TRADEMARK LICENSING AGREEMENTS IN LIGHT OF THE EC COMPETITION RULES

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Resumen: Uno de los problemas que plantean los contratos de licencia de marcas es la conciliación del interés de los contratantes con el Derecho de la competencia. Por un lado, es preciso garantizar a las partes la más amplia libertad contractual, al mismo tiempo que, no obstante, debe preservarse, por otro, la libre competencia en el mercado. El presente artículo constituye una aproximación al régimen de los contratos de licencia en dicho contexto, en el que la clave es encontrar el balance adecuado entre los legítimos intereses de los titulares de derechos sobre marcas y la protección de la competencia leal, dos conceptos que se complementan uno a otro y que constituyen elemento indispensable del mercado común Europeo.

Palabras clave: Contratos de licencia de marcas, Cláusulas contratuales individuales, Prohibición del art. 81(1) Tratado CEE, Cláusulas tie-in, licencia exclusiva.

Abstract: Licensing of trademarks is one of the areas where interests of trademark holders and competition rules overlap. On the one side, there is a need to guarantee to the parties the broadest possible freedom in shaping the licensing contract, on the other again, protection of other traders and of undistorted competition in the market remains the matter of concern for European authorities. The present paper provides an overview of the rules relating to trademark licensing agreements, as they were developed by the European institutions and shaped according to requirements of the EU competition law. It is to highlight the search for the right balance between legitimate interests of trademark holders and
protection of fair competition, the two concepts which complement each other and which constitute an indispensable element of the Common Market.

Keywords: Trademark licensing agreements, Individual contractual clauses, Prohibition of art. 81(1) EEC Treaty, Tie-in clauses


“The exercise of trade mark rights is particularly liable to contribute to the division of markets and therefore to prejudice the free movement of goods between States which is essential for the Common Market. Trade mark rights are distinguished from other industrial and commercial property rights in so far as the object of the latter is often more important and worthy of greater protection than the former.”

“Trade mark rights constitute an essential element of the system of undistorted competition which the EEC Treaty aims to establish and maintain.”

Introduction

As pointed out by G. F. Henderson ‘[t]rade marks law is not as technically or scientifically complex as patent law. It is not as trendy and glamorous as copyright law. However, it is, in many respects, the oldest, most pervasive, most legally complex, erudite and commercially impor-
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It has not been such a long time since these words were expressed by a distinguished Canadian scholar and it would be right to say that some things have already changed. For example, the object of trademark law in fact becomes more and more ‘trendy’ and sometimes also ‘glamorous’. Let’s take a case of fashion industry where trademarks very often constitute a core around which the growth of success of the holder of a mark and products it covers can smoothly continue. Not only that, trademarks have bravely surpassed the role and functions which have been traditionally assigned to them, namely from indicators of origins of goods, the guarantee of their constant quality and instruments which help consumers in their market choices, trademarks became signs that very often constitute commercial as well as cultural icons and that frequently represent the image which people wish to acquire and share. Then, there is no doubt today that trademarks have their role in transfer of new technologies and expansion of innovations in all fields, this particularly takes place when these technologies are sold or licensed together with trademark assignment or trademark licence respectively.

It is interesting to note, however, that the way to arrive up to this point was long and not always easy for trademarks. Still, few decades ago the Community law traditionally perceived intellectual property rights as a threat to market integration; consequently, free movement of goods and competition rules were designed to limit the partitioning of the market caused, among others, by intellectual property rights. It is not until relatively recently, that IP rights were recognized as important factors contributing to innovation and consumers’ benefits. What is extremely important, is the acknowledgment by the European judicial authorities that intellectual property rights do not create by themselves unfair market power for their holders, and as a result that such rights are not inherently anticompetitive.

Trademarks, as conferring for their holders exclusive rights, have often been accused of creating unfair monopolies. ‘Monopoly’ can be defined as the right to exclude others from the use of a particular resource, for instance from the use of a specific symbol as a trademark. But the truth

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is that without such a monopoly conferred to trademarks, they could not meet any of their functions. As rightly observed by a distinguished specialist in the area, industrial property in fact does not grant a monopoly to its owner, but only exclusive rights. The distinction between these two notions clearly explains the core of the issue. As the cited author specifies, exclusive rights, unlike monopoly, do not protect the owner from competition by substitute products and therefore do not hinder legitimate market competition. To the contrary, if properly protected, trademarks due to their functions constitute an important element of an effective competition system. In that respect it is right to say, as R. Joliet points out, that competition law and trademark law do not conflict, but complement each other. Nevertheless, it does not mean - the referred author continues - that trademark arrangements have never served to implement anti-competitive measures. It is therefore important to find the proper balance between these two concepts: guarantee of undistorted competition and legitimate protection of trademarks’ owners.

Licensing of trademarks is one of the areas where interests of trademark holders and competition rules overlap. On the one side, there is a need to guarantee to the parties the broadest possible freedom in shaping the licensing contract, on the other again, protection of other traders and of undistorted competition in the market remains the matter of concern for European authorities.

The present paper provides a brief overview of the rules relating to trademark licensing agreements, as they were developed by the European institutions and shaped according to requirements of the EU competition law. It is to highlight the search for the right balance between legitimate interests of trademark holders and protection of fair competition, the two concepts which complement each other and which constitute an indispensable element of the Common Market.

