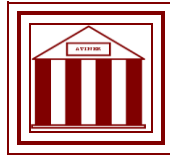


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**Obligations and Rights of Licensor and
Licensee in a Patent Licence**

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Obligations and Rights of Licensor and Licensee in a Patent Licence

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Abstract

This paper discusses one of the different aspects of licensing agreement to exploit patented technology. Such licensing agreements are important when considering technology transfers to developing countries. The study addresses whether the current Libyan legal framework are able to accommodate such licences in terms of identifying the right and obligations of the parties. Of course, the license agreement is the main source of these obligations based on the rule of a contract makes the law among parties. Thus, the patent holder is expected to take all necessary actions to convey the patentable invention and allow the licensee to manufacture the licensed technology. The licensee, on the other hand, is expected to pay royalties and exploit the licensed technology. The parties must agree on terms and conditions to rule such agreements because of the absence of special regulations governing such agreements.

Keywords:

Introduction

The patent licence contract creates offset obligations between the parties. The license agreement is the main source of these obligations based on the rule of ‘a contract makes the law between parties’. As a general rule, all of the terms contained in an agreement bind parties, regardless whether they read them or understand them, unless there is fraud.¹ Thus, the patent holder is expected to take all necessary actions to convey the patentable invention and allow the licensee to manufacture the licensed technology. The licensee, on the other hand, is expected to pay royalties and exploit the licensed technology. In practice, this may be an area where many disputes eventuate. The parties must agree on terms and conditions to rule such agreements because of the absence of special regulations governing such agreements.

The question arises: what happens if there is no contractual clause defining the relevant condition and the scope of the licensed right of use. To take one example (in the light of a clause regarding warranty), the patentee should warrant the effectiveness of patent right and there is no any actions that may disturb the enjoyment of exploiting the licensed invention. This would require an exploration of this issue under the relevant contract law governing the patent licence agreement at issue: this can prove to be complex in the absence of a specific solution governing such a contract. This is the issue under Libyan law with the absence of provisions that rule on the contract of technology transfer. In Libya, contracting parties also are generally obliged to contract in good faith according to the country’s laws, and principles governing usage and equity.² This study will examine the scope of the patent licence obligations under Libyan law, by outlining the typical obligations of a licensor in section one and obligations of licensee in section two.

Typical obligation of a licensor

The obligation of delivery

The meaning of the obligation of delivery refers to the fact that the licensors have to render the subject matter of the agreement at the disposition of their contractual partner.³ According to contract law, the obligation of delivering the subject matter of the contract to another party is a principle duty by the owner of that subject matter whether this contract is a contract for sale, a

¹*Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; 219 CLR 165, 43. However, judges referred to three possible circumstances in which ‘the party who signed the document might not have been bound by its terms. The first was if the document signed was not a contract but merely a memorandum of a previous contract which did not include the relevant term. The second was a case of *non est factum*. The third was a case of misrepresentation’. See *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd*, 56.

²*Libyan Civil Code 1959* art 148 (2).

³Arnold Vahrenwald, *Patent Licence Contracts in English, French and Italian Law* (PHD Thesis, The University of Saarbrücken, 1995) 135.

licensing agreement, or contract of lease.¹ For a patent licence agreement, the primary commitment for the patent holder is to deliver the patentable technology of the agreement to the licensee and enable him to exploit and benefit from that technology during the period of contract. In addition to delivering the patentable invention, a patent licence usually contains another clause which obliges the licensor to supply, on a one-off basis or on a continuous basis, useful technical assistance to practice and operate the licensed patent rights.²

In the absence of a particular contractual stipulation regarding these technical assistances or other useful information, the question is whether the licensor is obliged to provide to the licensee such methods so as to better achieve the purpose of manufacturing the patented invention. Of course, the licensing agreement is the main source that determines the rights and obligations of both parties, although terms may be implied in a contract through statutes or by courts.³ In Libya, judges may rely on general rules of contracting or commercial custom to solve this issue. These rules, in fact, are related to the obligation of delivery in the case of the contract in general and the contract of lease. For example, the lessor, in a contract of lease, has to 'derive the thing' comprised of its accessories to enable the lessee to benefit from it.⁴ By analogy to that rule, courts may oblige a licensor to deliver any assistance material that would enable the licensee to competently exploit the patent invention. According to the principle that contracts must be implemented in good faith and from the nature of things, the licensor should be imposed upon to deliver and explain any useful information to enable better use of the licensed technology.⁵

