

# PATENTS: THE ARBITRABILITY OF CONNECTED COMMERCIAL OBLIGATIONS AND CLAIMS

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## ABSTRACT

*Specific issues of arbitrability concerning patents forming the subject-matter of an underlying commercial contract are yet to be fully explored by the Indian Judiciary. While issues which directly claim invalidity of patents are not arbitrable, contentions arising out of breach of contractual obligations concerning the underlying patent demand a different approach. Such contentions may include damages for contractual breaches on the premise of infringement, reverse engineering or replication of the patent, licensing of patents or their validity. The article analyses the jurisprudence around arbitrability of patents and connected commercial claims in other jurisdictions and provides a holistic comparative overview.*

## 1. INTRODUCTION

Party autonomy is integral to arbitration as a dispute resolution mechanism. The jurisdiction of the arbitrator follows from the consent of the parties to refer disputes to it. As a result, the scope of the arbitrator's jurisdiction is strictly limited by the agreement between the parties. However, in arbitrations involving patents, apart from the nature of the agreement between the parties, there are other considerations that are intertwined which, at times, may cause ambiguity on how to proceed in an arbitration involving patents.

A patent right, like all intellectual property rights, is a right against the world i.e. right in *rem*. The nature of patent rights and whether they are arbitrable have often come into conflict. The Indian jurisprudence on

arbitrability of patents is at a nascent stage. However, progress has been made to determine arbitrability of connected commercial claims concerning underlying intellectual property rights in general.

Gary Born advocated that “*In principle, there is no reason that issues of patent...validity cannot be resolved by arbitration – but only insofar as the parties to the arbitration are concerned. An arbitral tribunal obviously cannot affect registrations or invalidate a patent generally, thereby affecting the rights of the public or third parties. There is no reason, however, that an arbitral tribunal cannot apply rules of intellectual property law in other contexts to decide claims between contracting parties that a particular intellectual property right is invalid or does not exist.*”<sup>1</sup>

Against this background, the authors have attempted to provide a brief snapshot of the manner in which Indian courts and international jurisprudence have dealt with the conflicting character of arbitration and patent rights.

## 2. DISPUTES THAT MAY ARISE

The kind of disputes that can arise from patent rights are wide-ranging. For instance, a dispute may arise from a licence agreement between parties to use or exploit or improve the technology which is protected by a patent. Under licence agreements, some of the most common disputes relate to whether royalties are payable, the extent of the licensed rights, the ownership of the improved patented technology, circumstances under which a licence can be terminated, damages for breach of the licence agreement, replication of the patent and reverse engineering.<sup>2</sup> In an acquisition agreement, wherein the seller transfers intellectual property to the buyer, disputes may arise out of the seller warranties provided against the transfer.<sup>3</sup> In the case of employment agreements, disputes may arise to determine the ownership of the patent for a technology developed in the course of employment with the company.<sup>4</sup>

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1. Gary Born, *International Commercial Arbitration* (2020) <International Commercial Arbitration - Gary B. Born - Google Books> accessed 28 December 2023.

2. ‘Final Report on Intellectual Property Disputes and Arbitration’ (ICC International Court of Arbitration Bulletin vol 09 no 1, May 1998) <ICC Digital Library (iccwbo.org)> accessed 28 December 2023.

3. *ibid.*

4. *ibid.*

Considering the complexity in the disputes involving patents which is not only limited to the underlying contract between two parties but can also extend to the interpretation of technical specifications and other statutory rights, parties prefer to file these disputes in court to avoid jurisdictional challenges. The Indian arbitration jurisprudence has not been fully explored as against the several scenarios in which disputes may arise out of connected commercial obligations and claims concerning the underlying patent. A brief snapshot of the Indian position is produced below.

### 3. INDIAN POSITION

The Supreme Court of India in *Booz Allen and Hamilton Inc v SBI Home Finance Ltd* held that all disputes relating to rights in *rem* are required to be adjudicated by courts and public tribunals. However, disputes relating to subordinate rights in *personam* arising from rights in *rem* are to be considered as arbitrable (“**Booz Allen Principle**”).<sup>5</sup> This principle becomes very important to understand the extent of arbitrability of disputes especially considering the complexity in patent related disputes.

