

EXHAUSTION IN THE AREA OF PATENTS IN THE EUROPEAN UNION – CONTEMPORARY ISSUES

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The ‘exhaustion’ of intellectual property (“IP”) rights is a principle holding that once genuine goods have been put on the market by the IP holder or with her consent, such holder should not be able to control further distribution and use of the goods.¹ Specifically for patents, the doctrine finds justification in the argument that the patent holder who puts, or consents to the goods being put on the market has already availed of the advantages of the patent process by producing goods under the protected procedure, which must then be supplemented by free market principles.² Hence, exhaustion seeks to balance the interests of the patentee in earning a reward for the publication of her invention, and of the general public with respect to legal certainty and the free movement of goods.³ In the European Union (“EU”), the free movement of goods in a common unified market which is not segmented or distorted by artificial barriers is a foundational principle embodied in the Treaty establishing the European Community.⁴ In a complex interplay between intellectual property rights (“IPRs”) and these free trade principles, the legal consequence of the ‘exhaustion’ doctrine essentially constitutes an exemption to patent infringement.

There are three theories of exhaustion in practice, international, regional and national exhaustion,⁵ and this paper establishes that the regional exhaustion regime prevails in the EU. It has also been argued that while national exhaustion is prohibited, international exhaustion stands largely unregulated. Further, the contract between the patent holder and the first purchaser may embody post-sale restrictions, such as a prohibition on import, export, further sale, restrictions on means and methods of use. The author has argued that contractual restrictions seeking to limit the effect of exhaustion by preserving the patentee’s right to control post-sale import, export or use are not likely to be upheld in the European Union. For a clear understanding, the United Kingdom (“UK”) has been taken up as a case study for exhaustion, and the likely impact of Brexit on the exhaustion regime applicable in the UK has also been analysed. It has been argued that upon sale of the product embodying the patent with the consent of the holder of a UK patent within the EU, regional exhaustion reigns for the time being. However, upon sale of such a product by the patentee outside the EU, she can use her rights to impose post-sale restrictions.

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¹ Friedrich-Karl Beier, *Industrial property & the Free Movement of Goods in the Internal European market*, 21 INT’L REV. INTELL. PROP. & COMP. L. 131 (1990).

² *Id.*

³ Wolfgang Von Meibom & Matthias Meyer, *Licensing and Patent Exhaustion*, BIRD & BIRD (2008), <https://www.twobirds.com/en/news/articles/2008/licensing--andpatent-exhaustion>.

⁴ Manfred Schmiemann, *Exhaustion of patent rights and the European Union*, 20 WORLD PAT. INFO. 193, 193 (1998).

⁵ *Id.*

I. ELEMENTS AND THEORIES OF EXHAUSTION

As mentioned earlier, there are three regimes of exhaustion, followed in different parts of the world – international, national and regional. The elements of the rule are similar across regimes – exhaustion occurs when goods are put on the market by the proprietor or with her consent.⁶ The main impact of exhaustion of patent rights is on parallel imports, i.e. genuine goods legally acquired from the right holder, and subsequently sold at differential prices in different markets, mostly through trade channels not authorised by the right holder.⁷ The regime of exhaustion applicable to such imports is often considered to be the regime prevailing in the country of import.⁸

National exhaustion means that patent owners cannot control the exploitation of goods within the domestic market.⁹ A national exhaustion regime facilitates segmentation of markets, as it allows producers to set different prices in different jurisdictions across the world.¹⁰ For example – ‘A’ puts her goods on the market in country X, and ‘B’ tries to import them into country Y. Assuming Y follows a model of national exhaustion, ‘A’ can take recourse to courts there to prevent imports of goods put on the market in X to Y.

Under the international exhaustion theory, once the patentee, or another person with her consent, puts the goods on the market anywhere in the world, the patentee’s rights stand exhausted worldwide i.e. she cannot prevent the resale, import, export or use of goods in any other country.¹¹ This model benefits consumers, as countries can import from the cheapest suppliers worldwide.¹²

Regional exhaustion occurs where the patent holder exhausts her rights over the product when the patented product is sold in a particular region.¹³ Exhaustion occurs only in that specified region, which makes this model a hybrid between national and international exhaustion. If ‘A’, ‘B’ and ‘C’ countries form a particular region and a proprietor puts a product based on a patent registered in ‘B’ on the market in ‘B’, her rights stand exhausted in the entire region comprising the three countries. The

⁶ Michelle Lindgren, *Post-sale Restrictions & Exhaustion of Intellectual Property Rights - An Analysis of Post-Sale Restrictions in the EU* (2014) (unpublished graduate thesis, Lund University) (on file with the Lund University Library system).

⁷ Shrabani Rout, *Parallel Imports And International Exhaustion* MONDAQ (May 21, 2018), <http://www.mondaq.com/india/x/703104/international+trade+investment/Parallel+Imports+And+International+Exhaustion>.

⁸ Shamnad Basheer & Mrinalini Kochupillai, *TRIPS, Patents and Parallel Imports: A Proposal for Amendment*, 2 INDIAN J. IP L. 66 (2009); International Exhaustion and Parallel Importation, World Intellectual Property Organisation (WIPO), https://www.wipo.int/sme/en/ip_business/export/international_exhaustion.htm.

⁹ See World Intellectual Property Organization, *supra* note 8.

¹⁰ Mark Halle, *The Exhaustion of Intellectual Property Rights- Should countries favour consumers or private interests*, INT’L. INST. SUSTAINABLE DEV. COMMENT. (June 2007), https://www.iisd.org/sites/default/files/publications/com_exhaustion.pdf.

