

# Implied Technical Warranties in Patent Licenses

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## Introduction

Economic evidence suggests that patent licensing has increased rapidly in importance over the last few years.<sup>2</sup> The income from licensing patents is one of the fastest-growing sources of profit for many companies. Large companies are realizing that they are sitting on ideas that could be of value to someone somewhere, even if they are of little use in house. Those ideas are increasingly being put up for sale. Smaller companies are also demonstrating the power of pure intellectual property. For example, a growing number of companies design chips, or parts of them, that other companies then churn out by the million. It is the intellectual property – not the physical products – of such companies that ends up in devices such as mobile phones, set-top boxes, personal computers or anything else that needs some built-in “intelligence”. However, most patent cases, as well as most of the literature on patents, emphasize the creation of patent rights, while the active market for the exchange of these properties is sometimes ignored. But in practice, enabling and facilitating technology transfer is arguably the most significant economic function of the patent system. By transforming technical knowledge into intellectual property the transfer of knowledge in society is vastly facilitated. Thus to view patent licenses and

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<sup>2</sup> A recent report by ETAN (European Technology Assessment Network, 1999) on intellectual property rights highlights several new implications that a rise in technology transactions has meant for corporations. But the report also recognizes that markets for technologies, ideas, knowledge and information, have significant difficulties in operating. See European Technology Assessment Network (ETAN), *Strategic Dimensions of Intellectual Property Rights in the Context of S&T Policy*, European Commission Report EUR 18914, Luxembourg.

assignments as peripheral aspects of the patent system is to miss a key point: these transactions are at the very heart of the patent system.

Despite the importance of patent transactions, there is only very limited statutory basis for them in Sweden or in other Scandinavian countries. Section 43 of the Swedish Patent Act provides that, unless expressly agreed to the contrary, a license is personal to the licensee, i.e. the licensee's right is non-assignable. But beyond this, the legislator's assumption is that private contract alone should guide technology transfer. True, it has been a long-standing debate in Scandinavian law about the possibility to rely on analogies from the Sale of Goods Act. But I think the dominant view is that such analogies are not really helpful, at least not with respect to patent licenses and maybe not even in the case of a sale of a patent.<sup>3</sup> The differences between transactions in patents and transactions in corporal goods are simply too great to allow for any analogies beyond what is self-evident. I subscribe to this position and therefore this article starts from the assumption that patent licenses have a *sui generis* character. They must be judged on their own merits without trying to put them into a regulatory straightjacket design for a different set of transactions. This reliance on contract only means that a patent license agreement must be very carefully drawn to fully express the agreement of the parties and to leave as little as possible to future interpretation by courts or, more frequently, by arbitration panels. Any disputes between the parties will have to be solved through a fact-specific and more or less hard-handed interpretation of the contract.<sup>4</sup>

However, the absence of statutory provisions does not lead to a legal vacuum. Though Scandinavian courts certainly have not been inundated with cases arising under patent licensing agreements, there are a few cases and also some doctrinal writing on patent licenses. The object of this article is to use this material to address the default rule applicable to technically defective but nevertheless licensed inventions. The overarching question is whether a licensee can take for granted that the licensed invention has some technical utility, without having received a specific guarantee from the licensor? This question can also be re-phrased as whether a patent license has a positive or only a negative legal content? Is the only consideration received by a patent licensee negative, i.e. forbearance of suit by the licensor, or does the grant of a license

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<sup>3</sup> The majority seems to favor a *sui generis* approach to interpretations of patent licenses due to the considerable differences between intellectual properties and corporal goods. See Plessner, M., *Nogle problemer i forbindelse med frivillig overdragelse af udnyttelseretten af patentrettigheder*, Juristen, 1955 p. 201 (223); Koktvedgaard, M., *Om købelovgivningens anvendelse på overdragelse af immaterialrettigheder*, Tidsskrift for Rettsvidenskab, 1965 p. 571; Sandgren, C., *Patentlicenser*, p. 112 ff (Stockholm 1974); Koktvedgaard, M., Levin, M., *Lärobok i immaterialrätt*, s. 387 (Stockholm 2000); Bernitz et al, *Immaterialrätt* p. 140 & 266 (Stockholm 1998); Rosén, J., *Upphovsrättens avtal*, p. 42 ff (Stockholm 1992); Runesson, E. M., *Immaterialrättsliga fel vid köp*, Festskrift till Gunnar Karnell p. 627 (Stockholm 1999); Stenvik, A., *Patentrett*, p. 383 f (Fagernes 1999); Schovsbo, J., *Immaterialrets aftaler*, p. 64 ff (København 2001). It has, however, also been pointed out, especially by specialists in the field of sale of goods, that the sale of a patent is an act directly regulated by the Sale of Goods Act and that some analogies from that Act can be made with respect to patent licenses, see Hultmark, C., *Köplagens tillämplighet på fel i patent*, Juridisk Tidskrift 1993-94 p. 687 ff; Cf. Hellner, J., Ramberg, J., *Speciell avtalsrätt I Köprätt*, p. 42 (Stockholm 1989).