However, the court, in a common law jurisdiction, may determine the meaning of implied terms by reference to the case of other documents.⁶ For example, the courts in England and Canada held that:

Where words or clauses are missing from a contract, to give effect to the reasonable expectations of the parties, terms may be implied, but only where and as necessary on the basis that those terms must be what the contract means, and those terms may be derived from custom and usage, fact, law or legislation, always with the goal of ensuring a sensible commercial result.⁷

The Courts have no jurisdiction to imply terms unless 'on considering the terms of the contract in a reasonable and business-like manner, an implication necessarily arises that the parties must have intended that the suggested

¹Libyan *Civil Code* 1953 arts 417 and 563.

²See, A *Model Patent License Agreement* <http://wiki.creativecommons.org/Model_Patent_License>.

³For example, 'unfair contract terms' is the terms that implied by law in *Australia Competition and Consumer Act 2010* (Cth) sch 2 ss 24-27.

⁴Libyan *Civil Code* 1953 art 563.

⁵Vahrenwald, above n 3, 136.

⁶Thorley et al, *Terrell on the law of patents* (Sweet & Maxwell, (17th ed, 2006).

⁷M H Ogilvie, 'Reconsidering the Interpretation and Implication Rules in the Law of Contract: An English-Canadian Comparison and a Proposal for a New Unified Rule' (2013) 28(187) *Banking & Finance Law Review* 187.

stipulation should exist'.¹ The interpretation of the obligation related to a patent licence agreement is not always clearly established – especially the obligation of delivery – because the subject of this obligation is usually secret information. According to common law legal analysis, courts are not likely to imply terms which oblige the patentee to provide additional information to another party, even if the patentable technology cannot be operated adequately without such assistances, where the parties fail to expressly draft them in the licence agreement.² However, if the licensor had undertaken to ensure that the licensed technology will operate as expected during the period of licensing, the question becomes how the licensor will ensure such an outcome without providing the necessary technical assistances. In this case, a judge may require the licensor to deliver any information that is needed for ensuring the licensed technology will be capable of being properly manufactured.

In contrast, the Egyptian Trade law 1999 provides special terms that shall be apply to any contract that contains technology transfer. One of these terms is that:

The supplier shall submit to the importer the information, data, and other technical documents as required for assimilation of technology, and also the necessary technical services to be requested by the importer for the operation of the technology, particularly expertise and training.³

The licensor, thus, is obliged by this article to provide technical assistances to another party to manufacture a patentable invention even if the parties did not expressly provide for it in licence agreement. Libyan legislators may benefit from the Egypt approach regarding the obligation of delivery in technology transfer contract and stipulate such provision in future technology transfer law.

The Obligation of Warranty

The obligation of warranty is one of the most important obligations of the licensor in a contract of transferring technology in general.⁴ The legal basis of this obligation is derived from the obligation of a licensor to deliver something that is not owned by anyone except the licensor and/or no one has the rights upon it and enables the licensee to enjoy quiet possession of the licensed technology.⁵ This possession will be disturbed when someone infringes a patent. Because the main purpose of the licence agreement is to provide the licensee with legal access to the patent holder's technology, the licensee should obtain a warranty that the patentee owns all rights related to the licensed

¹Thorley et al, above n 9, 398.

²Vahrenwald, above n 3, 82.

³Egyptian Trade Law No 17 of 1999, art 77 (1).

⁴Hossam al-Saghir, 'Licensing Intellectual Property and Technology Transfer' (Paper presented at the WIPO National Seminar on Intellectual Property for the members of the Shura Council, Organized by WIPO In collaboration with Ministry of Commerce and Industry And the Shura Council Oman 24 March 2004) 8.