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6 Ibidem, at 604.
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Part I

1. The notion of trademark licensing agreements and their uses

1.1. Definition of trademark licensing agreements

Intellectual property rights bestow upon their holders exclusivity with respect to their use, advertising, sale, etc. However, holders of these rights very often are not able to make the fullest possible use of them, and thus they decide to transfer their privilege to others. As pointed out in the literature, the ability of the owner of any intellectual property right to exploit it commercially is one of the chief attributes of such rights. The transfer of an intellectual property right can take a form of a sale (assignment) or a license. Licensing of IP rights significantly contributes to the development and greater availability of products and consequently to consumers’ benefits. Nevertheless, in order to fulfil these functions, the transfer of IP rights must observe certain rules which protect not only the owner, but also the rights in question.

It was observed that trademark licensing has relatively recent origin. The reason can be found in the original function of trademarks, i.e. indication of origin, which was to ensure that goods coming from another source could not carry an owner’s mark. The modern approach to IP rights is able to overcome the traditional concern that shared use of a trademark would amount to accepting confusion about the source of goods, such compromise could be reached through legal approval of ‘coexistence agreements’ between the right holder and third parties. To reconcile the apparent contradiction between the basic function of trademarks and economic as well as social importance of licensing, it is necessary to grant to the owner the possibility of control over the use of the trademark by the licensee, especially with regard to the quality of goods and marketing conditions. In addition, European trademark law provides a possibility for trademark owner to sue his licensee for trademark infringement if he breaks provision of the agreement relating

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10 Ibidem.
12 Introduction to Intellectual Property..., s. 216-217.
to its duration, the form of the mark, the scope of goods and services covered by the licence, the affixed territory as well as the quality of goods and services (art. 8(2) of the harmonization directive). The commercial practice shows that trademark licensing agreements are commonly used in business sectors such as beer, soft drinks, aperitifs, chocolates, cigarettes or clothing.

It is useful to start the analysis by determining what trademark licensing agreements are. The definition presented by R. Joliet properly characterizes such arrangements. He refers to trademark licences as to ‘contractual arrangements whereby a trademark owner permits another to use his trademark where, but for the licence, the other would be trademark infringer’. In his further explanation, the author points out that the owner of a trademark who grants a licence makes a promise to the licensee not to sue him for trademark infringement in case the licensee sells, under a given trademark, products which he himself manufactures, assembles, processes or completes.

Then, W.R. Cornish indicates that a licence to use a registered mark does not confer any proprietary interest on the part of the licensee, but it only allows him to use it, at the same time preventing the owner from any allegation of infringement.

For a clear picture of the discussed matter it is important to make a distinction between trademark licensing agreements and distribution agreements. The latter category are arrangements under which a legal entity, distinct from the trademark owner, has a right to resell the finished trademarked products. There may be certain doubts as to whether bottling, canning or repackaging are stages of the production process and by the same token they require the authorization from the trademark holder, or whether they fall within the distributor’s rights. It seems that rebottling or repackaging, considered as a completion process, need an express authorisation (in the form of a licence) of trademark holder. However, under certain conditions repackaging or relabelling may be allowed (namely in situations where the repackaging is not to affect the original condition of the product, or if it does not cause the damage to the reputation of the trademark, where the importer gave a prior notice

14 JOLIET, op. cit., at 758.
15 Ibidem, at 765.
16 Ibidem.
18 JOLIET, op. cit., at 766.
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to the trademark owner, and the new packaging clearly states who is responsible for repackaging). 19

Conclusion of the licence agreement is one of the ways through which trademark holder can exercise his rights. It enables him not only to set the limits of the use of his rights by other entities, but also to control such use. Nonetheless, although trademark licensing falls within the domain of freedom of contract, it is governed as well by the European Union rules on competition and free movement of goods. As a consequence, every such agreement must respect the relevant provisions of the EC legislation (i.e. art. 81, 82 EC Treaty). The reason for competition law capturing into its realm licensing of IP rights is that restrictive terms of a licence may give rise to creating dominant position, segmenting markets geographically and hindering objectives of the single market. 20 While the owner of an exclusive, intellectual property right deserves protection as regards its individual exploitation, the contractual exploitation of such right is of a different status, because resulting in a shared exclusivity it may have an impact on competition in the market. 21

1.2. EC Trademark licensing provisions

Under European law, the rules relating to trademarks are provided within the framework of two acts. One of them is the First Council Directive of 21 December 1988 to approximate the laws of the Member States relating to trade marks (89/104/EEC) 22, which aims at harmonizing trademark legislation in national systems. Another, the Council Regulation No 40/94 of 20 December 1993 on the Community trade mark 23, introduced a uniform regime for registration and protection of trademarks within the European Union. National trademark systems of the Member States and the Community trademark regime function in parallel and remain independent.

Both acts contain provisions on trademark licensing (art. 8 – trademark harmonization directive, art 22 – Community trademark regulation). Both acknowledge, that a trademark may be licensed ‘for some or

21 ULLRICH, op. cit., at 604-605.
all of the goods or services for which it is registered’ and respectively ‘for
the whole or part of the Member State concerned’ or ‘for the whole or
part of the Community’. In addition, the European legislator expressly
provides that a licence can be exclusive or non-exclusive.

