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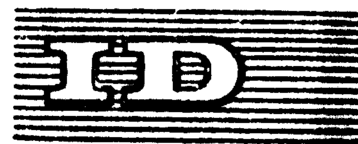

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THE EFFECT OF UNITED STATES AND EEC ANTITRUST LAW ON INTERNATIONAL LICENSING AND LICENSING INTO DEVELOPING COUNTRIES [1/]

by

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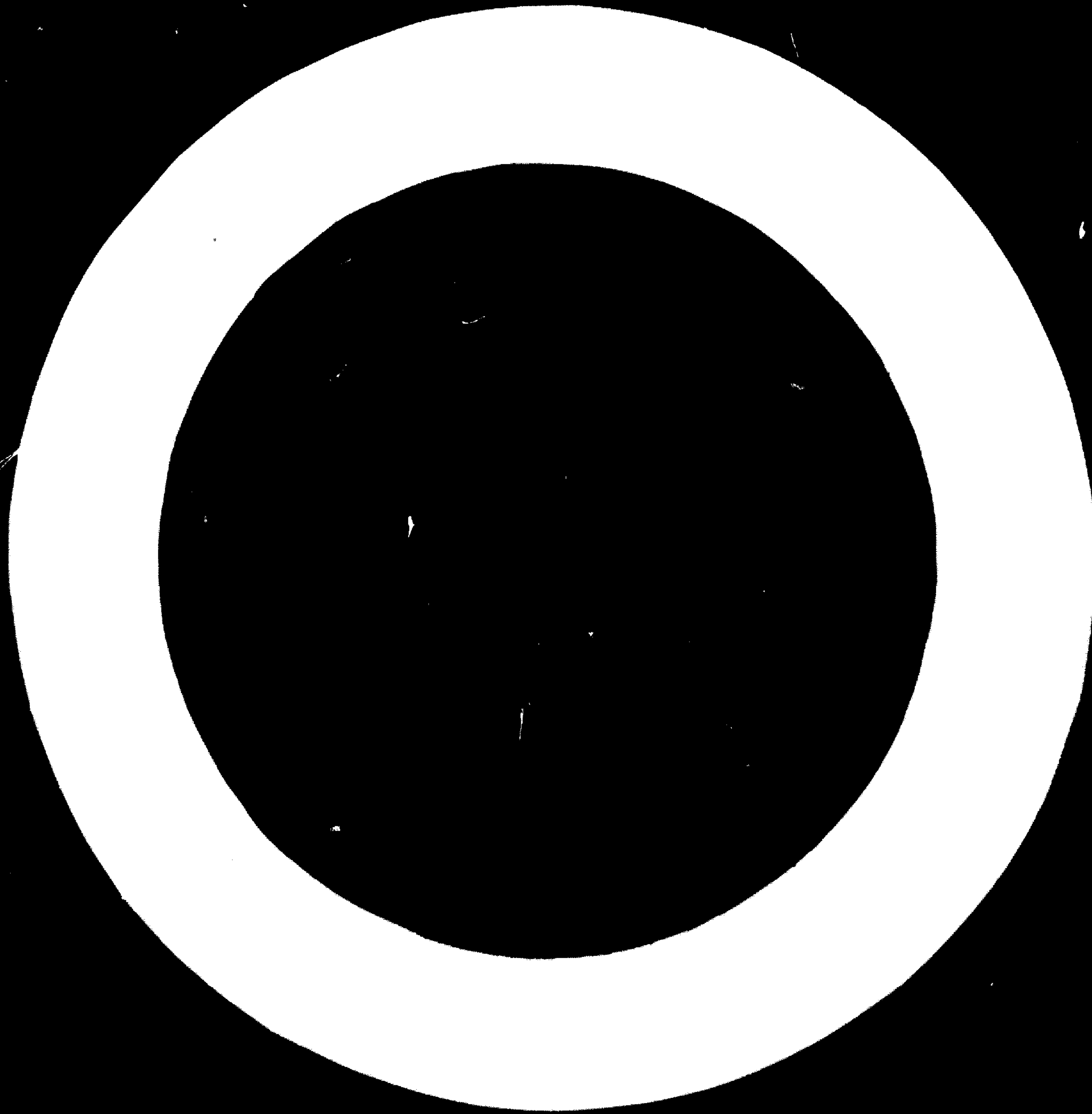

PART 1

ANTITRUST LAW OF THE UNITED STATES

I. INTRODUCTION -- THE GENERAL NATURE OF UNITED STATES ANTITRUST LAWS AND THEIR APPLICATION TO LICENSING TRANSACTIONS

A. A Brief Outline of United States Antitrust Statutes

The United States antitrust laws seek to prevent acts and practices which have anticompetitive effects. The actual antitrust statutes are brief and contain broad sweeping language.

It is usually necessary to look to case law to determine how the antitrust laws would be applied to a particular licensing transaction. For example, Section 1 of the Sherman Act prohibits contracts and conspiracies which unreasonably restrain trade. The express terms of the statute prohibit contracts, combinations and conspiracies in restraint of trade. Case law has supplied a "rule of reason." Thus, the law prohibits only _unreasonable_ restraints of trade. _Standard Oil Co. v. United States_, 221 U.S. 1 (1910).

In addition to Section 1 of the Sherman Act, the main antitrust statutes are: (1) Section 2 of the Sherman Act which bars monopolization, and attempts and conspiracies to monopolize, and (2) Section 7 of the Clayton Act which prevents corporate acquisitions which may substantially lessen competition or tend to create a monopoly.

In addition to the above-described provisions of the Sherman Act and the Clayton Act, Section 5 of the Federal Trade Commission Act prohibits "unfair methods of competition in commerce." Under this

In Sirena S. R. L. v. Eda S. R.L.Case No. 40/70 Court of Justice, February 18, 1971, the Court gave indications as to where lines were being drawn on industrial property rights. There an American company, Mark Allen had in 1933 registered the trademark "Prep" in Italy in respect of a shaving cream. In 1937, Mark Allen transferred this mark in Italy to Sirena, but did not assign any technical "know how." Sirena marketed a product in Italy under the "Prep" mark. Mark Allen subsequently allowed a German company to use the same mark in West Germany, and that company marketed shaving creams under the mark. The German company, through an import-export company began to sell its products in Italy at prices lower than Sirena's; Sirena brought action in an Italian court on its Italian trademark. The importing company contended that Articles 85 and 86 precluded Sirena from exercising the trademark rights. The Italian court submitted to the Court of Justice* the question relating to the applicability of Articles 85 and 86 to the case.

The Court squarely faced the problem, stating that the treaty is silent as to the relation between the Community law on competition

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* Article 177 of the treaty allows national courts to suspend proceedings and submit to the Court of Justice for a preliminary ruling questions on the applicability of the provisions of the treaty to the facts of the case.

American courts have established the principle that the right to license is governed by the law of contracts and the public interest is expressed by the antitrust laws, and not by the patent law.

United States antitrust policy and tradition drastically affects the options available to a patent owner who wants to license his patent rights.

C. The Application of the Antitrust Laws to the Restrictive Aspects of Know-How Licenses

(a) Restriction on Disclosure

The fundamental restriction imposed by a know-how licensor is the restriction against disclosure of the secret information or know-how to third parties. Such a restraint, however, is ordinarily not unreasonable under Section 1 of the Sherman Act.

It is a general practice in the United States to limit the obligation of secrecy to a period of years, or until the information becomes part of the public domain by activities of a third party. Such a time limitation is a practical recognition of the duration of the value of confidential know-how.

Confidential know-how lasts only so long as its discovery can be prevented by fair means. And, regardless of any elaborate protective systems, there is always rapid obsolescence, and the secrecy loses its economic value. The general practice is to limit the obligation of secrecy to a period of ten years, but there is no legal requirement to do so. Warner-Lambert Pharmaceutical Co. v. John J. Reynolds, Inc., 178 F. Supp. 655 (S. D. N. Y. 1959), aff'd, 280 F. 2d 197 (2d Cir. 1960).

(b) The Effect of the Know-How Going Into the Public Domain

United States courts will enforce know-how license agreements against the licensee only so long as a portion of the know-how transferred to the licensee retains its status as secret and valuable information, that is, the know-how license is not enforced if the knowledge forming the licensee's consideration becomes part of the public domain.

The strict application of the antitrust laws by the federal courts and the resulting effect on the enforceability of know-how licenses covering know-how that has become publicly available is shown by the following quotation from a recent Supreme Court decision, Lear, Inc. v. Adkins, 395 U. S. 653, 668 (1969).

> "[F]ederal [antitrust] law requires that all ideas in general circulation be dedicated to the common good unless they are protected by a valid patent."
>
> (Emphasis added.)

(c) Restrictions on the Licensee's Dealings in Products Produced Using the Licensed Know-How

There are few litigated cases concerning the legality of various restrictions placed on the licensee's freedom of action with respect to goods he produces. In general, the same principles applied in deciding the antitrust legality of patent licenses are applied to know-how license situations.

(d) The Concept of Patent Misuse As it is Used to Promote Antitrust Enforcement

A large number of court decisions, regarded as precedent for what is or is not a lawful exploitation of a patent, are found not in antitrust cases but rather in patent infringement actions where a defendant accused of patent infringement defends by showing that the patent owner misused his patent. This particular defense presents an appeal for the application of customary equity principles. Should patent

misuse be proven, the patentee loses any opportunity for relief, either by injunction or an accounting for lost profits. The patent infringer is relieved of all liability regardless of the fact that he may be totally uninjured by the misuse and despite the validity of the patent and its actual infringement.

Patent misuse has been found to include practices which amount to an attempt to extend the monopoly of a patent beyond its expiration date, Brulotte v. Thys Co., 379 U.S. 29 (1964); the use of exclusive dealer agreements to market a patented product, F. C. Russell Co. v. Consumers Insulation Co., 226 F.2d 373 (3d Cir. 1955); and tying of sales or leases of unpatented equipment to a patent license, United States Plywood Corp. v. General Plywood Corp., 370 F.2d 500 (6th Cir. 1966).

A temporary loss of royalties from licensees, or damages from infringers, is the result of a misuse judgment. The patent owner's loss of such income continues until he purges himself of the misuse; that is, until there has been an abandonment of the misuse and the consequences have been fully dissipated.