<sup>4</sup> Cf. Rosén, *supra* note 3 at 42.

also confer something positive, i.e. an opportunity for the licensee to achieve some desired technical result? Remedies available to the licensee are only superficially touched at in this article. Remedies would need to be addressed at length and is therefore largely beyond the scope of the article.

### **Commercial Practice – Contracting About Technical Qualities of Inventions**

It is evident that the default rule for technical qualities of a licensed invention is closely related to what the justified assumptions of parties are in the setting of a patent license negotiation. What general assumptions are parties justified in having when they enter into negotiations for a patent license? The default rule pertaining to this situation should preferably mesh with expected or conventional practice in a manner that will project a favorable impact on contracting about patent licenses. This is in contrast with rules that are meant to dictate terms and regulate behavior. Contract law generally does not intend to regulate practice. It seeks to sustain and facilitate it. As a matter of practice, default rules are common in commercial contexts, while consumer law contains many fixed rules designed to protect the consumer. In commercial contexts, such as patent licenses, default rules are means to pave the way for existing commercial practice. This is usually approached by trying to identify patterns of commercial practice and to follow them to the extent that they are not inconsistent with modern social policy. This is not due to simple faith in empirical sources for commercial law. It stems from the reality that, even though we may not know contract practice in all the details, we should in principle refer for guidance to the accumulation of practical choices made in actual transactions. The goal is congruence between the default rules and commercial practice, in order to achieve commercially intended and predictable results.

The difficulties involved in referring to commercial practice in respect of patent licenses lie in the fact that the circumstances leading up to licenses may be very different. The value of what the licensor has to offer varies greatly from case to case. In the preparatory works to the Swedish Patent Act it was even stated that it was inadvisable for the legislator to furnish any default rules for patent licenses, except Section 43 (mentioned above), due to the diversity of the practical circumstances.<sup>5</sup> The transactions will range from a deal between a small inventor and a local manufacturer to transactions between sophisticated businesses employing multiple lawyers and affecting billions of dollars of business. The legal approach needed in face of this diversity is probably not to try to identify rules that individual parties would draft tailored to each individual situation, but to select an intermediate or ordinary framework whose contours are usually appropriate, but whose terms will be altered in the more sophisticated environments. The inexperienced parties should probably be at the forefront. More experienced parties will anyhow not rely on the default rule, but use their freedom of contract to craft a license that suits their particular needs.

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<sup>5</sup> Swedish Government Proposition to the Patent Act 1966:40 p. 158.

In contract practice it is often the case that patent licensors do not warrant that the licensee can use the licensed technology to any useful extent. Most licensors are unwilling to do more than affirm that the licensee will not be sued by the licensor for use of the technology. If a royalty is involved the licensor often also maintain the right to cancel the contract if the licensee fails to achieve the inventions industrial realization. Provisions to this effect can e.g. have the following wording:

The Licensor does not warrant that the invention is capable of industrial realization nor shall he be responsible for the consequences of any failure so to realize it.

If the Licensee fails to achieve the invention's industrial realization within a period of ... the Licensor is entitled to terminate the contract and recover damages.<sup>6</sup>

This entails that the entire responsibility for the technical utility of the invention rests with the licensee. Parties to patent licenses often seem to opt for this *caveat emptor* policy with respect to the technical potential of an invention. For example the wording of the contract in a 1976-case from the Danish Supreme Court was very similar to the provisions above.<sup>7</sup> In § 6 of the contract pertaining to a patented wire-lock, it was laid down that the Danish licensor did not warrant that the invention was industrially applicable. Furthermore, the article declared that the German licensee was familiar with the invention and accepted the responsibility for its industrial realization. However, in § 21 of the contract it was also provided that the contract would not enter into force unless the necessary official approvals were awarded, in particular those related to foreign trade. The contract, including a minimum royalty clause running for at least three years, was signed in 1969. After signing the contract the licensee had an independent technical expert evaluate the invention, which was a necessary preliminary step in order to attain an approval of the lock's quality by the German trade association. Without such an approval it would be almost impossible to sell the product on the German market. The expert concluded that the product could in principle work, but required some additional engineering before it would be approved. On receiving this message the licensee tried to avoid the agreement, claiming that it had not entered into effect because the trade association approval was not forthcoming, i.e. that an official approval according to § 21 was lacking. The licensor replied that the approvals according to § 21 related to import permissions, currency regulations and possibly also competition law matters. A technical assessment of the lock had never been discussed during the negotiations and was not covered by § 21. The Danish Supreme Court in its ruling noted that § 21 was somewhat ambiguous. But § 6

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<sup>6</sup> Clause 10 in the MODEL FORM OF INTERNATIONAL PATENT LICENCE CONTRACT, prepared by ORGALIME (Organisme de Liaison des Industries Métalliques Européennes). ORGALIME groups the central engineering and metalworking trade associations in fifteen European countries and provides liaison between these bodies in economic, legal, technical and other matters of concern to the industries they represent.

<sup>7</sup> Ugeskrift for Retsvæsen 1976 p. 495 H.

laid down that the licensor did not warrant either the technical or commercial utility of the invention. Therefore the responsibilities for the particular technical conditions of the German market had to lie with the licensee, who could after all have made it an explicit condition in the contract that the lock would be approved by the trade association, if this had been decisive for him.