¹¹ World Intellectual Property Organization, *supra* note 8. *Supra* note.

¹² Halle, *Supra* Note 10.

¹³ See World Intellectual Property Organization, *supra* note 8.

European Union has adopted this regime, the mechanics and justifications of which have been analysed below.

II. REGIME OF PATENT EXHAUSTION FOLLOWED IN THE EUROPEAN UNION

The European Union was established on the cornerstone of free movement of goods, with the aim of establishing a single, un-fragmented internal market.¹⁴ The primary feature of such a market is that it would be an economic area without national barriers, allowing for the unrestricted movement and exchange of goods, services, persons and capital, promoting competition.¹⁵ Such a unified market is the foundation for integration and sustainable growth in Europe, and a vital strategic objective.¹⁶

These rules of free movement are enshrined in Articles 28, 30 and 34 of the Treaty on the Functioning of the European Union¹⁷. Article 28 provides for the establishment of a customs union between Member States, while Article 30 prohibits imposition of customs duties on imports and exports (and other measures of equivalent effect) which would discriminate between Member States, for goods originating in such States, and also for those from third countries in free circulation between the States. Article 34 and 35 disallow import and export quotas respectively, but these are subject to Article 36 which allows these restrictions for reasons of, *inter alia*, public policy, protection of health and life of humans, plants and animals, protection of national treasures, or the protection of industrial and commercial property. Similar obligations are found in Articles 11, 12 and 13 of the Agreement on the European Economic Area (EEA Agreement).¹⁸ Rules regarding free movement are supplemented by those on competition embodied in Title VII Chapter I Section 1. Article 101 bans certain activities distorting competition between Member States while Article 102 lays down the incompatibility of any abuse of dominant position by any undertaking in a Member State with the principle of internal market outlined above.

In light of these foundational objectives adopted by the EU, the doctrine of regional exhaustion is followed in that area, wherein once a particular good is put on the market of a Member State with the patentee's consent, her distribution rights stand exhausted

¹⁴ Lindgren, *Supra* Note 6 at 2.

¹⁵ Consolidated version of the Treaty on European Union -Protocol (No. 27) on the Internal Market and Competition, 2008 O.J. (C115) 309 (It is annexed to the Treaty of Lisbon amending the Treaty on European Union and the Treaty establishing the European Community).

¹⁶ Mario Monti, *A New Strategy for The Single Market: At the service of Europe's Economy and Society*, Report to the President of European Commission (May 9, 2010), http://ec.europa.eu/internal_market/strategy/docs/monti_report_final_10_05_2010_en.pdf.

¹⁷ Consolidated Version of The Treaty on the Functioning of the European Union, Oct. 26, 2012, 2012 O.J. (C 326) 47. [hereinafter Treaty on the Functioning of the European Union].

¹⁸ Agreement on the European Economic Area Jan. 3, 1994, 1994 O.J. (L 1) 3. <https://www.efta.int/sites/default/files/documents/legal-texts/eea/the-eea-agreement/Main%20Text%20of%20the%20Agreement/EEAagreement.pdf>. [hereinafter EEA Agreement]

in the entirety of the Union. The 1988 (updated in 2015) Trademark Directive,¹⁹ and 2001 Copyright Directive,²⁰ each harmonise the law across Member States, and create a common standard for the internal market by prescribing regional exhaustion for these IPRs. In the author's opinion, despite the lack of such a harmonising directive in the area of patents, such a regime is justifiable on several grounds.²¹ Firstly, a regime of national exhaustion, under which goods embodying a patent once put on the market in one Member State would be freely tradeable only in that State, would stand in square opposition to the concept of a single, unified market.²² The doctrine of regional exhaustion aims to prevent segmentation of the common market into smaller national markets. Moreover, if the holder of a patent in a Member State were allowed to restrict import and export of the good from the Member State where it has been put on the market to other States, it would lead to a violation of Article 28 of the TFEU.²³ The validity of contractual post-sale restrictions on import, export, use etc. have been examined later in this paper. Secondly, a regime of international exhaustion is likely to distort competition in the common internal market as well – there would be competition within Member States between products put on the market in the EU and those put on other global markets. This argument will be considered in more detail in the following paragraphs. Such limited patent protection could also disincentivise innovation and discourage patent holders from making their “first sale” in the EU.

The principle that exhaustion in the European Union cannot be limited to the sole jurisdiction of the Member State where the first sale is made, but must extend to all the other States forming part of the Union was first recognised in the *Deutsche Grammophon* case,²⁴ albeit in the context of copyrights. This stance has been reiterated by the Court of Justice of the European Union (CJEU) in several cases in patent-specific contexts. Following the *Deutsche Grammophon* case, the *Centrafarm BV & Adriaan De Peijper v. Sterling Drug Inc.*²⁵ judgement summarised the importance of a regional exhaustion regime for patents in fostering a unified market in the following words –

¹⁹ Directive 2015/2436, of the European Parliament and of the Council of 16 December 2015 to approximate the laws of the Member States relating to trade marks, art. 15, 2015 O.J. (L 336) 1.

²⁰ Directive 2001/29/EC of the European Parliament and of the Council of 22 May 2001 on the harmonisation of certain aspects of copyright and related rights in the information society, art. 4, O.J. (L 167) 10.

