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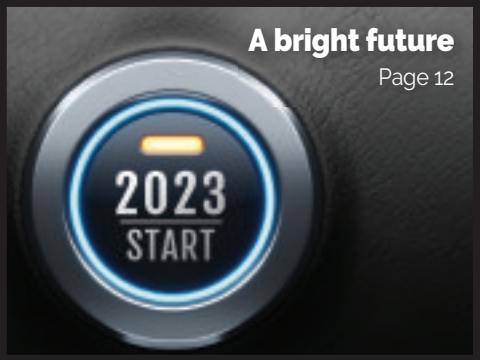
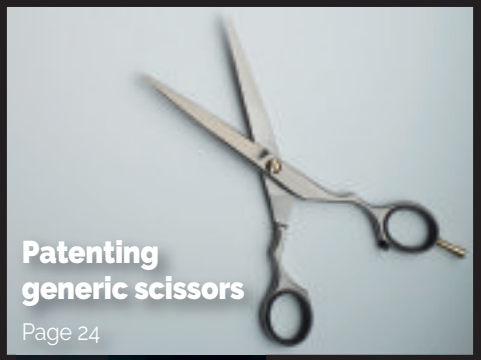
EU pharmaceutical reform

Will this reform put innovation and investment at risk?

A pivotal year of change ahead with increasing administrative complexities





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EU reforms in the pharmaceutical sector - a pivotal year of change ahead

Baker McKenzie's experts Fiona Carlin, Brussels, Hiroshi Sheraton, Tanvi Shah & Shira Sasson, London, lay out the momentous changes set to be implemented in the EU's Pharmaceutical Strategy reform which risk the scaling back of established IP and regulatory exclusivities while increasing administrative complexities.

The life sciences sector has long felt the tension between the desire to incentivize and reward medical innovations while enabling equitable access to medicines and containing national healthcare spending. Intellectual property and regulatory exclusivities reward innovation and allow the significant R&D investments required to develop new therapies to be recouped. However, those same rights inhibit the entry of cheaper, generic medicines and do not necessarily promote widespread affordable access to medicines. Forthcoming legislative changes at the EU level look set to alter that delicate balance.

At the beginning of March 2023, the European Commission is expected to publish reform proposals that are the culmination of its EU Pharmaceutical Strategy for Europe[1] (the "**Pharma Strategy**") and IP Action Plan[2], both of which launched in November 2020. The proposals are expected to include a significant realignment of regulatory exclusivities alongside the introduction of an EU-wide compulsory licensing regime. They should be seen in the context of other developments to encourage early generic market entry, including increased scrutiny by competition authorities of alleged abuses of the IP system, most recently in relation to the filing of divisional patents and patent litigation.

> **EU law and policy should encourage the development of those new medicines rather than stem their flow.**

Working documents outlining the Commission's initial thinking on the proposals were leaked in the summer of 2022 after they had been reportedly rejected by the Commission's own Regulatory Scrutiny Board (an internal body charged with quality control over impact assessments and evaluations at early stages of the EU legislative process). The leaked documents proposed to shift the balance away from rewarding innovation as such and towards a system which conditions those rewards on widespread availability of medicines and on addressing unmet patient needs. Having since gone back to the proverbial drawing board, the question is to what extent the Commission will deviate from its original intentions.

There is a lot at stake, not least in terms of Europe's relative global competitiveness in pharmaceutical innovation.

The current EU incentives regime

On top of the patent system, pharmaceutical innovation is incentivized through the availability of Supplementary Protection Certificates ("**SPCs**"), regulatory exclusivities, and orphan and pediatric extensions.

SPCs are a *sui generis* IP right that extend the term of a patent by up to five years in order to

compensate for the loss of effective patent protection caused by the lengthy testing and regulatory procedures before a new medicine receives a marketing authorization.