The licensee in this case thought that he could sign at an early stage of the negotiations after having learnt from the licensor that the lock was already in production in great numbers in other European countries, that most European markets were already licensed, and also that the licensor was simultaneously engaged in negotiations with other prospective licensees for the German market. This apparently made the licensee postpone a full technical and commercial evaluation of the invention's potential on the German market. If the technical and commercial information presented by the licensor had been colorably incorrect, this may have allowed the licensee to avoid the contract, but it seems that in this case it was rather the special conditions on the German market that led to the dispute. Licensees are presumably in most cases more cautious than this German licensee, but it will always remain a very difficult task to evaluate an invention. As long as the invention is not introduced on the particular market, the licensee has no sure means of judging whether the idea is commercially or even technically viable. Nevertheless, in most contracts the parties seem to place this responsibility on the licensee. This may particularly be the case where the licensee is dealing with an individual inventor, or an organization devoted solely to research.

Why then do patent licensors generally shun technical warranties? It is too facile to say that they seek to distribute bad inventions. A licensor typically avoids warranty provisions because the legal criteria for a technical warranty seldom work well for complex inventions. The difficulties involved in objectively monitoring and assessing technical qualities are considerable. Licensors disclaim warranties because they do not know what a warranty would mean and do not want to assume the risks and costs to find out. If e.g. the licensor in the Danish case had accepted to make a trade association approval a condition for the contract, he would e.g. be exposed to the risk that the licensee did not portray the invention in the best possible way. These monitoring problems and other uncertainties lead to a preference for a *caveat emptor* solution, even though the licensor often know more about the invention from a technical perspective than the licensee.

Most licensees understand that their licensors cannot live with an extensive warranty of e.g. merchantability of the patented products or fitness for a certain technical purpose that the licensee may have. Consequently, a licensee is regularly precluded in the contract from arguing that compensation is due when the invention is not as "good" as he expected. Licensees should respond by evaluating the invention fully before signing such a contract.

But what is the legal position if there has been no agreement or discussion pertaining to the technical quality of the invention? Would the situation be the same or are there some implicit warranties regarding the utility of a licensed invention imputed into the agreement by the Court? A few Scandinavian court cases actually indicate that this can sometimes be the case, chiefly with respect to information provided by the licensor in the patent specification. A minimum

level of technical quality of the invention seems to be tacitly warranted in patent licenses, through the reference in the license agreement to the patent. However, it must be remembered, that to avoid such an implied warranty the licensor only needs to disclaim it in the license, as exemplified by the provisions cited above. The only legal requirement, which must be fulfilled in order to avoid the tacit warranty, is that the licensor can demonstrate, through the circumstances of the negotiation or by language of the contract, that some sort of other agreement exists, even if the exact terms of that agreement are ill-defined.

In the remainder of the article I will first analyze the available cases suggesting the existence of some implied technical warranties. Thereafter I will discuss the kind of circumstances that may preclude implicit technical warranties, summarize and draw some conclusions.

### **Discussion of Cases on Implicit Warranties of Technical Qualities**

The Norwegian Supreme Court tried in 1959 the case *Oswald Tvetmark v. Brynjulv Abrahamsen*.<sup>8</sup> Abrahamsen was a trained chemist and had received a patent on a process for production of a new form of porous and heat preserving construction material consisting of sawdust, cement and mud in certain proportions. By an agreement signed on March 1, 1955 Abrahamsen received a down payment and also the right to a future royalty, in exchange for giving Tvetmark an exclusive right to use the patented production process in a particular part of Norway. After 4-5 months of experimentation the use of the production process was halted by Tvetmark. It was impossible for him to produce blocks with the strength prescribed for construction purposes in Norway (building standards required a strength of 40 kg/cm<sup>2</sup>). When the Norwegian National Testing Institute was asked to test three blocks made according to the process, one possessed a strength of 21,55 kg/cm<sup>2</sup>, while the other two had a strength below 20 kg/cm<sup>2</sup>.

In the Supreme Court judgment Tvetmark was allowed to avoid the contract and have his down payment returned. The Court explained that Tvetmark had been shown the patent specification by Abrahamsen before the license was signed. The patent claimed that the blocks made according to the invention had a strength of 45 kg/cm<sup>2</sup> and Tvetmark had not doubted this. When questioned, Abrahamsen could not remember on what grounds the figures had been introduced into the patent documents. The Court concluded that the licensee, Tvetmark, who was inexperienced in the field, had entered into the license agreement under the implicit condition that the statements in the patent specification were correct and therefore that the blocks would satisfy Norwegian building standards. Abrahamsen did or at least ought to have, realized that these figures had been vital for Tvetmark. When the conditions failed Tvetmark was allowed to avoid the contract and have his down payment returned. However, no damages were awarded for the losses that Tvetmark had incurred while trying to work the invention. The outcome was dictated mainly by what the licensor ought to have understood about the vital conditions that the licensee had. By not

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<sup>8</sup> Lettбетongdommen, Norsk Retstidende 1959 p. 801.

commenting on what the licensor should have understood to be decisive figures in the patent specification, the licensor implicitly warranted these figures.