²¹ Shubha Ghosh, *The Implementation of Exhaustion Policies: Lessons from national experiences*, 40 INT'L CEN. TRADE & SUNST. DEV. PROG. INNOVATION, TECH. & INTELL. PROP. 36 (2013), <http://www.ictsd.org/sites/default/files/downloads/2014/01/the-implementation-of-exhaustion-policies.pdf>.

²² Treaty on the Functioning of the European Union, *supra* note 17, at art.2.]; Treaty of Lisbon Amending the Treaty on European Union and the Treaty Establishing the European Community art. 2(3), Dec. 13, 2007, 2007 O.J. (C 306) 1[hereinafter Treaty of Lisbon].

²³ See World Intellectual Property Organization, *supra* note 8, at 17.

²⁴ Case 78/70, *Deutsche Grammophon Gesellschaft Mbh v. Metro-SB-Grossmarkte Gmbh and Co.*, [1971] E.C.R. 487 ; Darren E. Donnelly, *Parallel Trade and International Harmonization of the Exhaustion of Rights Doctrine*, 13 SANTA CLARA HIGH TECH. L.J. 445, 470 (1997), <http://digitalcommons.law.scu.edu/chtlj/vol13/iss2/4>.

²⁵ Case 15/74, *Centrafarm BV and Adriaan de Peijper v. Sterling Drug Inc.*, [1974] ECR 1147.

*“derogation from the principle of the free movement of goods is not, however, justified where the product has been put onto the market in a legal manner, by the patentee himself or with his consent, in the member state from which it has been imported, in particular in the case of a proprietor of parallel patents. In fact, if a patentee could prevent the import of protected products marketed by him or with his consent in another member state, he would be able to partition off national markets and thereby restrict trade between member states, in a situation where no such restriction was necessary to guarantee the essence of the exclusive rights flowing from the parallel patents.”*²⁶ It also held that deviations from the free movement principle are permissible only in so far as they safeguard rights comprising ‘specific subject matter’ of the patent.²⁷

The implication of the entirety of the EU being treated as a single market is that patent exhaustion should essentially be governed by the same considerations applying to exhaustion in a domestic market.²⁸ Conditions for exhaustion remain the same, i.e. when the good is put on the market by or with the consent of the patentee, where ‘putting on the market’ implies the sale of goods for consideration only,²⁹ while the relevant market would be anywhere in the entire EU.

It is vital to note that the patent regime in the European Union has not been harmonised like the trademark and copyright regimes. Article 7 of the 1988 Trademark Directive³⁰ provided for a regional exhaustion regime for trademarks (and the same language has been adopted verbatim in Article 15 of the 2015 Directive³¹ in force now), but it was unclear from its wording whether this was simply a minimum standard, leaving Member States free to apply rules even less or more restrictive to free trade like international exhaustion.³² However, the landmark judgement of the CJEU in *Silhouette International Schmied GmbH & Co. KG v Hartlauer Handelsgesellschaft mbH*,³³ (“Silhouette case”) expressly excludes the application of an international exhaustion regime, unless it is negotiated through an international agreement.³⁴ A similar ratio was also seen in *Laserdisken v Kulturministeriet*,³⁵ in the context of Article 4 of the

²⁶ *Id.* at 11, 12.

²⁷ *Centrafarm* at 11.

²⁸ WIPO, *Supra* Note 24 at 17.

²⁹ Case C- 324/09, *L’Oréal SA v eBay International AG*, [2011] ECR I-6011.

³⁰ First Council Directive 89/104/EEC of 21 December 1988 to approximate the laws of the Member States relating to trade marks.

³¹ Directive (EU) 2015/2436 of the European Parliament and of the Council of 16 December 2015 to approximate the laws of the Member States relating to trade marks

³² Irene Calboli, Trademark Exhaustion in the European Union: Community-Wide Or International? The Saga Continues, 6 Marq. Intellectual Property L. Rev. 47, 50 (2002). Available at: <https://scholarship.law.marquette.edu/cgi/viewcontent.cgi?referer=https://www.google.com/&httpsredir=1&article=1034&context=iplr>.

³³ Case C-355/96, *Silhouette International Schmied GmbH & Co. KG v Hartlauer Handelsgesellschaft mbH*, [1998] ECR I-4799.

³⁴ Case C-355/96, *Silhouette International Schmied GmbH & Co. KG v Hartlauer Handelsgesellschaft mbH*, [1998] ECR I-4799, para 30.

³⁵ C-479/04, *Laserdisken ApS v. Kulturministeriat*, [2006] ECR I-8089, para 26.

Copyright Directive,³⁶ reinforcing the wording of recital 28, “*The first sale in the Community of the original of a work or copies thereof by the rightholder or with his consent exhausts the right to control resale of that object in the Community. This right should not be exhausted in respect of the original or of copies thereof sold by the rightholder or with his consent outside the Community*”. Both cases based their ruling on the need to protect competition in the internal market.