⁵Ahmed Tareq Bacer Al Beshtawi, Licensing Contract to Exploit Patent (LLM Thesis, The University of An-Najah, 2011) 81.

technology.¹ The licensee usually negotiates a clause including performance guarantees, defence and reparation against third party's patent infringement actions and implementation of licensed technology against a third party.² But what is the legal position under Libyan law if there is no negotiation or agreement regarding the obligation of warranties by a licensor?

In other words, are there any implied warranties that may apply on the licensor's obligation of warranties in patent licence? There are no express provisions in Libyan law regulating the obligations of warranty whether in a licence agreement or in a contract of technology transfer in general. However, the implied obligation of warranty according to Libyan law is based upon the application of the general rules regarding the leasing contract or the contract of sale by way of analogy to a licence agreement;³ the licensor's obligation is to deliver a patented invention to the licensee without any defects, otherwise the licensor will be handed something that is not identical to what has been agreed upon. Achieving the results from the exploitation of a patent is associated with the validity of the patent itself. The patent holders should be bound to warrant against hidden defects of the patentable technology, and to warrant undisturbed enjoyment of exploiting the licensed invention.

The Warranty in the Case of Hidden Defects

The prevailing doctrine in civil law jurisdictions tends to state that the licensor is obligated by an implicit obligation of warranty against legal and technical hidden defects of the licensed patentable technology.⁴ The legal defects related to the legal status of patent rights, include the validity of patents, registration of patents and absence of mortgages or pledges of third parties on the patent rights, while the technical defects concern the applicability and practical usefulness of the patented invention and ensure that the patented technology will work as expected.⁵ Despite the fact that Libyan courts have not not faced these issue, the legal basis of this implied warranty may be found by analogy with leasing contract in article 575 of the Libyan Civil Code which establishes, in subsection 1, 'subject to any agreement to the contrary, the lessor warrants the lessee against all defects which prevent or appreciably diminish the enjoyment of the property ...'⁶ and subsection 2 of article 576, which states that 'if the defect caused any damage to the lessee, the lessor shall be liable to pay compensation, unless the lessor can establish that he was not aware of the defect'.⁷ According to article 576 (1) of the Libyan Civil Law, if

¹C Ben Huber, 'Patented Technology: Issues in Drafting a License' (2003) 32(9) *The Colorado Lawyer*, 106.

²Brian G Brunsvold, 'Negotiation Techniques for Warranty and Enforcement Clauses in International Licensing Agreements' (1981) 14(2) *Vanderbilt Journal Of Transnational Law* 282.

³*Libyan Civil Code 1954* arts 428-42 and 570-85. See Anes Attia Soleman, *Legal Warranties for Technology Transfer* (Dar Alnahda Al Arabia, 1969) 572.

⁴Vahrenwald, above n 3, 151.

⁵*Ibid.*

⁶*Libya Civil Code 1954* art 575 (1).

⁷*Ibid* art 576 (2).

the licensed technology is found to have a defect, the licensee may claim termination of the agreement or reduction of the royalties.¹

The justification for the obligation to warrant for the absence of hidden defects in the leasing contract ‘lies in the fact that the lessor is in a better position than the lessee insofar as the relation to the leased thing is concerned’.² One may argue that the difficulty of applying the rules regarding leasing contracts to the licence patent is because the position of the patentee is no better than the position of the licensee. Granting a patent requires a process of examination which is unlikely to impute a mistake of the patent office to the patent owner.³ Nevertheless, Prevailing doctrine and jurisprudence in civil law countries such as France, Libya and Egypt, apply the concept of warranty against hidden defects to the patent licence by relying of general rules of leasing contract.⁴

The warranty in the case of disturbing the enjoyment of the licensed invention

With regard to the warranty against disturbing the licensee’s right of enjoyment for exploiting the patented invention, the licensor should deliver the licensed invention to the other party without any hindrances whether, and this is due to facts caused by licensor himself or by third parties. Examples regarding the case of disturbance by a licensor are when a patentee attempts to enjoin an exclusive licensee from exploiting the licensed technology, or where the licensor does not communicate an improvement to the patented invention.⁵ The disturbance also concerns where there is an action of patent infringement proceeding by third parties.⁶ Usually, the licence agreement contains such warranties which bind the patent holder to warrant the enjoyment of a licensee to benefit from a licensed technology. In the absence of those warranties, article 570 (1) (2) of the Libyan Civil Code would be applied by way of analogy to the patent licence. These rules state that:

1. The lessor shall abstain from doing anything which may disturb the lessee in his enjoyment of the leased property, and shall not make any alternations to the property or its accessories that diminish such enjoyment.
2. The lessor not only warrants the lessee against his own acts and against those of his servants but also against any disturbance or damage based on a lawful claim by other lessees or by any successor in title of the lessor.⁷

¹Ibid art 576 (1).