The mentioning in European patents of technical results achieved by an invention usually stems from Rule 27.1 (e) in the European Patent Convention (EPC), which lays down that at least one way of carrying out the invention claimed must be indicated in the description. The examples of how the invention can be practiced are frequently furnished towards the end of the patent description. They are often quite explicit accounts of how the invention has been tested in the laboratory or elsewhere.

The Patent Office's grant of a patent should not be taken as verification in any way of these statements. The Office cannot for practical reasons test inventions experimentally and is not expected to question the statements made by the applicant from a simple theoretical standpoint. In the EPO Guidelines the general principles for evaluation of such statements are described as follows:

Facts adduced by a party will ... normally be deemed true, even without supporting evidence, if it is clear that no doubts exist concerning them, if they do not contradict one another or if no objection is raised.<sup>9</sup>

The requirements that an invention must be susceptible to industrial application and possible to practice for a person skilled in the art, are thus only tested at a theoretical level. Only if the examiner has serious doubts about the statements made in the application, e.g. if they appear contradictory or otherwise unlikely, will supplementary proof be demanded of the applicant, by means of new experiments.<sup>10</sup> An objection from the examiner can in practice only be expected if the invention according to the examples is alleged to operate in a manner clearly contrary to well-established physical laws, e.g. a perpetual motion machine, or if the statements in the description are self-contradictory. It is believed to be preferable to let competitors question incorrect statements and then allow them to file oppositions against the patent. That never happened in the prosecution of Abrahamsen's patent, but instead Tvetmark was allowed to avoid a license to the patent when the statements proved to be incorrect. Three things seem to have been particularly important in reaching this decision: the strength of the blocks was a vital aspect of the invention, it was also something that the licensor knew was important for the licensee and, finally, the licensee had good reasons to rely on the licensor's ability to determine the strength of the blocks.

In a Danish case a buyer was also allowed to avoid the agreement in a situation where the patent failed an official standard.<sup>11</sup> A patent on a life jacket had been sold, but the buyer later refused to pay. When sued by the seller/inventor, the buyer claimed that the life jackets did not live up to the claims made in the patent specification. The invention was a life jacket made of water-repellent vegetable fibers, e.g. Brazilian, East Indian or Egyptian cotton. The fibers were imbued with oil in order to enhance their water-repellent effect.

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<sup>9</sup> Guidelines E IV 1.2.

<sup>10</sup> Guidelines C VI 14.2.

<sup>11</sup> Ugeskrift for Retsvæsen 1910 p. 53.

According to the patent description the procedure would increase the lift of the material, which meant that only a very limited amount of fibers was necessary in order to produce a life jacket that kept a person afloat. However, the actual lift of the material proved to be minimal. The National Administration of Shipping and Navigation did therefore not approve the life jackets for use on ships.

The buyer of the patent claimed that he during the negotiations had made it an explicit condition that the patent lived up to the promises made in the patent specification. The Court did not consider it necessary to decide whether this was actually true. It sufficed that the possibility to have the life jackets approved had been a decisive condition for the buyer and one which the seller of the patent had to have been aware of. The buyer was allowed to avoid the contract. In this case it was technically possible to manufacture the patented life jackets according to the specifications in the patent, but such an endeavor filled no purpose since the products did not solve the problem that was indicated in the patent specification (to provide a life jacket with good lift in water).

In this case the misleading statements in the patent description were more vague than in the previous case. It was the general purpose of the invention, mentioned in the beginning of the description, which failed; the description did apparently not indicate that the lifejackets had a specific degree of lift, only that it was good. Such a general purpose for use of an invention is usually mentioned in the beginning of the patent description. In Rule 27.1 (c) of the European Patent Convention (EPC) it is provided that the applicant must disclose the invention in such terms that the technical problem and its solution can be identified, and that any advantageous effects of the invention are stated with reference to the background art. The applicant will usually dispose of this requirement by mentioning the practical technical problem that exists in the prior art and the advantages achieved by the invention in comparison to the prior art.

Do portions of a patent specification about the purpose for using the invention become implicitly infused into a license agreement pertaining to the patent? Can the licensee interpret statements about the general purpose of the invention as warranted by the licensor simply by the reference in the contract to the patent? The 1910-case indicates that the advantages mentioned in the patent create a justified assumption on behalf of the licensee/buyer that they can be attained and that the licensor/seller therefore is obliged to comment on them if he does not want to be held liable for them. The Supreme Court ruling in the case *Oswald Tvetmark v. Brynjulv Abrahamsen* is, I believe, more limited in this respect. It indicates only that precise technical accounts or figures in patent specifications are regarded as implicit warranties.

Some Scandinavian legal commentators argue the view that the patent specification creates implicit warranties, including a warranty pertaining to the object for using the invention. *Stenvik* attaches importance to statements made in the patent specification. He argues that if they do not hold true it is normally to be seen as a breach of the license. The basis for this is that usefulness of the invention is a patentability requirement. *Stenvik* concludes that the problem described as being solved by the invention, as well as more specific information furnished in the description, should probably be considered warranted.<sup>12</sup>

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<sup>12</sup> *Stenvik*, *supra* note 3 at 389.