While there is no strong body of case law precedent to support the proposition, it is likely that the misuse doctrine as applied against a patent owner is equally applicable against a know-how proprietor who

licenses his know-how and attempts to unreasonably restrict his licensee.

The misuse doctrine is a major factor in forcing U. S. businesses to comply with the antitrust laws in their licensing transactions. This doctrine is one that could probably be used to advantage in developing countries since it is administered by the courts and the economic self-interest of one party to a lawsuit.

II. THE "RULE OF REASON" AS APPLIED TO RESTRICTIONS ON THE CONDUCT OF A LICENSEE OF PATENTS OR KNOW-HOW

Section 1 of the Sherman Act prohibits all contracts that restrain trade or commerce. Every license agreement that places a restriction on a licensee's conduct thus is "literally" a violation of Section 1. However, the courts have limited the application of Section 1 to "unreasonable" restraints of trade.

The legality of restrictions in patent licenses has historically been viewed as based on reasoning from a 1926 Supreme Court decision, United States v. General Electric Co., 272 U. S. 476 (1926). The importance of this case justifies a discussion of its facts.

General Electric owned three basic patents which covered electric light bulbs having tungsten filaments. GE licensed the patents on condition that Westinghouse would follow prices and terms of sale from time to time, as fixed by GE, and would maintain the same conditions of sale as observed by GE in the distribution of the licensed bulbs. Between them, GE and Westinghouse controlled 85% of the light-bulb market.

The government attacked these license terms as a violation of Section 1 of the Sherman Act.

The Supreme Court, however, held the license restrictions to be legal. The court reasoned that since a patent owner can restrict a licensee to the mere making and using of the patented article, and withhold altogether the right to sell, a conditional right of sale may be given provided that "the conditions of sale are normally and reasonably adapted to secure pecuniary reward for the patentees monopoly."

The Court placed price fixing restrictions within the scope of permissible "conditions of sale" in the following words:

> "One of the valuable elements of the exclusive right of a patentee is to acquire profit by the price at which the article is sold. The higher the price, the greater the profit, unless it is prohibitory. When the patentee licenses another to make and vend and retains the right to continue to make and vend on his own

> account, the price at which is licensee will sell will necessarily affect the price at which he can sell his own patented goods. It would seem entirely reasonable that he should say to the licensee, 'Yes, you may make and sell articles under my patent but not so as to destroy the profit that I wish to obtain by making them and selling them myself.'"
>
> (Emphasis added.)
> 272 U.S. at 490-91

The rule of reason as it is applied today by United States Courts includes three important tests. First, the restriction or limitation must be ancillary to the lawful main purpose of a contract such as a patent or know-how license. Second, the scope of the limitation must not be substantially greater than necessary to achieve the lawful main purpose.

In applying this second criteria, courts first look critically to see if the licensee's activities are restrained in an area of commerce that is broader than the technology covered by the licensed patents and/or know-how. If the restraint is broader than the technology transferred, there exists a high probability that a court will find a misuse and possibly an antitrust violation.

The third important criteria in considering reasonableness is the duration of the restraint. A restraint having a duration of ten (10)

years might be reasonable, while a restraint extending for an indefinite period might be unreasonable.

The rule of reason is applicable to both patent and know-how licensing situations. As discussed above with respect to such know-how licenses, such licenses in order to support any restrictions must transfer technology not known to the public generally -- that is, the know-how must not be in the public domain. Otherwise, a restriction in a know-how license is a naked agreement in restraint of trade.

The reason for the requirement of secret subject matter can be illustrated in terms of the rule of reason. If technology is in fact in the public domain, anyone including a potential licensee is entitled to use it without paying any fee or other consideration to a licensor and without being subjected in his use of it to any restrictions imposed by the licensor. Accordingly, a contract for the transfer of technology, which is in fact known to the general public, can have no "lawful main purpose" under the rule of reason.

On the other hand, a contract for the transfer of technology not publicly available does have a lawful purpose. The purpose generally will be to enable the licensee to take advantage of something which he did not have before -- that is, the secret technology. The existence of

a lawful primary purpose, permits reasonable ancillary restrictions on the use of the technology to be imposed.

III. THE THEORY OF PER SE ILLEGALITY

A. The Reasons For and the Effect of the Per Se Theory

United States courts in administering the antitrust laws have found it convenient to designate certain restrictive practices as constituting *per se* violations. The courts have conclusively presumed that certain types of restrictions which always have strong anti-competitive effects, such as a horizontal division of markets among competitors, are illegal and thus do not apply the subtests under the rule of reason to such agreements.

In such situations, inquiry under the rule of reason is over once it has been decided that the conduct or agreement under review falls within the scope of a form of conduct previously adjudged to be illegal *per se*. The *per se* theory makes decision making by the courts easy in certain classes of cases, and promotes certainty in the minds of businessmen that certain practices are illegal.

B. The Per Se Theory As Applied to Licensing

Only a few patent licensing practices have been held by the courts illegal *per se*, because of a pernicious anti-competitive result which such a practice inherently produces.

One *per se* illegal practice is requiring a licensee to purchase unpatented materials from the licensor. As a matter of general antitrust law, tying agreements which affect commerce are unlawful if the selling party enjoys a degree of power over the tying product. When the tying product is patented the requisite economic power is presumed. The theory for this presumption is that the existence of a valid patent on the tying product, without more, establishes a distinctiveness sufficient to conclude that any tying arrangement involving the patented product would have anti-competitive consequences.

A *per se* violation also exists if a patentee restricts his licensee's right to deal in products or services not within the scope of the patent or know-how rights to be transferred. If he does so, he is attempting to extend the bounds of his exclusive position, which for a patent is the right to make, use, and sell the patented invention.

Another per se illegal licensing practice is a mandatory package license. In this situation, the licensor is using his patent position to affect free competition in products or services not covered by the patent under which a license is desired. The licensee is compelled by the power of the patent that he needs a license under, to take a license under patents or know-how he does not want. The mandatory imposition of a royalty based on total sales by the licensee is conceptually related to mandatory package licensing, and is also illegal per se. In the case of mandatory total-sales royalties, the power of the patent the licensee wants, compels the licensee to pay royalties on subject matter which is beyond the scope of the claims of that patent.

It should be noted that package licensing and the imposition of a royalty based on total sales are legal if the licensee voluntarily accepts such terms, and there is no coercion on the part of the licensor.

Another licensing practice which is illegal per se is the imposition of various types of restrictions on a purchasing licensee. Such illegal restrictions include an attempt to confine the areas or persons to whom the purchasing licensee can resell. As stated in United States v. Arnold Schwinn & Co., 388 U.S. 365 (1967):

> "Under the Sherman Act, it is unreasonable without more for a manufacturer to seek to restrict and confine areas or persons with whom an article may be traded after the manufacturer has parted with dominion over it. . . . Such restraints are so obviously destructive of competition that their mere existence is enough."
>
> 388 U.S. at 379.

The above language is generally applicable to the purchaser of a product, whether or not patented, because a purchaser under United States law automatically obtains an implied license to use and resell the purchased product.

A common principle runs through the antitrust treatment of each of the per se illegal licensing practices. That principle is that the owner of intellectual property may not use the power of his exclusive position to restrict his licensee's freedom with respect to matters outside the scope of the patent or know-how under which the licensee desires a license.

IV. LICENSING PRACTICES WHICH MAY CONSTITUTE AN ANTITRUST VIOLATION OR A MISUSE UNDER UNITED STATES LAW

In addition to the practices outlined above which are always illegal, there are a number of licensing practices that are subjected to

the rule of reason to determine their antitrust legality. Competent legal counsel is needed to determine the legality of specific restrictions that fall within the scope of applicability of the rule of reason.

A client-licensor can easily be advised of the realtively few things he clearly must not or should not require of his licensee today; that is, the per se illegal practices described above. Advising him how to negotiate now, an arrangement which will surely avoid antitrust and misuse problems over the life of an agreement, perhaps the next 10-17 years, is very difficult. This is true because the record of the last 40 years clearly demonstrates a tendency towards stricter application of the antitrust laws.

The discussion that follows is primarily based on existing decided cases, many of which are 10-25 years old. The United States Department of Justice and defendants in patent infringement suits, via misuse defenses, are constantly attacking the continuing validity of some of these old precedent cases. Where the Department of Justice position is sharply opposed to existing case law precedent, the reasons for the Department's position is noted.

a. Field of Use Restrictions on Manufacturing Licensees

Field of use licensing is a very general term covering situations in which the licensor grants a license for a restricted use of patented subject matter, but declines to license all the uses of the invention and reserves some uses for self-exploitation, or exploitation by other licensees.

Field of use restrictions permit a patent owner to increase royalty income; regulate the use of his patents; test the use of inventions in certain new fields; maintain exclusivity for a patentee or licensee; and meet the specific needs and capabilities of a licensee.

Field of use licensing, because of its advantages to the licensor, is a common practice in the United States.

Field of use restrictions (and almost all other restrictions) placed on a purchasing licensee are illegal per se as described above. Thus, under United States law, it is important to distinguish the situation where a restriction is placed on a manufacturing licensee (sometimes legal) and the situation where a restriction is placed on a purchasing licensee (illegal *per se*).

Under United States antitrust law, in the absence of any patent rights, a division of customers or markets has been considered per se illegal for over seventy years. Market allocation eliminates competition even more completely than price fixing. Under a price fixing agreement, competition in service or quality may still be possible. However, a market allocation scheme eliminates all forms of competition.

Field-of-use licensing can be used to divide markets or classes of customers to the public detriment. Use restrictions in licenses afford the opportunity for a patent owner to organize the market into a series of separate, noncompeting submarkets. The licensees in each of the submarkets are thus made immune from competition from their fellow licensees. The effect may be similar to a general horizontal agreement among competitors, all of whom benefit from the particular restrictions imposed.

On the other hand, field-of-use restrictions may benefit the public. For example, let's assume a small chemical company that makes only organic herbicides develops a new catalyst that can be used in a wide variety of organic chemical reactions. This small company might find it monetarily rewarding to grant a large chemical company a license to use the catalyst, but be unwilling to do so because of fear

that the large company would drive it from its marketing field. Thus, commercial exploitation of the patented catalyst for use in fields other than organic herbicides would be retarded unless the patent owner can grant a field restricted license that prevents the large company from making herbicides with the new catalyst.