A limitation arising from the lack of harmonising law and comparable case law for patents is that there is a theoretical possibility that Member States may adopt international exhaustion in the arena of patents. However, there is no reason to believe that the exhaustion doctrine would be construed differently for different IPRs,³⁷ since the foundational principles of the EU discussed previously remain the same. Interestingly, all proposals for harmonisation of patents in the European Union have prohibited international exhaustion, but none have been adopted so far.³⁸

Another potential limitation is that the principles of free movement are limited to governing situations which actually impact the free movement of goods. As explained above, these principles will forbid discriminatory limitations on the exhaustion of a patent, or those extending beyond the ‘specific subject matter’ of the patent. However, in other matters, Member States have the discretion to determine which regime of exhaustion they wish to apply. *Generics v. Smith Kline & French*,³⁹ decided by the CJEU is a case in point. This case concerned a rule promulgated by the United Kingdom which permitted patentees to object to imports only when they manufactured the product within the UK. However, for products manufactured outside the UK, the rule granted compulsory licenses for import under this patent, even if the manufacturing took place in another Member State of the EU. This was a form of international exhaustion. The Court held that this rule violated Article 30 of the TFEU as it was a measure of equivalent effect discriminating between Member States by favouring production in the UK.⁴⁰ However, the Court also opined that it was the national government’s prerogative to either grant compulsory licences in all such cases, or to refuse them where manufacture took place in the UK or anywhere else within the EU. This case stands for the proposition that since national legislations on patents have not been approximated,

³⁶ DIRECTIVE 2001/29/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 22 May 2001 on the harmonisation of certain aspects of copyright and related rights in the information society

³⁷ Ole-Andreas Rognstad, Spredningavverkseksemplar: om konsumpsjonavrettigheterieksemplaravvernedeåndsverk, Cappelenakademisk, (1999).

³⁸ Patents Working Group, *Proposals of the Benelux Delegations on Article 21 of the Preliminary Draft of the Convention relating to a European Patent Right*, Doc IV/6365/61-F at 2,5-6; Convention for the European Patent for the Common Market, Luxembourg arts.32, 81(1), Dec. 15, 1975, 1975O.J.(L17) 1[hereinafter Community Patent Convention].

³⁹ Case C-191/90, *Generics (UK) Ltd. & Harris Pharms Ltd. V. Smith Kline & French Labs Ltd.*, 1992 ECR I-5335.

⁴⁰ Case C-191/90, *Generics (UK) Ltd. & Harris Pharms Ltd. V. Smith Kline & French Labs Ltd.*, 1992 ECR I-5335, paras 24, 25.

national law defines the contours of protection granted under the patent, subject to Articles 28 and 30 of the TFEU.⁴¹

In the author's view, a regime of regional exhaustion is ideal to balance the EU's competing considerations of maintaining a unified market, advancing consumer preferences and fostering innovation and development. While national exhaustion undermines the free trade principle and limits consumer choice, international exhaustion lessens incentive for innovation due to limited scope of protection and interference after the first authorised sale. Under regional exhaustion, since commercial rights are exhausted (only) within the EU once goods are put on the market in any Member State, free trade and consumer preference is protected, and patentees retain the autonomy of commercialising their products outside the EU.

III. THE VALIDITY OF POST-SALE RESTRICTIONS VIS-À-VIS PATENT EXHAUSTION IN THE EUROPEAN UNION

The contract between the patentee and initial purchaser may embody certain post-sale restrictions on import, export, further sale or use, which reflects the patentee's intention to not have her rights exhausted. There are two ways to perceive the effect of post-sale restrictions on exhaustion of patent rights. First, that consent of the proprietor is the primary condition for exhaustion to occur, and contract restrictions could be proof of the scope of consent. Second, that the essence and objective of exhaustion i.e. free trade within the European Union would be defeated if the patentee were to be allowed to impose such contractual restrictions.

The second approach seems to prevail in the EU. The rationale is that of reinforcing regional exhaustion – once a patentee has put the goods on the market in a Member State, she cannot prohibit parallel importation from that country into other Member States or further sale by restrictive contractual terms, in accordance with the principles of free movement and competition. In this regard, the validity of restrictions on sales by a licensee outside the country in which the said licensee has been allowed to manufacture (including bans on exporting to other parts of the European Union) is also contested.⁴² While scholars such as Hurley, Devinsky and Hill believe that such restrictions would be upheld, the CJEU has adopted a contrary position,⁴³ which shall be examined shortly.

⁴¹ Case C-191/90, *Generics (UK) Ltd. & Harris Pharms Ltd. V. Smith Kline & French Labs Ltd.*, 1992 ECR I-5335, para 39; Christopher Stothers, *Patent Exhaustion: the UK perspective*, 16th Annual Conference on Intellectual Property Law and Policy of Fordham University School of Law, (Mar. 27-28, 2008), <https://perma.cc/7XMN-Q5ZP>.

⁴² Michael Hurley, Paul Devinsky & Justin Hill, *The Supreme Court decides Quanta v. LGE - US versus European Perspectives*, McDermott Will & Emery LLP (2008), <http://www.ipo.org/wp-content/uploads/2013/03/Supremecourtdecidesquantavlge.pdf>.

⁴³ Case 193/83, *Windsurfing International Inc. v Commission of the European Communities*, [1986] ECR 611.

The CJEU has been suspicious of contractual post-sale restrictions, and has expressed its opinion against them in several cases. In the case of *Dansk Supermarked, A/S v. A/S Imerico*,⁴⁴ there was an agreement for manufacture and delivery of china services between a Danish company and an English manufacturer. A limb of the agreement was that some average pieces not delivered to the former could be sold in the UK, but could not be exported to Denmark or even to other Scandinavian countries. Another Danish enterprise bought such china services in the UK and then marketed them in Denmark, which formed the cause of action for this case. The CJEU relied on the free movement principle and regional exhaustion to say that trademark and copyrights in the average china stood exhausted when they were put on the UK market with the consent of the Danish company.⁴⁵ The restrictive contract term prohibiting export to Scandinavian countries was found to be contrary to free movement rules and could not be relied upon. This case also interpreted the “*protection of industrial and commercial property*” exception to free trade in Article 36 of TFEU as only applying to measures necessary (and least restrictive) to prevent unfair competition, and clarified that the exception cannot be used to impose arbitrary restrictions on free trade.⁴⁶