Despite the Booz Allen Principle, the Bombay High Court in *Steel Authority of India Ltd v SKS Ispat and Power Ltd*<sup>6</sup> (“**Steel Authority of India case**”) took a rigid approach and held that an infringement and passing off suit was not amenable to arbitration as it was related to a matter in *rem*. This was a case where the Steel Authority of India Limited (“**SAIL**”) sought an injunction for infringement of its trademark. However, the court concluded that such a claim was not under the contract between the parties containing the arbitration agreement.

Subsequently, the Bombay High Court in *EuroKids International (P) Ltd v Bhaskar Vidhyapeeth Shikshan Sanstha*<sup>7</sup> and *Eros International Media Ltd v Telemax Links India (P) Ltd*<sup>8</sup> took a more liberal approach in determining the arbitrability of disputes in relation to intellectual property rights.

In *EuroKids International (P) Ltd v Bhaskar Vidhyapeeth Shikshan Sanstha*<sup>9</sup> an agreement to license the proprietary marks of the Petitioner

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5. *Booz Allen and Hamilton Inc v SBI Home Finance Ltd* (2011) 5 SCC 532.

6. *Steel Authority of India Ltd v SKS Ispat and Power Ltd* 2014 SCC OnLine Bom 4875.

7. *EuroKids International (P) Ltd v Bhaskar Vidhyapeeth Shikshan Sanstha* 2015 SCC OnLine Bom 3492.

8. *Eros International Media Ltd v Telemax Links India (P) Ltd* 2016 SCC OnLine Bom 2179.

9. *EuroKids International (P) Ltd* (n 7).

for an initial period of 3 (three) years was entered into with the respondent. A dispute arose between the Petitioner and Respondent as the Petitioner alleged that the Respondent pre-maturely started advertising (without waiting for confirmation from the petitioner) and also failed to pay the royalty fee. A petition under Section 9 of the Arbitration and Conciliation Act, 1996 seeking an interim injunction against the Respondent was filed and the Respondent as a defence contended that the Arbitration and Conciliation Act, 1996 cannot be invoked as the dispute involves infringement of intellectual property rights, which is a right in *rem*. The court held that the dispute did not concern the ownership of the trademark or of the copyrighted material. Hence, it was not a dispute involving a right in *rem*.

Similarly, in *Eros International Media Ltd v Telex Links India (P) Ltd*,<sup>10</sup> which was a dispute where Eros International Media Limited (“**Eros**”) had filed a suit for infringement of copyrighted material against Telex India Private Limited (“**Telex**”) and others, the question arose whether the infringement of copyrighted material against Telex could be considered as a subordinate right in *personam* arising from a right in *rem*.

The Bombay High Court elucidated that a dispute opposing an application filed for registration of trademark would be an action in *rem* and hence, non-arbitrable because such an application would result in the granting or non-granting of the registration, which affects the world at large. On the contrary, an infringement or passing off action binds only the parties to it and is hence, arbitrable. The Bombay High Court provided an example where ‘A’ may succeed in a suit of infringement and passing off by ‘B’; however, this does not necessarily mean that ‘A’ will succeed in a similar action against ‘C’. This would be an action in *personam*. The right which would be considered in *rem* is the registrant’s entitlement to bring that action, since such entitlement is a result of acquiring copyright. The Bombay High Court distinguished the Steel Authority of India case on the ground that the dispute in that case was not arising out of the contract between the parties.

The decision of the Supreme Court in *Vidya Drolia v Durga Trading Corpn*<sup>11</sup> (“**Vidya Drolia judgment**”) now holds the field in determining arbitrability of disputes. In brief, the Supreme Court discussed the question

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10. *Eros International Media Ltd* (n 8).