General Talking Pictures Corp. v. Western Electric Co., 305 U.S. 124 (1938), decided in 1938 remains as the leading case sanctionin field-of-use restrictions. In that case, the Supreme Court recognized that a patentee could limit the licensed use of a sound-system device to speakers for home radios, while restricting both a licensee as well as a buyer (from the licensee) from using the speakers in movie theaters. Thus, despite the fact that in the United States the first authorized sale of a patented article "exhausts the patent monopoly," the General Talking Pictures decision holds that certain non-price limitations on manufacturing licensees and their purchasers are justified.

The Justice Department is, however, eager to challenge the continuing validity of General Talking Pictures as a broad sanction for all field-of-use restrictions. The Justice Department is urging a rule of reason approach to all field restrictions placed on a manufacturing licensee.

b. Price-fixing

When a patentee controls or fixes a licensee's first-sale price, the competitive impact is somewhat similar to that caused by field-of-use restrictions. For years, licensing agreements controlling a first-sales price of a patented article were grounded on the decision in *United States v. General Electric Co.*, 272 U.S. 476 (1926). This decision discussed in Section II above, permitted a manufacturing and marketing patentee to set the price at which his manufacturing licensee may sell a finished product.

Beginning with a 1948 case, *United States v. Line Material Co.*, 333 U.S. 287 (1948), and extending through the proceedings in *United States v. Huck Mfg. Co.*, 227 F.Supp. 791 (E.D. Mich. 1964), *aff'd per curiam*, 382 U.S. 197 (1965), the Justice Department has unsuccessfully attempted to overrule the holding of the *G.E.* decision.

The precedent value of *General Electric* has been largely diluted, however, by court determinations that: a patentee cannot control the resale price of a patented product once he has sold it; *e.g.*, *Simpson v. Union Oil Co.*, 377 U.S. 13 (1964); nor fix the price to be charged by his licensee if his patent covers only a portion of a product,

United States v. General Electric Co., 80 F. Supp. 389 (S. D. N. Y. 1948). Similarly, a patent owner loses license pricing control if his patent covers the process and the machine used to produce the product, but not the product itself, Barber-Colman Co. v. National Tool Co., 136 F. 2d 339 (6th Cir. 1943); if more than one license is issued, Newburgh Moire Co. v. Superior Moire Co., 237 F. 2d 283 (3d Cir. 1956); Tinnerman Products Inc. v. George K. Garrett Co., 185 F. Supp. 151 (E. D. Pa. 1960); United States v. U. S. Gypsum Co., 340 U. S. 76 (1950); if the arrangement is part of a mutual agreement among distributees of competing products, United States v. Masonite Corp., 316 U. S. 265 (1942); or if there are several patent owners participating in a cross-licensing arrangement, United States v. Line Materials Co., 333 U. S. 287 (1948).

c. Territorial Restrictions

Territorial licensing practices should first be viewed from the perspective of Section 261 of the Patent Code, which specifically authorizes a patent owner to "convey an exclusive right under his application for patent, or patents, to the whole or any specified part of the United States." As a consequence, patent licenses can be legally granted under which a licensee is territorially restricted to United States

geographical and trading areas of use, Deering, Milliken & Co. v. Temp-Resisto Corp., 160 F. Supp. 463 (S. D. N. Y. 1958). The Justice Department has not directly questioned such an interpretation of this portion of the patent code. See, Gibbons, Domestic Territorial Restrictions in Patent Transactions and the Antitrust Laws, 34 Geo. Wash. L. Rev. 893, 925 (1966).

The rights under Section 261 are limited to dividing domestic markets into sales territories or regions, under the patent owner, and any combination of patent owners, for example, dividing world markets, runs afoul of the Sherman Act. U. S. v. National Lead Co., 63 F. Supp. 513 (S. D. N. Y. 1945), aff'd, 332 U. S. 319 (1947) and United States v. Singer Mfg. Co., 374 U. S. 174 (1963).

The Department of Justice has not, over the years, been highly active in attacking license agreements between a United States firm and a foreign firm that prohibit the foreign firm from exporting into the United States, but do not prohibit the United States firm to export. It is clear, however, that the United States antitrust laws are applicable to agreements limiting imports to the United States if they have an adverse impact on competition within the United States.

If a U. S. licensor imposes restrictions on a Kenyan licensee, that prohibits the Kenyan firm from selling in Britain, there is no substantial effect on the foreign commerce of the United States, and the United States antitrust laws are inapplicable. If, however, the Kenyan firm is prevented from exporting to the United States, there may be a substantial effect on the foreign commerce of the United States which would make the antitrust laws apply.

The recent Justice Department complaint against Westinghouse and the Japanese Mitsubishi companies is of great interest in the field of international licensing.

The Westinghouse case is not a simple know-how license with territorial restrictions. Neither does it involve a simple license of a foreign patent owned by Westinghouse accompanied by a refusal to license a counterpart U. S. patent.

The following facts clearly alleged in the complaint describe several practices which are illegal per se in domestic patent licenses:

(1) Not only where patented products subject to territorial restrictions, but so also were a great number of other products of the same general type covered by the license agreement (the complaint states a veritable laundry list of electrical products) -- even though

such products might not incorporate any of the transferred technology.

(2) The agreements together with their territorial restrictions cover products as to which Mitsubishi did not wish to be licensed. This is alleged evidence of a clear mandatory package licensing policy.

(3) The agreements had been in existence for over forty years, an unreasonable length of time by anyone's standards. Moreover, the agreements still had years to run.

The Westinghouse-Mitsubishi case involves the following general fact pattern. Two major manufacturers in different countries exchanged technology, in broad fields, with the intent and effect of precluding each from exporting a range of products that was broader in scope than the technology transferred to the other's country. A similar agreement that covered broad fields not confined to patent or know-how rights was held illegal in U. S. v. National Lead Co., 63 F. Supp. 513 (S. D. N. Y. 1945), aff'd, 332 U.S. 319 (1947).

d. Grant-backs

An exclusive "grant-back" provision is a legal and valid covenant, under Transparent-Wrap Machine Corp. v. Stokes and Smith Co., 329 U.S. 637 (1947), on remand, 161 F.2d 565 (2d Cir. 1947), cert. denied,

331 U.S. 637 (1947), if such a provision is not linked with any other anti competitive activity. In Transparent-Wrap, a licensee was required to assign improvement patents back to his licensor. The grant-back provision was found to not constitute an illegal extension of the licensor lawful monopoly.

The United States Department of Justice views exclusive "Grant-back" requirements on all improvement patents as extending the patent monopoly and thereby stifling innovation, i.e., research and development efforts, on the part of licensees. The Justice Department is seeking to overrule the Transparent-Wrap case.

In contrast to a requirement that the licensee assign improvement patents, non-exclusive licensing-back is generally a legitimate provision in the licensing of a basic patent.

e. Other Types of License Restrictions That Can Create Antitrust and Misuse Problems

For the sake of brevity, the existence of the following types of restrictions is noted, but not discussed. These restrictions are generally not as widely used in the United States as the restrictions described in detail above. A citation to pertinent decisions of United States courts with respect to each type of restriction follows each individual listing.

i. Differential (discriminatory) Royalties

LaPeyre v. F.T.C., 366 F.2d 117, 151 U.S.P.Q. 79 (5th Cir. 1966).

Laitram Corp. v. King Crab, Inc., 244 F.Supp. 9, 146 U.S.P.Q. 640, mdf'd, 245 F.Supp. 1019, 147 U.S.P.Q. 136 (D. Alaska 1965).

Peelers Co. v. Wendt, 260 F.Supp. 193, 151 U.S.P.Q. 378 (W.D. Wash. 1966).

Bela Seating Co. v. Poloran Products, Inc., 297 F.Supp. 489, 160 U.S.P.Q. 646 (N.D. Ill. 1968), aff'd on a more limited ground, 438 F.2d 733, 168 U.S.P.Q. 548 (7th Cir. 1971).

Carter-Wallace, Inc. v. United States, ____ F.Supp. ____, 167 U.S.P.Q. 667 (Comm'r Op. Ct. Cl. 1970), adopted in part and denied in part, ____ F.2d ____, 171 U.S.P.Q. 359 (C. Cl. 1971).

ii. Post-expiration Royalties (royalties required after expiration of patent rights)

Brulotte v. Thys Co., 379 U.S. 29 (1964).

iii. Pre-issuance Royalties
(royalties required prior to issuance of a patent)

Lear, Inc. v. Adkins, 395 U.S. 653 (1969).

Pollack v. Angelus Block Co., 171 U.S.P.Q. 182 (Calif. Super. Ct. 1971).

Epstein v. Dennison Mfg. Co., 314 F.Supp. 116 (S.D.N.Y. 1969).

iv. Patent Pools and Cross-Licensing

United States v. Birdsboro Steel Foundry & Machine Co., 139 F.Supp. 244 (W.D. Pa. 1956).

United States v. National Lead Co., 63 F.Supp. 513 (S.D.N.Y. 1945), aff'd, 332 U.S. 319 (1947).

United States v. Singer Mfg. Co., 374 U.S. 174 (1963).

United States v. Line Material Co., 333 U.S. 287 (1948).

Standard Oil Co. (Indiana) v. United States, 283 U.S. 163 (1931).

Hartford-Empire Co. v. United States, 323 U.S. 386 (1945).

Kobe, Inc. v. Dempsey Pump Co., 198 F.2d 416 (10th Cir. 1952).

United States v. New Wrinkle Inc., 342 U.S. 371 (1952).

United States v. Imperial Chem. Indus., 100 F. Supp. 504 (S.D.N.Y. 1951).

United States v. Besser Mfg. Co., 96 F. Supp. 304 (E.D. Mich. 1951), *aff'd*, 343 U.S. 444 (1952).

Standard Sanitary Mfg. Co. v. United States, 226 U.S. 20 (1912).

Zenith Radio Corp. v. Hazeltine Research, Inc., 395 U.S. 100, 161 U.S.P.Q. 577 (1969).

v. *Power to Veto Further Licenses*

United States v. Besser Mfg. Co., 96 F. Supp. 304 (E.D. Mich. 1951), *aff'd*, 343 U.S. 444 (1952).

United States v. Krasnov, 143 F. Supp. 184 (E.D. Pa. 1956), *aff'd per curiam*, 355 U.S. 5 (1957).

vi. *Quantity Restrictions*

American Equipment Co. v. Tuthill Bldg. Material Co., 69 F.2d 406 (7th Cir. 1934).