²Vahrenwald, above n 3, 151.

³Ibid.

⁴See *ibid*; and al-Saghir, above n 14. See also Al Beshtawi, above n 15, 82. There is no decision by Libyan courts regarding this issue, but I think the Libyan courts will not hesitate to take the same decision of the French courts in the absence of contractual terms or express provisions regulating the warranty in patent license.

⁵Vahrenwald, above n 3.

⁶Ibid.

⁷Libyan *Civil Code 1954* art 570 (1), (2).

In Libya, the licensor, therefore, must warrant a lack of disturbance to the licensee's rights to exploit the subject-matter of patent licence whether this warranty is included in licence agreement or not.

An important question is whether the licensor, by contract, can exclude any warranties in licensing agreement. Generally, the variation of warranty in patent licence is possible under Libyan law by way of analogy with other nominated contracts under the Civil Code. For example, article 577 of the Libyan Civil Code stipulates that 'any agreement excluding or limiting the warranty against disturbance or defects is void if the lessor has fraudulently hidden the cause of such warranty.'¹ Thus, the contracting parties in a licence agreement can exclude any terms of warranty unless the licensor was intentionally concealing the defects of licensed invention. However, article 435 (1) of the Libyan Civil Code provides that any agreement is void if the contracting parties agreed that the seller does not warrant any entitlement arising by his or her act.² The parties cannot, thus, agree to exclude the licensor himself from a warranty not to disturb the licensee's capacity to exploit patented rights, because such a warranty is mandatory in contracts and may apply to a patent licence.

Typical Obligation of a Licensee

Delivering the patentable technology to the licensee and warranting that technology to work as expected offsets an obligation of the licensee to pay compensation and to exploit licensed technology.

The Obligation to Pay Royalties

A royalty is an amount of money reserved by the licensor of a patent right and is payable proportionate to the exploitation made of the right by the licensee.³ The licensee must pay the price of the technology to the licensor as agreed upon in the licence agreement. This amount is usually determined according to a number of factors. For example, the licensor estimates the price of licensed technology based on his or her effort to discover that technology and based on the returns of manufacturing technology.⁴ The licensee estimates the price of the technology based on the benefit that will return from the exploitation of such technology through the license period.⁵ Licensing

¹See Libyan *Civil Code* art 577. Also art 442 states that 'the contracting parties, by specification or agreement, increase, restrict or abolish the warranty. Nevertheless, any clause abolishing or restricting the warranty is void if the vender intentionally and fraudulently conceals the defects of thing sold'.

²Libyan *Civil Code 1954* art 570 (1).

³Henry Campbell Black, *Black's Law Dictionary* (West Publishing Company, 4th ed, 1968) 1496.

⁴Al Beshtawi, above n 15, 83.

⁵*Ibid.*

agreements usually provide for some methods of royalty payments.¹ For example, the parties may stipulate a payment of a lump sum or royalty compensation or other type of payments.

Lump Sum Licence Fees

A lump sum payment may be paid up-front or in instalments, and it usually exacted where the technology can be conveyed at one time and quickly accommodated by the licensee, or where the patentee has endured significant research and development and may be reluctant to share its knowledge without some guarantee in advance that 'it will receive appropriate reimbursement for a share of the development costs'.²