11. *Vidya Drolia v Durga Trading Corpn* (2021) 2 SCC 1.

of arbitrability in depth and laid down a four-fold test<sup>12</sup> for determining when the subject-matter of a dispute in an arbitration agreement is not arbitrable:

- (i) *when cause of action and subject-matter of the dispute relates to actions in rem, that do not pertain to subordinate rights in personam that arise from rights in rem;*
- (ii) *when cause of action and subject-matter of the dispute affects third party rights; have erga omnes effect; require centralized adjudication, and mutual adjudication would not be appropriate and enforceable;*
- (iii) *when cause of action and subject-matter of the dispute relates to inalienable sovereign and public interest functions of the State and hence mutual adjudication would be unenforceable; and*
- (iv) *when the subject-matter of the dispute is expressly or by necessary implication non-arbitrable as per mandatory statute(s).*

The Supreme Court held that actions in *rem* give rise to judgments in *rem* which determine the status of a person or thing against all persons whether parties, privies or strangers to the proceeding. By contrast, an action in *personam* gives rise to a judgment in *personam* which merely determines the rights of the litigants *inter se*. While an action in *personam* may be concerned with a right in *rem*, it does not give rise to a judgment that has the effect of binding the world. In other words, it does not have an *erga omnes* effect which would require centralised adjudication. Decisions and adjudicatory functions of the State that have a public interest element are non-arbitrable as the State alone has the exclusive right and duty to perform such functions.

Applying the four-fold test laid down by the *Vidya Drolia* judgment brings some assurance insofar as non-arbitrability of disputes is concerned. Therefore, going by the Booz Allen Principle and the law laid down in the *Vidya Drolia* judgment, an action for the issue/grant of patents or for determining the validity of a patent will be non-arbitrable. However, the Indian jurisprudence, insofar as patent disputes are concerned, does not have any conclusive precedent where claims are made by a party in an indirect manner as a matter of claim/counter claim which would decide the validity of a patent and consequently be entitled to relief (monetary or

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12. *Vidya Drolia* paras 76.1 to 76.4.

injunctive reliefs). There may be instances where such an indirect claim will be put to the test of trial despite such claim not being arbitrable. There is a lack of defined framework that an arbitral tribunal must follow when such indirect claims are made. It is mandatory that when an application seeking to question the jurisdiction of the arbitral tribunal is filed by a party, the same leads to a conclusive finding whether *prima facie*, the dispute or such indirect relief claimed is arbitrable or not.

#### 4. INTERNATIONAL POSITION

##### A. Hong Kong & Singapore

In Singapore, under the Singapore Arbitration Act, 2001 and the International Arbitration Act, 1994 (collectively, “**Singapore Arbitration Laws**”), a dispute over the enforceability, infringement, subsistence, validity, ownership, scope, duration or any other aspect of an intellectual property right; a dispute over a transaction in respect of an intellectual property right; and a dispute over any compensation payable for an intellectual property right are arbitrable (“**IPR Dispute**”).<sup>13</sup> An IPR Dispute is arbitrable whether it forms the main issue or the incidental issue in the arbitration.<sup>14</sup> The Singapore Arbitration Laws also clarify specifically that validity of a patent may be put in issue in arbitral proceedings.<sup>15</sup> Awards under an IPR Dispute cannot be set aside for being incapable of arbitration and/or for being contrary to public policy.<sup>16</sup> In line with the consensual nature of arbitration, such awards are only binding between the parties to the arbitration and on any person claiming through or under them.

The arbitration law of Hong Kong is largely similar to the Singapore Arbitration Laws.<sup>17</sup>

##### B. Australia

In the case of *Larkden Pty Ltd v Lloyd Energy Systems Pty Ltd*,<sup>18</sup> the arbitrability of intellectual property disputes and connected commercial obligations was contested. In this case, Larkden Pty Limited (“**Larkden**”) and Lloyd Energy System Pty Limited (“**Lloyd**”) had entered into a licence

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13. Singapore Arbitration Act 2001, s 52A; International Arbitration Act 1994, s 26A.