In the more recent case of *Peak Holding v. Axolin-Elinor AB*,⁴⁷ the CJEU refuted the position that contract restrictions demonstrate a lack of the patentee’s consent, which is essential for exhaustion to occur. The Court opined that a sale made by the patentee is not subject to the additional condition of consent, and triggers exhaustion *per se*.⁴⁸ This case restrained conditions such as territorial restrictions on the right to resell as a mere arrangement between the parties with no impact on exhaustion, which took place regardless.⁴⁹

Even though these cases have been decided in the context of trademarks, in the author’s opinion, the same rationale can be extended to cases of patents for mainly two reasons. First, the previous part has clarified the applicability of at least a regional exhaustion regime by all the Member States in the area of patent, similar to trademark. The official European Commission Guideline on Interpretation of Article 101 of the TFEU itself has recently clarified that once regional exhaustion occurs, “*...the right holder has no right under (all) intellectual property laws to prevent sales by licensees or buyers of such products incorporating the licensed technology*”.⁵⁰ There is no reason why the sanctity accorded to the regional exhaustion doctrine and the impact of post-sale restrictions for both these IPRs should be any different. Secondly, these cases, though decided in the

⁴⁴ Case 58/80, *Dansk Supermarked A/S v A/S Imerco*, [1981] ECR 181.

⁴⁵ *Dansk* judgement, page 186, para (b); page 187, para (c).

⁴⁶ *Dansk* judgement, page 188, para (d).

⁴⁷ Case C-16/03, *Peak Holding AB v Axolin-Elinor AB*, [2004] ECR I-11313).

⁴⁸ *Id.* at 52, 53.

⁴⁹ *Peak Holdings* at 54, 55.

⁵⁰ Communication from the Commission — Guidelines on the application of Article 101 of the Treaty on the Functioning of the European Union to technology transfer agreements, 2014 O.J. (C. 89) 3.

context of trademarks, have ratios applicable to all kinds of IPRs since they are based on the overarching regional principles of free trade in a unified market.

In 1986, a landmark judgement on licensing of patent rights was passed by the CJEU in *Windsurfing International v. European Community Commission*.⁵¹ The plaintiff had concluded license agreements with several European Companies in Member States for development and distribution of its patented products, but reserved the right to cancel them if the licensees produced or distributed goods (other than in a bundle of the patented and an unpatented product) in countries where the plaintiff did not hold valid patents. The Court opined that restrictive terms preventing the manufacture in or export of goods to any Member State where patent protection is not available are prohibited under Article 85 of the EEC Treaty, as they distort and restrict competition in the common market and hamper free trade between Member States⁵².

Admittedly, this case does not address exhaustion. However, there is an argument to be made, that if such strict standards have been applied with respect to non-enforceability of restrictive contract terms in licensing arrangements, the same (if not more stringent) standards should logically apply for an authorised first sale made within a Member State.⁵³ This decision is also relevant in light of the fact that the CJEU has assumed exhaustion even in cases where goods were sold by the patentee in EU countries in which no patent protection exists.⁵⁴

IV. THE UNITED KINGDOM – A CASE STUDY

A. Exhaustion Regime Applicable in the UK

Although the UK Patents Act, 1977 does not explicitly provide for exhaustion of patent rights, regional exhaustion within the European Union applies under the TFEU and the European Communities Act, 1972.⁵⁵ This principle is also applied by virtue of Article 10 of the European Commission's Council Regulation on the Community Patent, which endorses regional exhaustion as a consequence of marketing by consent. In the UK, exhaustion of patent rights applies through a combination of the common law doctrine of implied licensing (for sales made outside the EU) and the doctrine of regional exhaustion (for sales made within the EU).⁵⁶ This distinction has implications while gauging the validity of post-sale restrictions, which will be examined shortly.

B. Impact of Brexit on the Exhaustion Regime

⁵¹ *Windsurfing International*, *Supra* Note 48.

⁵² *Windsurfing judgement*, para 53, 59.

⁵³ Michael Gold, *European Patent Law and the Exhaustion Principle*, 1 U. CHICAGO LEGAL FORUM 441 (1992), <http://chicagounbound.uchicago.edu/cgi/viewcontent.cgi?article=1124&context=uclf>.

⁵⁴ Case 187/80, *Merck & Co. Inc. v. Stephar BV and Petrus Stephanus Exler*, [1981] ECR 2063.

⁵⁵ STOTHERS, *Supra* Note 25 at 4.

⁵⁶ Ben Allgrove, Ruth Burstall & Baker McKenzie, *Intellectual property rights: why exhaustion matters*, THOMSON REUTERS PRACTICAL LAW (July 27, 2017), [https://uk.practicallaw.thomsonreuters.com/w-009-1126?transitionType=Default&contextData=\(sc.Default\)&firstPage=true&bhcp=1](https://uk.practicallaw.thomsonreuters.com/w-009-1126?transitionType=Default&contextData=(sc.Default)&firstPage=true&bhcp=1).

It is interesting to study what the scope of exhaustion of patent rights would be once the United Kingdom exits from the European Union. Two sets of agreements must be considered here – one between the United Kingdom and the European Union, and another between the former and the European Economic Area. If the former agreement is reached, United Kingdom will remain part of the single market with the present regime of regional exhaustion of patents continuing. However, outside of this single market, UK would not be bound by the doctrine of regional exhaustion vis-à-vis the rest of the European Economic Area unless the latter agreement is also negotiated. In such a situation, placing of goods within the UK market would not exhaust the patentee's rights in those countries of the European Economic Area which are not part of the European Union. Currently, the intention of the UK seems to be to maintain *status quo* with the EEA. Outside of the single market of the European Union, the United Kingdom can continue to decide what regime of patent exhaustion to apply, either through legislation or case law.