*Plessner* argues that a licensor who shows the patent specification to the licensee creates the expectation that the results mentioned in the description are attainable. By making references to the patent in the negotiation the licensee is led to believe that the invention has at least some meaningful purpose of use (“Ausführbarkeit” and “Brauchbarkeit”). Utility or industrial applicability are patentability requirements and the patent document makes the licensee assume that these conditions are fulfilled. Therefore, the qualities that the invention has according to the patent description – in particular the advancement made in the technical field – can be seen as warranted.<sup>13</sup> *Plessner’s* and *Stenvik’s* positions thus seem to be that both precise technical figures in the description and more general statements about advantages of the invention are warranted. *Koktvedgaard* appears to be more hesitant about the existence of silent or inherent warranties concerning technical utility. He notes that the licensor is clearly not liable for the commercial utility of the invention and that the scope for a purely technical liability, apart from its commercial consequences, must be very limited, if it exists at all.<sup>14</sup> *Koktvedgaard* asks what the justified technical assumptions of a licensee really are with respect to an invention? Maybe there are no justified assumptions at all and that any liability therefore must be based on positive statements made by the licensor?<sup>15</sup>

I will suggest here that some statements in a patent specification do give rise to justified assumptions and that they are therefore rightfully considered as warranted. Whether they are to be categorized as implicit or explicit warranties, probably depends on the circumstances of the individual license. The distinction is not clear-cut between what has been incorporated in the agreement and what has not. But in any discussion of technical warranties I do think that it is vital to distinguish between different kinds of statements in a patent specification. A licensee, or buyer of a patent, should be able to rely on detailed examples given in the patent. If there is doubt concerning them the licensor is obliged to inform the licensee of it. The important feature of this information is that it purports to represent real-life experiences of the invention. For example, to assert a technical testing, which has not actually taken place, will probably impose liability on the licensor under breach of the license contract.<sup>16</sup> I think Scandinavian law takes the position that misleading but vital technical tests of the invention described in the patent lead to invalidity of a license pertaining to the invention, at least if the tests are fraudulent provided or significantly misleading. Specific technical data, thus, can form exceptions carved out of the *caveat emptor* doctrine, which in other respects control patent licenses. In fact tacit warranties about specific technical data are the opposite of the *caveat emptor* doctrine; they require that licensors behave cautiously.

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<sup>13</sup> “De egenskaper, som opfindelsen i patentbeskrivelsen siges at have – d. v. s. specielt et teknisk fremskridt på det pågældende område – må ’anses for tilsikrede’ ... ligesom disse egenskapers tilstedeværelse må være relevante forudsætninger, der, hvis de svigter, giver hævedgang.” See *Plessner*, *supra* note 3 at 218f.

<sup>14</sup> *Koktvedgaard*, M., *Lærebog i Immaterialret*, p. 367 f, København 1999.

<sup>15</sup> *Koktvedgaard*, *supra* note 3 at 579.

<sup>16</sup> This has been concluded by the German Federal Supreme Court (BGH), *Hubroller*, GRUR 1961, 494.

I would, however, argue that the same does not hold true with respect to more general statements made in a patent specification. Probably one should require a sizeable degree of precision before a statement about the invention is considered as an implied warranty. General praise of the invention during the negotiations is unlikely to impose any liability on the licensor. A statement concerning the general purpose of use for the invention or its technical advantages compared to the prior art, are often of an equally imprecise nature. One can therefore question the present-day relevance of the life-jacket decision from 1910. The statement in the description regarding the general purpose for using the invention (to provide a life jacket with sufficient lift in the water) is, in my mind, too imprecise to impose any liability on the seller, even if the seller of the patent realized that this was an important aspect for the buyer. The decisive question is, I believe, whether the buyer was led to believe, through the patent specification, that the seller had some previous experience that supported his technical claim.

A random but rather typical example of how the general purpose of an invention is indicated can be seen in the European patent (EP) 1110808 filed on December 23, 1999. The title is “An inflatable restraint device for the luggage space of a motor vehicle”. The invention is basically an airbag system designed to prevent luggage from hurting passengers in the event of a collision. It carries the following statements pertaining to the purpose of the invention:

The present invention relates to a restraint device for the luggage space of a motor vehicle arranged in an area behind the backrest of a rear seat. In the case of a frontal impact, any items contained in the luggage space can hit the back of the said rear seat or seats. In the prior art, car seats immediately in front of the luggage space need to be made sufficiently robust and strong to be deformed only to a limited extent as a result of an impact from luggage or other items carried in the luggage space. The manufacture of seats to a good standard from this point of view is therefore expensive. One object of the present invention is to provide a restraint device which is able to alleviate the aforesaid problems which occur in the event of a vehicle being in a substantially frontal collision. This and other objects are achieved according to the invention by providing a restraint device having the characteristics claimed in the appended Claim 1. Further characteristics and advantages of the invention will become apparent from the detailed description which follows ...