Royalty Payments

A royalty is a payment to the patent owner, which reflects the exploitative value of the technology by the licensee and is often made on the basis of sales royalties or fixed royalties depending on the subject matter being licensed, the relevant industry and the respective leverage between parties.³ The most commonly encountered forms of compensation in patent licences are those based on sale of products, gross receipts, net sale or profits.⁴ The rates of this royalty method are often graduated to increase or decrease over the volume of product sold or produced, and the royalties are usually less in the early years of the license agreement as an incentive to the licensee.⁵ To reach a win-win status in a license agreement, parties usually agree that the royalty rates are to be variable. For instance, a royalty rate of 10 per cent might reduce to 7.5 per cent after the sale of one million units, then to 5 per cent after five million units.⁶ Also, the licensee may require paying the licensor an annual minimum royalty. Hence the sum of US\$75,000 might be payable for year two of the license, increasing to US\$100,000 for year three and US\$125,000 for each year thereafter.⁷

The price of technology may not always be a royalty or lump sum payment method but it can be a product of licensed technology or another patentable technology. As an article 82 (1) of Egyptian Trade Law 1999 provides that:

The charges may be a total amount payable altogether or in several instalments. They may also be a share in the capital invested in operating the technology or a portion of the yield of this operation. The charges may as well be in the form of a certain quantity of the commodity in which the technology

¹Thomas M Apke, 'Acquisition and Licensing of Intellectual Property' (1998) 40(6), Managerial Law 9.

²Ibid.

³Huber, above n 16, 104.

⁴Philip Mendes, 'Royalty Terms in Licences' (WIPO, Special Feature: Valuation and Acquisition of IPR, 2003) 33.

⁵Apke, above n 35, 9.

⁶WIPO, 'Exchanging Value: Negotiation Technology Licensing Agreements: A Training Manual' (WIPO, 2005) 58.

⁷Ibid.

is used for its production, or a primary material the importer produces and undertakes to export to the supplier.¹

The payment may take the form of a certain quantity of products of licensed technology. In this case, the licensee provides identifying percentage of goods to the licensor to be rather kind for the exploiting the licensed technology.² The payment of technology may also take a method of swap with another technology such as in cross licence agreement. In this regard, each party will have the right to use another party's technology without paying royalties to each other. In general, Libyan law does not restrict parties to a patent licence agreement that follows special types of payments unless the subject-matter of the contract is contrary to public policy or morality.³ For example, licensors cannot transfer technology for alcohol or other prohibited drugs as payment. Also, if the object of an obligation is a sum of money, the licensee is bound only to the extent of the actual figure specified in the licence agreement regardless of the increase or decline in the value of such money at the date of payment.⁴ Whatever methods used as payment, parties to a licence agreement must identify the price of the technology in the agreement or how the price is to be set (such as by agreement to determine price by a third person).⁵ If the price is not determined or is incapable of being set, the license agreement is void.⁶

Licensee's Obligation to Exploit the Patented Invention and Maintain Confidentiality of the Technical Information

Licensing agreements give licensees the right to exploit the licensed technology within the limits set by the agreement. At the same time, the licensee is responsible to work a patented invention in good faith to produce the goods that provide, often, the royalty incomes.⁷ In the case of an exclusive license, the licensee must be reasonably diligent in exploiting the licensed technology,⁸ most legislation requires that the patented technology must be exploited within a certain period of time. Otherwise it must be cancelled or a compulsory licence will be granted to others.⁹

According to Libyan law, licensees, whether exclusive or non-exclusive, are obliged to exploit the patented technology. This is not only inferred from the fact that, in the absence of adequate exploitation, the patent owner is exposed to the risk of a compulsory licence, but also from the requirement to

¹Egypt *Trade Law No 17 1999* art 82 (1).

²Al Beshtawi, above n 15, 85.

³Libyan *Civil Code 1954* art 135.

⁴Ibid art 134.

⁵Mohammed Ali Al-Badawi, *The General Theory of Obligations* (the National Library, Tripoli, Vol 1, 1999) 143.

⁶Libyan *Civil Code 1954* art 133 (1).

⁷Hossam al-Saghir, above n 14..

⁸Gordon W Hueshen, 'Patents: Exclusive Licenses: Licensor and Licensee Relationship: Licensee's Obligations' (1951) 49(5) *The Michigan Law Review* 740.