There have been several rounds of discussion and guidance from the UK regarding its relations with the EU and EEA after Brexit in the matter of IPR, beginning with the position paper on Brexit and IPR released by The European Commission Brexit Task Force in September 2017.⁵⁷ The paper recommended that if exhaustion of patents has already occurred in the European Union before Brexit, these rights should remain exhausted after Brexit too, in both, the European Union and the UK. This proposal has also found favour with the Chartered Institute of Patent Attorneys.⁵⁸ However, the paper did not address how negotiations on exhaustion would be approached, which rules would likely be applied and what exemptions would be carved out to tackle this issue.⁵⁹

In 2018, the UK Government released the draft Intellectual Property (Exhaustion of Rights) (EU Exit) Regulations⁶⁰ The explanatory note to the regulations clarifies that the after the UK withdraws from the European Union, there need to be regulations in place to curb a situation where “*goods that have been legitimately put on the market in the EEA would no longer be able to be legitimately re-distributed or resold in the UK*”. The aim of the regulations was to amend primary legislation such as the Registered Designs Act 1949, Copyright, Designs and Patents Act 1988 and the Trade Marks Act 1994 and subordinate legislation to specifically add references to the UK along with the EEA, “*to ensure that the question of whether an article has been lawfully placed on the market for the purposes of the exhaustion of intellectual property rights, continues to*

⁵⁷ *Position paper transmitted to EU27 on Intellectual property rights*, at 1.3, COM (2017) 11 final (Sept 6, 2017).

⁵⁸ *The impact of Brexit on Intellectual Property*, THE CHARTERED INSTITUTE OF PATENT ATTORNEYS (October 11, 2017), <http://www.cipa.org.uk/policy-and-news/briefing-papers/the-impact-of-brex-it-on-intellectual-property/>.

⁵⁹ *Id.*

⁶⁰ Draft Statutory Instruments - The Intellectual Property (Exhaustion of Rights) (EU Exit) Regulations 2018, http://www.legislation.gov.uk/ukdsi/2018/9780111175255/pdfs/ukdsi_9780111175255_en.pdf.

be assessed in relation to an area which includes the UK.” These regulations have been made into law on 14 February 2019, and will come into effect on exit day, 31 October 2019.⁶¹

A Guidance Note on the exhaustion of intellectual property rights in case of a no-deal Brexit was also published in September 2018,⁶² which clarified that the UK would continue to recognise regional exhaustion once goods were put on the market with the right holder’s consent anywhere in the EEA. These goods can be legitimately imported into the UK without the right holder’s permission. However, since there was no similar offer from the EEAs end in the draft Withdrawal Agreement⁶³, the note acknowledged that the EEA may not recognise exhaustion of IP rights for goods placed on the UK market with the right holder’s consent, and that exporters and importers of such goods may require the right holder’s authorisation. This note was replaced by an updated guidance on 11 September 2019⁶⁴, which seems to indicate that the UK will recognise the EEA regional exhaustion regime after the exit day only for a temporary period. No details of this period, or what happens after it, have been provided.

Since the UK is now free to introduce its own exhaustion regime, several arguments have been in favour of international exhaustion. Before the concept of regional exhaustion was introduced in the EU, UK courts ruled in favour of such a regime, at least in the area of trademarks.⁶⁵ As mentioned previously, a system of international exhaustion favours consumers by allowing them the benefit of price arbitrage arising out of competition between the patent holder and importers. This is especially important in industries such as pharmaceuticals. However, there are also concerns surrounding counterfeiting and lower quality product being imported into countries with higher quality standards for domestic manufacturing⁶⁶, although this can presumably be resolved through import regulation and spot inspections, which can co-exist with the concept that the patentee herself should not be allowed to restrict such

⁶¹ 2019 No. 265 - The Intellectual Property (Exhaustion of Rights) (EU Exit) Regulations 2019, <http://www.legislation.gov.uk/uksi/2019/265/made>.

⁶² Dept. for Business, Energy & Industrial Strategy, Intellectual Property Office, Guidance - Exhaustion of intellectual property rights if there’s no Brexit deal (2018), <https://www.gov.uk/government/publications/exhaustion-of-intellectual-property-rights-if-theres-no-brexiteal/exhaustion-of-intellectual-property-rights-if-theres-no-brexiteal>.

⁶³ Draft Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community, as agreed at negotiators’ level on 14 November 2018, https://ec.europa.eu/commission/publications/draft-agreement-withdrawal-united-kingdom-great-britain-and-northern-ireland-european-union-and-european-atomic-energy-community-agreed-negotiators-level-14-november-2018_en.

⁶⁴ Dept. for Business, Energy & Industrial Strategy, Intellectual Property Office, Guidance - Exhaustion of intellectual property rights if there’s no Brexit deal (2019) <https://www.gov.uk/government/publications/exhaustion-of-intellectual-property-rights/exhaustion-of-intellectual-property-rights>.

⁶⁵ Revlon Inc. v. Cripps & Lee Ltd (1980) FSR 85 (1980) 11 I.I.C. 372, Colgate Palmolive v. Markwell Finance Ltd. (1989) R.C.P. 497.