1.3. Other trademark agreements - mention

Apart from licensing contracts, there are other kinds of arrange-
ments leading to exploitation of industrial property rights by parties
other than its first owner. First, such rights may be assigned to third par-
ties. A transfer of ownership of a trademark may be total or partial; it can
be done in respect of some or all of the goods or services for which the
mark is registered. Moreover, holders of trademark rights may enter into
delimitation agreements with each other, on behalf of which they decide
about the manner and the extent to which each of them will use specific
trademarks. Such delimitation arrangements constitute a way to settle a
dispute regarding the entitlement of each party to use a particular mark
or particular marks. It is frequent in arrangements aiming at the settle-
ment of intellectual property litigation, that one party is granted some
form of a licence to continue its prior activities (up to that time: perhaps
infringing). The rationale for concluding such contracts lies in their
purpose to bring to an end the confusion or conflict between particular
trademarks.

These agreements, although having basically different functions
from licensing arrangement, may possess some similar features and simi-
larly fall within the provisions protecting competition.

1.4. Relevant competition law provisions

The present analysis requires a brief look into certain aspects of the
provision of article 81 EC Treaty, in order to assess to what extent tra-
demark licensing agreements may fall within its scope. Art. 81(1) prohi-
bits ‘all agreements between undertakings, decisions by associations of
undertakings and concerted practices which may affect trade between
Member States and which have as their object or effect the prevention,
restriction or distortion of competition within the common market’.

The notion of ‘agreement’ is very widely perceived. ‘Agreements, decisions and concerted practices’ referred to in the text of the Treaty include not only legally enforceable contracts, but also all kinds of informal understandings, gentlemen’s agreements, protocols reflecting a genuine concurrence of will between parties, conditional or partial agreements reached during a bargaining process, as well as guidelines and recommendations by trade associations.26 The provision of art. 81(1) requires for an agreement to be prohibited as incompatible with the Common Market so that its object or effect are prevention, restriction or distortion of competition. As pointed out in the literature, ‘the object’ in this context does not refer to the subjective intention of parties entering into agreement, but to the objective meaning and purpose of an agreement considered in its economic framework.27 If an agreement does not have as its object the restriction of competition, it must have an anti-competitive effect to infringe art. 81(1). This effect is understood broadly, to be precise, an actual or potential, direct or indirect effect on inter-state trade is taken into consideration.28 The Court of First Instance in one of its decisions clarified that assessment of an agreement under art. 81(1) cannot be done in isolation, but it requires consideration of the actual conditions in which it functions, like the economic and legal context, products and services covered by the agreement as well as the structure of the market, unless there are clauses containing obvious restrictions of competition such as price-fixing, market-sharing or the control of outlets.29 

An infringement may be found only when an agreement appreciably restricts competition, i.e. when it has an appreciable effect on trade between Member States, given that art. 81(1) does not apply to agreements of minor importance (de minimis doctrine).30 The Court of Justice stated that an agreement falls outside the scope of application of art. 81(1), if it has an insignificant effect on the market; an insignificant effect is assessed on the basis of the weak position which the entity concerned has on the market of the product in question.31 The more precise guidance on the agreements on minor importance may be found in the Commission

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27 Ibidem, at 92-93.
30 WHISH (2001), at 93-94.
Notice on agreements of minor importance, which does not have a legally binding effect, but may help as an indicator of possible resolutions by the Commission.

Another aspect is the delimitation of the term ‘undertaking’. The European jurisprudence provides that ‘the concept of an undertaking encompasses every entity engaged in an economic activity regardless of the legal status of the entity and the way in which it is financed’. The notion is very broad, and includes companies, partnerships, state owned corporations, agricultural cooperatives, public authorities, bodies entrusted by the state with particular tasks, trade associations, as well as individuals and members of the liberal professions. The absence of a profit motive or of an economic purpose of an undertaking does not disqualify it with respect to application of art. 81, as long as it carries on some commercial or economic activity. However, the provision in question has no application to agreements between such undertakings which form a single economic entity, even though they have separate legal personality (i.e. firms within the same corporate group, a parent and subsidiary companies).

Art. 81(2) provides that any agreement which is prohibited as anti-competitive is automatically void. Then comes an exemption to the prohibition of art. 81(1), which can be declared inapplicable under certain conditions specified in art. 81(3). The declaration of inapplicability of art. 81(1) is granted by the Commission in the form of an ‘individual exemption’ for a particular agreement or by way of passing a regulation which specifies conditions for the ‘block exemption’. An agreement may benefit from the exemption provided by art. 81(3), if it fulfils all four conditions described therein. First, an agreement must contribute to improving the production or distribution of goods or to promoting technical or economic progress. Second, an agreement must allow consumers a fair share of the resulting benefit. At the same time, an arrangement must be consistent with the principle of proportionality, and cannot impose on the undertakings restrictions which are not indispensable to attain its objectives. Finally, an arrangement may not contribute to the elimination of competition in respect of a substantial part of the re-

34 WHISH (2001), at 67-68.
36 Ibidem, at 123.
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levant products. Further detailed clarification on the conditions of art. 81(3) and their application is provided in the Commission Guidelines on the application of Article 81(3) of the Treaty.37

In the light of the above, trademark licensing agreements may well fall within the scope of the competition provisions of the Treaty, as far as they fulfil the above requirements. For that reason, they are subject to control by the relevant European and national institutions. It should also be remembered that trademark licensing is in practice often combined with licensing of other intellectual property rights (i.e. patent, know-how) and for that reason it can be dependent on the right it goes together with.