14. Singapore Arbitration Act 2001, s 52B; International Arbitration Act 1994, s 26B.

15. Singapore Arbitration Act 2001, s 52F; International Arbitration Act 1994, s 26G.

16. Singapore Arbitration Act 2001, s 52D; International Arbitration Act 1994, s 26E.

17. Arbitration Ordinance, pt 11A.

18. *Larkden Pty Limited v Lloyd Energy Systems Pty Limited* [2011] NSWSC 268.

agreement whereunder Larkden granted a licence to Lloyd to *inter alia* use, commercialise, exploit and improve certain technologies. As per Clause 5.4 of the licence agreement, Larkden was to own any improvements or modifications to the technologies developed by Lloyd. Patent applications were filed by Solfast Pty Ltd. (“**Solfast**”), a wholly owned subsidiary of Lloyd and Areva Inc (formerly Ausra Inc) (“**Ausra**”) each covering inventions which Larkden alleged were modifications of, or improvements to, the technologies. Lloyd argued that Larkden did not have any right, title or interest in the inventions or the patent applications.

Consequently, Lloyd commenced an arbitration against Larkden. Larkden disputed the jurisdiction of the arbitrator on the ground of arbitrability. Larkden argued that *firstly*, Lloyd’s notice of dispute raised issues for determination by the arbitrator which were exclusively within the province of a statutory body and *secondly*, the arbitration would affect Solfast and Ausra, who were not parties to the arbitration.

Lloyd argued that the arbitrator merely has to determine whether Clause 5.4 of the licence agreement is engaged. The relief claimed is not “*in rem*”.

The Court decided that the powers to grant a patent, to make a declaration of eligibility and to decide the case where the grant of a standard patent is opposed, are powers conferred by the provisions of the Patents Act on a statutory body. While these statutory powers cannot, by private arrangement, be conferred by parties on an arbitrator, there is no impediment to the parties investing in the arbitrator power to resolve a dispute as between themselves as to their rights in and entitlements to a patent application, or for that matter an invention. The Court noted that neither the notice of dispute nor the pleadings in the arbitration call for the arbitrator to make any declaration as to eligibility or to grant a patent. The arbitrator has only been called upon to resolve the dispute which has arisen between Larkden and Lloyd as to their respective rights and obligations under Clause 5.4 of the licence agreement. The Court asserted that any arbitral determination regarding whether the patent applications were ‘improvements or modifications’ to the technologies would not prevent Solfast or Ausra from pursuing their patent applications or prevent Larkden from pursuing its applications under Section 36 of the Patents Act for determining eligibility of Ausra.

### C. USA

The Patent Act of the United States of America<sup>19</sup> provides for voluntary arbitration of patent related disputes. The Act provides that a contract involving a patent or any right under a patent may contain a provision requiring arbitration of any dispute relating to patent validity or infringement arising under the contract. In the absence of such a provision, the parties to an existing patent validity or infringement dispute may agree in writing to settle such dispute by arbitration. The Act clarifies that any award issued by the arbitrator shall be final and binding between the parties to the arbitration only. The Act requires that where an award is issued by an arbitrator, the patentee, licensee, or his assignee shall give notice of the award in writing to the director of the United States Patent and Trademark Office (“**Director**”). The Director shall, upon receipt of the notice, enter the same in the record of the prosecution of such patent. The award shall be unenforceable until the notice is received by the Director.

### D. United Kingdom

The United Kingdom’s Patent Act, 1977 states that arbitration is available only in very limited cases with specific sanction of the courts. The validity of patents, however, is an arbitrable issue, but binds only the parties privy to the arbitration.<sup>20</sup>

### E. Japan<sup>21</sup>

Disputes concerning infringement of patent rights are considered arbitrable. However, disputes that decide the validity or invalidity of the patent right have commonly been contested and decided as non-arbitrable.

## 5. SUGGESTIONS AND CONCLUSION

A holistic analysis of the international position reveals that arbitration is being given an impetus and many disputes arising out of an underlying patent, including disputes where the validity of the underlying patent

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19. Patent Act 2006, s 294.