What justified assumptions could a prospective licensee draw from the above statement in the specification? Could a contract be avoided if e.g. the airbags do not allow a car manufacturer to reduce the strength and robustness of the seats in front of the luggage space? This appears to be the main purpose of the invention, although it is said that there are also other objects achieved by the invention. However, I doubt that the “background” or default rule, which would indicate the terms of a license agreement in the event that the parties did not otherwise agree, could provide that. The statements in the description are known to be one-sided and made with the particular purpose of obtaining a patent at an early stage of an on-going research process. They are often composed without any practical experience of the invention and therefore without detailed information on behalf of the inventor. There must probably be some specific details in the statements for them to be considered warranted by the licensor. Only if the above patent

would (which it does not) include an account of collision impact tests or similar test results, would a licensee be justified in canceling the contract if the statements were fictitious or colorably incorrect. The purpose of the invention is probably governed by the *caveat emptor* doctrine.

Accounts of experiments with the invention are different in principle from a statement of the general purpose for the invention, in that the examples purport to refer to actual practical tests. The examples in the patent can therefore have the same function as when a licensor during the negotiation presents test results to the licensee. It is reasonable to hold the licensor to these and entitle the licensee relief if they prove to be inaccurate. Precise information of this sort is often also explicitly guaranteed in the license agreement. But statements about actual experiences with the invention made during the negotiations are probably binding even without an explicit warranty, unless of course the licensor expressly excludes liability or it is shown that the test results did not actually influence the licensee.<sup>17</sup>

There are two Danish cases that to some extent buttress the proposition that there is a legal distinction to be made between statements that indicate previous practical experience with the invention and statements that only suggest possible uses for the invention. The former are probably warranted, while the latter, without some practical support, probably belongs to the category of unsubstantiated general praise. In one case from 1934, relating to a patent on a fluorescent paint, the Court held that a representative for the seller had indicated to the buyer that the paint would glow in the dark for 8 hours, while in reality it would only glow for 20 minutes.<sup>18</sup> The seller thus misled the buyer, which allowed the buyer to avoid the contract and have his money returned. The claim to 8 hours of glow indicated practical experiences on behalf of the licensor. In a second Danish case, a representation by the licensor of the current phase of technical development controlled the outcome of the case.<sup>19</sup> The Court ruled that the licensee was misled by the licensor regarding the degree of completion of the technology when the licensor led the licensee to believe that serial production could begin within a near future. The licensee was therefore allowed to avoid the agreement after the licensor's representative had failed for four months to put the invention (a coating similar to enamel which was to be applied to timber) into practice at the licensee's premises. Obviously, these cases turned on explicit oral guarantees, but perhaps equally important, the guarantees were in these two cases of a nature that indicated previous practical experience with the invention on behalf of the licensor. What mattered to the courts was not solely a discrepancy between statements about the invention and the true qualities of the invention, but that the statements were precise accounts of what appeared to be tested and were not general in character. My conclusion from this is that precise technical data, provided by the licensor in the patent or during the negotiations, form exceptions to the *caveat emptor* doctrine that in most other aspects controls patent licenses. The importance of a policy in which detailed test results are seen

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<sup>17</sup> See Plessner, *supra* note 3 at 207; Koktvedgaard, *supra* note 3 at 580; Hultmark, *supra* note 3 at 694; Koktvedgaard, Levin, *supra* note 3 at 407.

<sup>18</sup> Ugeskrift for Retsvæsen 1934 p. 672.

<sup>19</sup> Ugeskrift for Retsvæsen, 1937 p. 683.

as warranted should not be underestimated. In a French survey from 1997 it was noted that in 78,6% of the technology licensing agreements the licensor provided the licensee with technical test data and development data.<sup>20</sup>

The available relief in case of breach of a technical warranty seems to be that the licensee can avoid the license and have a payment already made reimbursed. Damages for losses that the licensee incurred while trying to use the invention appear, however, to be difficult to attain. There seems to exist profound doubt in courts about imposing full contractual liability on licensors for breach of a warranty of technical quality. Courts have tended to compromise on the remedy by refusing to grant consequential damages for breach of implied warranties. For a licensee to be able to collect full damages for breach of a specific technical warranty, it would probably require explicit provisions in the license agreement stipulating such a right to damages.<sup>21</sup>

## Summary and Concluding Remarks

With the exception of the Danish 1976-case concerning the wire-lock, Scandinavian court cases regarding technically flawed but licensed inventions seem to have come out in favor of the buyer/licensee, in the respect that the contract has been possible to avoid. Even so, it is important to stress that it is very difficult for anyone to successfully claim that the licensed invention was not as good as he expected. A comparison between the objective facts mentioned in the patent specification and the actual quality of the invention, has not in itself sufficed in any of the cases to allow a buyer/licensee to avoid the contract. Subjective factors relating to the parties' technical knowledge and also to the awareness of the other party's technical purpose, appear to be inescapable considerations. To view the patent documents as only one circumstance in the totality of the license negotiation, accords well with Scandinavian legal tradition, which favors an approach to contract interpretation in which all factors in the negotiation are taken into account and balanced against each other.<sup>22</sup> Scandinavian contract law does not quite put the same weight on a narrow interpretation of words as common law does, but looks more at the spirit of the agreement and searches for harmony and compromise in it. No one circumstance is usually singled out in the legal reasoning, instead there is a balancing of all factors pertaining to the negotiation. In this exercise, statements in a patent

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<sup>20</sup> The proportion for other transfers to the licensee reached 76% for technical support, 67,4% for prototypes and physical resources, the same percentage for plans and manuals, 65% for employee training, 60,8% for commercial data, and 56,5% for employee delegation in the licensee's facilities. In the study questionnaires were mailed to 450 leading French firms. See Bessy, C., Brousseau, E., *Technology Licensing Contracts – Features and Diversity*, *International Review of Law and Economics*, 18:451 (461) 1998.