Q-Tips, Inc. v. Johnson & Johnson, 109 F. Supp. 657 (D.N.J. 1951).

PART 2

ANTITRUST LAW OF THE EUROPEAN ECONOMIC COMMUNITY (EEC)

I. INTRODUCTION--A BRIEF OUTLINE OF THE FORMAL ANTITRUS STATUTES

EEC antitrust law is embodied in Articles 85 and 86 of the Trea of Rome of March 25, 1967. Articles 85 and 86 somewhat resemble, respectively, Sections 1 and 2 of the Sherman Act, the most basic part of United States Antitrust Law.

A. Article 85; Prohibited Practices

1. The following practices shall be prohibited as incompatible the Common Market: all agreements between undertakings and all concerted practices which areliable to affect trade between Member States which are designed to prevent, restrict or distort competition with the Common Market or which have this effect. This shall, in particular,

(a) the direct or indirect fixing of purchase or selling prices or of any other trading conditions;

(b) the limitation or control of production, markets, technical development, or investment;

(c) market sharing or the sharing of sources of supply;

(d) the application of unequal conditions to parties undertaking equivalent engagements in commercial transactions, thereby placing them at a competitive disadvantage;

(e) making the conclusion of a contract subject to the acceptance by the other party to the contract of additional obligations, which, by their nature or according to commercial practice have no connection with the subject of such contract.

2. Any agreements or decisions prohibited pursuant to this article shall automatically be null and void.

3. The provisions of paragraph 1 may however, be declared inapplicable in the case of:

--any agreement or type of agreement between undertakings;

--any decision or type of decision by associations of undertakings; and

--any concerted practice or type of concerted practice which helps to improve the production or distribution of goods or to promote technical or economic progress, while allowing consumers a fair share of the resulting profit which does not:

(a) subject the concerns in question to any restrictions which are not indispensable to the achievement of the above objectives; or

(b) enable such concerns to eliminate competition in respect of a substantial part of the goods concerned.

B. Article 86; Abuse of Dominant Market Position

Any improper exploitation by one or more undertakings of a dominant position within the Common Market or within a substantial part of it shall be deemed to be incompatible with the Common Market and shall be prohibited, in so far as trade between Member States could be affected by it.

The following practices, in particular, shall be deemed to amount to improper exploitation:

(a) the direct or indirect imposition of any unfair purchase or selling prices or of any other unfair trading conditions;

(b) the limitation of production, markets, or technical development to the prejudice of consumers;

(c) the application of unequal conditions to parties undertaking equivalent engagements in commercial transactions, thereby placing them at a commercial disadvantage;

(d) making the conclusion of a contract subject to the acceptance by the other party to the contract of additional obligations which by their nature or according to commercial practice have no connection with the subject of such contract.

C. Enforcement Procedures

Compliance with Articles 85 and 86 is insured by:

(1) The Commission of the European Economic Community. The Commission may itself initiate proceedings under the Articles, or it may act on the complaint of a Member State, or "natural and legal persons and associations of persons who show a justified interest." (Reg. 17, Art. 3)

(2) Domestic courts of Member States may also act pursuant to Articles 85 and 86. There is some overlap between jurisdiction of domestic courts and jurisdiction of Community institutions which is best viewed by the types of cases which arise relating to competition law:

(a) The Commission, under judicial control of the Court of Justice, has exclusive jurisdiction to impose fines and penalties for Community antitrust violations; it has exclusive jurisdiction over the granting of Article 85(3) exemptions.

(b) Community and domestic national courts have concurrent jurisdiction to declare a restrictive agreement null and void applying 85(1) and 85(2), and/or declare that such an agreement is not restrictive. In this situation, decisions of the Court of Justice take priority over decisions of domestic courts.

In this regard, the Court of Justice in Wilhelm v. Bundeskartellamt, Court of Justice Case No. 14/68, February 13, 1969, held that in cases of conflict between Community and national rules on competition, the Community rules prevail, and national authorities must respect Commission decisions relating to restrictive practices or agreements.

(c) Some cases give rise to parallel jurisdiction between the Community and Member States. That is, where some course of action violates Community antitrust law and the same activity also violates separate national antitrust laws of Member States, the business concerns involved may be subject to prosecutions in both jurisdictions for

different offenses arising out of the same set of operative facts. The Wilhelm case held that there is no provision in the Treaty which prevents dual prosecutions under national and Community law so long as the national action does not frustrate the uniform application and implementation of Community law.

(d) Article 177 of the Treaty permits national courts to refer to the Court of Justice for preliminary rulings questions of Community law that arise in the court of national proceedings; where such questions arise in domestic proceedings from which there is no appeal under domestic law, Article 177 provides that those questions must be referred to the Court of Justice.

(3) Administrative authorities of Member States may also apply Articles 85 and 86 when they receive a complaint which falls within the ambit of those Articles.

D. Regulation 17 Implements Articles 85 and 86.

Articles 85 and 86 were implemented by Council Regulation No. 17 of February 6, 1962.

Article 2 of Regulation 17 entitles any enterprise or association of enterprises in doubt as to the legality of an agreement or practice under Article 85(1) or 86 to ask the Commission for a negative clearanc Issuance of such a clearance by the Commission indicates a decision by it that on the facts of which the Commission has been notified, it will no challenge the agreement or practice.

This negative clearance procedure enables a business concern to obtain a Commission ruling prior to committing itself to a course of action. It thereby removes one element of uncertainty from the decisio making process of that business, and is advantageous to both the Commission and the regulated business concern.

The provision for a negative clearance is separate and distinct from the exemption provision provided for by 85(3). The negative clearance procedure evidences a decision by the Commission that some agreement or activity is not violative of the antitrust provisions of the treaty; the exemption procedure applies when some agreement or practice falls within the scope of 85(1), but for the policy reasons of 85(3) is exempted from legal sanctions.

Only the Commission of the EEC may grant 85(3) exemptions. The procedure for obtaining the exemptions is for the business concern

involved to notify the Commission of the agreement or practice. Notification will protect the business from being fined for violation of 85(1), and also fixes the date at which any exemption takes effect.

The Commission decisions on whether or not to grant the exemption are subject to review by the Court of Justice of the European communities. That court has held, in S. A. Portelange v. S. A. Smith Corona Marchant International, Court of Justice, Case No. 10/69 (July 9, 1969), that the filing of notification for the purpose of obtaining an 85(3) exemption does not constitute an admission that Article 85(1) is applicable.

Article 4 of Regulation 17 specifies certain agreements, decisions and concerted practices are exempt from the notification requirements. These are:

(1) Where businesses of only one Member State are involved, with no imports or exports between Member States;

(2) Where only two concerns take part and the only effect is to (a) restrict the freedom of one party to fix resale prices or conditions of sale or (b) restrict the rights of any person acquiring or using patent, trademark, or other industrial property rights;

(3) Where the only object is (a) the development or uniform application of standards or (b) joint research to improve techniques for all parties.

These exceptions to the requirement that firms wishing to obtain the exemption allowed by 85(3) give notice to the Commission, do not place the concerns affected outside of the scope of 85(1). Rather, such arrangements are presumptively exempt from 85(1). Nevertheless, businesses involved in such exempt activity may comply with the notification requirements and receive formal 85(3) exemption; or the Commission itself may request such businesses to inform it of agreements or practices which are exempt from notification.

When the Commission decides to grant either a negative clearan or an Article 85(3) exemption it must, pursuant to Article 19 of Regulation 17 publish the content of the application or notification, and invite comment from other enterprises or associations of enterprises or natur or legal persons who show a sufficient interest. A business concern ha the right to a hearing before the Commission (1) in applying for a negati clearance or an Article 85(3) exemption, (2, in a suit to enjoin violation Articles 85 and 86, and (3) in proceedings to impose fines or penalties.

Article 14 of Regulation 17 gives the Commission authority to make all investigations necessary to enforce Articles 85 and 86. It

has subpoena and visitation powers, and may, by decision, order a business concern to submit to investigation. The Commission is empowered to levy fines for violations of Articles 85 and 86.

The Commission may, pursuant to Article 15 of Regulation 17, impose on a business concern fines ranging from 100 to 5,000 units of account* for willfully or negligently:

(1) Supplying false or misleading information in an application for a negative clearance or exemption;

(2) Supplying false information in response to a Commission request for information;

(3) Failing to supply information within the time fixed by a Commission decision;

(4) Submitting incomplete information in an investigation;

(5) Refusing to submit to an investigation ordered by the Commission.

The Commission may fine a business enterprise from 1000 to one million units of account, or 10% of the turnover of that business for the preceding year, where the concern willfully or negligently:

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* A unit of account is the value in currency of 0.88867088 grams of gold. Prior to the December 1971 dollar devaluation it was equivalent to one dollar. Since the devaluation, a unit of account is worth 1.085 dollars.

(1) Violates Article 85(1) or 86;

(2) Violates the terms of a stipulation in an exemption granted under 85(3).

This power to fine was first applied in 1969 on a Commission finding that six drug firms conspired to fix prices and restrain competition in the European quinine market. An aggregate fine of $500,000 was imposed. International Quinine Cartel, Commission Decision of July 16, 1969.

Fines for violation of 85(1) cannot be imposed for activities occurring: (1) after notification to the Commission under 85(3), and (2) prior to the Commission decision on the exemption. Once the Commission has informed parties they do not qualify for an exemption, fines may be imposed for activities coming within the scope of the notification.

The Commission may, under Article 16 of Regulation 17, impose daily penalties on an enterprise which fails to comply with a Commission decision. These penalties range from 50 to 1,000 units of account per day, and may be imposed where a concern fails: (1) to discontinue Article 85 or 86 violations; (2) to discontinue any action prohibited in a decision revoking or modifying an exemption granted under Article 85(3); (3) to completely and truthfully supply information required by the Commission; or (4) to submit to an investigation.

Article 17 of Regulation 17 provides that the Court of Justice has full jurisdiction to review Commission decisions made under Articles 85 and 86. The Court may cancel, reduce, or increase the fine or penalty imposed by the Commission.

II. SUBSTANTIVE LAW--ARTICLE 85 AND ITS APPLICABILITY

The Commission has been slow paced in initiating and deciding actions. Only a small number of cases have been decided under Articles 85 and 86 that deal with licensing transactions. Consequently, strong predictions of what licensing restrictions are safe from attack under EEC antitrust law are difficult to make at this time, and most predictions must be made from decided cases not involving the transfer of rights of patents or know-how. Thus, most of the decided EEC cases involve no lessening by a licensor of his exclusive position through the grant of a license, a fact pattern that has had an ameliorating effect on the legality of license restrictions under United States antitrust law.

