treatment the *United Brands* case, [1978] 1 C.M.L.R. 429, and for tying-in practices *Hoffman-La-Roche v. Comm.* [1979] E.C.R. 461.

121 *Suiker Unie v. Commission* (the *Sugar Cartel* case) [1973] E.C.R. 24.

activities[122], predatory pricing[123], refusal to supply[124], and certain kinds of mergers and takeovers[125].

Section 2 of the Sherman Act provides no such list, but reasoning that it is an antitrust violation to attempt to reach every act which produces the result of a monopoly, and using that monopoly to exclude actual or potential competitors from any part of the trade among the several States, US courts have elaborated their own list of reprehensible behaviour. Those actions constitute a violation of the antitrust laws to the extent that their perpetrators enjoy a monopoly power. They would otherwise not be caught by section 2. One of the most recent Supreme Court formulations of the monopolization offense is found in *Apen Skiing*[126]. The Court defined unlawful monopolizing conduct as "*anti-competitive*", "*exclusionary*" or "*predatory*" behaviour that "*impaired competition in an unnecessarily restrictive way*" or "*attempted to exclude rivals on some basis other than efficiency*"[127]. As far as intellectual property rights are concerned, we shall focus on three specific kinds of abusive behaviour.

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122 *Italy v. Comm.(Re British Telecom)* [1985] E.C.R. 873.

123 *AKZO Chemie Bv. v. Commission.* [1986] E.C.R. 1965.

124 *Instituto Chemioterapico Italiano & Commercial Solvents* [1973] C.M.L.R. D.50.

125 *Europemballage & Continental Cans* [1973] E.C.R. 215.

126 *Apen Skiing Corp. v. Apen Highlands Skiing Corp.* 472 US, 585 [1985].

127 *Ibid* at 602, 605, 597.

A/ REFUSAL TO DEAL

> *The purpose of the Sherman Act is... to preserve the right of freedom of trade.* ***In the absence of any purpose to create or maintain a monopoly,*** *the Act does not restrict the long and recognized right of traders or manufacturers engaged in an entirely private business, freely to exercise his own independent discretion as to the parties with whom he will deal...*[128] (emphasis added).

The US *Colgate* doctrine, established by the Supreme Court in 1919, made it clear that a refusal to deal is not *per se* unlawful. Manufacturers are free to decide whether they want to stop selling to a distributor[129]. The only restriction to the *Colgate* doctrine is where the purpose of the practice is to create or maintain a monopoly.

There is a similar principle under EEC law, whereby a refusal to deal by an undertaking that enjoys no dominant position of its own does not violate article 86. In *Metro-SB Grossmarkte v. Saba*, the plaintiff alleged that Saba, having a dominant position, had no right to refuse to sell its products. Indeed Saba was a subsidiary of Thomson, and only the parent company was in a dominant position. As it was established that Saba and Thomson did not constituted a single economic unit, but two separate entities, Saba had no dominant position of its own and was therefore entitled to refuse to sell to Metro[130].

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128 *US v. Colgate & Co.* 250 US, 300 [1919].

129 *Ibid* at 307.

130 [1986] E.C.R. 150; see also *Instituto Chemioterapico Italiano & Commercial Solvents Co. v. Comm.* [1973] C.M.L.R. D.50. This latter case established that the EC Commission, when deciding whether a refusal to deal was likely to fall within article 86, took into account the risks of competition distortion and the immediate protection of consumers, but also the protection of competition at a manufacturing level, preventing smaller firms from suffering at the hands of powerful competitors. By contrast, US antitrust laws are said to protect competition and not competitors; see HAWK, supra note 63 at 828. See also *Berkey Photo Inc. v. Eastman Kodak Co.* 603 F.2d, 263 (2nd Cir. 1979]; *Transamerica Computer Co. v. IBM Corp.* 698 F.2d, 1377 [9th Cir. 1983]; *Aspen Skiing Co. v. Aspen Highlands Skiing Co.* 472 US, 585 [1985].

In the recent *Renault* and *Volvo* cases, the question arose whether a refusal to grant licences for the manufacture of car spare-parts amounted to an abuse of dominant position[131]. Renault and Volvo owned industrial design rights in the spare-parts, and it was argued by the plaintiffs that the refusal to licence those rights to spare-parts manufacturers constituted an improper exercise of intellectual property rights by companies which had a dominant position in the market of spare-parts for the cars they manufactured, which was likely to distort trade between EEC Member States. Considering the specific subject-matter of industrial design rights, the European Court of Justice held that:

> *...the right of the proprietor of a protected design to prevent third parties from manufacturing and selling or importing, without its consent products incorporating the design constitutes the very subject-matter of its exclusive rights. It follows that an obligation imposed upon the proprietor of a protected design to grant to third parties, even in return for reasonable royalty, a licence for the supply of products incorporating the design would lead the proprietor thereof being deprived of the substance of its exclusive rights, and that a refusal to grant such a licence cannot in itself constitute an abuse of dominant position.*

Since Renault and Volvo manufactured and marketed the spare-parts themselves, at fair prices, competition within the Common Market was not distorted by the mere existence and a proper exercise of intellectual property rights.

A parallel may be drawn between those European cases and the

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131 *Conzorziono Italiano delle Componentistica di Ricambio v. Régie Nationale des Usines Renault* [1990] 4 C.M.L.R. 906; *AB Volvo v. Eik Veng* [1989] 4 C.M.L.R. 122. See also KORAH, "No Duty to Licence Independent Repairers to Make Spare-Parts: the Renault, Volvo and Bayer Cases" [1988] 12 E.I.P.R. 381.

American *SCM Corp. v. Xerox Corp.* decision, where the Second Circuit affirmed a lower court holding that if there was a lawful acquisition of a patent, this was not made unlawful by the fact that subsequently the patent would dominate the market. There, the Xerox Corporation had acquired patents in 1956 on plain paper copiers before there was any market for such product. Xerox's refusal to license the patents, it was held, should not result in damages under section 2 for monopolization[132].

However, a crucial difference between those cases is that, under EEC law, the refusals to licence by Renault and Volvo were excused because both firms were manufacturing and marketing their products. The reasoning in *SCM Corp. v. Xerox Corp.* was not justified on the same basis. There the refusal to license was held lawful because it was not a concerted practice. With respect to refusal to license, a unilateral decision cannot attract antitrust liability[133].

Another difference in the approaches adopted by the American and European antitrust authorities can be derived from the following decisions. In *Magill TV Guide v. ITP/BBC/RTE*, the Magill company wished to publish the TV programmes of three British channels in a single weekly guide[134]. Each of them was already publishing its own programmes in its own guide,

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[132] 645 F.2d, 1195 [2nd Cir. 1981]. See also *Van Dyck Research Corp. v. Xerox Corp.* 478 F.Supp. 1268 [CA 3rd. 1980]; and *GAF Corp. v. Eastman Kodak Co.* 519 F.Supp. 1203 [DC.NY 1981] where a manufacturer of photography equipment, an alleged monopolist, did not violate section 2 by refusing to license any photochemical patents until five years after they were issued. But compare with *Eastman Kodak Co. v. Southern Photo Co.* 273 US, 359 [1927], where a refusal to deal by a dominant firm was violative of section 2.

[133] 645 F.2d, 1204 [2nd Cir. 1981]; This decision is reversing *Eastman Kodak Co. v. Southern Photo Corp.* 273 US, 359 [1927], where a dominant firm which was not acting in concert with anyone else violated section 2 by refusing to license its intellectual property rights. See also *US. v. Westinghouse Co.* 648 F.2d, 642 [9th Cir. 1981]; and *E.I Dupont De Nemours Co.* 96 FTC 653 [1980] (refusal to licence know-how not violative of Sherman Act).

[134] [1989] 4 C.M.L.R. 749.

in which some copyrights were vested. The Commission concluded that the three television companies had abused their dominant position in relation to their own listings by refusing to make them available in advance. The specific subject-matter of copyrights, in this case, did not prevail over the risk of distortion of competition in a substantial part of the Common Market (the United Kingdom), and with respect to the product market (the programmes listings) in which some dominant positions were held[135].

The American approach in *Berkey Photo Inc. v. Eastman Kodak Co.* was to distinguish refusals to deal from refusals to pre-disclose competitive information. Refusals to deal were said to constitute monopolizing conduct because the chances of success of a refusal to deal correlates directly with the market power of the defendant firm. But a refusal to pre-disclose competitive information to another competitor was said not to rest on market power. The advantage gained would be the same whether or not the firm had a total monopoly or no market power at the time of the introduction of the new product[136].

Therefore, both EEC and US systems tend to censure refusals to deal from dominant firms, but the bases on which they act are not similar. Once again, it must be recalled that the ideologies and goals of the respective antitrust laws are different. The results obtained are, however, often identical.

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135 The question has been raised as to whether this decision was consistent with the *Renault* and *Volvo* cases: whereas the latter held that compulsory licences could not be insisted upon under article 86, the *Magill* case had the effect of granting a compulsory licence of programme information. Indeed, the distinction to be made between these decisions is that Volvo and Renault supplied the spare-parts that were the subject of the intellectual property rights, although they were refusing to grant licences. On the other hand, the television companies were refusing to supply the listings at all, except to their own publications. See WISH, *Competition Law* (1985) at 676.

136 603 F.2d, 263 [2nd Cir. 1979]; see also *Telex Corp. v. IBM Co.* 510 F.2d, 894 [10th Cir. 1975].

B/ UNFAIR PRICES OR TRADING CONDITIONS

As emphasised in *Volvo* and *Renault*, it would have been an abuse of dominant position to licence a right or to supply a good at an excessive price, or to do so in an arbitrary manner. It would also be an abuse for a firm to stop producing spare-parts for models still in circulation, and refuse to licence the right to manufacture them.

In *Eurofix Banco v. Hilti*, the Commission held it was an abuse of dominant position to demand excessive royalties with the sole object of blocking a licence right which was available under the Patent Law of a Member State. This was seen as part of Hilti's strategy of hindering competition in respect of its products[137].

In *Basset v. SACEM*, the Court was asked whether SACEM (the French copyright collecting society) was entitled to charge a 1.65% supplementary mechanical reproducing fee above its normal royalty for performances at discotheques, on juke-boxes and radios, where the recordings in question were imported from other Member States in which no such fee was payable[138]. The Court held that the extra charge was not contrary to article 86, as it amounted to a normal exploitation of copyrights and was not an act of arbitrary discrimination or a restriction on inter Member States trade. However, the activities of such national collecting societies may breach article 86 when they tend to discriminate against people from other Member States[139].

A similar view was taken in the United States with respect to patent

137 [1989] 4 C.M.L.R. 677.

138 [1987] 3 C.M.L.R. 173.

139 See *Re GEMA* [1971] C.M.L.R. D.35.

royalties. In *W.L Gore & Associates Inc. v. Carlisle Corp.*, a thirty percent royalty demand by a patentee was neither patent misuse or monopolization offense[140]. A further unfair or abusing trading condition likely to be caught by section 2 of the Sherman Act is unreasonable prosecution or threats to sue by a monopolist. In *Kobe Inc. v. Dempsey Pump Co.*, the plaintiff, who brought an infringement action against the defendant, was found guilty of predatory practices: "*... The real purpose of the infringement action... was to further the existing monopoly and to eliminate Dempsey as a competitor*"[141]. However, the infringement suit, or threat of action, only falls under section 2 if it is unreasonable and not justified. In *Bryan v. Sid W. Richardson*, the appellant, who had been charged with infringing two patents, entered a defense that the respondent had been guilty of monopoly abuse by giving written and oral notices of infringement actions to several prospective users of the appellant's device. The Court rejected that defense:

> *... This is a reasonable thing for businessmen to do since it is hardly to be thought that it is a sign of bad faith to warn friendly customers... that if they purchased a competing infringing tool, litigation against them might be necessary.*[142]

Thus, both EEC and US laws censure unfair monopolist behaviours that tend to exclude competitors, or at least affect their competitiveness.

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140 529 F.2d, 614 [CA 3th. 1976]; see also *Westgo Industries v. W.J. King Co.* 63 F.Supp. 984 [DCND 1981].

141 198 F.2d, 416 [CA 10th. 1952]; see also *International Visible Systems Corp. v. Remington Rand Inc.* 65 F.2d, 540 [CA 6th. 1933]; *US v. General Electric Co.* 82 F.Supp. 753 [DNJ 1949].

142 254 F.2d, 191 [CA 5th. 1958].

C/ ACQUISITION AND ACCUMULATION OF INTELLECTUAL PROPERTY RIGHTS

The mere acquisition or accumulation of patents is not in itself illegal under the Sherman Act or the Rome Treaty[143]. But the acquisition of patents or licenses from patentees for the purpose of obtaining a monopoly or eliminating competition is illegal.