<sup>21</sup> The Swedish Supreme Court held in case NJA 1992 s 403 that the right to damages should be spelled out explicitly in a retail and distribution contract for a patented product. If it has not, then the right to cancel the contract, a remedy that was explicitly mentioned in the contract in this case, was the only available.

<sup>22</sup> Sandgren, C., *Vad gör juristen? Och hur? – del II*, *Juridisk Tidskrift* 1999/2000 p. 873.

specification carry some weight but are not solely decisive or sufficient for determining the outcome. Subjective factors related to the parties and their perceptions during the negotiations are equally important.

An essential subjective aspect in Scandinavian law seems to be whether the licensor during the negotiations knowingly conveyed incorrect assumptions about the invention to the licensee.<sup>23</sup> For this to be the case the licensor must have understood that the information was vital for the licensee, but the licensee should also have had reasons for relying on the licensor in this particular respect. In e.g. the case of *Oswald Tvetmark v. Brynjulv Abrahamsen* it was concluded that the licensor should have understood that the strength of the material was vital for the licensee. Moreover, the licensee had reasons to rely on the figures in the patent specification considering their detailed nature, the licensor's background as the inventor and as a trained chemist. In the 1976-wirelock-case, on the other hand, the licensee's suit failed because the particular conditions on the German market were not known by the licensor and furthermore the licensee was not justified in relying on the licensor's knowledge of the market conditions.

To summarize, the starting point for patent licenses is *caveat emptor*. The exceptions to it made in case law are based either on explicit statements by the licensor during the negotiations or on situations where there is a vital condition for the licensee, which was known to the licensor and on which the licensee was justified in relying on the expertise of the licensor. It has in this article been suggested that this default rule entails in particular that a licensor has a duty to inform a licensee of problems with practicing the invention according to important and precise details that have been furnished in the patent description. If the licensor is aware that they are misleading he bears a duty to inform the licensee. It is therefore advisable that a licensor, who is uncertain about the reliability of the patent description, explicitly excludes any liability for any technical qualities of the invention. It is, however, much more questionable whether general statements about advantages with the invention in relation to the prior art, fulfill the legal requirements and therefore should be seen as implicit warranties. Only precise statements seem to fulfill the requirement developed in case law that the licensee has to have been justified in relying on the expertise of the licensor. It must be remembered that the grant by the Patent Office says nothing certain about the qualities of the invention and that unspecific praise of the invention is not creating any liability.

In this Scandinavian legal environment, where the contracting parties subjective perceptions are taken into account, and not only the patent specification and the actual technical qualities of the invention are compared, it may be that licensors very often are absolved of any liability. A number of circumstances in a negotiation should probably preclude a prospective licensee from relying on the licensor. Licensor's liability may e.g. be excluded if the licensee was aware of the fact that the invention was still in a stage of development. The licensee's knowledge of an on-going test program may exclude licensor liability for technical utility.<sup>24</sup> Another situation, in which the

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<sup>23</sup> Koktvedgaard, Levin, *supra* note 3 at 407.

<sup>24</sup> Cf. German law in this respect „Außerdem wird zu berücksichtigen sein, daß die Haftung des Lizenzgebers für anfängliches Unvermögen ... nur eintritt, wenn die Parteien nichts

licensee is not always justified in relying on the licensor, may be the case where the licensee is generally more technically knowledgeable than the licensor and therefore better able to assess the invention. The Norwegian Supreme Court in *Oswald Tvetmark v. Brynjulv Abrahamsen* addressed the technical competence of the two parties, although it does not seem to have controlled the outcome of that case. However, it may be important in other cases. A technical claim of an unusual or extraordinary nature should also inspire the licensee to a particularly critical examination. If a claim is contrary to common experience or perhaps even a severe tax upon credulity, so that a person of even ordinary technical skills would have been led to make a most exhaustive test before going into the venture, then the licensee is certainly not justified in relying on the claim.

At this point, I will broaden the scope of this article a little and briefly compare technical warranties to some other issues pertaining to patent licenses. Warranties in patent licenses often cover the licensor's title in the invention, but even without an explicit warranty with respect to proprietary issues, remedies are probably available to the licensee. Compensation is due if e.g. the patent had already been licensed exclusively to someone else, if an employee licenses an invention that rightfully belongs to his employer, or if a licensee unlawfully sublicenses an invention. The same would hold true if the patent is charged with a lien that does not permit the grant of licenses or if the patent has been invalidated already when the license is signed (but if the patent is invalidated during the term of the license agreement, the licensee probably cannot get any compensation in the absence of an explicit warranty).<sup>25</sup>

There are, on the other hand, no tacit warranties that licensed inventions have any commercial utility or are fit for serial production. Neither the presentation of historical sales figures to the licensee during the negotiation, nor the stipulation of a minimum royalty in the contract, can be interpreted as implicit warranties by the licensor that the invention has some commercial utility. The licensee is solely responsible for the profitability and marketability of the invention. Commercial utility is dependent on too many factors over which the licensor has no control, for a liability to exist, in the absence of any explicit agreement. The factors determining the commercial outcome include manufacturing costs, market acceptance of the invention and also subsequent occurrences of superior technology which might make the invention outdated. These circumstances lie beyond the control of the licensor.