Article 85(1) is applicable to agreements, decisions, or concerted practices which "are liable to affect trade between Member States." That is, the activity must prevent, restrict or distort competition within the Common Market. If effects of some activity are felt outside the Common Market, and there is no internal effect, 85(1) does not apply.

The principles set forth in Consten and Grundig-Verkaufs-GmbH v. EEC Commission, Cases No. 56/64 and 58/64, July 13, 1966, as to the interplay between industrial property rights and the provisions of Article 85(1) on anticompetitive behavior and its effect on trade are still valid. There Grundig, a German tape recorder manufacturer, entered an exclusive sales agreement with Consten, a French firm, prohibiting importation into and sales in France of the Grundig product by anyone other than Consten, and prohibiting Consten from resale of the Grundig products outside of France. Grundig also assigned to Consten Grundig's French trademark, GINT; Consten used this mark to oppose importation into France of products bearing the GINT mark.

A French importer of Grundig products from Germany was then sued by Consten for infringement of the GINT mark. A ruling was sought from the Commission on whether the Grundig-Consten agreement violated Article 85(1).

The Court of Justice upheld the Commission's decision finding that where an agreement between a producer and a distributor prevents other distributors from importing the producer's goods into his country, and also prohibits the distributor from exporting such goods to other countries in the Common Market, it affects trade between Member States and falls within the scope of Article 85(1). The case noted that even if an agreement had the effect of substantially increasing trade between Member States it

would not for that reason fall outside of 85(1).

The Court concluded that the thrust of the arrangement in Grundig was to restore the national partitions in trade that the EEC was designed to diminish. As such, it came into conflict with the basic objectives of the Community, and could not be allowed to stand.

Under 85(1) agreements, decisions, and concerted practices are to be judged by their effect on trade between Member States; i. e., an objective test. All objective elements of fact or law are relevant in determining whether the article has been violated. The activity is evaluated in the context of the market in which the concern operates, and the existence of other similar activities in that market will mitigate in favor of the propriety of the action. The Court of Justice has held in S. A. Brasseries de Haecht v. Consorts Wilkin-Janssen, Case No. 23/66, December 12, 1967, that agreements or concerted acts may be judged by their aggregate effects, and the impact of the aggregate effects on the flow of trade between Member States.

The language of 85(1) applicable to "concerted practices" applies not only to formal agreements to embark on a course of action, but also to more tenuous relationships. In the Commission Dyestuffs decision of July 24, 1969, the Commission found that there was a concerted arrangement among ten European dyestuffs producers to raise prices. This conclusion was based on circumstantial evidence short of a showing of actual express arrangements among the producers.

The Commission found that there had been successive price increases in various European countries which were the same for all the countries, for the most part applied to the same dyes, and were implemented in the various countries within a short time of each other. The Commission further found that the instructions sent by the dye manufacturers to their subsidiaries were virtually identical, and that the various manufacturers exchanged information regularly at meetings.

In light of the above findings, the Commission held that the price increases could not be explained simply by the oligopolistic structure of the dyestuffs market, and decided that disciplinary action was appropriate even absent a specific showing of formal agreements to fix prices. The evidence accepted by the Commission here was of the same type that is often successfully used by the United States Department of Justice to establish antitrust conspiracy cases in the United States.

Pursuant to Article 15 of Regulation 17, nine of the companies were fined $50,000 each and one was fined $40,000. This represents the most substantial monetary sanction yet applied by the Commission.

Article 85(1) applies to restraints "within the Common Market." That is, it has no foreign commerce provision. The Commission has granted negative clearances to export cartels whose effect is not felt within the community.

For example, in the Dutch Engineers and Contractors Association (DECA) Commission Decision 64/599 of October 22, 1964, the Commission acted for the first time on an agreement among Common Market firms concerning exports to non-member countries. A Dutch organization of construction firms acting for themselves, associates and subsidiaries, agreed to cooperate on building and construction orders from outside the community where the value of the order exceeded 2 million guilders.

In reviewing the arrangement, the Commission took the position that Article 85 does cover services as well as goods. However, the Commission held that the purposes and effects of the DECA agreements amounted solely to restriction of competition in markets lying outside the Common Market, to which treaty rules on competition do not apply. The Commission reiterated:

> "The fact that several associated undertakings established in other member states are also part of the group in no wise changes this, for their activity under the rules is restricted solely to relations with third countries. Therefore, the object of the internal rules of the group is not to prevent, restrict or distort competition within the Common Market."

The Commission has, however, exercised its power upon acts committed outside of the Common Market which affect trade within the

market. In Dyestuffs, the Commission levied fines against British and Swiss corporations which owned the Common Market subsidiaries directly involved, reasoning that those subsidiaries were acting within the "sphere of influence" of those parent companies, even though the parents were not themselves engaged in business in the Common Market.

Earlier in S. A. Mertens & Straet, Commission Decision No. 64/344 (1964), Bendix, a United States corporation had in 1953 entered into a distributorship agreement allowing Mertens to distribute its products without territorial restriction, but reserving the right to name other distributors in any country in which Mertens distributed, or to directly sell products itself. Mertens agreed to do everything necessary to protect the reputation of Bendix, to provide satisfactory service and maintain adequate stock of products. Mertens was permitted to set its own prices and conditions of sale, and could sell products of Bendix competitors.

The Commission in Mertens found the agreement not to have the effect of necessarily preventing, restricting, or distorting competition, and granted a negative clearance. The Commission did make it clear that nationality of one of the parties would not provide an automatic exemption from 85(1), stating:

> "The mere fact that the conceding undertaking is situated outside of the Common Market is no obstacle to application of Article 85 of the treaty so long as the agreement has effects within the Common Market."

The EEC rules on competition and antitrust apply to industrial property rights; there is no provision in the treaty for special treatment for these rights, and the Court of Justice in the Grundig-Consten case, supra, held that where a holder of an international trademark attempted to authorize a single distributor to obtain a monopoly right over that mark in one Member State, through a national trademark, competition could be sufficiently restricted to amount to a violation of Article 85(1). That is, abusive use of national trademark rights are violative of the community antitrust provisions.

The Court clarified its position on industrial property rights in Parke, Davis & Company v. Probel, Court of Justice, Case No. 24/67, February 29, 1968. There Parke, Davis, an American company, held Dutch patents relating to antibiotics. The defendant companies marketed the same antibiotics in Holland without permission of Parke, Davis; the antibiotics sold in Holland by the defendants had been imported from Italy, where they were freely sold under Italian law which does not grant patent protection for pharmaceuticals.

Defendants contended that Parke, Davis was using its Dutch patent to frustrate the purposes of Articles 85 and 86 by attempting to prevent sale in Holland of a product freely available in Italy.

The Court held that the existence of national patent rights was not in itself violative of the antitrust provisions; the exercise of a patent right would fall within 85(1) only if it were the subject of a prohibited agreement, decision or concerted practice; it would be within the scope of Article 86 only if it were the subject of an abuse of dominant position. It found that neither 85 nor 86 prevent the holder of a patent of a Member State from seeking an injunction against importation of the protected product from another Member State, absent a showing of "arbitrary discrimination, or a disguised restriction on trade between Member States."* The Court found that the existence of a higher sales price of the patented product compared with the non-patented product coming from Italy was not in itself sufficient to show abuse of ownership of a patent.

* Article 36 of the Treaty permits prohibitions or restrictions in respect to importing, exporting, or moving goods which are necessary to protect industrial or commercial property, so long as such prohibitions do not constitute "either a means of arbitrary discrimination or a disguised restriction on trade between Member States."

broad mandate, the Federal Trade Commission (FTC) can proceed against a business on the same antitrust theories as are set forth in the Sherman Act and the Clayton Act.

The text of the United States antitrust laws most frequently applied against licensing transactions are attached to this paper as an Appendix.

Certain uses of patents and know-how, and license restrictions in connection with the use, manufacture, or sale of products, which embody, or are the result of patents or know-how, are subject to the antitrust laws.

The United States antitrust laws are designed to protect and promote competition. They prohibit agreements or collaboration among persons to limit competition unreasonably. They prohibit attempts to create -- and the exercise of -- illegal monopoly power, that is, the power to control market prices or to exclude competition.

B. The Nature of United States Patent Rights

Eash holder of a United States patent receives from Congress a limited and temporary monopoly, that is, ". . . the right to exclude others from making, using or selling (an) invention throughout the United States." 35 U.S.C. § 154. The patent grant, by statute, vests its owner with an interest, the right to exclude, having certain attributes of personal property (35 U.S.C. § 261) in that it may be disposed of by the patent owner *in toto* (by assignment), or *in part* (by license).

and national laws on industrial property rights and that:

> "Since the national provisions regarding the protection of industrial property rights have not yet been unified at the Community level, the national nature of this protection may create obstacles for the free movement of branded products and for the competition system of the Community."

The Court reaffirmed the position it took in the Parke, Davis case, that Article 36 permits restrictions on imports that are justified on the grounds of protecting industrial and commercial property. Restrictions on imports based on rights granted by national legislatures to protect commercial and industrial property are not *per se* affected by Articles 85 and 86 provided the restrictions do not constitute a means of arbitrary discrimination as a disguised restriction on trade between Member States. The Court noted, however, that certain methods of exercising industrial property rights may nevertheless fall within the antitrust prohibitions.

The Court reasoned that trademark rights can be distinguished from other industrial property rights in that the objects of latter are often deemed "more important and worthy of protection that the object of the former," and that the exercise of trademark rights is particularly liable to contribute to the division of markets and to hinder the free

movement of goods. The court concluded that:

> "The simultaneous assignment to several concessionaries of national trade mark rights for the same product, if it has the effect of re-establishing rigid frontiers between member-states may prejudice trade between states and distort competition in the Common Market."

The Court therefore held:

> "Article 85 therefore applies where, by virtue of trademark rights, imports of products originating in other member-states, bearing the same trademark because their owners have acquired the trademark itself or the right to use it through agreements with one another or with third parties are prevented."