Part II

2. Individual contractual clauses within the prohibition of art. 81(1) EEC Treaty

Nowadays, it is no longer in question that the grant of a licence increases competition; this instrument allows a licensee to enter the market, a licensee who might not be there at all without the licence.38 Although competition law is not less interested in promoting research, innovation and development, than intellectual property law is39, it still essentially aims at safeguarding the single market against division which may result from the misuse of the IP rights. This part examines the most common clauses that parties insert into their trademark licensing contracts and which may potentially create the distortion of competition. While agreements which include contractual restrictions do not automatically result in restricting competition and it depends upon specific circumstances whether an agreement satisfies the conditions of art. 81(1), there are nonetheless certain clauses which, not being essential for trademark protection, are deemed to be anticompetitive per se (such as price-fixing or restrictions with respect to customers40).

39 WHISH (2001), at 676.
2.1. Territorial protection, exclusive licensing

2.1.1. Exclusivity in trademark licensing – general remarks

Territorial exclusivity constitutes one of the most controversial aspects of intellectual property licensing. On the one side, there is a strong policy against isolation of national markets and partitioning of the Common Market. The other side of the problem lies in the protection of the party who takes a risk by investing into an uncertain undertaking.

It is a common practice that the licensor gives the licensee an exclusive right to manufacture and to sell the products in a given territory and there are different levels of such exclusivity. A ‘sole’ licence is granted if the licensor promises not to give similar rights to anyone else but to the licensee over the same territory, while the licensor himself retains the right to produce and to sell the goods in the given area.\(^{41}\) By an ‘exclusive’ licence, the licensor additionally agrees not to manufacture himself the goods in the licensee’s territory. However, if the licensor promises to prohibit other licensees and their customers from selling the goods into the licensed territory, he creates an ‘absolute’ territorial protection.\(^{42}\)

It is interesting to observe the evolution of the Commission’s position towards the exclusivity arrangements. At present, while the grant of territorial exclusivity does not by itself generate the prohibition of art. 81(1), an absolute territorial exclusivity very likely amounts to an infringement of the provision in question. Nonetheless, such thinking has not always been the rule. In \textit{Re Vélocro/Aplix}\(^{43}\), the Commission held that the exclusive licences could escape the prohibition of art. 81(1) only if they concerned the introduction and protection of a new technology.

Also, in its decision in \textit{Re The Agreements of Davide Campari-Milano Sp.A}\(^{44}\) the Commission stated that as a rule ‘an exclusive trademark licence is a restriction of competition under Article 81(1)EEC’. The Commission further explained in this case the reasons for such finding, namely the exclusive right given to the licensees prevented the licensor from concluding licensing contracts with other parties, it prevented him from manufacturing those products and by the same token made him lose his freedom and the gains coming from the competitive activity.\(^{45}\) Although, according to the Commission, such was the rule, it eventually

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\(^{41}\) WHISH (2001), op. cit., at 678.
\(^{42}\) Ibidem.
\(^{43}\) (1985) O.J. L 233/22.
\(^{44}\) Case 78/253, [1978] 2 C.M.L.R. 397 [hereinafter: \textit{Campari}].
\(^{45}\) Ibidem, at 406.
exempted the said agreements (entered into by Davide Campari-Milano SpA and the respective parties in the Netherlands, Germany, France, Belgium, Luxemburg and Denmark), as fulfilling the conditions set in art. 81(3). The agreements by which Campari-Milano granted its licensees an exclusive right to use its trademark for the manufacture of its aperitifs and for their sale in specific territories, and at the same time undertook not to manufacture its aperitifs itself in these territories, contributed to: improving the production and distribution of the products, concentrating sales efforts and allowing to develop existing plants as well as to built new plants by each licensee; it also provided better supply to consumers in their territories.\textsuperscript{46}

Currently, several legislative acts contain express provisions as to the admissibility of exclusive licensing. To begin with, the trademark harmonization directive (89/104/EEC)\textsuperscript{47} provides in art. 8(1) that a licence may be exclusive or non-exclusive. The same provision is found in the Community trademark regulation\textsuperscript{48}. The latter act precises that a Community trademark may be licensed for the whole or part of the Community.

There is no doubt today as to legality of the exclusivity as such in a trademark licensing agreement. To the contrary, some authors suggest that exclusivity in licensing of trademarks is closely related to intrinsic and traditional role of these signs, namely indication of origin of products. It is argued that to safeguard the source indication function of a trademark, non-exclusive licence should be limited to situations where there is assured an active contribution of the mark owner to the production by the licensees, be it in the form of supply of particular products or the right to control the manufacture of licensees in order to assure the necessary uniformity of production process.\textsuperscript{49}

To find out whether particular territorial protection amounts to infringement of art. 81(1), it is necessary to examine the effects it would have on the market. Therefore, each situation needs to be considered in the light of all the accompanying circumstances.