Monopolization under the meaning of section 2 of the Sherman Act was found to have taken place where a company acquired substantially all of the patents covering an important aspect of oil-well-digging equipment with intent to monopolize and control the industry. All licences and patents involved were found to have been acquired for the purpose of obtaining a monopoly[144]. In *US v. Parker Rust-Proof Co.*, it was held that although patents may be purchased like any other property, the mere fact that patents were involved in a contract for the purchase of a competing company could not justify the contract when it had the object or effect of restraining trade or stifling competition[145]. In the *GE Incandescent Lamp* case, the Supreme Court held that General Electric had monopolized patents in the incandescent lamp field, and in the *RCA* case, the US Government charged that Radio Corp. of America had monopolized the patents in the communications field. General Electric, Philips, and the other defendants in the *GE Incandescent Lamp* case were required to *"dedicate to the public any and all existing patents on lamps and lamp parts"*[146]. In the judgment

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143 *Automatic Radio Mfg Co. v. Hazeltine Research Inc.* 339 US, 827 [1950]; *Zenith Radio Corp. v. RCA* 106 F.Supp. 561 [DC Del. 1952]; *Parke Davis v. Probel* [1968] E.C.R. 55.

144 *Kobe Inc. v. Dempsey Pump Co.* 97 F.Supp. 342 [ND Okla. 1951]; see also *US v. Besser Mfg Co.* 343 US, 444 [1952].

145 61 F.Supp. 805 [DC.Mich. 1945].

146 *US v. General Electric Co.* 115 F.Supp. 835 [DNJ. 1953].

in *RCA*, that company was required to licence domestic patents at a reasonable royalty[147].

The EC Commission and the European Court of Justice recently adopted the same position. As stated in *Europemballage/Continental Cans*, a takeover bid leading to a concentration, for the sole purpose to eliminate competitors in a given market, is an abuse of dominant position[148]. The same ruling was adopted with regard to patent rights in the *Tetra Pak* case, but the decision has been subject to sharp criticism[149]. Tetra Pak had a dominant position in the market for cartons and machines for packaging milk. Another company acquired a patent for a new process of sterilising cartons suitable for long-life milk, which was likely to threaten Tetra Pak's dominant position. Tetra Pak launched a (successful) takeover bid for Liquipak, the parent company of the patent holder. The Commission objected on the grounds that this takeover would enable Tetra Pak to dominate the milk packaging market for another twenty years: it was an abuse of dominant position to acquire a monopoly over a technology with a view to excluding competitors from a market. Tetra Pak raised a defence based on article 85 of the Treaty, and pointed out that it took all the necessary steps to have the exclusive patent licence in question fall within the scope of Regulation 2349/84, which constitutes an exemption under article 85-3 permitting a licence agreement deemed prohibited under article

147 *US v. Radio Corp. of America* 1958 Trade Cases (CCH) 69, 164; see also *US v. United Shoe Machinery Co. of New Jersey* 247 US, 32 [1918].

148 [1973] E.C.R. 215.

149 *Tetra Pak I (BTG Licence)* O.J.1988 L.272/27; on appeal *Tetra Pak Rausing S.A v. Commission* [1990] 4 C.M.L.R. 47; See DAVIES & GRAYSTON, "Mergers and Acquisitions in the EEC" [1991] 40 Trademark World. 22.

85-1[150]. The Commission answered that although Tetra Pak was eligible for an article 85-3 exemption, article 85 was not in issue, and sustained its allegation of breach of article 86. In the light of this decision, one might wonder whether the boundary between the prohibition of unfair competition and free competition has been erased by the Commission.

The American cases seen above are in accord with US antitrust policy and the spirit of the Sherman Act; a wilful intent to acquire a monopoly is condemned in the USA, while it is not censured under EEC law. Article 86 requires an abuse of dominant position to be put into play. The *Tetra Pak* case would have most likely been judged in the same manner before a US court, but it should not have been considered this way by the European Court of Justice. The Court has effectively condemned the mere acquisition of a monopoly. Besides, the question of whether articles 85 and 86 must be read in a complementary manner may also arise, given that a practice authorized under article 85-3 is likely to be prohibited under article 86.

Another important distortion of trade and competition, lies in "tying-in" practices. Article 86 defines them as "*making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts*"[151]. Tying-in generally occurs between suppliers and retailers within the context of contractual relationship, and we shall now examine the role of intellectual property rights within the framework of such connections.

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150 See infra note 211 and accompanying text.

151 Article 86(d) of the EEC Treaty; see appendix A.

PART TWO : CONTRACTUAL USE OF INTELLECTUAL PROPERTY RIGHTS: LICENCE AGREEMENTS

A specific kind of contractual relationship involving intellectual property rights, and capable of affecting the competition policies of the EEC and the USA, is the license of rights agreement. The mere existence of such a contract is lawful as such[152], but an improper exercise of licenses of intellectual property rights may infringe article 85-1 of the EEC Treaty or section 1 of the Sherman Act. Broadly speaking, both provisions are concerned with distortions of competition resulting from restrictive arrangements between two or more parties. In consequence, article 85-1 and section 1 can, and frequently do affect agreements dealing with intellectual property. After comparing the general conditions of application of those provisions, we will balance the competitive and anti-competitive effects of intellectual property licensing. We will then examine various specific clauses of licence agreements capable of falling within the prohibitions set out in article 85-1 of the EEC Treaty and section 1 of the Sherman Act.

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152 See *Consten & Grunding v. EC Commission* [1966] E.C.R. 229; *Parke Davis v. Probel* [1968] C.M.L.R. 47; In US law, see for instance section 261 of the Patent Code, 35 USC, s.261 [1952] : *"The applicant, patentee, or his assigns or legal representatives may... grant and convey an exclusive right under his application for patent... to the whole or any specified part of the United States"*. See also *Ethyl Gasoline Corp. v. US* 309 US, 436 [1940]: *"Patent owners may grant licenses extending to all uses or limited to use in a defined field. Unquestionably, the owner of a patent may grant licenses to manufacture, use or sell upon conditions not inconsistent with the scope of the monopoly."*

CHAPTER I : SECTION 1 OF THE SHERMAN ACT, ARTICLE 85-1 OF THE EEC TREATY AND LICENCES OF INTELLECTUAL PROPERTY RIGHTS.

Section 1 : General Principle and Application of Section 1 of the Sherman Act and Article 85-1 of the EEC Treaty.

The Sherman Act was enacted in 1890, and the Rome Treaty entered into force in 1957. The US system of competition law was the pioneer which served as a model for that of the EEC, although some differences in the interpretation and application of certain closely resembling provisions must be observed.

A/ Trade "Between Member States" and "Among the Several States".

Section 1 of the Sherman Act reads:

> *Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal...*

Article 85-1 states:

> *The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings, and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market...*

It must be pointed out, as a first noteworthy difference between the two provisions, that the latter presupposes that trade *"between Member States"* will be affected by the agreement or practice, whereas the former requires restraints *"among the several States"*. These requirements seem almost identical, but they are interpreted differently. The European Court of Justice has made it clear that the aim of this formulation was to limit the jurisdiction of the EEC rules in relation to the national rules on competition[153]. It is often decided by the Commission and the Court whether trade between Member States has been affected, and much interest is attached to the fulfilment of the requirement[154]. The requirement of the Sherman Act has, however, not aroused the same kind of interest. Instead it may be regarded as an occasionally necessary condition, given that American judges do not have to implement a policy similar to that in Europe, namely the integration of a common market[155].

Article 85-1 takes the form of a general prohibition followed by a non exclusive list of specific prohibited practices. The general prohibition itself may be divided into three requirements. First, there must be an agreement, a decision, or a concerted practice between at least two undertakings. Second, there must be the possibility that the agreement, decision or concerted practice will affect trade between Member States. Third, the object or effect of the agreement, decision, or concerted practice must be the prevention, restriction, or distortion of competition within the EEC.

B/ Operations of Two or More Parties

For the purpose of article 85 (as well as article 86), the definition of an undertaking is a natural or a legal person capable of carrying on

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153 See the *Hugin* case [1978] C.M.L.R. D.19.

154 In *Hugin*, supra note 153, the European Court of Justice found that Hugin's contested practices toward a British firm did not affect trade between Member States since the plaintiff was functioning on a purely local scale in London.

155 See *US v. Women Sportswear Manufacturer Assoc.* 336 US, 460 [1949]; *Hospital Buildg.Co. v. Trustees of the Rex Hospital* 425 US, 738 [1976]. And see generally FEJO, supra note 20 at c.1.

some commercial or economic activity[156]. Since it takes at least two undertakings for article 85 to come into play, it is particularly relevant to know whether a parent and its subsidiary constitute a single unit or two separate undertakings: the test to be applied is the same as that applied to article 86, namely the degree of control of the parent over its subsidiary[157]. Agreements, decisions, and concerted practices are to be broadly understood. Mere co-operation between undertakings, a legally enforceable contract, the constitution of a trade association, or a mental consensus have been held by the Commission to fall within article 85-1[158]. EEC and US laws are in accord on this point.

Section 1 of the Sherman Act refers to the operations of two or more persons or units in restraint of trade. The participating entities must therefore be separate. Intra-corporate combinations or conspiracies are not transactions involving separate entities[159]. Thus, mere unilateral action by one person or firm is not sufficient to put section 1 into play[160].

C/ Object or Effect of Distorting Competition

With respect to the object or effect of preventing or distorting competition, as stated in article 85-1, the *Société Techniques Minières* case emphasised that object and effect are not cumulative conditions, but have to be read disjunctively. Thus, if the purpose of an agreement is to distort

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156 See *Nungesser KG v. Commission* [1982] E.C.R. 2015.

157 As explained earlier at p.45.

158 See *Polyprolène* [1988] 4 C.M.L.R. 347; *IAZ International Belgium v. Commission* [1983] E.C.R. 3369; *Suiker Unie v. Commission (the Sugar Cartel case)* [1975] E.C.R. 1663.

159 *Fashion Originators Guild of America v. FTC* 312 US, 457 [1941]; *US v. Columbia Steel Co.* 334 US, 495 [1948]; *Northern Pacific Railways Co. v. US* 356 US, 1 [1958].

160 "Person" in the Sherman Act must be understood as including partnerships and corporations; see *Western Laundry & Linen Rental Co. v. US* 424 F.2d, 441 [CA 9th Cir. 1970].

competition, there is no need for the Commission also to conclude that it might have an anti-competitive effect. Similarly the prevention, restriction, or distortion of competition need not be actual: even a potential risk is sufficient to put article 85 into play[161].

Under US law, intent, purpose and effect are also the elements that determine the illegality of conduct under the antitrust laws. In assessing the intent of a defendant, three categories of actions must be distinguished. First, there are acts which are illegal *per se*, and with respect to those acts the defendant's intent is irrelevant. The courts will hear no justifications whatsoever for such conduct. Secondly, there are acts which turn out to be unlawful because of a defendant's intent, as seen earlier with respect to monopolization. Finally, there are acts which are illegal, irrespective of intent, because their **probable** effect may be substantially to lessen competition or to create a monopoly. The word "may" as used in the antitrust laws has been the source of a debate, about whether it was intended to prohibit *"the mere possibility of the consequences described"*[162], or any *"reasonable probability"*[163]. The latter view prevails today[164].

D/ *Per se* Concept and the Rule of Reason

Section 1 of the Sherman Act outlaws any contract or combination effecting a restraint of trade, characterized as undue either because it is illegal *per se* or unreasonable under the "rule of reason". Unlike article

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161 *Société Techniques Minières v. Mashimbau Ulm* [1966] E.C.R. 235.

162 *Standard Fashion Co. v. Margrane Houston Co.* 258 US, 346 [1922].

163 *Anheuer-Busch Inc. v. FTC* 289 F.2d, 835 [CA 7th. 1961].

164 See EWING, "Antitrust Enforcement and the Patent System: Similarities in the European and American Approaches" [1980] 11 I.I.C. 279.