The Court found that it was not precluded from jurisdiction by the fact that the agreements in question were concluded before the entry into force of the treaty. It said the fact that the effects of the agreement continued after the effective date of the treaty was sufficient.

As to the applicability of Article 86 to the facts of Sirena, the Court said that an Article 86 violation requires three conditions: (1) the existence of a dominant position; (2) the improper exploitation of that position; (3) the possiblity of prejudice to trade between Member-States. It found that the ability to prohibit third parties from marketing

products bearing a certain mark in a Member-State does not in itself constitute a dominant position under Article 86. The Court stated that a finding that a dominant position must extend to a "substantial part" of the Common Market was absent here. And thirdly, the Court said the improper exploitation of a dominant position is not established by the higher price of a trademarked product in one area, although cautioning that such a higher price could certainly be considered in some cases as part of a broader picture.

The Court in Sirena made obvious efforts to base its holdings as to the applicability of Article 85(1) to the particular facts before it. Nonetheless, there appear to be some inconsistencies between the Sirena holding applying 85(1) and the Parke, Davis holding refusing to apply 85(1).

Further development in the law relating to industrial property came in Deutche Grammophon v. Metro, Court of Justice, Case No. 78/70, June 8, 1971. Deutche Grammophon, a German record producer, marketed its products under several marks and supplied its products to retailers or wholesalers who directly supplied retailers. Retail prices were generally controlled, and all records sold under the "Polydor" mark were subject to a price maintenance system

requiring retailers to so agree and requiring the retailers to apply the price maintenance system to Deutche Grammophon records acquired from third parties. The agreement specified that such products could be imported only with consent of Deutche Grammophon and subject to the price maintenance system. Deutche Grammophon agreed to sell only to retailers signing the agreement, and to protect the price maintenance system and proceed against infringements. The products were marketed in Germany and abroad.

Metro purchased "Polydor" brand records from Deutche Grammophon but failed to observe the price maintenance system. Dutche Grammophone thereupon broke off business with Metro, but Metro obtained "Polydor" brand records from a third party in Germany through a French subsidiary of Deutche Grammophon. Deutche Grammophon obtained in German court a provisional injunction against sale or distribution by Metro of records bearing the "Polydor" mark. Metro appealed the injunction, and the appellate court submitted to the Court of Justice the question of the applicability of Articles 86 and 86.

The Court decided that the question facing it in Deutche Grammophon was:

> "Whether Community law is infringed if the exclusive right conferred on a manufacturer of recordings by national legislation to distribute the protected products can be used to prohibit the domestic marketing of products that have been brought into the market in the territory of another Member State by this manufacturer or with his consent."

The Court said that the provisions of 85(1) going to agreements, decisions or concerted practices which may affect trade and prevent, restrict, or distort competition in the Common Market may be applicable to the exclusive distributorship arrangements in Deutche Grammophon. The necessary facts to establish the applicability of Article 85(1) were found to include a showing that the arrangement effects a division of the Common Market by prohibiting imports from other Member-States of products duly brought onto the market in those states. The Court continued, however, saying that even if the arrangement in question does not fall within the 85(1) requirements of an agreement or concerted practice, the inquiry does not end there. Article 5(2) of the treaty commands Member States to "abstain from any measures which could jeopardize the attainment of the objectives of [the] Treaty." In light of this, the Court reasoned that it must also look to whether the exercise of the protection right in Deutche Grammophon conflicts with any provisions of the treaty, particularly those

relating to free movement of goods.

The Court then looked to Article 36, which permits restrictions on movement of goods between Member-States if the restrictions do not amount to "either a means of arbitrary discrimination or to a disguised restriction on trade between the Member-States." Conceding the purpose of Article 36 to be protection of industrial property rights, and conceding the rights owned by Deutche Grammophon were analogous to copyright and covered by Article 36, the Court nevertheless noted that the grant of Article 36 was not absolute, but rather, allows only those restrictions on the free movement of goods that are justified for the protection of the rights "that form the specific object of this property." The Court stated:

> "If a protection right analogous to a copyright is used in order to prohibit in one member-state the marketing of goods that have been brought onto the market by the holder of the right or with his consent in the territory of another member-state solely because this marketing has not occurred in the domestic market, such a prohibition maintaining the isolation of the national marke s conflicts with the essential aim of the treaty, the integration of the national markets into one uniform market. This aim could not be achieved if by virtue of the various legal systems of the member-states private persons were able to divide the market and cause arbitrary

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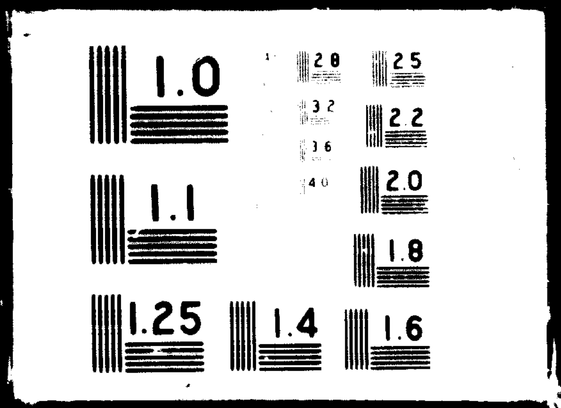


discriminations or disguised restrictions
in trade between the member-states."

Accordingly, the Court held that an attempt by the holder of a national copyright, granted by a national legislature, to prohibit marketing in that state of products sold by him or with his consent in another member-state, violated the treaty.

As to a possible Article 86 violation, the Court found that a manufacturer granted an exclusive distribution right by national legislation does not thereby per se have a dominant position within the meaning of Article 86. This holding was consistent with the entire line of cases dealing with industrial property rights.

The Deutche Grammophon decision, while not based solely or even explicitly on Article 85(1), certainly is a large step from the Parke, Davis case, where antitrust sanctions were held inapplicable to the exercise of patent rights to prevent importation of the same product across national boundaries. If Deutche Grammophon is to be applied to all industrial property rights in the Common Market, it would seem to come close to abolishing the "territorial principle" traditionally associated with the protection of such rights. While abolition of that principle would certainly be consistent with the overall

objectives of the Community, it would represent a significant break with the past.

The Burroughs/Geha and Burroughs/Delplanque decisions by the Commission of Dec. 22, 1971, are an effort by the Commission to clarify applicability of EEC antitrust law to industrial property rights, with particular reference, for the first time, to license agreements. The German firm Geha and the French firm Delplanque obtained non-exclusive production licenses for some patents and exclusive production licenses for others, all relating to the production of a new carbon black paper. The licenses did not include any territorial restrictions on sales, and left both licensor and licensee free to sell the products throughout the Common Market on a non-exclusive basis, though under different trademarks.

The case came before the Commission on an application for a negative clearance. The clearance was granted, on a finding of no appreciable effect on competition because of a relatively small market share of the parties to the agreement and because the licensor and licensees sold the product everywhere in the Common Market.

More importantly, in the Burroughs cases, the Commission included guidelines it would use in evaluating non-exclusive patent and

"know-how" licenses in future cases. It stated that the following obligations would not be deemed violations:

> 1. The obligation to grant no sublicenses, except to wholly dependent companies. This allowance acknowledges that only a patent owner can authorize exploitation of the patent, and that secret know-how can be protected only if not communicated to third parties without the owner's consent.
>
> 2. The obligation to keep the know-how secret.
>
> 3. The obligation preventing the licensee from using the know-how after termination of the license agreement. While difficult to control, the Commission decided this was necessary to encourage communication of know-how.
>
> 4. The obligation to produce the licensed products in sufficient quantities and to follow the technical instructions of the licensor.
>
> 5. The obligation to mark the products fabricated under the license so that their origin can be detected.
>
> 6. The obligation to settle disputes by arbitration.

The Commission in Burroughs stated that exclusive production licenses could fall within Article 85(1) prohibitions, by restricting the ability of the patentee to exploit his patent and limiting the access of non-licensees to new technology.

Burroughs would seem to indicate that the Commission accepts the reservation of reasonable rewards as a proper part of ownership of industrial property rights. The Commission also seems to have rejected the notion that antitrust considerations should be based on the property right owner's reasonable efforts to exclude others from unauthorized use of the right.

Article 85(2) states: "Any agreements or decisions prohibited pursuant to this article shall automatically be null and void." The article makes agreements or decisions violative of 85(1) and not exempted by 85(3) unenforceable; that is, Article 85(2) could be asserted by a party to an agreement as a defense to a legal action by another party to enforce the agreement.

The Court of Justice has held that the automatic nullification of 85(2) extends only to the unlawful portion of an agreement and does not void the entire agreement in Societe Technique Miniere v. Maschinenbau, Court of Justice, Case No. 56/65, June 30, 1966. The Court held that the entire agreement would be voided only if the prohibited parts cannot be separated from the agreement; a construction which reads out of an agreement or decision the offensive sections while validating the larger purposes will be preferred.

Article 85(2) applies only to agreements or decisions. Concerted practices fall outside its scope because there is no legal transaction to be nullified. This is, of course, not to say that concerted practices escape sanction, since the action of fines and penalties still apply to them.

Article 85(3) Exemptions

Any agreement, decision, or concerted practice may be exempted from the provisions of Article 85(1) if it falls within the policy considerations of Article 85(3). Such an exemption will apply if the behavior:

1. Contributes to the improvement of production or improvement of products, or to the promotion of technical progress, and

2. Allows consumers a fair share of the resulting profit.

At the same time, the behavior must not:

1. Subject concerns to restrictions not essential to the affirmative objectives above, or,

2. Enable concerns to eliminate competition in respect of a substantial part of the products involved.

All of these conditions, both affirmative and negative, must be met before an 85(3) exemption will be granted.

The Commission has issued guidelines explaining the kinds of cooperation which would go to qualifying for an 85(3) exemption:

1. Where small and intermediate size concerns cooperate to increase economy and productivity, the Commission will look favorably on such activity. In some cases, cooperation between large concerns may also be found economically justifiable.

2. Where cooperation occurs between concerns whose market position is too weak to be a threat to Common Market competition or to impair Community trade, the Commission will be inclined to permit such cooperation.

These considerations reflect concern by the Commission that not only was it important to protect competition within the market, but it was also important to allow enterprises the ability to compete in the world market with large international firms. The Commission has attempted to strike a balance between the two.

The Commission first declared an Article 85(3) exemption applicable in DRU-Blondel, Commission Decision 65/336 July 8, 1965.