\textsuperscript{46} Ibidem, at 400, 410-411.
\textsuperscript{47} O.J. L 40, 11/02/1989, p. 1.
\textsuperscript{48} O.J. L 11, 14/01/1994, p. 1.
\textsuperscript{49} G. SENA, Il diritto dei marchi. Marchio nazionale e marchio comunitario, 4 ed. (Giuffrè Editore, 2007), at 172.
2.1.2. Specific circumstances as a basis for infringement of competition rules

The analysis of the Commission’s decisions regarding trademark licensing agreements demonstrates how specific circumstances are being assessed on a case-by-case basis. A good illustration can be found in the decision *Moosehead/ Whitbread*. The decision concerned the agreement upon which Moosehead (Canadian brewer) granted to Whitbread (British brewer) the sole and exclusive right to produce and promote, market and sell beer manufactured under the trademark ‘Moosehead’ in the licensed territory, using Moosehead’s secret know-how. In order to ascertain whether the agreement falls within art. 81, it is not enough to consider its sole wording. At the outset of its analysis the Commission stated that the exclusive trademark licence for the production and marketing of beer and prohibition of active sales outside the specific territory infringes art. 81(1), since it excludes third parties (i.e. five other large brewers in the United Kingdom) from the use as licensees of the Moosehead trademark, as well as it restricts Whitebread from selling the product in other markets within the Common Market. However, consideration of specific characteristics of the United Kingdom beer market leads the Commission to the exemption of the agreement in question on the basis of art. 81(3). These particularities of the UK beer market are as follows: most beer in the UK is sold in public houses licensed for the consumption of liquor; in order to achieve substantial sales of a new beer it is necessary for the seller to have access to a number of public houses; however the majority of these public houses are bound by contract to purchase beer from one brewer alone; it is therefore very important for a foreign brewer to get the assistance of a large national brewer in order to enter the United Kingdom market. In light of the above, the agreement between Moosehead and Whitbread contributes to the improvement of the production and distribution of beer, because the product need no longer be imported from Canada, which reduces transport costs, in addition it will benefit from Whitebread’s distribution network, and also will give consumers a wide choice of products.

The same line of reasoning was presented by the Commission in its previous decision in *Re Carlsberg Beer*. Here, the agreement between

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51 Ibidem, at 35.
52 Ibidem, at 33.
53 Ibidem, at 36-37.
De forenede Bryggerier A/S Copenhagen (Carlsberg) and its United Kingdom subsidiary was a part of long-standing cooperation arrangements, on the basis of which both parties were to develop the production and sale of Carlsberg brand lager beers in the United Kingdom. The Commission acknowledged that ‘with the British beer market dominated by a small number of large groups, it is virtually impossible for a foreign brewery to enter this market without the certainty of being able to sell its products through the distribution network of one of large groups’.55

Another aspect has been considered in the decision Re the ‘Tyler’ Trade Mark56. Here, the Commission concluded that the grant of an exclusive trademark licence to last for 10 years in a Member State constituted protection against competition from the grantor or his licensees for an ‘unreasonable length of time’57.

A further interesting example is given by the case of Hershey/ Herschi58. The matter concerned the trademark settlement, which were to end an ongoing litigation between Hershey Foods Corporation (a large U.S. chocolate manufacture famous for its Hershey trademark throughout the world) and Schiffers Onroerend Goed Exploitatie BV (Dutch company producing soft and other drinks) over the right to use the ‘Herschi’ trademark for certain food products by the latter. Both trademarks were of independent origin. The settlement provided that Schiffers assigns its ‘Herschi’ trademark to Hershey for valuable consideration, and Hershey licenses to Schiffers this trademark to be used on an exclusive basis for five years for a defined group of products (the licence may be renewed at the request of the licensee). Schiffers agrees not to introduce new products in association with the trademark. The positive attitude of the Commission towards the agreement in question lies in the fact that it is to resolve the problem of confusion of the trademark and at the same time it does not partition the Common Market on territorial lines.
2.1.3. Policy considerations with regard to exclusive licensing

While the decisions rendered by the Commission reflect the existing provisions and in a sense draw the line for the development of the rules regarding competition, in fact it is what the European Court of Justice delivers that constitute the actual and comprehensive strategy of the European Union in the area in question. Not only the decisions of the Commission can be overruled by those of the Court, but as the ECJ case law demonstrates, the judicial authority tends to give the thorough justification and general policy considerations for a chosen attitude towards the licensing agreements in conjunction with the competition rules.

In its early case law, the European Court of Justice clearly stated that an agreement, which confers an absolute territorial protection on a distributor, restricts competition and is not eligible for exemption under art. 81(3) – *Consten and Grundig v. Commission*\(^{59}\). It was held in this case that the agreement between the licensor (Grundig-Verkaufs GmbH) and the licensee (Établissement Consten) for the sole distribution of goods (i.e. radio receivers, recorders, televisions, as well as their spare parts and accessories) in the French territory attempted to isolate the French market for Grundig products and to artificially maintain separate national markets within the community. Territorial protection granted to the licensee - contrary to the Treaty - was to control and to prevent parallel imports.

The decision in *Consten and Grundig* should not be perceived as a strict approach represented by the Court in the 60’s. In the same period of time, in *Société Technique Minière v. Maschinenbau Ulm*\(^{60}\) the Court admitted that a clause granting exclusivity on a distributor may escape from the prohibition of art. 81(1), if it is absolutely necessary for the penetration of a new area by an undertaking, and which at the same time does not affect the freedom of third parties through imposing export bans and preventing parallel trade.