85-1, section 1 of the Sherman Act contains no list of specific prohibited practices and very early on American courts perceived that the wording of the Sherman Act was too broad. Those statutory provisions were simply stated and comprehensive in their reach. However, they also condemned all sorts of things that could benefit competition and consumers. Ways of making the statutes sufficiently flexible to permit desirable agreements and behaviour were developed. The most important of these flexibility factors is the so-called "rule of reason". This approach involves dividing business practices into two classes. As already stated, certain practices are so clearly anti-competitive that they are *per se* illegal[165]. That means that they are held to be unlawful without any analysis of their effect on competition. All other practices are examined under the rule of reason, which calls for the courts to make an economic study of the effects of the act in question. Thus, the distinction between *per se* violations and unreasonable restraints is that the former are unlawful *in abstracto*, irrespective of the surrounding circumstances, whereas the latter are illegal by virtue of their specific surrounding circumstances. The elaboration of the rule of reason in the United States involved three steps. In 1898, Chief Justice Peckam introduced the premises of the rule of reason in *US v. Addyston Pipe & Steel Co.*, relying upon the common law concept of "ancillary restraint", whereby any agreement in restraint of trade is void if its sole purpose or effect is to eliminate competition. If, however, the restraint is ancillary, that is, collateral and incidental to another

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165 See *US v. Trans-Missouri Freight Ass'n* 166 US, 290 [1897]: the Supreme Court, passing upon a price-fixing agreement, held that every such agreement was a contract in restraint of trade and therefore illegal under the Sherman Act irrespective of the reasonableness of the price fixed.

legitimate and lawful primary purpose, the agreement is valid[166]. In 1911, Chief Justice White coined the phrase "rule of reason" in *Standard Oil Co. of New Jersey v. US*, and formulated the prohibition of:

> *... all contracts or acts which were unreasonably restrictive of competitive conditions, either from the nature or character of the contract or act or where the surrounding circumstances were such as to justify the conclusion that they had not the legitimate purpose of reasonably forwarding personal interest and developing trade...*[167]

But in *US v. American Tobacco Co.*, Justice White used other language to clarify the rule of reason: *The words "restraint of trade"... only embraced acts or contracts... or combinations which, either because of their inherent nature or effects or because of the evident purpose of the acts...*[168]. Indeed, the phrase "inherent nature", instead of clarifying the rule of reason, confused many lawyers as it appeared to suggest the *per se* concept.

The rule of reason, as it is nowadays interpreted, was formulated in 1918 by Justice Brandeis. In *Chicago Board of Trade v. US*, he stated the principle as follows:

> *... the legality of an agreement or regulation cannot be determined by so simple a test, as whether it restrains competition. Every agreement concerning trade... restrains. To bind, to restrain, is their very essence. The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition. To determine that question, the court must ordinarily consider the facts peculiar to the business to which the*

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[166] 85 F.2d, 271 [1898].

[167] 221 US, 58 [1911].

[168] 221 US, 179 [1911].

restraint is applied.[169]

Thus, a rule of reason analysis must take into account the surrounding circumstances of the practice or agreement under consideration.

These principles inspired the EEC competition authorities. When implementing article 85-1, the Commission and the Court draw a distinction between agreements which constitute a violation *per se* of the Treaty, and those which, although they seem to distort competition, are not caught by article 85-1, by virtue of a *rule of reason*[170]. For example, certain restriction clauses are held to fall outside article 85-1 because the risk undertaken by a distributor, licensee, or franchisee is so great that some exclusivity must be conferred upon him[171]. Further, some agreements which affect competition within the meaning of article 85-1 may nevertheless not be caught because they do not have an appreciable impact either on competition or on inter-State trade. This *de minimis* doctrine was first formulated by the Court in *Volk v. Vervaecke*[172], and the Commission provided clear guidance for the application of this principle in its "Notice on Agreements of Minor Importance"[173].

However, EEC and US rules of reason differ on three points. First, under EEC law, an agreement or practice which is *prima facie* unlawful may, by virtue of the rule of reason, be validated. Under the US antitrust

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169 246 US, 231 [1918]; see generally on this subject BORK, "The Rule of Reason and the Per Se Concepts: Price-Fixing and Market Division" [1965] 74 Yale L. J. 815; LOEVINGER, "The Rule of Reason in Antitrust Law" [1964] 50 Val. L. Rev. 23.

170 See generally STEINDORFF, "Article 85 and the Rule of Reason" [1984] C.M.L. Rev. 639.

171 However, an absolute territorial protection is always prohibited. See *Consten & Grunding v. Commission* [1966] E.C.R. 299; and *Nungesser KG v. Commission* [1982] E.C.R. 2015.

172 [1969] E.C.R. 295.

173 O.J 1986, C.231/2, replacing the previous 1977 and 1968 notices.

laws, the rule of reason is deemed negative. It declares an otherwise reasonable act or contract to be unreasonable[174]. Second, unlike the European rule of reason, American antitrust laws do not give an undertaking the opportunity to justify its contested practice by establishing that the beneficial effects of its conduct compensate for its restrictive effects. The US rule of reason does not permit to balancing the pros and cons of a restrictive practice. Judges only determine by an analysis of the object and effect of conduct whether it harms competition. They may take into account the fact that certain agreements will provide incentives for competition, but the reasoning that a prohibition of the practice under consideration would produce even less desirable effects is not regarded as a valid excuse[175]. Third, measures unique to EEC legislation and unknown to American law, are the exemption procedures provided by article 85-3. In fact, article 85 consists of three paragraphs, and must be considered in conjunction with Council Regulations 17/62 and 19/65[176].

E/ The EEC Exemption System

We have just examined article 85-1. Article 85-2 states simply that *"any agreements or decisions prohibited pursuant to this article shall be automatically void"*. Thus, the provisions contained in article 85-1 are *ab initio*. The violations are automatically and immediately prohibited, and

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[174] But this original view may be altered. It may happen that, conversely, the rule of reason be applied positively so that an agreement or practice which is normally *per se* illegal is deemed reasonable by virtue of special circumstances. This is nevertheless an exception to the principle. See CALLMAN, supra note 5, c.4 at 106.

[175] See ALEXANDER, *Brevets d'Invention et Règles de Concurrence du Traité CEE* (1971) at 61; also *American Column & Lumber Co. v. US* 257 US, 377 [1921].

[176] Respectively, OJ 1962, 204 and OJ 1965, 533.

there is no need for the Commission or the Court to declare them to be so.

An agreement that falls within article 85-1 of the Treaty is not necessarily automatically void as article 85-2 states. A broad range of agreements which restrict competition may be permitted because of the beneficial effects they produce by virtue of an exemption granted by the Commission under article 85-3. The Commission may declare article 85-1 inapplicable by means of an individual exemption, provided that the agreement or practice in question satisfies four requirements: it must contribute to improving the production or distribution of goods or to promoting technical or economic progress[177]; it must allow consumers a fair share of the resulting benefit[178]; it must not impose upon the relevant undertakings any restrictions which are not indispensable to the attainment of the objectives specified in the previous two conditions; and, it must not afford the relevant undertakings the possibility of eliminating competition in respect of a substantial part of the products in question[179].

The competition provisions of the Treaty are implemented by Regulation 17/62. Article 4-{2} of the Regulation refers to licences of intellectual property rights, and count them among agreements which may benefit from exemptions. In addition, Council Regulation 19/65 gives power to the Commission to issue block exemption for certain categories of agreements and concerted practices, thus envisaging exemptions on a

177 See *Metro-SB Grossmarkte v. Commission* [1977] E.C.R. 1875.

178 See *VBBB v. Commission* [1984] E.C.R. 19.

179 See *Van Landewyck v. Commission* [1980] E.C.R. 3125; and more generally on that issue EVANS, "European Competition Law and Consumers: The Article 85-3 Exemption" [1981] 2 E.C.L.R. 425.

generic basis. A block exemption takes the form of a Regulation which describes certain restrictions of competition which, although falling within article 85-1, are exempted. It also provides a list of "black" provisions, the inclusion of which in an agreement will remove it from the benefit of the exemption[180]. To benefit from a block exemption, an agreement must be of the generic type envisaged by the Commission when producing the Regulation in question. Among others, the Commission has issued block exemptions relating to specialisation agreements, exclusive distribution agreements, exclusive purchasing agreements, franchise agreements, and as we shall see further, on patent and know-how licensing[181].

The absence of such exemptions procedures in US antitrust laws can be justified by the fact that US law regards licence agreements as *prima facie* lawful. But, by virtue of the *per se* approach or the rule of reason, they may turn out to be violative of the Sherman Act. Conversely, EEC law considering license agreements as *prima facie* anti-competitive, it must provide exemptions for those agreements which indeed are much more beneficial for competition than they appear.

Whether licenses of intellectual property rights are harmful or beneficial to free competition is the topic of our next section.

180 The Commission may also issue "negative clearance" for agreements which do not fall within article 85-1. The difference with an 85-3 exemption which, after noting that the agreement is likely to distort competition, declares article 85-1 inapplicable, is that a negative clearance merely emphasises that the agreement needs no exemption since it is not capable of being caught by article 85-1.

181 Respectively, Regulation 417/85 O.J 1985 L.53/1, Regulation 1983/83 O.J 1983 L.173/1, Regulation 1984/83 O.J 1983 L.173/5, Regulation 4087/87 O.J 1987 C.214/2, Regulation 2349/84 O.J 1984 L.219/15, Regulation 556/89 OJ 1989 L.61/1.

Section 2 : Intellectual Property Licensing

A licensing agreement is an important form of contract. As its name indicates, such an agreement gives the licensee permission to use intellectual property rights. Licensing agreements are extensively used in modern industrialized countries, and great economic interests are attached to them. The general principles of antitrust laws previously described are potentially applicable to licenses of intellectual property rights. The test for the application of article 85-1 is the same as it is with any other agreement, namely whether the licence or any of its provisions may adversely affect trade between Member States and prevent, restrict, or distort competition within the Common Market to an appreciable extent. If article 85-1 does apply to the agreement in question, there remains the possibility of obtaining an exemption under article 85-3. American antitrust law has taken a special interest in patent licensing agreements, and within this area of law *per se* prohibitions and the rule of reason have been employed.

A/ Know-How, Trademark and Copyright Licenses

Any kind of intellectual property right can be licensed. Thus, it is common for the owner of a trade secret or particular know-how to make it available to another party in exchange for a royalty calculated on production using the information[182]. Know-how agreements are frequently, but not necessarily, coupled with patent licenses, and in general the Commission treats the restrictions in know-how licences as falling within

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[182] As an alternative to obtaining a patent, an inventor may decide to keep his invention or discovery secret. The advantages are that he does not have to disclose his invention to the public at large and it does not become available by falling into the public domain after 17 or 20 years (as with patents). On the other hand, he has no adequate protection if someone else independently arrives at the same invention or if it becomes known by means other than a breach of confidence.

article 85-1. However, a draft block exemption for such licences was issued in 1987[183]. Thus, a mere obligation to keep know-how confidential is not caught by article 85-1, nor is a reciprocal obligation to communicate improvements or a grant of non-exclusive licences to use such improvements. Under US law too, the disclosure of the trade secret or know-how is the consideration for the royalty[184]. However, unlike patent licensing, the corresponding law regarding confidential information is unsettled in the United States. Restrictions in such licences are generally permissible if they are ancillary to a legitimate business purpose[185].

A license from a trademark owner may be necessary primarily because it allows use of the mark which would otherwise constitute an infringement. Also, without a license, there would be no centralized control over the product or service received. This, in turn, would eventually result in the public's inability to rely on a certain trademark as indicative of either the product's source or its quality. The very purpose of a trademark would thereby be thwarted[186].

Trademark licenses generally occur in distribution or franchise networks, and also in connection with know-how or patent licences, sale of businesses or joint venture agreements. The exercise of licensed trademark

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183 O.J 1989 L.61/1.

184 See *Hooker Chemical Corp. v. Velsico Chemical Corp.* 235 F.Supp. 412 [1964].

185 See *A & E Plastik Co. v. Monsanto Co.* 396 F.2d, 710 [CA 9th. 1968].

186 Trademarks are words, names, symbols or devices, separately or in combination, adopted, used, or intended to be used by a manufacturer or trader to identify his goods or services and to distinguish them from those manufactured or sold by others. However, the property in a trademark is closely linked to its use; *"It is not an article in commerce in the sense that it may be consumed by the consuming public. It is property only when used to indicate the origin or ownership of goods."*; MEINERS & STAAF, "Patents, Copyrights and Trademarks: Property or Monopoly ?" 13 Harvard J. L. & Public Policy. 911 at 930. See generally "Restrictive Business Practices Relating to Trademarks" O.E.C.D. Report. [1978].

rights to prevent the importation of lawfully marked goods from another Member State may be contrary not only to articles 30/36 as seen earlier, but also to article 85-1[187].

In the United States, trademark licences are held lawful, but the Supreme Court will apply the rule of reason where a manufacturer - licensor seeks to restrict and confine areas or persons with which a trademarked article may be traded after the manufacturer has parted with dominion over it[188]. Trademark licenses that allocate exclusive territories among competitors have been held illegal *per se*[189].

Copyrights or similar protection may exist in many different creations, including literary and artistic works, sound recordings, motion pictures, TV broadcasts, or industrial designs. The only occasion when the European Court of Justice has considered a copyright licence under article 85 was the *Coditel* case, where it was held that an exclusive licence to exhibit a film did not infringe article 85-1[190]. However, the Court left open the possibility that article 85-1 might apply in the event of unreasonable exploitation of the right:

> *...it is for the national courts... to establish whether or not the exercise of the exclusive right to exhibit a cinematographic film creates barriers which are artificial and unjustifiable in terms of the needs of the cinematographic industry, or the possibility of charging fees which exceeds a fair return on investment, or on exclusivity the*

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187 See *Consten & Grunding v. Commission* [1966] E.C.R. 299; *Sirena v. Eda* [1971] E.C.R. 69.