Under the current regulatory exclusivity regime, manufacturers of new medicines benefit from:

- Eight years of regulatory data protection (preventing generic/biosimilar applicants from referencing innovator data in an application for marketing authorization);
- Two further years of market protection (prohibiting the placing on the market of the referencing generic/biosimilar); and
- One further year of market protection if an additional indication that shows significant clinical benefit in comparison with existing therapies is authorized during the initial eight-year period.

In addition, the orphan drug regulatory framework, among other incentives, grants a 10-year market exclusivity period (preventing grant of a marketing authorization for similar medicines for the same indication) for each approved therapeutic indication that has been granted orphan designation. Orphan designation is available for any medicine (1) treating a life-threatening or chronically debilitating disease, with a prevalence in the population of not more than five in 10,000 persons (or where the size of the patient population means that it is unlikely that marketing of the medicine would generate sufficient returns), and (2) where there already is a current method of diagnosis/prevention/treatment, the medicine offers a significant benefit to those affected by the condition.

> **The proposals are expected to include a significant realignment of regulatory exclusivities alongside the introduction of an EU-wide compulsory licensing regime.**

Finally, where manufacturers comply with an agreed pediatric investigation plan ("PIP"), they are rewarded with either a six-month extension to their SPC for non-orphan drugs, or a two-year extension to their market exclusivity for orphan drugs.

EU pharma strategy: scaling back and conditionality of regulatory exclusivities

At the core of the Pharma Strategy is revision of the EU general pharmaceutical legislation and the orphan and pediatric medicines regulations. Legislative proposals are expected to be published by the Commission at the beginning of March, followed by a lengthy[3] legislative process involving the European Parliament and Council.

In its initial Impact Assessments from last summer in relation to the **general pharmaceutical regulation**, the Commission initially proposed a so-called "modulated" (or "carrot and stick") approach. This primarily envisaged the reduction of the period of standard data protection from eight years to six, but allowed for an additional two years (or potentially just one year) to be clawed back provided that the product is placed on all EU markets within two years of receiving

[1] Pharmaceutical Strategy for Europe (Brussels, 25.11.2020 COM(2020) 761 final), available online: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52020DC0761&from=EN

[2] Intellectual property action plan implementation, available online: https://single-market-economy.ec.europa.eu/industry/strategy/intellectual-property/intellectual-property-action-plan-implementation_en

[3] and potentially contentious - given recent news reports of disagreements expressed ---by different groups of MEPs

a marketing authorization. The proposed approach would maintain the existing two years of market protection as well as provide an additional one year of data protection for medicines that address an unmet medical need ("**UMN**"), and an additional six months' data protection for comparative trials. However, the maximum duration of protection would be capped at 11 years in total (the maximum available today).

The reduction of existing rights with the possibility of regaining them being conditional on manufacturers placing their products on all 27 EU markets within two years has been criticized as an unrealistic and political goal. Healthcare spend and pharmaceutical pricing and reimbursement decisions are the exclusive competence of the Member States. There are many administrative reasons outside the manufacturers' control as to why this two-year deadline will be challenging to meet, not to mention multiple commercial and other factors (such as diverse patient populations or disease epidemiology) that may make launch of a product in a particular territory impossible or uneconomical.

The Commission also proposed a change to the definition of UMN as being treatment of a life-threatening or seriously debilitating disease where, in case there is an existing treatment, the new treatment can satisfactorily **cure** the disease. This is a higher bar than the current schemes that reward additional indications with an extra year of market protection and products meeting the definition of orphan diseases with orphan designation, both of which recognize the value of "significant benefit" to patients (rather than requiring a satisfactory cure) where there are existing treatments. This narrow approach effectively limits exclusivity for indications where there is already an existing treatment to the extent that it requires a new treatment to attain what may be an impossible goal. This would likely disincentivize innovation where it is needed most and seems misaligned with the Commission's New Innovation Agenda[4] ambitions for the EU as a world leader in innovation.