Then, the decision in *Nungesser KG v. Commission*\(^{61}\), although not relating to the trademark licensing, contains several important remarks, that may apply not only to the licensing of a plant breeder’s rights, as was the case here, but also to licensing of other intellectual property rights. First, the Court gives a definition of ‘an open exclusive licence’ and ‘absolute territorial protection’, clarifying that the former is not in itself in-
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compatible with art. 81(1) EEC Treaty, but the latter – eliminating all competition from third parties and resulting in artificial maintenance of separate national markets – is contrary to the Treaty.\(^6\) In addition, the court admits that specific nature of products (i.e. whose growth is very complicated and whose reproduction depends on the hazards of climate and soil) may justify the stronger protection of the licensee, especially in cases where considerable financial commitment is made to achieve the risky results. The analysis of the court has a broader application; it is suggested by the court itself, saying that many other products forming the subject-matter of a trademark or a patent, are in a similar situation as the seeds in question.\(^6\) Therefore, the majority of the court’s argumentation can be applied to trademark licensing so long as its subject-matter possess special characteristics that justify the grant of a territorial exclusivity. A commentary on the essence of this decision points out that exclusive licence may escape prohibition of art. 81(1), ‘if in view of the pioneering character of the technology licensed and the risks associated with its introduction on the geographical market covered by the licence, the exclusivity of the licence is warranted as a matter of encouraging the diffusion of the new technology over the entire Common Market by competing with existing substitutes’.\(^6\) The same reasoning could possibly apply to the licence of a trademark which does not possess yet a significant reputation in a given market and therefore investment of the licensee involves his considerable risk.

The analysed case law demonstrates that the infringement of art. 81(1) is an empirical matter,\(^6\) and therefore every agreement should be assessed in its particular economic and market background. The need to protect the parties to an agreement, their rights (licensor) and investment (licensee) may justify certain restrictions, provided such restrictions are properly limited ‘in time, space and subject-matter’.\(^6\)

For a more complete picture of the matter in question, it should be mentioned that trademark delimitation agreements may also adopt certain restrictions, which makes them capable of infringing competition law provisions. These restrictions usually are of two different kinds. First, they may limit the territories in which a company is allowed to use its trademark. Second, they may restrain a company from using on a specific

\(^{62}\) Ibidem.
\(^{63}\) Ibidem, para 35.
\(^{64}\) ULLRICH, op. cit., at 605-606.
\(^{65}\) WHISH (2001), at 101.
\(^{66}\) Ibidem, at 100-101.
kind of product the trademark which it has established for other kinds of product.\textsuperscript{67} If such provisions constrain a party to the extent that is greater than necessary, they fall within the scope of art. 81(1). In particular, they cannot lead to the geographical partitioning of markets. As the Commission held in \textit{BAT Cigaretten-Fabriken GmbH v. Commission}\textsuperscript{68}, delimitation agreements are lawful as long as they serve to delimit the spheres in which the parties’ respective trademarks may be used, but they are not allowed if they aim at dividing the market or restricting competition in other ways.

2.1.4. Legal effects of exclusivity

It is important to remember, that trademark licensing agreements like any other kind of contracts cannot create obligations for anyone else, but for their parties (legal effects \textit{inter partes} only, but not \textit{erga omnes}). Therefore, also provisions granting exclusivity for the parties do not have an effect to restrict the third parties from exercising the rights, which are guaranteed by the legal system itself. Parties to the licensing arrangements, who break their obligations as to territorial manufacturing restrictions or sale restrictions may be liable for the breach of contract. However, the proprietor of a trademark may also invoke his rights conferred by the trademark against the licensee who violates any provision in the licensing contract, including the obligation as to the territory in which a trademark may be affixed (art. 8(2) of the trademark directive, and art. 22(2) of the Community trademark regulation). This extended protection for trademark owners (a trademark infringement action, instead of a simple breach of contract action) proves the importance bestowed upon industrial property rights within the European system.

On the other hand, the principle of exhaustion of rights (adopted in art. 7 of the trademark directive) places a barrier on the unlimited protection that trademark rights may give to their holders. This concept permits a third party to purchase a product, which was put on the market in the Community under the trademark by the proprietor or with his consent, and to sell it on any market a third party wishes.\textsuperscript{69} The proprietor of a trademark may not oppose such a sale by invoking the infringement of his trademark rights, he cannot prevent the subsequent free circulation of the product. He can only oppose such further commercialisation of

\textsuperscript{67} McKNIGHT, op. cit., at 278; SINGLETON, op. cit., at 50.
\textsuperscript{68} Case 35/83, [1985] 2 C.M.L.R. 470.
\textsuperscript{69} WALSH, TREACY & FEASTER, op. cit., at 259.
goods, if there exist legitimate reasons (art. 7(2)), for example when in specific circumstances the given use of a trademark seriously damages the reputation of the mark (Parfums Christian Dior v. Evora70).

2.2. Quality control, manufacturing and marketing of product

A very interesting observation was made in the American literature at the beginning of the 20th century, which subsequently adopted by the U.S. Supreme Court acquired its practical merit for the domain of trademarks. F. I. Schechter claims that consumers develop a mental association between the trademark and the product, and not between the trademark and the producer; it is psychological association of the trademark and the product, that inspires customers to purchase given goods.71 This phenomenon may be due to the fact that nowadays, the expansion of merchandising, where the mark is used by a number of licensees, has turned attention from the mark as ‘identifier of source of the goods’ to the mark as ‘the essence of the goods themselves’.72 It illustrates the importance of these features of products that consumers appreciate and get used to, as well as the significance of the constant maintenance of their quality.