188 See *Continental TV v. GTE Sylvania* 433 US, 36 [1977].

189 *US v. Topco Associates Inc.* 405 US, 596 [1972]; See also *Timken Roller Bearing Co. v. US* 341 US, 593 [1967], where the Supreme Court has rejected the position that a horizontal arrangement can be justified if it occurs in the context of a trademark licensing agreement.

190 [1982] E.C.R. 3381.

> *duration of which is disproportionate...and whether...such exercise...is such as to prevent, restrict, or distort competition within the Common Market.*[191]

Transfer of copyright ownership is defined by the US Copyright Act as "*an assignment, mortgage,* ***exclusive licence*** *or any other conveyance, alienation or hypothecation of a copyright or any of the exclusive rights comprised in a copyright*"[192] (emphasis added). As to the implications for such copyright licenses of antitrust law, US courts apply section 1 of the Sherman Act in the same manner as they apply it to other intellectual property rights licences[193].We shall focus here on patent license agreements.

B/ Patent Licenses

The relationship of the monopoly granted to inventors to the basic principles of antitrust laws has long been, and is still, the source of questions and debates. Specific problems arise with respect to restriction clauses included in the agreements. In this respect, the view of the EEC has been influenced by American treatment of the matter. This can be seen from the way the Commission has dealt with restrictions in patent licensing agreements. In American law, a number of decisions have been made on which restrictions could be tolerated in licensing agreements and which restrictions would be regarded as illegal under section 1 of the Sherman

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[191] *Ibid* at 3384.

[192] 17 USC. s.101 (1976).

[193] See generally BROWN, *Copyright, Unfair Competition and Other topics Bearing on the Protection of Literary, Musical and Artistic Works* (1974).

Act[194]. When the EEC Commission received a number of applications as a result of the introduction of the exemption system, it published a Patent Notice known as the "Christmas Message"[195]. In that document, the Commission stated that the terms and conditions of patent licensing agreements were not affected by the prohibition in article 85-1. The terms and conditions listed were exactly the same restrictions as were legal in the United States. However, the Commission later parted from the US view, as it had some difficulties regarding the most appropriate manner of considering certain aspects of licensing agreements in connection with Community Law. This hesitancy is especially reflected in the change of attitude of the Commission toward patent licensing agreements, where the fear that their effects will be a means which prevents the maintenance or establishment of a large common market has come to prevail with the new Regulation 2349/84 (block exemption for patent licensing agreements)[196], replacing the 1962 Patent Notice. We will study this block exemption after balancing the pros and cons of patent licenses with respect to free competition.

A few common and fundamental principles of the legal systems of the USA and the EEC merit emphasis. In both systems, the purpose of patent legislation is to confer the exclusive rights on inventors to make, use, and sell their inventions within a limited period of time. At the same time, the principal purpose of the patent system is to promote technology by

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194 See *US v. General Electric* 272 US, 476 [1926]; *Andrea v. RCA* 14 F.Supp. 226 [1936]; *General Talking Pictures v. Western Elec. Co.* 305 US, 124 [1938]; *RCA v. Hygrade Sylvania Corp.* 10 F.Supp. 879 [1934]; *US v. Besser Mfg Co.* 96 F.Supp. 304 [1951]; *Brulotte v. Thys Co.* 379 US, 29 [1964]; *Ethyl Corp. v. Hercules Powder Co.* 232 F.Supp. 453 [1963].

195 As described earlier at p.71.

196 O.J 1984 L.219/15.

encouraging innovation and its publication. In parallel, the USA and the EEC wish to promote innovation by recourse to patent laws, but meanwhile wish to promote competition through antitrust legislation. Would it be possible to imagine that the patent system - which aims at creating monopolistic positions by virtue of a right to exclude others - can exist side by side with monopoly rules which are intended to combat monopolies? Indeed, the basic view in the USA is like that in Europe, namely that patents in themselves are not detrimental to the competition system to the extent that they should be offset by antitrust laws[197]. Both systems consider that although the patent right allows the patentee to prevent others from making, using, and vending the invention in question, it does not mean that the patentee is conferred a monopoly right. Often, a patent will only give its owner a very limited market power, and it will by no means create a monopoly in economic sense. Legally speaking, property rights confer upon their owner a certain exclusivity. However, market power is not determined by law, but rather by the economic rules of the market related to the demand for the product in question. We have already seen that demand is subject to the existence of substitute products. Patented goods may therefore have to compete on a given market with other inventions that serve the same purpose, in which case a monopoly cannot be said to exist[198].

[197] See MACHLUP, "An Economic Review of the Patent System" Study No 15 of the Sub-Committee on Patents, Trademarks and Copyrights of the Committee on the Judiciary, US Senate, 85th Congress, 2nd Session, Washington D.C. [1958]; ROSEN, "Competition Policy and Intellectual Property" [1989] 3 Antitrust. 32; LEHMANN, "Property and Intellectual Property: Property Rights as Restrictions on Competition in Furtherance of Competition" [1989] 20 I.I.C. 1.

[198] See generally on this topic LEHMANN, supra note 197; GELLHORN, *Antitrust Law and Economics in a Nutshell* (1981); LANDES & POSNER, "Market Power in Antitrust Cases" [1981] 94 Harv. L. Rev. 937; LAVEY, "Patents, Copyrights and Trademarks as Sources of Market Power in Antitrust Cases" [1982] 27 Antitrust Bull. 433.

Another crucial consideration, taken into account by competition systems of both the EEC and the USA, is that though the patent may give the patentee an important exceptional position, it can be to the advantage of individual consumers and society at large. Patent rights may help a new enterprise or a new product to overcome barriers which would otherwise prevent free access to a particular market[199].

As regards license agreements, it is commonly recognized that such contracts do not necessarily harm competition. A recent OECD report listed five consequences of licence agreements restriction clauses that were beneficial to competition. Patent licensing helps to maximize profits, contribute to the development of technology and stimulate demand, improve the management of risks and transaction costs[200], provide means to maintain reputation and quality[201], and secure effective productivity. As long as profit maximization permits a widespread dissemination of technological progress, productivity and consumers' welfare are improved[202]. In other words, intellectual property rights give a monopoly to their owners over their exploitation, and thanks to licences of rights, this monopoly can be shared. Production and distribution of particular goods or services will therefore increase, enabling a greater number of consumers to benefit from the products. Hence, it may be argued that any

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199 See generally BOWMAN, *Patent and Antitrust Law: A Legal and Economic Appraisal* (1973) at c.2.

200 By sharing risks and diminishing costs, profits are increased, allowing a wider distribution of the patented goods.

201 For instance, a licensor may ensure that the licensed product will be properly manufactured or marketed by imposing to the licensee the purchase of an ancillary product, necessary to the functioning or efficiency of the licensed product. We shall see further that such "tying-in" practices may have adverse effects on competition.

202 "Politique de Concurrence et Propriété Intellectuelle" O.E.C.D. Report [1989] at 19-25.

limitations in licence agreements do not constitute "restrictions", but merely determine the extent of the license: such limitations should not be prohibited. American antitrust laws rest on such an assumption[203]. That American approach was the one adopted in the 1962 Patent Notice, but the EC Commission's present position involves a rejection of the "limited licence" concept[204]. For instance, limitations as to the quantity of goods to be produced is regarded as a "restriction", falling under article 85-1, as well as a geographic delimitation for the sale of the licensed product. The Commission also considers the fact that certain restrictions indirectly affect competition by damaging the competitiveness of licensees. In *AOIP v. Beyrard*[205], and *Windsurfing International v. Commission*[206], the Commission objected to various methods of royalty calculation on the grounds that the method chosen could affect the competitiveness of the licensee, by placing the latter at a competitive disadvantage.

Competition authorities must also be aware that an absolute ban on restriction clauses might discourage licensing. From the point of view of either the licensor or the licensee, some restrictions on the freedom of the other party may be an essential condition for entering into the agreement. Thus, where a licensee is incurring heavy costs and risks, he legitimately expects to be granted exclusivity and may not take a licence on any other

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203 See *Windsurfing Int'l Inc. v. AMF Inc.* 782 F.2d, 995 [1986]; *Continental TV v. GTE Sylvania Inc* 433 US, 36 [1977]; and generally FINNEGAN, *The Law and Business of Patent and Know-How Licensing* (1978); BAXTER, "Legal Restrictions on Exploitation of the Patent Monopoly: An Economic Analysis" [1966] 76 Yale L. J. 62.

204 See *Windsurfing International v. Commission* [1984] 1 C.M.L.R. 1.

205 [1976] 1 C.M.L.R. D.14.

206 [1984] 1 C.M.L.R. 1. For a comparison of the US *Windsurfing* case and the European *Windsurfing* decision, see ROSEN, "Licensing Restrictions in the United States and the EEC" [1986] 55 Antitrust L. J. 383.

basis. Equally, a licensor might be more willing to give a licence if he can keep a licensee out of his territory. Therefore, there is a conflict where the restrictions imposed by the terms of the agreement distort competition and at the same time foster the dissemination of a new technology and its exploitation[207]. US and EEC competition authorities must be very cautious when balancing those conflicting issues[208].

However, patent licensing agreements, as well as restriction clauses they may include, can have anti-competitive effects. Concerted practices may result from such licenses, and can become a means to fix prices, limit production, or divide up markets[209]. Restriction may also close markets and set apart or eliminate actual or potential competitors[210]. Thus, experience has shown that agreements and restriction clauses on the part of enterprises can result in serious interference in the freedom of competition.

In the light of these considerations, US courts apply the *per se* concept as well as the rule of reason to determine which licences or which restriction clauses are detrimental or beneficial to competition. The EC

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207 See *Velcro/Aplix v. Commission* [1985] 4 C.M.L.R. 157.

208 Particularly in the EEC, the specific subject-matter of the right at issue, as already stated, is the criteria on which the Commission and the Court rely to draw a distinction between the existence and the exercise of intellectual property rights, and thus determining whether the agreement or practice is caught by the prohibition set out in article 85-1. Precise and accurate definitions of these subject-matters therefore constitute decisive factors. See Commission's Fourth Report on Competition Policy (1975) at No 20; and JOHANNES, "La Propriété Industrielle et le Droit d'Auteur dans le Droit des Communautés Européennes" [1973] R.T.D.E. 369.

209 It is especially relevant to draw a distinction between vertical and horizontal agreements; it is generally recognized that the former are not as anti-competitive as the latter, and both US and EEC legislation are more lenient with respect to vertical arrangements. See *US v. A.Schwinn Co.* 388 US, 365 [1967]; *Consten & Grunding v. EC Commission* [1966] E.C.R. 429. We shall see further, however, that certain vertical conducts are as dangerous as horizontal ones. See HAWK, supra note 63 at c.10.

210 O.E.C.D. Report [1989] supra note 202 at 25-30.

Commission and the European Court of Justice also have to decide whether a licence agreement, or its specific clauses, fall within article 85-1, and if so, whether they are eligible for an exemption. Given the number of agreements entered into every day and referred to the competition authorities, the Commission undertook to issue guidelines defining in advance the kind of restrictions that it would consider contrary to the Treaty. A good example of such guidance is provided by the draft block exemption of 1984 on patent licences[211]. The adoption of Regulation 2349/84 is the last major step in a series of developments which started in 1962 with the publication of the Notice on Patent Licensing Agreements[212].

C/ EEC Regulation 2349/84[213].

This Regulation provides an exemption under article 85-3 for certain patent licences and agreements combining patent and know-how licences ("mixed agreements") which are capable of falling within the scope of article 85-1[214]. Thus, article 1 of the block exemption declares article 85-1 inapplicable to licence clauses imposing obligations on the licensor not to license other undertakings to exploit the licensed invention, or to exploit it himself, in the licensed territory "*in so far and as long as one of the licensed patents remains in force*"(article 1-1{2}). Also exempted are obligations on the licensee not to exploit the licensed patent in territories

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211 Regulation 2349/84 of 23 July 1984 on the application of article 85-3 to certain categories of patent licensing agreements. O.J 1984 L.219/15; See appendix C.

212 O.J 1962 C.139/2922.

213 See generally ALEXANDER, "Block Exemption for Patent Licensing Agreements: EC Regulation 2349/84" [1986] 17 I.I.C. 1; and KORAH, *Patent Licensing and The EEC Competition Rules - Regulation 2349/84* (1985).