To limit the set of tacit warranties to specific technical assertions made by the licensor in the patent specification or during the negotiation, and in addition proprietary issues, will distinguish patent licensing from the sale of corporal

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anderes vereinbart haben. Der Wille der Parteien, von der gesetzlichen Risikoverteilung abzuweichen, kann sich auch aus den besonderen Umständen des Falles ergeben. So könnte zum Beispiel eine Haftung des Lizenzgebers für die technische Brauchbarkeit ganz oder teilweise ausgeschlossen sein, wenn die Lizenznehmerin bei Abschluß des Vertrages wußte, daß das Verfahren noch nicht ausreichend erprobt war und deshalb weitere Versuche erforderlich sein würden, um Gewißheit über die Eignung des Verfahrens für den bestimmten vertraglich vorgesehenen Zweck zu erlangen.“ *Mineral Wolle*, BGH 28 06 1979, GRUR 1979, 768 (771).

<sup>25</sup> Koktvedgaard, *supra* note 3 at 580; Sandgren, *supra* note 3 at 223f; Koktvedgaard, Levin, *supra* note 3 at 388.

goods. The seller of a corporal good usually takes some general responsibility for the quality of the goods. The default rule in sale of goods is often that the goods do not conform to the contract unless they are of merchantable quality or fit for a particular purpose expressly or implicitly made known to the seller at the time of the contract. In patent transactions that is hardly the case with respect to technical qualities of the invention. Even if the licensee's purpose is known to the licensor there is no general implicit warranty that it will be achieved. A technical warranty of such a nature could have far-reaching consequences for the licensor. Patent licenses are, I believe, positioned further in the direction of a *caveat emptor* policy. Without any explicit warranty the licensee will, with a few exceptions, have to pay the agreed price even if the invention does not satisfy the licensee's technical intentions.

To require a thorough technical evaluation by the licensee prior to the signing of the contract is hardly too much to ask. Private individuals rarely if ever license patents and businessmen are unlikely to license a patent without a prior careful investigation of it. Patent licenses are not mass-markets, with the possible exception of some patented software and perhaps some biotechnology research tools such as RPC. However, if mass-markets were to develop for patent licenses it may become necessary to extend the use of implicit warranties to e.g. merchantability of the invention or fitness for a purpose made known to the licensor, in order to better economize on transaction costs. But so far and for the foreseeable future a patent license will remain a very different kind of legal instrument than a sales contract. The amount of resources that go into the individual negotiation of a patent license seems to lead to a legal preference for the *caveat emptor* doctrine. A further reason for the *caveat emptor* policy in patent licenses is that the majority of all inventions are never applied industrially or commercially. This sets patents apart from corporal goods. The risky nature of new technology in general entails that few licensors are able to warrant anything in this respect. Licensors also shun liability because the future for the invention depends considerably on the licensee's individual capacity and requirements, more so perhaps than the use of the average corporal good depends on its buyer.

With all these arguments in favor of no or only very limited implicit technical warranties, one can rightfully ask if they are justified at all in the context of patent licenses. Could it not be expected of prospective licensees to verify the tests and technical figures that the licensor has provided in the patent specification? The most important argument marshalling against this view may be that a default rule in this context should primarily be designed for unsophisticated parties. It is important that a default rule reflects the conventional or common sense in the community that depends on the rule. This entails that the default rule concerning technical qualities should especially reflect the tacit assumptions of inexperienced parties. It will for them underscore the important social functions of consent in agreements to transfer of technology. It is telling that all the cases that have been discussed in this article concern more or less unsophisticated parties. They probably tend to put special trust in statements made in the granted patent. Background rules tied to their perceptions provide a legal base that ameliorates problems from lack of legal knowledge and legal precautions, by supplying common sense outcomes.

Therefore, chiefly to protect unsophisticated parties, I believe that precise technical statements, test results etc., in patent documents are to be considered as warranted. The more sophisticated parties will resolve any questions about the technical qualities of the inventions during the negotiations and through explicit agreements.

However, even unsophisticated parties to patent licenses probably understand that general statements in a patent are often based on no more than wishful thinking. Furthermore, the patent system may at times induce persons to submit questionable patent applications and thereafter to try to “extort” money from others with only minimal self-exposure to risk. To alleviate the worst forms of this practice non-negligible costs should probably be linked to any attempts to extract license fees from patents that have been obtained fraudulently. I believe that someone who has knowingly made incorrect claims about the technical qualities of an invention should be held liable for the costs that a later licensee suffers while trying to work the invention according to the incorrect description. It is reasonable to place the full commercial liability for all damages incurred, on the licensor in cases of fraudulently obtained and later licensed patents.