One of the aspects of trademark protection is a recognition of the significance of their owner’s investment into the quality and presentation of the product.73 They enable a manufacturer, who produces high quality goods, to expand his reputation from one market to another without the need to start from the outset each time he wishes to enter into a new area.74 Trademarks encourage their owners to maintain and improve the quality of products sold under the mark, because of their capacity and power to create transparency of goods available to consumers in the market place. By the same token, they stimulate economic progress.75 All these objectives continue to matter also after the right to use a trademark has been licensed. Such a conclusion is allowed in light of the provision

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70 Case C-337/95, (1998) 1 C.M.L.R. 737.
73 PICKERING, op. cit., at 157.
74 GOYDER, op. cit., at 290.
75 Introduction to Intellectual Property..., op. cit., at 183.
of art. 15(3) of the Community trademark regulation, saying that the use of a trademark with the consent of the proprietor shall be deemed to constitute use by the proprietor himself.

It is a natural consequence that in case of trademark licensing serious problems can arise with respect to the consistency of quality of products and, as a result, there is a risk of consumer deception.76 Trademarks, reflecting the quality of the goods, accustom consumers to a certain level of quality, make consumers to expect the same products’ characteristics as those of goods previously purchased.77 In addition to the consumer protection aspect, the quality maintenance is equally essential for safeguarding the trademark holders’ good will and commercial image. Therefore, it should not be surprising that the quality control is an important matter to be decided upon in the licensing agreement. Monitoring of quality is particularly essential with respect to trademark licensing, since unlike the distributor who only sells goods finished by others, the licensee is responsible for their manufacture, selection and distribution. Consequently, the licensee becomes ‘the alter ego of the licensor vis-à-vis third parties with respect to the use of the mark’78. For that reason, an important degree of control over the licensee is justified and desirable.

The importance of quality control in trademark licensing is fully acknowledged by the Commission. In the *Campari* decision, the clauses restricting manufacture of the product only to the plants capable of guaranteeing its quality, as well as the obligation on licensees to follow the licensor’s instructions relating to the manufacture and the quality of the ingredients were found to be compatible with art. 81(1). It is interesting to note, that while the Commission found territorial protection and obligations on licensees not to handle competing products for the duration of the licensing agreement to restrict competition within art. 81(1), and on the basis of specific nature of products granted the exemption provided in art. 81(3), at the same time it rightly considered the restrictions arising out of quality of products not to be covered by the said provision. However, the obligation on the licensees to supply to certain customers (namely: diplomatic customers, ships’ victuallers, foreign armed forces, and other organizations with duty-free facilities) not their own product, but the original product of the licensor himself was found to restrict competition. This clause, justified by the marketing reasons

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76 KAMPERMAN, op. cit., at 413.
77 VUK, op. cit., at 875.
78 WILKOF, op. cit., at 264.
and maintenance of the same original taste for the product being served to customers usually required to move frequently from one territory to another, was subsequently exempted on the basis of art. 81(3).

The same reasoning was adopted in case of Moosehead/Whitbread, where the British licensee agreed to comply with the Canadian licensor’s specifications with regard to the quality of beer as well as with the type and quality of the raw materials.

In light of these decisions it seems justified to say, that quality control and restrictions relating to maintenance of the same characteristics of products are usually compatible with the rules on competition. However, such restrictions should respect the principle of proportionality, because - as pointed out in the Campari case - control measures should not go beyond a legitimate concern for quality control.

Usually, trademark licensing contracts impose upon licensees not only the manufacturing standards, but also the right of the licensor to examine samples of products and to inspect the licensee’s manufacturing facilities. Although such obligations restrict the licensee’s freedom, they do not fall into the prohibition of art. 81(1), since they guarantee the uniformity and quality of products; it seems unlikely that a trademark holder would license his right without such clauses.

Licensee may also be bound to achieve a certain level of sales, the failure to do so may result in termination of a contract. Moreover, he might be obliged to spend a minimum amount on advertising the product, and the advertising is usually subject to the control by the licensor. All these provisions do not create any harm for the competition on the market, and therefore escape the prohibition of art. 81(1).

It was held in IHT Internationale Heiztechnik GmbH v. Ideal-Standard GmbH that one of the decisive factors in a licence contract is the possibility of control over the quality of goods by the licensor, and not the actual exercise of that control. In view of that, if a licensor wants to oppose importation of the licensee’s products on grounds of poor quality, such action would not be allowed as contrary to art. 30 and 36 of the EC Treaty. The rationale behind this solution is that a licensor must bear responsibility, if he tolerates the manufacture of poor quality products, despite having contractual means of preventing it. The opposite view, expressed by some authors who claim that the Court’s position represents

79 JOLIET, op. cit., at 775.
80 Ibidem, at 785.

an ‘unduly strict enforcement of Community law’ and that ‘Community law continues to disregard the trademark right holder’s legitimate interest in protecting its marketing strategy, and instead encourages parallel importers to interfere with distribution systems’\textsuperscript{82}, does not seem to be proper. It is perfectly right to put a responsibility for the quality differences between products bearing the same mark on a producer or a group of producers, since they are in a position to avoid it. It is all the more appropriate, if such differences are intentional. If a producer purposely manufactures goods having different quality according to their destination, such quality differentiation leads to some kind of partitioning of markets, and should be deemed as contrary to certain moral standards in commerce. Therefore, it is right to say, that the Court’s standing, not so strict though, is just; not only it prevents the partitioning of markets, but it also aims at protecting consumers’ interest.