DRU, a Dutch firm granted Blondel, a French firm, the sole selling rights in France for DRU's enamel household goods, some of which were specially manufactured for French users. DRU agreed to forward to Blondel all requests and orders received from France. Blondel was free to establish its own sales prices, and was not forbidden to export out of France.

The Commission found that because Blondel was the only company allowed to import directly from DRU, the agreement constituted a territorial restriction affecting trade between member states, and within the prohibitions of 85(1). However, the Commission found that the arrangement allowed for a less complex distribution arrangement which in turn allowed Blondel to more easily get the products onto the French market. This was seen to be of benefit to the French consumer desirous of purchasing the Dutch manufactured products. The Commission noted that parallel imports of rival products were not inhibited, which would tend to keep the prices for the products at a competitive level; in fact, indirect deliveries from DRU into France of the same products were not precluded by the agreement. In the Commission's view, the agreement allowed easier access by French consumers to the products, at

no increase in price. This was sufficient for the Commission to grant a five-year exemption from the stricture of 85(1).

In Hummel-Isbecque, Commission Decision 65/426, September 17, 1965, the Commission again granted an 85(3) exemption. Hummel, a German firm, granted to Isbecque, a Belgian firm, the sole selling rights for tractors and farm machinery. Hummel agreed not to sell to anyone else in Belgium, but did not agree to prevent indirect deliveries of its products into Belgium by third parties. Isbecque was not required to refrain from re-exporting the products to other countries, and could set its own selling prices. Isbecque also undertook to have special accessories made for the machinery which made it particularly adapted for use in the Belgian countryside.

The Commission found the agreement to be covered by 85(1). The granting of a sole distributorship by a manufacturer in one country to a seller in another, was restrictive in effect and affected commerce between member-states of the community. Nevertheless, the Commission concluded that the impact of the agreement was to increase the efficiency of production and distribution of a product of a superior nature for the uses of Belgian consumers. It found price discrimination to be improbable, since parallel importation was allowed by the agreement, that

the consumer was well served by the arrangement, and that this consumer benefit could not be better accomplished by any other less restrictive approach. An exemption was therefore granted.

Other cases granting the 85(3) exemption have followed the same general pattern: (1) A product particularly suitable or useful for the area covered by an agreement; (2) A sole agency agreement which has the effect of simplifying the distribution system; (3) Consumer benefit, either in the form of lower prices or better availability of desirable products with no increase in price.

The Colgate-Palmolive/Henkel case is a recent application of the 85(3) exemption. The American firm Colgate-Palmolive and the German firm Henkel entered into a joint venture for the purpose of inventing and producing a new cleansing agent for textiles. The patents and know-how falling within the agreement were to be available to both parties without restriction.

Upon notification to the Commission to obtain an 85(3) exemption, the Commission requested that provisions providing different rates of royalties for Henkel and Colgate in certain territories, and a covenant restricting each concern to the geographic area within which it was traditionally influential, be amended. This was accomplished, putting the parties on a more or less even plane.

In evaluating the exemption request, the Commission first looked to the applicability of 85(1). It found the Community market share of each enterprise was significant, and that the joint research undertaking was an appreciable restraint of competition. The reasoning was that the freedom to proceed with research work independently was, in the area covered by the agreement of no practical value because the parties had agreed to license the joint research company with respect to results achieved independently. The Commission therefore found the agreement within the scope of 85(1).

Applying the standard criteria for exemptions, the Commission decided that the agreement should stand. The product which would be created by the joint efforts was a useful one, and the fact of its creation would be improbable absent a cooperative effort. Subsequent to the amendments requested by the Commission, the agreement was not unduly restrictive, in light of the objectives.

The granting of the exemption in Colgate/Henkel is significant in that it indicates a readiness on the part of the Commission to allow cooperative research efforts among large firms, if the standards of 85(3) are satisfied. There is clearly an inclination by the Commission to allow

minor restrictions if they are offset by affirmative cooperation which promises to lead to results not otherwise achievable.

Article 86 Adjudications Have Been Rare

In contrast to the relatively frequent applications of Article 85 of the treaty, there has been very little activity with regard to Article 86, prohibiting "abuse of a dominant position." The Commission did not render any decisions pursuant to Article 86 until 1970, and there is very little fixed law with regard to it.

Article 86 makes it unlawful for one or more business concerns to abuse a dominant position in the Common Market or within any substantial part of it if trade between member-states is affected thereby. The elements of an Article 86 violation are:

1. A dominant position;
2. An abusive exploitation of that dominant position;
3. An effect on trade within the Common Market or a substantial part of it.

It is significant to note that Article 86 is made applicable by conduct rather than status; i.e., a dominant market position is not a per se violation.

The first very important applications of Article 86 have come in two recent cases; the GEMA decision by the Commission, and the complaint filed against Europemballage, a subsidiary of Continental Can, Inc.

In GEMA, Commission Decision 71/224, June 2, 1971, GEMA, a German concern representing composers of musical works for the purpose of exploiting their copyrights, was an economic association formed and operated pursuant to German statutory authorization. The Commission had entered into negotiations with several European firms of this sort in an attempt to bring their practices into conformity with the community competition rules. Only GEMA had refused to modify its behavior.

Under GEMA's rules, only German nationals could obtain membership, and GEMA was the only firm in Germany that managed copyrights of musical works. GEMA's statutes provided that records sold in Germany by its members, exclusively German, paid one set of copyright royalties, while records imported into Germany were required to pay higher royalties. GEMA also placed severe restrictions on the activities of German music publishers in other member-states. It required that a composer assign all of his composition rights for

the whole world to GEMA, which had the effect of preventing GEMA members from doing business with any other copyright concern in any other member-state.

The Commission concluded that the activities of GEMA violated Article 86. It held that a dominant position was clearly established, in that GEMA held a de facto monopoly in Germany, a country which is a substantial part of the Common Market. This dominant position was found to be used in an abusive way by:

1. Discriminating against nationals of other member-states because they are precluded from membership in GEMA;

2. Imposing unjustifiable conditions on GEMA members, particularly the requirement that members assign all copyrights to GEMA. This requirement prevented an author from doing business elsewhere in the Community.

3. Preventing the establishment of a single larger market for music composers and publishers. This third abuse is in direct opposition to the specific aim of the Common Market -- the creation of a single economic area for all member-states. The impact of the GEMA arrangement was to erect a barrier along national boundary lines.

As to the effect on trade between member-states, the Commission held that the statutory provisions precluding membership in GEMA to non-German nationals, and the extra royalty imposed on records imported into Germany demonstrated such an effect on trade between states to justify application of Article 86.

The Commission therefore ordered GEMA to take steps to correct noted Article 86 violations within six months of the Commission decision. GEMA filed an appeal of the decision, but subsequently withdrew it.

In the Europemballage proceeding, the Commission filed in March of 1971 a complaint under Article 86 which for the first time attempted to apply prohibitions against abuse of a dominant position to a merger situation. Europemballage was an American subsidiary of Continental Can, Inc. The complaint charged:

1. That Continental Can, through Schmalbach Lubeca (SLW), an 86% owned German subsidiary, had a dominant position in a substantial part of the Common Market in the area of light metal containers for meat and fish, and closures for glass jars.

2. That Continental Can transferred its interests in SLW to Europemballage, and subsequently directed Europemballage to acquire

majority control over Thomassen Drijver Verbifa (TDV), a strong Dutch competitor of Continental Can in the light metal container market. This attempted acquisition was alleged to be an abuse of a dominant position.

The Commission invoked Article 3 of Regulation 17, which empowers it by means of a decision to oblige enterprises to cease their infringements of Articles 85 and/or 86. The Commission gave its definition of "dominant position":

> "Enterprises are in a dominant position when their scope for independent behavior is such that they can act without making substantial allowance for competitors, buyers, or suppliers. In this event, they are in a dominant position when their share of the market, or their share of the market in conjunction with command of technical know-how, raw materials or capital, enables them to determine prices or to control production or distribution of a substantial proportion of the relevant goods."

The Commission then proceeded to define broadly what constitutes an "abuse of dominant position":

> "An enterprise or a group of enterprises in a dominant position may take improper advantage of said position by acquiring a majority holding in a competing enterprise.

"In the first place, the Commission considers that action taken by an enterprise on the basis of its dominant position constitutes abuse of said position when it is objectively prejudicial to the objectives of the EEC Treaty, more particularly 'the establishment of a system ensuring that competition shall not be distorted in the Common Market' [Article 3(f)]. This is the case when the combination of an enterprise in a dominant position with another enterprise strengthens the said dominant position in such a manner as to eliminate competition for a substantial part of the relevant products.

"Now the acquisition by the Continental Can group of the TDV competitor enterprise, which itself holds a strong position in a market adjoining the German market, is an industrial operation leading to an irreversible change in the structure of supply which hampers maintenance of workable competition in a substantial part of the Common Market."

The Commission ultimately ruled that Continental Can's acquisition of SLW constituted an Article 86 violation, finding attempts to monopolize a market or effect structural changes in the market are within the coverage of 86. Consistent with the wording of Article 86, the Commission focused not on the merger itself, but on the elimination of actual or potential competition. The thrust of the decision was that the acquisition by a firm in a dominant position of a competitor, which

results in diminished competition, has the effect of violating Article 86(b), which prohibits exploitation of a dominant position resulting in "the limitation of production, markets, or technical development to the prejudice of consumers." That is, an activity which diminishes the freedom of choice of consumers as to product utilization is a detriment to consumers within Article 86.

It is worth noting that the Commission's decision did not depend on a finding that the dominant position was used in order to achieve the disapproved result. It is sufficient that the result does occur, whatever the motivations of the parties involved, and that its occurrence is attributable to the actions of an enterprise in a dominant position. This is consistent with the broader policy of the EEC competition provisions that behavior is to be judged by objective standards and its actual impact on competition, rather than by subjective factors.

The Commission decision directed Continental Can to submit divestiture plans before July 1, 1972 with respect to its acquisition of SLW.

The decision indicates that the Commission may in the future eliminate the reluctance it has previously evidenced in applying Article 86. Such a change in attitude could create a change in the Commission's previously stated positions that a patent or trademark do not confer a "dominant position."