214 Pure know-how licensing arrangements are governed by their own block exemption, but an ancillary trademark licence or registered user agreement is also covered by the Regulation; see *Hydrotherm v. Compact* [1984] E.C.R. 2999.

reserved to other licensees or to the licensor (article 1-1{3}/{4}), and not to pursue an active sale policy in these territories (article 1-1{5}). Interestingly, a distinction is drawn between restrictions on manufacture and use on the one hand, and restrictions on sales on the other. Manufacturing or using the licensed products in territories where they are already exploited by the licensor or other licensees can be prohibited by the terms of the agreement. As regards sales, a further distinction is made between active sales (whether the licensee pursues a policy of active sales promotion, in particular whether he engages in advertising or establishes branches or distribution depots) and passive sales (where the licensee merely responds to orders received). Whereas the former can be lawfully prohibited, a limitation on passive sales is more likely to be caught by article 85-1. However, article 1-1{6} of the Regulation provides that the licensee may be restricted from marketing the licensed product in other licensees' territories for five years from when the product was first marketed in the Community by the licensor or with his consent. It appears that this five-year prohibition applies to passive sales as well, in so far as they do not occur in the licensee's own territory. Indeed, both active and passive sales can be restrained for so long as parallel imports remain in force. Finally, article 1-1{7} permits an obligation on the licensee to use only the licensor's trademark or get-up, "*provided that the licensee is not prevented from identifying himself as the manufacturer of the licensed products*".

Article 2 enumerates a list of provisions which are generally not restrictive of competition, such as an obligation on the licensee to procure from the licensor goods or services if they are "*necessary for a technically* *satisfactory exploitation of the licensed invention*", a minimum royalty or minimum quality or quantity to be produced, a restriction on the exploitation of the patent right to certain fields of application covered by the latter, an obligation on the licensee not to grant sub-licences or not to disclose know-how communicated by the licensor. The licensee may also be required to take steps against an infringer of the licensed patent. The clauses enumerated in this "white" list may nevertheless fall within article 85-1 in certain circumstances, and may also benefit from an exemption under article 1.

Pursuant to article 5, agreements related to patent pools or joint ventures are excluded from the scope of the Regulation, as are plant breeders' rights and agreements whereby parties grant to each other "*reciprocal patent or trademark licences or reciprocal sales rights for unprotected products or exchange know-how, where the parties are competitors in relation to the products covered by those agreements*". The Commission may withdraw the benefit of the block exemption if an agreement, although exempted under the Regulation, nevertheless is found inconsistent with article 85-3, as the result of an arbitration award, if there is a lack of effective competition between licensed products and identical or equivalent goods or services, if the licensor cannot terminate the exclusivity granted to the licensee within five years in the event of non-exploitation of the invention by the latter, or if parallel imports are obstructed[215].

It must be borne in mind that for an exemption under the Regulation to be granted, it is crucial that the licence agreement not be tainted with

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215 Articles 9(1), 9(2), 9(3), 9(4), 9(5).

any of the matters referred to in article 3. Article 3 provides a "black" list of restrictions which cannot benefit from article 1 exemption because of their intrinsic anti-competitive nature. Among them, we may cite clauses prohibiting the licensee from challenging the validity of the licensed patent, provisions prolonging the duration of the licence beyond the expiry of the patent right, non-competition clauses, limitations on quantities to be produced, price or customer restrictions, grant-back and improvements clauses, or tying obligations. Obviously, the net effect of those provisions is to treat territorial restrictions as *prima facie* unlawful, subject to possible exemptions.

This view is contrary to the American approach where territorial restrictions are held lawful *per se*. It is a fundamental principle of US patent law that a licensing agreement is lawful so long as it merely transfers all or part of the patentee's rights under his patent rather than purporting to enlarge his monopoly[216]. Thus, under US law, the right to grant territorially exclusive licenses is an inherent part of the patent monopoly[217]. Underlying this principle is a policy whereby it is thought that a properly limited restraint merely restricts competition which would not exist at all without a license. If territorial restrictions are not permitted, the patentee may decide not to license. Another noteworthy difference between EEC and US policies concerns quantity restrictions They are blacklisted in the Commission's Regulation, whereas they are legal under US law.

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216 See *Int'l Salt Co. v. US* 332 US, 392 [1947]; As early as 1836, section 261 of the Patent Act already stated that a patentee *"may grant and convey an exclusive right under his application for patent... to the whole or any specified part of the United States"*.

217 See *Bloomer v. Mc Quewan* 55 US, 539 [1852]; *Browmell v. Ketcham Wire Co.* 211 F.2d, 191 [1954]; *Dunlop Company Ltd v. Kelsey Hayes Co.* 484 F.2d, 407 [6th Cir. 1973].

By contrast, Regulation 2349/84 is in accord with US law on the issue of field of use restrictions. They are deemed not restrictive of competition in article 2(3) of the Regulation, and were held lawful *per se* as early as 1938 in the USA, in the Supreme Court's decision in *General Talking Co. v. Western Electric Co.*[218].

Further details on these kinds of clauses are to be provided in the next chapter, where we shall survey several licence clauses typically found in patent, know-how, trademark or copyright licenses, and toward which the EEC and US authorities have adopted a negative attitude or shown approval.

CHAPTER II : SPECIFIC CLAUSES IN LICENCE AGREEMENTS

Section 1 : Exclusivity and Restriction Clauses

Serious problems have been caused by agreements containing restrictions on territory or customers, such as agreements prohibiting a dealer from selling outside his territorial area or selling to specific categories of customers. Similar restrictions may also impose on production quantities, sale prices, or intellectual property rights fields of use. Such restrictions are vertical ones, and vertical agreements are generally regarded as harmless for competition. However, where a manufacturer establishes an allocation of territory or customers among his dealers, the effect is, in substance, a restraint of competition between the dealers. In this respect, a vertical agreement may have the same effect as a horizontal one.

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218 305 US, 124 [1938]; this decision was antedated by *Rubber Co. v. Goodyear* 76 US, 788 [1869].

A/ Territorial and Customer Restrictions

We have seen earlier how such clauses are capable of concurrently restricting competition and fostering the development and exploitation of technology (and thereby ensuring a fair advantage to consumers). It is the function of Regulation 2349/84 to balance these two characteristics. Community Law does not permit a licensee to enjoy absolute territorial protection, but a limited degree of exclusivity and some partial territorial protection is possible. Indeed, the reasoning followed by the Commission when drafting the Regulation on patent licences appears to be consistent with the views of the Court with respect to exclusivity and restriction clauses, as stated in the *Nungesser* case (also known as the *Maize Seed* case)[219].

In *Nungesser*, the French institute INRA held plant breeders'rights related to a new variety of maize seed, and licensed Eisele in West Germany for the production and sale of the product in that country. The agreement granted Eisele exclusive protection by means of restrictive clauses. It was agreed that INRA and its other licensees would prevent third parties from exporting the relevant seeds to Germany without Eisele's authorization, and would also refrain from having the seeds produced or marketed by other licensees in Germany, or by any other licensee in the Common Market. The Commission opposed all three clauses, relying on the *Consten & Grunding* case with respect to the restriction on third parties' export, and took the view that the licensing of a single undertaking in a single territory was inherently anti-competitive[220]. The Court drew the same distinction as

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[219] *Nungesser KG v. Commission* [1982] E.C.R. 2015.

[220] [1966] E.C.R. 299.

between the first clause and the two others, but accepted the argument raised by Eisele that the grant of exclusive rights for a limited period is capable of providing an incentive to innovative efforts:

> *...in the case of a licence of breeder's right over hybrid maize seeds newly developed in one Member State, an undertaking established in another Member State which was not certain that it would not encounter competition from other licensees for the territory granted to it, or from the owner of the right himself, might be deterred from accepting the risk of cultivating and marketing that product; such a result would be damaging to the dissemination of a new technology and would prejudice competition in the Community between the new product and similar existing products...The Court concludes that...the grant of an open exclusive licence, that is to say a licence which does not affect the position of third parties such as parallel importers and licensees for other territories, is not itself incompatible with article 85-1 of the Treaty.*[221]

As regards the first restriction, the Court upheld the Commission's view and found that a licence which is not open but which eliminates competition from third parties will fall under article 85-1:

> *The Court has constantly held...that absolute territorial protection granted to a licensee in order to enable parallel imports to be controlled and prevented results in the artificial maintenance of separate national markets, contrary to the Treaty.*[222]

Thus, territorial restriction clauses provide incentives for innovation, but they should not be employed as a means to distort competition or affect trade. Hence, absolute territorial protection is banned.

The position of the Court in *Nungesser* with respect to territorial exclusivity and restriction clauses is be applied to other intellectual

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221 [1982] E.C.R. 2069.

222 *Ibid* at 2070.

property rights and other restrictions. For example, a similar standpoint was adopted in relation to an exclusive license to broadcast a motion picture[223]. Equally, an exclusive licence of know-how which restricts the area in which the licensee may manufacture or sell products , even if passive sales are permitted, will fall under article 85-1[224], and the grant of an exclusive trademark licence may also give rise to an absolute territorial protection[225]. Thus, it can be said that exclusive territorial restriction are *per se* illegal under EEC law. The European Community remains adamant in its opposition to territorial protection primarily because of the political goal of single market integration.

American law is not so strict on that point. In fact, there is a principle and an exception. The principle is that territorial restrictions are not *per se* illegal, but subject to the rule of reason. The exception, as already stated, is that territorial restrictions included in patent licenses are *per se* lawful. It took three decisions for the Supreme Court to set out that principle. It was first held in the *White Motor* case that territorial and customer restrictions were vertical agreements and, as such, could not be allowed under a *per se* approach, as it was with horizontal arrangements. The Supreme Court's viewpoint was that such restrictions could in no way be compared with similar horizontal restrictions[226]. However, this view was reversed four years later in the *Schwinn* case[227]. The Supreme Court

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223 *Coditel v. Ciné Vog Films* [1982] E.C.R. 3381.

224 *Windsurfing International v. Commission* [1984] 1 C.M.L.R. 1.

225 *Consten & Grunding v. Commission* [1966] E.C.R. 299; *Campari v. Commission* [1978] 2 C.M.L.R. 397.

226 *White Motor Co. v. US* 372 US, 253 [1963].

227 *US v. Arnold Schwinn & Co.* 388 US, 365 [1967].

found it appropriate to declare territorial protection illegal *per se*: "*Where a manufacturer sells products to his distributor subject to territorial restrictions upon resale, a per se violation of the Sherman Act results*"[228]. Hence, horizontal and vertical restrictions were to be given the same treatment. But the *Schwinn* decision was widely criticized[229]. There was eager anticipation of a reversal by the Supreme Court in the subsequent *Sylvania* case of 1977[230]. Sylvania produced television sets and sold them to independent wholesalers, who resold them to a large number of retailers. From 1962, Sylvania reconstructed its marketing strategy and started to sell its products directly to a smaller, selected group of retailers. Sylvania required of its dealers that television sets were to be marketed only from recognized locations. A dispute arose between Sylvania and one of its retailers, Continental TV. The latter claimed that Sylvania had violated section 1 of the Sherman Act by making and enforcing distributor agreements banning the sale of Sylvania products outside their specific locations. The District Court and the Court of Appeals followed the *Schwinn* trend, but the conclusion of the Supreme Court was that the *per se* rule applied in *Schwinn* had to be overruled. Since the *Sylvania* decision, the American judicial practice has consequently been that vertical territorial and customer restrictions are subject to the rule of reason.

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228 *Ibid* at 379.

229 See POLLOCK, [1968] 63 Nw. U. L. Rev. 537; AVERILL, [1969] 15 N. Y. L. F. 39; BAKER, [1975] 44 Antitrust L. J. 537; Mc LAREN, [1968] 37 Antitrust L. J. 137; POSNER, [1975] 75 Colum. L. Rev. 282. Furthermore, many inferior courts refrained from making judgments in accordance with the *Schwinn* decision, in spite of its clear and extensive wording. See e.g., *Janel Sales Corp. v. Lanvin Parfums Inc* 396 F.2d, 398 [2nd Cir. 1968]; *Goods Investment Promotion Inc v. Corning Glass Works* 493 F.2d, 891 [6th Cir. 1974]; *Colorado Pump & Supply Co. v. Febco Inc.* 472 F.2d, 637 [10th Cir. 1973].

230 *Continental TV v. GTE Sylvania Inc* 433 US, 36 [1977].

In parallel, section 261 of the Patent Code which declares that the patentee may convey an exclusive right under his patent *"to the whole or any specified part of the United States"*, has been interpreted to mean that it is legal to divide American territory geographically through the grant of patent licenses for restricted areas. Thus, territorial restrictions have been held legal *per se*[231].It is, however, agreed that if reciprocal patent licensing agreements contain territorial restrictions that may form part of a large cartel arrangement with a view to dividing markets, those clauses are not included in the principle of section 261 of the Patent Code, but can be comprehended by the prohibitions of the antitrust legislation[232]. The basic idea here is that American patent law entitles the patentee to grant territorial licenses as part of his patent monopoly. It is important to note that territorial restrictions are considered legal under patent law, which means that antitrust legislation is not relevant to such licenses. It has nevertheless been pointed out that the consequence of antitrust law would be the same because of the recognized ancillary restraint doctrine[233].