2.3. Tie-in clauses

Closely related to the quality control are obligations on the licensee to buy exclusively from the licensor certain products or specific materials necessary for the exploitation of the licensed technology. Such ‘tie-in’ clauses are by some commentators regarded to be anticompetitive, since they prevent the licensee from acquiring its supplies from other undertakings, perhaps on more favourable terms.\textsuperscript{83} Nevertheless, it should be remembered that such obligations are frequently the only way to meet the prescribed standards of production and they help to achieve the required quality of products.

The Commission in the \textit{Campari} decision held that the obligation on the licensees to buy certain secret raw materials (secret mixtures of herbs and colouring matters) from the licensor was compatible with art. 81(1). Similarly, the exclusive purchasing obligation regarding yeast (\textit{Moosehead/Whitbread}) did not fall under the said provision, because it was necessary to ensure technically satisfactory exploitation of the licensed technology and an identity between the beer produced originally by Moosehead and the product manufactured by Whitbread. It is obvious though, that in the same way as in quality control restrictions, tie-in clauses should observe the proportionality principle to avoid confusion with the competition rules.

\textsuperscript{82} REINDL, op. cit., at 820.
\textsuperscript{83} DIMAS, op. cit., at 72.
2.4. No-challenge clauses

Sometimes the owner of an industrial property right wishes to include in a licensing agreement a provision under which the licensee is obliged not to challenge the validity of the right in question. The rationale lying behind such an obligation is that the licensee is in the best position to show that a subject-matter of a right lacks certain necessary characteristics.

For a long time, both the Commission and the Court maintained that no-challenge clauses are against the public interest and that they restrict the licensee’s freedom, and therefore fall under art. 81(1). Such was the position in Windsurfing International Inc. v. Commission, where the matter concerned a patent no-challenge clause, and the Commission stated clearly that a patent licensing agreement may not be used to induce the patent licensee to acknowledge the validity of a trademark belonging to the licensor. As to the validity of a no-challenge clause relating to a trademark in a trademark licensing agreement, the Commission held that this matter could be left undecided for the purpose of the matters being then discussed. The first published decision where the Commission analyses a no-challenge clause relating to trademarks is Moosehead/Whitbread, which is after six and a half years after the question was left open in its Windsurfing decision. It was held, that trademark no-challenge clauses as such do not automatically fall within the scope of art. 81(1). Whether or not such obligations violate the provision in question depends on the particular economic context. With regard to trademarks, a no-challenge clause may constitute an appreciable restriction on competition, if a use of a particular trademark constitute an important advantage to a company entering or competing in a given market. Since the ownership of a trademark only gives the holder the exclusive right to sell products under that name, other parties are free to sell the product under a different trademark. Only the use of a well-known trademark, which constitutes a significant barrier to any other company, may constitute an appreciable restriction on competition. In a decision in question, because the trademark ‘Moosehead’ was relatively new in the licensed territory, its maintenance would not constitute an appreciable barrier for any other company to enter or compete in the United Kingdom beer market.

85 Ibidem.
87 Moosehead/Whitbread, at 36.
This demonstrates that no-challenge clauses should not be regarded as unlawful *per se*, however a careful consideration should be given to all the circumstances, including the situation on a given market.

3. Conclusion

The examination of relevant case law and literature relating to trademark licensing illustrates, that an ostensible opposition between exclusive rights, on the one side, and rules protecting undistorted competition in the market, on the other can be eliminated. Although certain arrangements may intentionally aim at distorting competition, contracts with respect to exclusive trademark rights do not conflict *per se* with competition rules.

Recently, it became common in literature to point out that trademark law aims not only at the protection of goodwill and the prevention of public confusion, but also at the protection of competition.\(^8\) As a matter of fact, the efficient competition on the market is guaranteed, among other things by the legitimate protection of owners of intellectual property rights. Neither of these concepts can exist separately, and their proper mutual functioning is an indispensable element of the Common Market and consumers’ rights.

Territorial protection of particular parties is one of the core issues in trademark licensing agreements. It is very important, that judicial authorities recognize its significance and do not consider this concept as inherently anti-competitive. Generally, exclusivity is allowed as long as it does not appreciably affect the position of third parties, for example other potential exclusive licensees for other territories. The case law of the European Court of Justice and decisions of the Commission demonstrate that every agreement should be analysed in light of all the accompanying circumstances and particularities of a given sphere of trade, as well as the advantages it produces for a market as a whole. The principle of proportionality, the fundamental idea of the European system, is applied to assess the legitimacy of particular contractual clauses. One should however be aware of several problems which may arise of specific contractual arrangements and which were not carefully considered at the time of their conclusion; therefore a thorough examination of individual

\(^8\) VUK, op. cit., at 880.
licensing contracts in light of the existing case law is necessary to avoid the infringement of competition rules.

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