PART 3

ANTITRUST ENFORCEMENT IN DEVELOPING COUNTRIES -- A SUGGESTION

An inspection of the domestic licensing practices of United States firms is enough to show that strict antitrust enforcement would not be a panacea for spurring industrial growth in underdeveloped countries. In the United States, businesses are generally unwilling to license their know-how to their direct domestic competitors. This reluctance to domestically license know-how stems at least in part from the effects of strict antitrust enforcement. It is not possible to write domestic know-how licenses that will withstand antitrust scrutiny and still protect the licensor from what he usually views as potentially ruinous competition.

On the other hand, United States firms freely license their mainstream technology to foreign concerns which are potential competitors. A variety of barriers to the United States markets, including, national patent laws, tariffs and customs, transportation charges, and the opportunity to impose license restrictions, all contribute to the increased willingness to license valuable know-how.

A developing country that embarks on a program of strict antitrust law enforcement aimed at eliminating license restrictions on exports from the country runs the risk of creating a strong disincentive to license. The elimination of restrictions on exports to the licensor's home territory would effectively eliminate one of the bases frequently used by businesses in justifying a decision to license its mainstream technology.

Another potential problem facing a developing country that looks to strict antitrust law enforcement in the field of licensing ventures as a means for increasing its ability to export, is providing the degree of certainty of decision on which businessmen can rely. Nothing bothers businessmen more than uncertainty. Indeed, in the United States where strict antitrust enforcement is an accomplished fact, the most frequent criticism of the antitrust laws is the uncertainty they creat. This uncertainty results from the necessarily broad language used in the underlying statutes.

Because lawyers can draft agreements that literally fall outside the scope of any set of precisely drafted rules, broad language, such as used in the United States Sherman Act and EEC Articles 85 and 86, is probably the only solution to use in drafting antitrust laws.

After 80 years of enforcement history, most United States businessmen and many lawyers are still unsure of the scope and thrust of the Sherman Act.

The complexity and uncertainty of substantive antitrust law suggests that developing nations rather than making an attempt to rapidly develop a body of substantive antitrust law, should initially focus their attention on the <u>duration</u> of licensing and other restrictive commercial agreements. This approach would provide a grace period of antitrust immunity or relaxed enforcement for each new commercial agreement or venture, and would be followed by more strict antitrust enforcement.

Such an approach would make easier and more certain the initial administration of the implementing national legislation, and would promote certainty for a length of time sufficient to reassure most businessmen. Antitrust enforcement after a grace period would ultimately raise questions, but with a less disastrous effect on the incentive of foreign businessmen to license. Further, such an approach would harmonize with the actual ability and needs of the developing country.

For example, a developing country must first obtain the know-how and capital to build and operate a production facility. The first products produced by a new industry in a developing country may not be able to compete in world export markets. Later, as the local business enterprise develops its technical and marketing skills, exports become more of a commercial reality.

A permissive policy by a developing country towards restraints on competition for periods of strictly limited duration thus offers several advantages. Such a policy retains as an inducement to license, the prospect of fat early profits for the licensor. Enforcement and administration problems for the developing country are minimized, and certainty of decision during the initial grace period is promoted. Finally, such a policy would permit the industry in the developing country to compete in the export market at the time its skill level makes it a viable competitor.

The implementing legislation for establishing an initial lenient policy towards restrictions on competition with a subsequent strict policy would desirably be in simple broad language and could take many forms. For example, the legislation could require that (a) any agreement or business venture of a duration longer than 5 to 10 years,

and (b) any agreement extending a pre-existing business relationship, should be submitted to a government body for inspection as to compliance with a national policy of promoting exports and the growth of national industries. Unreasonably restrictive agreements of extended duration would be made unenforceable and subject to sanctions.

One effect of such a policy would probably be to cause foreign businesses to immediately begin to draft highly restrictive license agreements of a time duration just short of the time limit selected in the implementing legislation. Another probable effect is that subsequent or continuing agreements would be drafted to be much less restrictive. These two effects would lighten the enforcement and administration burden, and not remove incentive to grant the initial license. Most importantly, the freedom to compete in export markets would be a natural result.

APPENDIX A

SECTION 1 OF THE SHERMAN ACT (15 U.S.C. § 1)

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 hereby declared to be illegal.

SECTION 2 OF THE SHERMAN ACT (15 U.S.C. § 2)

Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a misdemeanor. . . .

SECTION 3 OF THE CLAYTON ACT (15 U.S.C. § 14)

It shall be unlawful for any person engaged in commerce, in the course of such commerce, to lease or make a sale or contract for sale of goods, wares, merchandise, machinery, supplies, or othe commodity, whether patented or unpatented, for use, consumption, or resale within the United States . . . or fix a price charged therefor, o discount from, or rebate upon, such price, on the condition, agreeme or understanding that the leasee or purchaser thereof shall not use or deal in the goods, wares, merchandise, machinery, supplies, or othe commodity of a competitor or competitors of the leasor or seller, whe the effect of such lease, sale, or contract for sale or such condition, agreement, or understanding may be to substantially lessen competitic or tend to create a monopoly in any line of commerce.

SECTION 4 OF THE CLAYTON ACT (15 U.S.C. § 15)

Any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee.

SECTION 7 OF THE CLAYTON ACT (15 U.S.C. § 18)

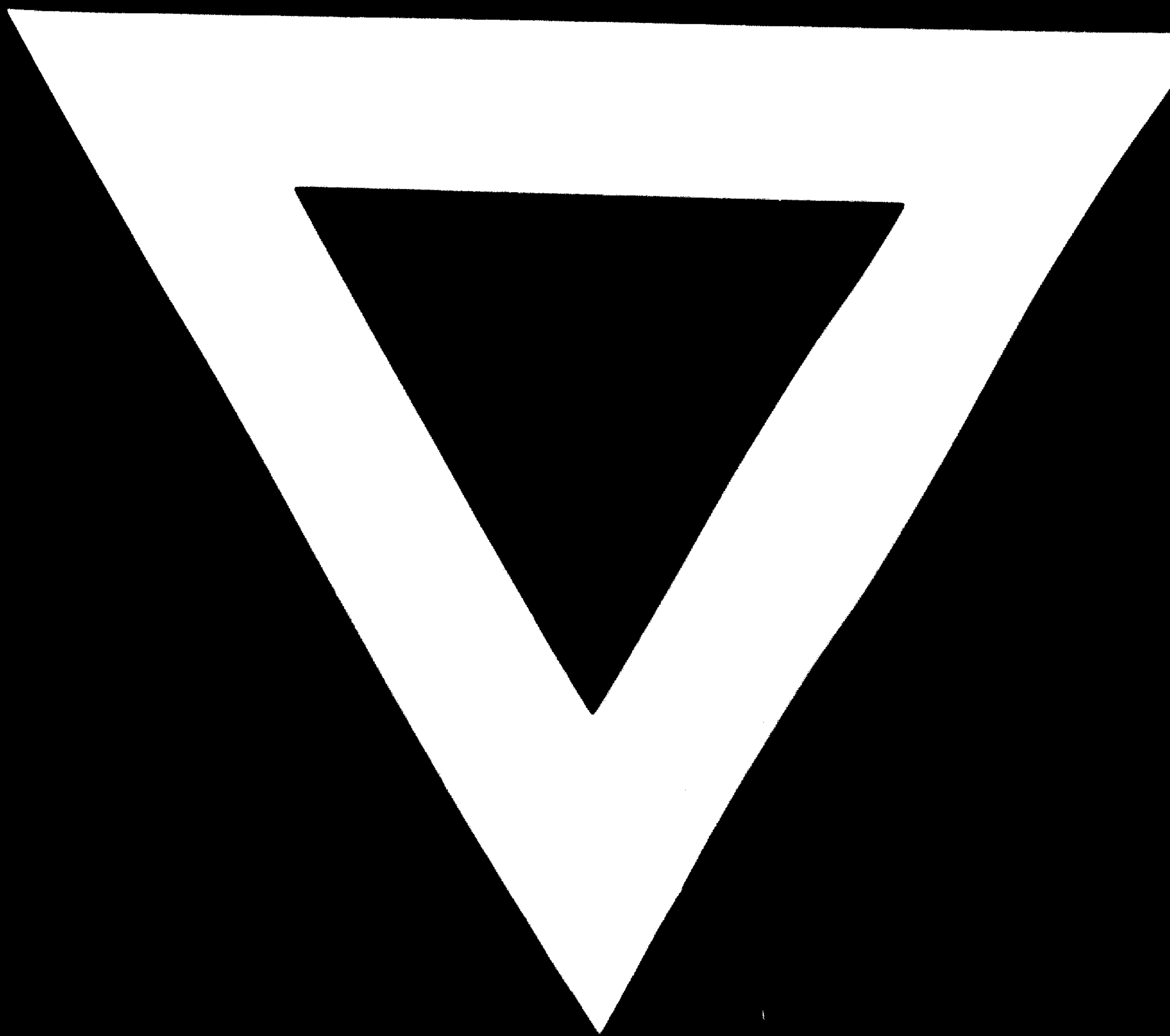
No corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no corporation subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another corporation engaged also in commerce, wherein any line of commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition or to tend to create a monopoly.

SECTION 5 OF THE FEDERAL TRADE COMMISSION (15 U.S.C. § 45)

(a)(1) Unfair methods of competition in commerce, and unfair or deceptive acts or practices in commerce, are hereby declared unlawful.

. . . (b) Whenever the Commission shall have reason to believe that any such person, partnership, or corporation has been or is using any unfair method of competition or unfair or deceptive act or practice in commerce, and if it shall appear to the Commission that a proceeding by it in respect thereof would be to the interest of the public, it shall issue and serve upon such person, partnership, or corporation a complaint stating its charges in that respect and containing a notice of hearing. . . . If upon such hearing the Commission shall be of the opinion that the method of competition or the act or practice in question is prohibited by this Act it shall make a report in writing in which it shall state its findings as to the facts and shall issue and cause to be served on such person, partnership, or corporation an order requiring such person, partnership, or corporation to cease and desist from using such method of competition or such act or practice.

. . . (2) Any person, partnership, or corporation who violates an order of the Commission to cease and desist after it has become final, and while such order is in effect, shall forfeit and pay to the United States a civil penalty of not more than $5,000 for each violation, which shall accrue to the United States and may be recovered in a civil action brought by the United States. Each separate violation of such an order shall be a separate offense, except that in the case of a violation through continuing failure or neglect to obey a final order of the Commission each day of continuance of such failure or neglect shall be deemed a separate offense.



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