There is thus a difference between the American approach based on the the traditional attitude to exclusive licenses as permissible, and the attitude of the EC Commission which has been that exclusive licenses are in contravention of article 85-1. However, certain remarks concerning the

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231 See among others *Dunlop Cpy Ltd v. Kelsey-Hayes Co.* 484 F.2d, 407 [6th Cir. 1973]; *Browmell v. Ketcham Wire Co.* 211 F.2d, 121 [9th Cir. 1954]; *American Optical Co. v. New Jersey Optical Co.* 58 F.Supp. 601 [D.Mass. 1944]; *US v. Crown Zellerbach Corp.* 141 F.Supp. 118 [ND Ill. 1956].

232 See LADAS, "Licensing Agreements on Know-How in The USA" [1972] 3 I.I.C. 335. As the EEC Regulation 2349/84 on patent licensing agreements does not include reciprocal patent licensing of any kind (see article 5(1)(3)), this aspect of territorial restrictions will not be dealt with.

233 See HANDLER & BLECHMAN, "The Proposed EC-Group Exemption for Patent Licenses: A Comparison with the US Antitrust Law" [1980] 11 I.I.C. 295 at 298. And on the ancillary restraint concept, see the *Addyston Pipe* case 175 US, 211 [1899].

opinion of the European Court of Justice on this topic should be made. In the *Maize Seeds* case, the Court declared that exclusive licenses are not generally in contravention of article 85-1, but may be so. Moreover, the European Court of Justice has clearly avoided taking a position on whether the clause in the agreement under consideration could have been exempted pursuant to article 85-3[234].

It must finally be noted that, under US law, there appears to be no distinction between territorial and customer restrictions, as underlined in *Sylvania*[235]. That distinction is, however, relevant in EEC law. Customer restrictions, whereby a licensee is not free to sell to the customers of his choice, are deemed to violate article 85-1, and are almost never eligible for exemptions. Such restrictions are blacklisted in Regulation 2349/84 (unlike territorial restrictions which can be exempted).

B/Price Fixing and Quantity Restrictions

As for price restrictions, US and EEC law are only in accord as long as patent rights are not involved. The American approach is a *per se* prohibition of price agreements between competitors[236]. As to vertical agreements, the Supreme Court stated in 1911 that resale price maintenance agreements between a manufacturer and his dealers were void[237]. Price-fixing agreements are also categorically prohibited by article 85-1{a} which makes no distinction between horizontal and vertical agreements. By its

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234 A similar careful attitude is also observed under the *Coditel* case, supra note 74.

235 433 US, 46 [1977].

236 See *US v. Trans-Missouri Freight* 166 US, 290 [1897]; *Addyston Pipe & Steel Co. v. US* 175 US, 211 [1899]; *US v. Trenton Potteries Co.* 273 US, 391 [1927]; *US v. Socony-Vacuum Oil Co.* 310 US, 150 [1940].

237 *Dr Miles Medical Co. v. Pak & Sons Co.* 220 US, 373 [1911]; also *Monsanto Co. v. Spray-Rik Service Co.* 465 US, 752 [1984].

very nature, such an arrangement constitutes a restriction on competition within the meaning of both section 1 of the Sherman Act and article 85-1 of the EEC Treaty[238]. However, article 85-1 may be infringed by mere price recommendations, whereas the US Supreme Court recognized the legality of price recommendations in *US v. Colgate & Co.*[239].

With respect to patent licensing agreements, Regulation 2349/84 blacklists vertical price agreements, and this prohibition is contrary to the US Supreme Court's 1926 decision in *US v. General Electric Co.*[240]. The Supreme Court ruled that a patent license agreement which required the manufacturing licensee, in its sales of the patented article, to conform to the licensor's sale prices schedule was lawful. This right of the patentee does not rest upon the patent statute, but is justified because it is necessary to secure pecuniary reward to the patentee's monopoly. The *General Electric* case, therefore, applies the rule of reason to price fixing agreements included in patent licences[241].

Restrictions may also be imposed on quantities of licensed goods to be produced. A minimum quantity restriction generally does not fall within article 85-1, since the object of such a clause is usually to ensure an adequate exploitation of intellectual property rights. On the other hand, a maximum quantity requirement prevents the licensee from increasing his

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238 However, exemptions under article 85-3 have been granted in exceptional circumstances in certain service industries. See *Nuovo CEGAM* [1984] 2 C.M.L.R. 484.

239 250 US, 300 [1919].

240 272 US, 476 [1926].

241 In *US v. Line Material Co.* 333 US, 287 [1948], the Supreme Court limited the licensor's right to restrict the manufacturing licensee's sale price to situations where only one licensee is involved and neither the licensor nor the licensee control any substantial part of the relevant industry.

output and may have an effect similar to an export ban (such quantity restrictions are included in Regulation 2349/84 black list). There is a striking difference between the European view and that of US law on quantities restrictions. As noted in *US v. E.I Dupont De Nemours & Co.*: *"The cases are to the effect that the owner of a valid product patent may by license restrict production of the licensee to a specified quantity, at a specified place"*[242]. Quantity restrictions are upheld in American cases because they are deemed to be inherent to the patent statutory monopoly[243].

C/ Field of Use Restrictions

In the case of field of use licenses, the licensee's use of the patented invention is restricted in one way or another, such as when the licensee may employ the patent for some purposes but not for others. Field of use restrictions is the term used for restrictions not directly concerning price, territory, or restrictions that do not amount to tying clauses, but which curtail the licensee's right to exploit the license he has been granted in one or more specific ways. Field of use restrictions, whereby a licensee is restricted in his exploitation of the licensed product, may be permitted if the restriction fits the technical field of application covered by a patent. Nevertheless, a prohibition from supplying a certain class of users, or employing certain forms of distribution, will be regarded as contrary to the Treaty. Similarly, a mere restriction on the use of a

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[242] 118 F.Supp. 41 [1953].

[243] See *Q-Tips Inc. v. Johnson & Johnson* 207 F.2d, 509 [3rd Cir. 1953], where it was held that quantity restrictions did nothing to improperly expand the scope of the patent monopoly.

trademark is deemed contrary to article 85-1[244], but an exemption is possible where such a clause is a reciprocal one between owners of identical or confusingly similar trademarks. These "delimitation agreements" are lawful and useful if they serve to delimit, in the mutual interest of the parties, the spheres within which their respective rights may be used and are intended to avoid confusion or conflict between them[245]. Hence, it can be said that it is under a rule of reason that the European competition authorities consider field of use restrictions.

The US Supreme Court's 1938 holding in *General Talking Pictures Co. v. Western Electric Co.* is the leading decision on field of use restrictions[246]. The patentee had granted a license for his patented amplifiers to be used in the "home" field, meaning that the license was not permitted to use the licensed amplifier in the "commercial" field. The Supreme Court held that this field of use restriction fell within the scope of the reward to which the patentee was entitled, and was therefore lawful. Thus, the validity of such restrictions under US law is justified by the fact that they are inherent in the patent right[247].

The European Commission takes the view that field of use restrictions may have consequences of a competition-reducing character. They can operate as territorial restrictions, price restrictions, or tying clauses. On

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244 *Sirdar/Phildar v. Commission* [1975] 1 C.M.L.R. D.93.

245 See *BAT v. Commission* [1985] E.C.R. 363; *Penneys v. Commission* [1978] 2 C.M.L.R. 100; *Persil Washing Powder* [1978] 1 C.M.L.R. 395. See also Commission's 7th Report on Competition Policy, at No 138.

246 305 US, 124 [1938].

247 See *A & E Plastik Pak Co. v. Monsanto Co.* 396 F.2d, 710 [9th Cir. 1968]; *Duplan Co. v. Deering Milliken Inc* 444 F.Supp. 648 [DSC 1977]; *Deering Milliken & Co. v. Temp-Resisto Co.* 274 F.2d, 626 [2nd Cir. 1960].

the other hand, field of use restrictions which reserve a territory for the patentee so that he can manufacture products himself or exploit the patent should not be censured. These are some of the reasons that the Commission did not consider field of use restrictions as illegal *per se*, and provided exemption possibilities under certain conditions. In this respect, the American approach is not very different. US courts consider that field of use restrictions only limit competition which would not exist otherwise, and also promote the development and dissemination of technology[248]. The most important distinction to be made between the American and the European views is, once again, that the latter regards field of use restrictions as *prima facie* anti-competitive, but is ready to grant exemptions, whereas the former makes the legality of these restrictions a principle, subject to certain exceptions under the rule of reason.

Section 2 : Non-Competition Clauses

The inclusion of a non-competition clause in an intellectual property rights license agreement is intended to prevent the licensee from competing with the licensor. For the purpose of this section, we shall include under the general heading of non-competition clauses no-challenge and grant-back provisions, which tend to achieve the same result.

A/ Covenants Not to Compete

Obligations that restrict the licensee in respect of the acquisition, manufacture, use or sale of competing products, or a restriction on the licensee preventing him from carrying out independent research and

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[248] It is thus held that patentees would be unwilling to license if they could not reserve some designated areas for themselves. See HANDLER & BLECHMAN, supra note 233 at 313; HANDLER, *Patents and Antitrust* (1983) at 82.

development, will normally fall within article 85-1 prohibition[249]. US law appears less categorical. Though non-competition clauses have been held unlawful in a number of cases, these decisions were generally justified by the fact that the obligation not to compete was disproportionate. For instance, in *Compton v. Metal Products Inc*, a patent license agreement provision that required the licensee not to engage in any activity relating to the manufacture or sale of equipment of the type exclusively licensed constituted misuse of the patent monopoly, since the agreement covered equipment which may not have embodied any of the patents[250]. On the other hand, where a covenant not to compete is made as an ordinary incident to enhance the value of the thing conveyed, it is not deemed to contravene section 1 of the Sherman Act[251].

B/ No-Challenge Clauses

A licensor may also impose on his licensee a non-challenge clause, meaning that the licensee is not allowed to challenge the validity of the patent right or trademark right he was licensed. Regarding such restrictions, EEC law is very similar to that of the USA. At the beginning of the black list in article 3 of Regulation 2349/84, no-challenge clauses are stipulated. Thus, they may not benefit from an exemption as they are deemed illegal *per se*. The Commission's position is in line with the European Court of Justice's decision in the *Raymond-Nagoya* case, where

[249] See *Velcro/Aplix v. Commission* [1985] 4 C.M.L.R. 157.

[250] 453 F.2d, 38 [CA 4th. 1971]. Even if the provision were viewed as a covenant not to compete ancillary to the sale of a going business, it would be an unreasonable restraint of trade. To the same effect see *Krampe v. Ideal Industries Inc* 347 F.Supp.1384 [DC Ill. 1972]; *Stewart v. Motrim Inc* 1975-2 Trade Cases, 60.531 [DC Ohio.1975].

[251] See *Blount Mfg Co. v. Yale & Towne Mfg Co.*166 F. 555 [CC Mass. 1909]; and *Mitsubishi Electric Co. v. US* 648 F.2d, 642 [CA 9th. 1981].

it was held:

> *In principle, this type of no-challenge clause brings about a restriction in the licensee's freedom to act which is not part of the essence of the industrial property right.*[252]

The no-challenge clause amounted to deprive the licensee of his opportunity to have the royalty reduced through the challenge, and have the restrictions repealed, thus strengthening his position as a competitor[253]. A no challenge clause was also dealt with in *AOIP v. Beyrard*, where the Commission interfered and made it clear that the licensee should always have the opportunity of challenging the validity of the patent since it is of general interest that patents issued erroneously are nullified. Furthermore, the Commission stated that a no-challenge arrangement does not depend on the existence of the patent right, but rather amounts to a contractual restraint of trade[254]. The Commission's decision in this case is very similar to the basic view in the American *Lear v. Adkins* case.

Under US law, licensing agreements barring the licensee from contesting the validity of the licensed patent or trademark during the life of the agreement did not constitute patent misuse[255]. No-challenge clauses became null and void on the day *Lear v. Adkins* was decided[256]. The

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252 *Raymond/Nagoya v. Commission* [1972] C.M.L.R. D.45; see also *Davidson Rubber v. Commission* [1972] C.M.L.R. D.52.

253 And the position of the consumers and other undertakings willing to manufacture the licensed product would also improve. See BELLAMY & CHILD, supra note 100 at 366-367.

254 *AOIP v. Beyrard* [1976] 1 C.M.L.R. D.14.

255 See *Steiner Sales Co. v. Schwartz Sales Co.* 98 F.2d, 999 [CA 10th. 1938]; *Westinghouse Electric Co. v. Building Electric Prod.Co.* 179 F.2d, 139 [CA 4th. 1950].

256 395 US, 653 [1969]. See generally STERN, "Antitrust Implications of *Lear v. Adkins*" [1970] 52 J.P.O.S. 213.