⁶⁶ Patrick Cantrill, Rose Smalley & Tim Barber, Brexit and exhaustion of rights - an update Lexology.com (2019), <https://www.lexology.com/library/detail.aspx?g=cfdea6e5-bb0b-4f60-95dc-ab47e7619fea>.

imports. Other concerns pertain to lesser incentive to innovate due to narrower scope of IP protection, parallel importers being allowed to free-ride on the investment of IP owners, reputation of the product, traceability of products to ensure quality etc., which have prompted stakeholders such as the International Trademark Association to advocate for a regime of national exhaustion.⁶⁷

In the context of international exhaustion, it is interesting to note that the *Silhouette* judgement constitutes a 'retained EU case law' in the UK under Section 6 of the European Union (Withdrawal) Act 2018,⁶⁸ but sub-section 4 also states that the Supreme Court is not bound by any retained EU case law. Further, the case prohibited international exhaustion in domestic regimes of Member States to protect the internal EU market and competition within it.⁶⁹ This does not apply to the UK any longer, and will definitively cease to be a consideration after the expiry of the Brexit transition period.

C. Validity of Post-Sale Restrictions vis-à-vis Patent Exhaustion in the UK

At the outset, it is vital to clarify that the operation of the doctrine of regional exhaustion cannot be contracted out of the UK. The UK has clarified its stance in this regard, categorically stating that if the patented products are put on the market inside its jurisdiction, contract terms restricting further sale, use, import by or export to other Member States will not be upheld, in line with Article 28 of the TFEU, which the patentee cannot override.⁷⁰ In this context of regional exhaustion, any restrictions beyond basic subject matter of patents (like competition restrictions, import, export, price restrictions, limitations on trade) do not hinder the effects of exhaustion, as discussed in previous parts. However, exhaustion does not occur if the restrictions are about subject matter – if the content has been changed and the product has been reconstructed.⁷¹

Within the UK, the patent exhaustion regime materialises by operation of the doctrine of implied licence. The applicability of the doctrine of international exhaustion, though

⁶⁷ International Trademark Association, Exhaustion of Trademark Rights after Brexit, (2018), [https://www.inta.org/TopicPortal/Documents/INTA%20letter%20on%20exhaustion%20principle%20in%20Brexit%20\(002\).pdf](https://www.inta.org/TopicPortal/Documents/INTA%20letter%20on%20exhaustion%20principle%20in%20Brexit%20(002).pdf), pages 9-11.

⁶⁸ Katharine Stephens, Exhaustion of Intellectual Property rights post Brexit Lexology.com (2019), <https://www.lexology.com/library/detail.aspx?g=0dd1dde6-68cf-4452-bdd5-f0e599fff563> (last visited Sep 25, 2019).

⁶⁹ Case C-355/96, *Silhouette International Schmied GmbH & Co. KG v Hartlauer Handelsgesellschaft mbH*, [1998] ECR I-4799, para 24, 27.

⁷⁰ World Intellectual Property Organisation [WIPO], *Exceptions and Limitations to Patent Rights: Exhaustion of Patent Rights*, WIPO Doc.SCP/21/7 (October 11, 2014), http://www.wipo.int/edocs/mdocs/scp/en/scp_21/scp_21_7.pdf.

⁷¹ *Id.*

theoretically permitted, may not stand if the patent regime were to be harmonised. In the area of trademarks, as explored previously, the *Silhouette* judgement held that regimes of international exhaustion adopted by Member States violate the Trademark Directive, and it seems likely that a potential patent harmonisation directive will adopt the same approach.

A number of cases have considered whether third parties would be bound by restrictive terms,⁷² which suggest that there is a distinction between sales by the patentee (where any restrictions would have to have been brought to the attention of the alleged infringer to prove infringement) and sales by a licensee (where the alleged infringer's knowledge is irrelevant).⁷³ The rule regarding the latter case of express licenses is that a licensee cannot transfer better rights than she herself has, and hence, the patent is deemed to be infringed even if the subsequent purchaser does not have notice of the restrictive conditions.⁷⁴ However, this part of the paper shall deal with the former case, since exhaustion occurs as a consequence of consensual sale.

Betts v. Willmott,⁷⁵ is the leading judgement on the doctrine of implied license outlined hereinbefore. In this case, patented metallic capsules were sold by the English patent holder in France, and they were then retailed in England. The retailer was not held liable for infringement, but the Court did not rely on the doctrine of exhaustion. It used the doctrine of implied license to say that the patentee could not prevent further import or sale, since with the goods, the patentee had also transferred the rights to use the product in any way whatsoever. However, in tune with the concept of a license, it was also held that such parallel importation could be prevented by express contractual terms made known to the purchaser. This case established the current position which can be best summarised as follows - The patentee is free to make a *sub modo* sale with restrictive conditions which would not apply in cases other than those of the patented product. These conditions are not assumed, but have to be made express. The ordinary presumption is that the purchaser has acquired all rights in the product, along with those of use, resale and export, unless such conditions are brought to her notice at the time of conclusion of the contract.⁷⁶

In another case where the patent holder (manufacturer) had sold the goods to a wholesale chemist on conditions prohibiting export, it was held that a prima facie case of infringement of the patent is contingent on whether adequate notice of restrictive

⁷² *Gillette Industries v. Bernstein* [1942] Ch. 45 (Eng.); *Dunlop Rubber v Longlife Battery Depot* [1958] 1 WLR 1033 (Eng.).

⁷³ *Badische Anilin und Soda Fabrik v. Isler* (1906) 1 L.R. Ch 605 (Eng.), *Beecham Group v International Products* [1968] RPC 129 (Eng.).