⁹For example, Libyan *Patent Law no 8 of 1959* art 28-30.

serve the public interest in exploiting the patented technology¹ and from the duty to perform agreements in good faith.² Civil legal doctrine makes a differentiation between the obligation to achieve a result and the obligation to use due diligence.³ The obligation of exploiting patented technology is an obligation to use due diligence, which means that ‘in the absence of a special clause establishing the scope of this obligation, the exploitation must be serious and effective with regard to quantity as well as to quality’.⁴ Unless there are ‘insurmountable difficulties’ such as technical or commercial issues in the industrial practicality of the technology, the licensee may be free from the obligation of exploiting licensed technology.⁵ For example, the technology is not exploitable, if ‘it can only be put to practice in a laboratory and at a price which prohibits access to the market’.⁶ Hence, the exploitation of technology must be industrially and commercially possible. If the difficulties of exploiting the licensed invention are due to a mistake of licensee, the obligation to exploit does not elapse and the court may oblige the licensee to compensate the licensor in accordance with the contractual responsibility.⁷

The licensee also should keep confidential the technical information that he obtained due to contract. So, the licensee is obligated not to disclose any information whether related to the patent documents, methods regarding manufacturing the patented invention or know-how information, and, in addition, other information that is considered confidential which may harm the patentee if it is revealed.⁸ The legal basis of this obligation in Libyan law is inferred from the fact that the contract must be executed in good faith,⁹ and patent information must not be disclosed to competitors to take advantage of.

By comparison, article 83 (1) of the Egyptian Trade Law expressly provides that, in a technology transfer contract, the transferee must maintain the confidentiality of the transferred technology he or she obtains, and of the improvements introduced to it. The importer may be ‘accountable for the damage occurring from divulging this secrecy whether it takes place in the stage of contract negotiations or after’.¹⁰ Thus, in formulating this obligation, it is preferable for the parties to accurately identify the information that is considered as confidential and, usually, each party negotiates to expand the scope of what is considered secret or narrow according to his interests.¹¹ For example, the patentee, typically, seeks to establish a broad meaning of what

¹Vahrenwald, above n 3, 168.

²Libyan *Civil Code* 1959 art 148 (1).

³Vahrenwald, above n 3, 168.

⁴Ibid.

⁵Libyan *Civil Code* 1959 art 161 states that ‘when an obligation arising out of a bi-lateral contract is extinguished by reason of impossibility of performance, correlative obligations are also extinguished and the contract is rescinded ipso facto.’

⁶Ibid.

⁷Al-Badawi, above n 46, 226.

⁸Al Beshtawi, above n 15, 86.

⁹Libyan *Civil Code* 1959 art 148 (1).

¹⁰Egyptian *Trade Law No 17 of 1999* art 83 (1).

¹¹Al Beshtawi, above n 15, 87.

should be secret so as to restrict the provision of as much confidential information as possible, while the licensee seeks to narrow the scope of secrecy. The obligation of exploitation and maintaining the confidentiality of technical information is not only for the original patented invention, but also extend to the improvements of the patented technology which have been provided to the licensee.

Summary

Patent licences have effects not only during the process of exploitation of the patented invention, but also after termination of the patent license agreement. While exploiting the licensed technology, for example, the licensor must provide technical assistance that may help licensee to better exploit the patent rights and the licensor should warrant the capacity of the licensee to benefit from exploiting the patent rights without interference. The licensee, however must pay for the use of the patent rights, whether by through a lump sum, with royalties or another patentable technology. For the purposes of patent rights, licensees also have to exploit the licensed technology to avoid the licence becoming a compulsory license and to benefit society. In addition, the licensee is bound to keep confidential the know-how and any technical information during the patent licence period and after its terminating, especially if the patent rights have not expired.

Almost of these rights and obligations may be a subject of future disputes between parties. Therefore, it is necessary to carefully draft the terms and conditions of license agreement to include all possible contingencies. If such disputes occur in Libya, with its lack of a legal framework regarding contracts of technology transfer, judges would struggle to find the legal norms to support their decisions because of the uniqueness of the nature of patent licenses; sometimes it is difficult to apply the general rules of the Civil Code. The Libyan approach to the transfer of technology could benefit from the provisions of technology transfer in Egyptian Trade Law.

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