Supreme Court held that the public should have the right to benefit from knowledge which has not been patented, and therefore licensees should be permitted to challenge the validity of a patent. This would foster free competition in the use of ideas which were found to be part of the public domain. The Court also noted that, given licensees' economic interests, they were more likely than anyone else to challenge the patentability of a process[257].

No-challenge clauses are not accepted within the EEC or in the USA. In both systems, the competition authorities have adopted the view that these restrictions obstruct free competition. There is a general agreement that no-challenge arrangements are contractual restrictive practices that do not depend on the existence of the patent right.

C/ Grant-Back Clauses

Another principle is that a clause providing that the licensee's improvements of a patented product belong to the licensor will infringe article 85-1 of the EEC Treaty. Article 3{8} of Regulation 2349/84 prevents exemption where the licensee is obliged to assign wholly or in part to the licensor rights in or to patents for improvements or for a new application of the licensed patents. However, such grant-back clauses may be permitted so long as they are non-exclusive and impose a reciprocal obligation on the licensor[258]. Furthermore, clauses concerning grant-backs of non-exclusive licenses to the licensor only do not infringe article 85-

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[257] See generally *Bendix Corp. v. Balax Inc* 471 F.2d, 149 [CA 7th. 1972]. It was also held in *Panther Pumps & Equipment Co. v. Hydrocraft Inc* 468 F.2d, 225 [CA 7th. 1972], that a no-challenge clause, although unenforceable under *Lear v. Adkins*, was not in itself a misuse that prevented the licensor from recovering damages from an unlicensed infringer.

[258] Article 2(1){10} of Regulation 2349/84.

1[259]. In *Kabelmetal/Luchaire*, an agreement whereby the licensee was to grant the licensor non-exclusive licenses for any patents for improvements of techniques that he might evolve was found in violation of article 85-1 by the Commission. The latter took the view that such a grant-back covenant would reduce the licensee's incentive to develop the improvements in question[260]. Thus, regarding grant-back clauses, European competition authorities adopt a rule of reason approach, since a provision requiring the licensee to disclose improvements to the licensor and to grant him back the licence may not breach the Treaty provided that the licensor is under a similar obligation with regard to improvements, and provided that the grant-back clause is non-exclusive. In this respect, EEC and US laws are not very different.

In the United States, license provisions requiring a licensee of a patent to grant back to the patentee improvement patents that he might obtain are not unlawful in and of themselves. Such clauses are evaluated under the rule of reason. The leading American judgment on the legality of grant-backs is the Supreme Court's 1947 decision in *Transparent Wrap Machines Corp. v. Stokes & Smith Co.*[261]. The Court upheld the legality of grant-back clauses, and found there was no disincentive for the licensee to make inventions. However, that case was decided with reference to the specific agreement in question, whereby the licensor allowed the licensee to employ the granted back improvement patents. Adopting a more general

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259 See *Raymond-Nagoya* and *Davidson Rubber*, supra note 252.

260 [1975] 2 C.M.L.R. D.40. Note, however, that since the agreement was found to have no perceptible effect on trade between Member States, it did not infringe article 85-1.

261 329 US, 637 [1947].

view, the Supreme Court recognized that a licensee might be discouraged from innovating where he was required to assign the licensor all rights to improvement patents. Such grant-back provisions might give the licensee "*less incentive to make inventions when he is bound to turn over the licensor the products of his inventive genius*"[262]. Thus, grant-backs are generally upheld unless they are exclusive, or used with other practices that have a cumulative anti-competitive effect or as part of a plan to monopolize an industry[263].

Hence, with respect to exclusive grant-back clauses, US and EEC legislation is in accord, except that the European requirement that grant-back provisions should be reciprocal (the licensor must be subject to a like obligation, namely to license future improvement patents to the licensee) has no parallel in American law[264].

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262 *Ibid* at 646. It is also held that exclusive grant-back provisions that prevent the licensee from using his own technology are rare in the USA, and that they are of little consequence *vis-à-vis* third parties. See OPPEINHEM & SCOTT, "Empirical Study of Limitations in Domestic Patent and Know-How Licensing: A Second Report" [1970] 14 I.D.E.A. 123, cited in HANDLER & BLECHMAN, supra note 233 at 319.

263 See *US v. General Electric Co.* 80 F.Supp. 989 [DC NY. 1948].

264 It is thought that such reciprocity would discourage the patentee from licensing his rights. See HANDLER & BLECHMAN, supra note 233 at 320.

Section 3 : Tying Clauses

Tying arrangements are agreements whereby one party undertakes to take other goods or services, not wanted or unnecessary, than the product or service he wants. The direct effects of tying arrangements on competition are that competitors are excluded from selling substitutes for the tied product and, conversely, the buyer of tying goods or services is prevented from turning to another supplier[265]. The present position of US case law is ambiguous. Tying covenants seem to be treated under a *per se* concept, but this *per se* illegality is not as strict as in the case of price agreements or concerted refusals to deal. In fact, only certain categories of tying arrangements are subject to the *per se* rule, whereas other types are treated under a rule of reason, and thus are not necessarily illegal. Tying clauses have not been dealt with in great detail in EEC law. However, there is also a distinction between certain tying provisions which can be exempted by virtue of the rule of reason, and other categories that are *per se* unacceptable.

In the United States, tying is regarded as a means to exclude competing enterprises. Further, licensing of a patented machine on the condition that the licensee use, in conjunction with the machine, supplies manufactured or sold by the licensor is unlawful under the antitrust laws as an illegal extension of the patent monopoly[266]. The present US law on

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265 In a 1984 decision, the US Supreme Court listed four harms resulting from tying conducts: 1) harms to existing competitors in the tied product market; 2) creation of barriers to entry in the tied product market; 3) increased social costs of market power in the tying product market through facilitation of price discrimination; and 4) restriction on buyers' freedom to select the best bargain in the tied product market resulting from the need to buy the product, and an inability to evaluate the true cost of either products when they are only available as a package. However, this case, *Jefferson Parish Hospital Dist. No 2 v. Hyde* 466 US, 2 [1984], does not involve intellectual property law.

266 See generally WOLLENBERG, "An Economic Analysis of Tie-in Sales: Re-Examining the Leverage Theory" [1987] 39 Stanford L. Rev. 787.

this subject is the result of a long evolution that we shall attempt to summarize and clarify. We may start with the Supreme Court's 1911 decision in *Henry v. A.B Dick Co.*, where the legality of tying practices was upheld on the ground that tying clauses were a regular way for a patentee to ensure the profits to which he was entitled[267]. But that favourable attitude toward tying clauses was to be reversed in *Motion Picture Patents Co. v. Universal Film Manufacturing Co.*, where the Supreme Court invalidated a tying provision which was intended to extend the patentee's statutory monopoly[268]. This sudden shift of opinion may be explained by the enactment, between *Henry v. A.B Dick* and *Motion Picture Patents*, of the Clayton Act. Section 3 of that statute prohibits tying sales which substantially lessen competition[269]. The question of whether when a tying arrangement was illegal and when it was illegal *per se* was settled in the *Times-Picayune Publishing Co. v. US* case. The owner of two newspapers obliged advertisers to buy space in both newspapers. They were not permitted to advertise in just one of them. The Court held:

> *When the seller enjoys a monopolistic position in the market for the "tying" product, or if a substantial volume of commerce in the "tied" product is restrained, a tying arrangement violates the narrower standards expressed in section 3 of the Clayton Act because from either factor the requisite potential lessening competition is inferred... And because for even a lawful monopolist it is "unreasonable, per se, to foreclose competition from any substantial market", a tying arrangement is banned by section 1 of the*

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267 244 US, 1 [1911].

268 243 US, 502 [1916].

269 A number of cases followed, see e.g., *International Salt Co. v. US* 332 US, 392 [1947]; *Mercoid Co. v. Minneapolis Honeywell Regulator Co.* 320 US, 680 [1943]; *US v. Paramount Pictures Inc.* 334 US, 131 [1948]. In this latter case, it was stated that the principles of the patent cases also applied to copyrighted films.

> *Sherman Act whenever* ***both*** *conditions are met.* (Emphasis added)[270]

In other words, a tying arrangement constitutes a violation of section 3 of the Clayton Act if one of two conditions are fulfilled: that the seller had a monopolistic position in the market with respect to the tying product; or, that a substantial part of commerce in the tied product was restricted. Section 1 of the Sherman Act is infringed *per se* if both of these conditions are fulfilled[271].

In the subsequent *Northern Pacific Railway v. US* decision, the Supreme Court gave up the "monopolistic power" standard set out in *Times-Picayune*, and replaced it with the broader concept of "sufficient economic power":

> *They [tying arrangements] are unreasonable in and of themselves whenever a party has sufficient economic power with respect to the tying product to appreciably restrain free competition in the market for the tied product and a not insubstantial amount of commerce is affected...*[272]

If sufficient economic power is established, then the tying clause is *per se* illegal. In *Northern Pacific Railway*, however, no sufficient market power with respect to the tying product could be proven[273].

In *US Steel Corp. v. Fortner Enterprises*, an allegation that the defendant had violated section 1 of the Sherman Act by means of a tying

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270 345 US, 594 at 608-9 [1953].

271 Note also that in either case section 5 of the Federal Trade Commission Act would be infringed, since that provision registers violations of the Clayton and the Sherman Acts.

272 356 US, 1 at 6 [1958].

273 In *US v. Loew's Inc* 371 US, 38 [1962], the Supreme Court defined more precisely what was to be understood under "market power" and "tying". Power to control prices and exclude competitors constituted market power, but even without those two elements, the decisive economic power could flow from consumers desirability for the tying product. A number of cases followed the *Times-Picayune* and *Northern Pacific* cases, among them we may cite *Dawnson Chemical Co. v. Rohm & Haas Co.* 448 US, 176 [1980].

clause was dismissed, on the ground that the defendant had no sufficient economic power in the market to render the agreement illegal[274]. The decision of the Supreme Court was based on the view that although the defendant had a competitive advantage over other enterprises, no violation of the antitrust laws was involved if the competitors were able to react against the tying arrangement by taking counter measures. Thus, the surrounding circumstances of the alleged illegal agreement were taken into consideration, as US courts usually do when they analyze an agreement under the rule of reason.

Therefore, under US law, tying arrangements are seen as illegal *per se* where the undertaking in question has a sufficient market power in the tying product, and if the agreement is likely to affect, in a substantial manner, trade in the tied product. If both of these standards are not satisfied, the arrangement is to be treated under the rule of reason[275].

EEC case law on the topic of tying agreements is not so abundant. Nevertheless, it can be seen not only from these cases, but also from the Rome Treaty provisions and certain secondary legislation, that tying clauses may be subject to a rule of reason or to a *per se* concept according to what they contain. The definition of tying arrangements provided by article 85-1{e}, namely "*to make the conclusion of contracts subject to the acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts*", is similar to the definition

[274] 429 US, 610 [1977].

[275] See generally MONTGOMERY, "The Presumption of Economic Power for Patented and Copyrighted Products in Tying Arrangements" [1977] 85 Colum. L. Rev. 1140; and FEJO, supra note 20 at c.10. See also "Politique de Concurrence et Propriété Intellectuelle" O.E.C.D. Report [1989] at 87-93.

adopted by US law. Article 85-1 states a *per se* illegality of tying clauses requiring the licensee to obtain certain products, components or spare-parts from the licensor, and no exemption is available where one party is induced when contracting to accept further licences, or to use intellectual property rights, goods or services he does not want. Equally, a provision to the effect that the licensed products be sold only in conjunction with other products, not covered by the patent, infringes article 85-1[276]. However, article 85-1 does not apply to tying clauses indispensable for the exploitation of the patent, for example, where the licensor reasonably insists on standard of quality in respect of semi-finished products, raw materials or components[277].

This notion of reasonableness is also found in Regulation 2349/84 which provides an exemption for tying provisions *"in so far as such products or services are necessary for a technically satisfactory exploitation of the licensed invention"*(article 2(1){1}). As already stated, article 2 is a white list which includes type of agreements that are not *a priori* anti-competitive, but which may become harmful for competition. Article 2 therefore leaves the door open to a rule of reason analysis. On the other hand, article 3(9) of the Regulation does not allow exemptions where one party is **induced** when entering into the agreement to accept further licenses he does not want, or to use patents, goods, or services he does not want or need, unless necessary for a technically satisfactory

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[276] See *Windsurfing International* [1984] 1 C.M.L.R. 1. Under US law too, misuse of patent is recognized where an unpatented article is tied to licensed patents. See *Cardox Co. v. Armstrong Coalbreak Co.* 1952 Trade Cases [CA 7th. 1952].

[277] See *Pronuptia v. Schillgallis* [1986] 1 C.M.L.R. 414, accepting the same principle in franchise agreements.

exploitation of the invention[278]. Finally article 1 of the Regulation provides an obligation on the licensee to use the licensor's trademark or get-up determined by the latter only to distinguish the licensed products, provided the licensee is not prevented from identifying himself as the manufacturer of the licensed goods[279].