⁷⁴ *Société Anonyme des Manufactures de Glaces v. Tilghman's Patent Sand Blast Company* (1884) LR 25 Ch D 1 (Eng.).

⁷⁵ *Betts v. Willmott* (1871) LR 6 Ch App. 239 (Eng.).

⁷⁶ *National Phonograph Company of Australia Ltd. v. Menck* (1911) 28 RPC229 (PC) 248 (appeal taken from Austl.).

conditions was given to the defendant.⁷⁷ In this case, the patentee had sent the defendant a letter detailing these terms, and the chemist had issued an invoice clarifying that the manufacturer's terms would apply. These indicators were taken as sufficient proof of notice. A similar principle was upheld in *Roussel Uclaf v. Hockley International*,⁷⁸ where merely affixing labels to the goods was not considered as conclusive proof of notice.

In the 2001 judgement of *Zino Davidoff v A&G Imports*,⁷⁹ the High Court considered the scope of *Betts v Willmott* in the context of sale by the right holder. The plaintiff had requested a summary judgment on infringement of trademark of its perfumes which had been parallel imported from Singapore. The question was whether the plaintiff could prevent import into the EEA of a good placed on the market outside the EEA, and Justice Laddie found that in the absence of any terms restricting the same, consent to importation into the EEA can be presumed in light of *Betts v Willmott*. Later, the CJEU overturned this ruling for conflicting with the harmonising Trademark Directive, but the decision can be applied to patents where no such harmonising law exists.⁸⁰

Though delivered in 1870, the judgement in *Betts v Willmott* has recently been upheld once again as currently binding precedent in *HTC v. Nokia*.⁸¹ It is interesting to note that *Betts v Willmott* was delivered before the formation of the European Union and applied the doctrine of implied license even as between two current Member States. In the author's opinion, the case forms binding precedent only as to the scope and application of the doctrine, since regional exhaustion in the EU and non-restriction of its scope through contracts has since been adopted by the UK.

CONCLUSION

This paper has established that out of the three theories of patent exhaustion examined in Part II, the doctrine of regional exhaustion applies in the EU. This fundamentally stems from the idea of a single, unified, un-fragmented market allowing for free movement of and trade in goods, as detailed in the *Centrafarm* judgement. Further, it can be concluded that the CJEU leans towards disallowing contractual post-sale restrictions from undermining the effects of regional exhaustion, on the premise that such restrictive terms are incompatible with free movement of goods and competition (as held in *Dansk Supermarket*). *Peak Holding* also held that once the patentee has put the goods on the market or consented to such as act, consent for further use and distribution is assumed for the purpose of exhaustion. The *Windsurfing* case also indicated the CJEU's tendency to disallow contractual terms seeking to extend patent rights where none exist. The position in the United Kingdom is more relaxed whereby

⁷⁷ *Sterling Drug v CH Beck* [1972] FSR 529 (Eng.).

⁷⁸ *Roussel Uclaf v. Hockley International* [1996] RPC 441 (Eng.).

⁷⁹ *Zino Davidoff v. A&G Imports* [2000] Ch 127 (Eng.).

⁸⁰ W. Meibom & M. Meyer, *Supra* Note 3.

⁸¹ *HTC Corporation v. Nokia Corporation* [2013] EWHC 3778 (Pat), [2014] RPC 30 (Eng.).

the patentee can protect her rights by bringing such contract terms to the purchaser's attention when selling her goods in a non-EU country.

The limited scope of patent protection in the EU becomes evident on a combined reading of *Centrafarm* and *Windsurfing*. While the former has crystallised the principle of regional exhaustion, the latter prevents patentees from restoring to restrictive contractual terms to give extraterritorial effect to its patented manufacturing rights.⁸² However, it is important to note that such restrictive IP protection risks deterring innovation in the long run.

The position in the UK on post-sale restrictions may be summed up as follows – currently, upon sale of the product embodying the patent by or with the consent of the holder of a UK patent within the EU, regional exhaustion applies and she cannot save her rights through contractual restrictions and stipulations. However, upon sale of such a product by the patentee outside the EU, she can use her rights to prevent re-sale and impose other restrictions under the contract, which will of course be subject to national and EU competition law, and must be brought to the purchaser's attention. This stems not from a rule of international exhaustion, but from the doctrine of implied license under contract law.⁸³ Further, in the UK, exhaustion will not occur if the sale is made by a (express) licensee in breach of a legally enforceable contractual condition.⁸⁴

While the UK has chosen to continue applying a regional exhaustion model at least till the end of the transition period, this decision is expected to create hurdles for parallel imports into the UK due to lack of reciprocity from the EEA. The UK has a myriad of options after this period – it may choose to continue with regional exhaustion (with or without reciprocity from the EU), apply national exhaustion, adopt international exhaustion or cast the net of the doctrine of implied license wide to include EU countries. The implications of each of these models will make for an interesting study.

⁸² Gold, Michael A., *European Patent Law and the Exhaustion Principle*, [1992] University of Chicago Legal Forum 441, 446. Available at: <http://chicagounbound.uchicago.edu/uclf/vol1992/iss1/19>

⁸³ Roland Mallinson et al., *Report Q 156 - Exhaustion of Industrial Property Rights*, INTERNATIONAL ASSOCIATION FOR THE PROTECTION OF INTELLECTUAL PROPERTY (AIPPI) (2001), https://aippi.org/download/committees/156/GR156united_kingdom.pdf.

⁸⁴ *Id.*