20. Kenneth R Adamo, ‘*Overview of International Arbitration in the Intellectual Property Context*’ 2 *Global Bus L Rev* 7 (2011) <Overview of International Arbitration in the Intellectual Property Context (csuohio.edu)> accessed 29 December 2023.

21. Matthew R Reed, Ava R Shelby, Hiroyuki Tezuka and Anne-Marie Doernenburg, Wilson Sonsini Goodrich & Rosati and Nishimura & Asahi, ‘Arbitrability of IP Disputes’ (21 December 2022) <Arbitrability of IP Disputes - Global Arbitration Review> accessed 29 December 2023.



is in question (directly or indirectly) are being accepted as arbitrable. There is fair reason for such impetus being given to arbitration given the commercial nature of the disputes, speed and efficiency of the mechanism, confidentiality of the proceeding, forum neutrality and expert decision makers.<sup>22</sup>

However, such impetus will lead to conflicting decisions as the award will be binding only between the parties to the arbitration and may further cause a disruption insofar as the ownership of an invention is concerned. Even indirect claims, where the arbitral tribunal may be deciding damages for unauthorized use of the intellectual property will not be conclusive in nature since claims will be dependent on the validity of the patent or a decision may have to be rendered on the ownership of the patent. This is inherently an *in rem* action, though not directly so since such relief of declaration may not be explicitly claimed by a party to the arbitration. The settled principle of law – what cannot be done directly, cannot be done indirectly either, must be kept in mind insofar as India as an arbitration jurisdiction is concerned.

Therefore, it is absolutely necessary that an arbitral tribunal deciding claims in relation to patents, keep the following guidelines (which are mere suggestions) in mind. An arbitral tribunal in India must:

1. Decide whether the claims fall within its jurisdiction or in any manner relate to a decision which would decide on the validity of the patent, either *suo motu* or if an application challenging the arbitral tribunal's jurisdiction is filed by a party challenging such claims being made.
2. Such disputes touching upon validity of patents are to be held as non-arbitrable at the very threshold. The position of law in *Vidya Drolia* judgment is clear.
3. The arbitral tribunal must put a party making indirect claims to the test of *prima facie* establishing that such claims do not have an element of an *in rem* action. If a party making a claim fails to establish such *prima facie* case, such claims should be held as being beyond its jurisdiction.
4. The arbitral tribunal must not defer the decision in such indirect claims, as far as possible, to be dependent on trial/evidence, where

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22. WIPO, 'Why Arbitration in Intellectual Property' <Why Arbitration in Intellectual Property? (wipo.int)>.

a party fails to establish *prima facie* that such claims do not have an element of an *in rem* action. Delay can be counter-productive as, should a decision be reached after conclusion of evidence/trial that the disputes are not arbitrable, there could be a risk of limitation having expired to make necessary claims before a court.

The authors would like to leave you with a simple example of where a tribunal has been set up under the Singapore Arbitration Laws and a party's patent has been held invalid in an arbitration and consequent damages have been awarded to the claimant. This finding will be binding only between the parties to the arbitration. To conclusively invalidate the party's patent *in rem*, a fresh suit may have to be filed before a Singapore court or the prescribed authority (based on Singapore law). At that stage, the limitation period for filing of a suit for invalidation of patent may be questioned. Another layer of complexity would arise if the decision of such court/authority is that the patent is a valid patent. Would the parties then have to return to the tribunal to review its finding based on the court/authority's decision which is of a wider ambit?

The Supreme Court in the *Vidya Drolia* judgment asserted that “*various countries have already allowed inter parties arbitration with respect to in rem rights concerning intellectual property through a statutory framework. It is worthwhile to study the feasibility of the same, if we want to provide impetus to arbitration.*”

While the authors are in agreement that an arbitration friendly approach must be adopted when determining arbitrability of disputes, it is essential that this approach is applied keeping in mind the private nature of arbitration, and the logistical and practical hurdles in using arbitration to determine disputes that touch upon the validity of an underlying patent. It is best for any *in rem* actions to remain with courts.