In the *Vaessen/Moris* case, the Commission condemned an agreement clause whereby the owner of a patent concerning a method and an apparatus to manufacture "Boulogne Sausages", required of his licensees that they buy casings for the sausages from him. The Commission found that this tying clause was not necessary for the exploitation of the invention, and that it prevented the licensees from purchasing casings from other suppliers. Thus, it was in contravention of article 85-1 and was not eligible for an 85-3 exemption. The clause constituted an unlawful contractual extension of he patent monopoly[280]. In this respect, the EEC approach is similar to the American view. Tying practices are also prohibited under article 86 of the Rome Treaty, as emphasized in *Hoffman La Roche v. Commission* and *Eurofix-Banco v. Hilti*[281]. However, those cases do not allow the drawing of a parallel between the European concept of "dominant position" and the American notion of "sufficient economic power".

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278 Article 3 constitutes the black list of agreements *per se* illegal. But from the moment article 3(9) uses the word "unless", thus foreseeing an exception, it is questionable whether this a genuine *per se* approach. Note that a similar wording is adopted in the block exemption on know-how licensing supra note 183 at articles 2(1){5} and 3(3).

279 *Velcro/Aplix v. Commission* [1985] 4 C.M.L.R. 157. To the same effect, see the American decision *Switzer Bros Inc. v. Locklin* 297 F.2d, 39 [CA 7th. 1961].

280 [1979] E.F.T.L. 19.

281 Respectively, [1979] E.C.R. 461 and [1989] 4 C.M.L.R. 677.

Section 4 : Duration and Royalty Clauses

A patent or copyright licence may fall under the prohibition set out in article 85-1 if its duration is automatically prolonged beyond the expiry of the licensed intellectual property rights[282]. Thus, provisions extending the term of the agreement by the inclusion of improvement patents have been struck down in several cases[283]. Exemption under Regulation 2349/84 will not be available unless the agreement provides each party with the right to terminate it at least annually after the expiry of the licensed patent. As far as US law is concerned, we have seen earlier that any attempt to extend the monopoly granted by a patent is a violation of the antitrust laws, and constitutes patent misuse. Therefore, an arrangement whereby a licensee would be required to pay royalties even after the licensed patent has expired, is considered unacceptable as it amounts to prolong the duration of the licensing agreement. In *Brulotte v. Thys Co.*, the Supreme Court emphasized that:

> *The exaction of royalties for use of a patented machine after the patent has expired is an assertion of monopoly power in the post-expiration period when... the patent has entered the public domain.*[284]

It may be said that there is a similarity between American practice and that of the EEC in this respect.

As to use of know-how after termination of the licensing agreement,

[282] Whereas patents, copyrights and allied rights give to their owners a limited period of protection (a maximum of 17 or 20 years with a patent right, the author's life plus 50 years with copyrights), trademark rights last as long as the mark is used in connection with the business to which it is associated.

[283] *AOIP v. Beyrard* [1976] 1 C.M.L.R. D.14; *Peugeot/Zimmern* [1977] 1 C.M.L.R. D.22. See also Commission's 6th Report on Competition Policy at No.159.

[284] 379 US, 29 at 33 [1964].

a parallel can also be established between the relevant provisions in the EC Commission's block exemption on know-how licensing and US case law. In both systems, the licensee is entitled to continue employing know-how he was licensed to use after termination of the agreement, provided the know-how in question has meanwhile become publicly known[285]. However, the licensor may insist that his know-how be returned, and restrict the licensee to use it after the agreement has expired, as long as the know-how is still secret[286]. It can be seen from the above discussion that one of the means frequently used by licensors to misuse their rights and extend their monopolies is royalties.

Royalties are the financial cost of the license, from which the licensor derives an income. In exchange for the right to employ intellectual property rights, a licensee pays a certain amount of money to the licensor in consideration of the use he is going to make of those rights. And a frequent abusive clause that may be found in licensing agreements is the settlement of a royalty to be paid on products or processes not covered by the license.

Both EEC and US systems allow royalties to be charged on unpatented products used in connection with patents, or on sales of a product that is composed of patented and unpatented ingredients. Neither section 1 of the Sherman Act nor article 85-1 of the EEC Treaty will apply if the reason for this is that the number of patented items manufactured

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[285] Article 3(1) of Regulation 556/89 on know-how licensing, supra note 183.

[286] Article 2(3) of Regulation 556/89; and *Painton & Co. v. Bourns Inc* 442 F.2d, 216 [2nd Cir. 1971]; *Kewanee Oil Co. v. Bicron Corp.* 416 US, 470 [1974].

or consumed or their value are difficult to evaluate separately[287].

Another similarity, but also a contrast, is to be observed between American and European approaches to royalties on unpatented products. In both competition systems there is a principle that a licensee can only be obligated to pay royalties for the licensed patents he receives. Hence, where royalties are calculated upon non patented products or technologies, violation of antitrust laws may be committed. Article 3(4) of the black list of Regulation 2349/84 precludes exemption if:

> *The licensee is charged royalties on products which are not entirely or partially patented or manufactured by means of a patented process, or for the use of know-how which has entered into the public domain otherwise than by the fault of the licensee or an undertaking connected with him...*

Moreover, the *Windsurfing* case established that if the effect of the royalty is to discourage the licensee from meeting any separate demand for the product in question, article 85-1 is contravened[288]. The Commission has held that a clause that requires the licensee to pay royalties for the manufacturing of the licensed products, without making any use of the licensor's patent, falls under article 85-1. Such a provision imposes a financial burden on the licensee, and thereby weakens his competitiveness[289]. Similarly, US courts regard as illegal an exorbitant or oppressive royalty which may cause the licensee to increase his prices

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287 See *National Foam System Inc. v. Urquhart* 202 F.2d, 659 [CA 3rd. 1953]; and *Windsurfing International v. EC Commission* [1984] 1 C.M.L.R. 1.

288 See *Windsurfing International v. Commission* [1984] 1 C.M.L.R. 1. See also STONE, "Some Thoughts on the *Windsurfing* Judgment" [1986] 8 E.I.P.R. 242.

289 *AOIP v. Beyrard* [1976] C.M.L.R. D.14.

correspondingly, and thus affect his position as a competitor[290].

The illegality of royalties charged on unlicensed patents or unpatented technology was emphasized by the US Supreme Court in *Automatic Radio Manufacturing Co. v. Hazeltine* and *Zenith v. Hazeltine*[291]. However, we shall focus on another consideration discussed in those cases. In *Automatic Radio Manufacturing Co. v. Hazeltine*, although the Court insisted on the general principle that an agreement about royalty payment in proportion to the total sales or about payment of a minimum royalty may be one way for the patentee to obtain payment for non patented products, it upheld the agreement under consideration. The license provided for a calculation of royalties on the basis of the total sales accomplished by the licensees, and the Supreme Court found this method to be a practical way of fixing royalties. In the subsequent *Zenith v. Hazeltine* decision, the Supreme Court held, on the contrary, that the licensee was entitled to have the royalties evaluated according to the actual use of the licensed technology, rather than on total sales. But unlike the situation in *Automatic Radio v. Hazeltine*, the defendant here was found to have attempted to extend its patent monopoly[292]. It can thus be concluded that where no abuse of monopolistic position is involved or intended, a licensor has the right to assess royalties on the basis of total sales[293].

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290 *American Photocopy Equipment Co. v. Rovico Inc.* 359 F.2d, 745 [CA 7th. 1966].

291 Respectively 339 US, 827 [1950], and 395 US, 100 [1969].

292 339 US, 100 at 139 [1969].

293 It is thought by American doctrine that *"where such royalty provisions are adopted by mutual agreement, and without coercion, they have no anti-competitive or other socially undesirable effects... They clearly do facilitate commercial dealings and transfers of technology that provide important benefits for society"*; HANDLER & BLECHMAN, supra note 233 at 317.

By contrast, article 3(4) of the EC Commission's Regulation 2349/84 states that:

> *... without prejudice to the arrangements whereby, in order to facilitate payment by the licensee, the royalty payments for the use of a licensed invention are spread over a period extending beyond the life of the licensed patents or the entry of the know-how into the public domain"*

Thus, royalty clauses providing for payment for a fixed period, whether or not the patent or intellectual right has fallen into the public domain, may be valid if the genuine objective of the provision is to spread royalties over a period to facilitate payment. Presumably this provision implies that block exemption does not apply if under the agreement the royalty is charged on the licensee's total sales[294].

We have emphasized in this chapter certain common points between the European and American policies regarding intellectual property rights licensing agreements provisions relating to field of use restrictions, no-challenge and grant-back clauses, tying arrangements, and duration and royalty provisions. We have also highlighted noteworthy differences with respect to territorial, customer, price and quantity restrictions, and non-competition arrangements.

Both European and American licensors may restrict the field of use of a licensed patent, provided that restriction is justified by technical

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[294] However, individual exemptions under article 85-3 may be still possible. See FEJO, supra note 20 at 347: *"If the group exemption is not authorized in connection with the agreement in question, this only means that the parties making the agreement in question must apply for exemption for their licensing agreement to the Commission pursuant to article 85-3. If this factor is compared with the conditions in the USA, it is worth noticing that in the USA group exemptions cannot be granted, but one has to enter into licensing agreements among others at risk of the Monopolies Authorities and the courts finding the agreements in question in contravention of the antitrust legislation, and prohibited."*

reasons. They may also impose grant-back obligations provided the clauses are non exclusive. On the other hand, they are not supposed to prevent their licensees from challenging the validity of the licensed patents, trademarks or copyrights, nor can they impose tying obligations on their licensees unless this is necessary for the exploitation of the licensed products. And neither European nor American licensors are entitled to charge royalties on expired or unlicensed patents or know-how.

The American patentee, unlike his European colleague, is entitled to impose territorial limitations on his licensees' freedom of resale or use, as well as customer restrictions. The European licensor is also prohibited from fixing prices or maximum quantities to be produced, whereas a licensor established in the United States is recognized such rights. Eventually, unlike the latter, the former is not entitled to prevent his licensees from competing with him or his products.

CONCLUSION

The apparent conflict between the monopolies afforded by intellectual property rights and the ideal of free competition fostered by the antitrust laws of the USA and the EEC can be overcome, if one adopts a long term view. It is not the patent, the trademark, or the copyright in itself which may have adverse effects on competition, but the way these rights are handled by their owners.

Thus, intellectual property rights holders may undertake to prevent parallel imports of genuinely (not counterfeit) patented, trademarked, or copyrighted products. Both European and American systems allow their nationals to oppose parallel importations from foreign countries. On the other hand, whereas within the EEC a strict application of the doctrine of exhaustion constitutes a barrier against the prevention of parallel imports from one Member States into another, parallel importations from one American State into another are not so inexorably restricted. If the American doctrine of exhaustion appears well-established with respect to patent rights, this is not true as regards other intellectual property rights. Besides, the US exhaustion of rights being rooted in the principle that contractual restrictions do not bind third parties, it is only the latter who may rely on the exhaustion doctrine. Underlying the more general application of that principle in the EEC is the single market integration policy.

Intellectual property rights owners may also be tempted to exploit the monopolistic position they are granted by their patents, copyrights, or allied rights, with a view to acquiring or strengthening their market power. Article 86 of the EEC Treaty considers monopolies or dominant positions as legal in themselves, but it condemns abuses of dominant positions, whereby a monopolist would engage in unfair practices to exclude competitors. Similarly, US antitrust law, and in particular section 2 of the Sherman Act condemns monopolistic conducts intended to close markets and eliminate potential or actual competition. But unlike EEC law, US legislation also censures wilful acquisition of monopolies, and regards the latter as suspicious anti-competitive practices. Such a negative attitude may be traced to the traditional capitalist and freedom to enterprise and compete ideology which guided the enactment of the US antitrust laws.

That difference in the approaches to restrictive business practices between EEC and US laws is also to be observed with respect to contractual use of intellectual property rights, but in a reverse order. European competition authorities have adopted a hostile attitude toward licensing agreement restriction clauses. Such provisions are generally held anti-competitive by nature. On the other hand, US law considers similar clauses as lawful, and very often as part of the intellectual property rights' legal monopoly. However, these views are not adamant. Both systems recognize that restriction clauses are never wholly anti-competitive or pro-competitive. Therefore, the EC Commission is entitled to grant exemptions for those *prima facie* unlawful licensing agreements provisions which appear to be truly beneficial for competition, and US courts can prohibit license clauses which, though generally lawful, prove to be harmful for free competition, by virtue of a rule of reason.

Hence, despite the differences of goals and means between EEC and US competition laws, it is frequent that both systems adopt similar attitudes with respect to certain misuses of intellectual property rights.

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