In relation to the **orphan regulation**, the Commission's initial preferred approach would fundamentally alter incentives by replacing the fixed 10-year period of market exclusivity with a variable-duration exclusivity period based on the characteristic of the orphan medicine. In the leaked Impact Assessment, the durations proposed were: (i) eight years for products targeting the "highest" unmet medical needs (which has yet to be fully defined); (ii) six years for innovative products (new active substances); and (iii) five years for all other orphan products. An additional two years of market exclusivity would be granted to orphan drugs targeting the highest unmet medical needs or for innovative products, again conditional on the product being made available in all 27 Member States (or additionally based on a lack of return on investment for the developer).

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For the **pediatric regulation**, the preferred proposal would retain the six months SPC extension as the main reward for completion of a PIP, but would add a limit of five years after the adult marketing authorization for deferral of completion of the PIP studies and an obligation, where the adult product is intended for a disease that does not exist in children, to identify if it might also be effective to treat a different condition in children (based for example on the mechanism of action).

The Commission's initial proposals were designed to address accessibility (by threatening to reduce existing rights and thereby allowing earlier generic entry) without costing Member States more money but without due consideration to innovation incentives. It is of scant comfort that the current EU incentives regime is more generous than other jurisdictions[5], not least since the European regulatory approval pathway is significantly longer than in many other places. Policy choices about medicines accessibility are best made at the expert regulatory and payer level in the country-specific context of each Member State. EU law and policy should encourage the development of those new medicines rather than stem their flow.

IP action plan: harmonization - and promotion of generic manufacturing

The stated aim of the IP Action Plan is to promote the harmonization of the EU's IP system, ostensibly in order to drive economic growth and strengthen the EU's economic resilience and recovery. The core pillars are proposals for centralization of the SPC application system (which currently operates on a fragmented national basis), the introduction of a Unitary SPC in conjunction with the Unitary Patent system, and harmonization of the EU's compulsory licensing regime.

[4] The New European Innovation Agenda, available online: https://research-and-innovation.ec.europa.eu/strategy/support-policy-making/shaping-eu-research-and-innovation-policy/new-european-innovation-agenda_en

[5] For example, market exclusivity for small molecule new chemical entities in the US is granted for five years (though biologics are granted 12 years exclusivity). Canada provides for six years of data protection plus two years market protection. Six years total exclusivity is available in China, eight years in Japan.

[6] Call for evidence for an impact assessment, regarding compulsory licensing in the EU, available online: https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/13357-Intellectual-property-revised-framework-for-compulsory-licensing-of-patents_en

SPCs

Harmonization is designed to improve the effectiveness and efficiency of the SPC system by removing red tape and extra costs for business by doing away with national examination and grant procedures. The uniform system will also improve transparency since, under the current regime, it can be difficult to trace what SPC protection exists for which products in which markets. Ultimately this will aid generic entry as well.

At the outset, the Commission was not minded to propose any further erosion of SPC protection after the introduction of the manufacturing waiver provision into the SPC Regulation in 2020. Under this waiver, manufacturing of the SPC-protected ingredient in the EU is permitted during the final six months of SPC protection if carried out either for the purpose of exporting to non-EU markets, or for stockpiling. However, there are concerns that the so-called "modulated" two-year launch conditionality foreseen in the general pharmaceutical legislation review will be carried over into the SPC review in support of the goal of improving patient access across all 27 EU Member States. This would be a further major blow to innovation incentives.

Compulsory licensing

Under the TRIPS Agreement, WTO members are able to authorize the use of patented subject matter without the consent of the patent holders if certain strict conditions are met. Most WTO members have enacted a compulsory license framework. In the case of the EU, this has been done on a Member State level. Following the COVID-19 pandemic, the Commission has prioritized measures to ensure that the EU is better prepared to respond more rapidly and effectively to cross-border threats to public health, including the establishment of the European Health Emergency Preparedness and Response Authority (HERA). In this broader context, the fragmented and uncoordinated national approach to compulsory licensing is seen as a risk.

The Commission has therefore published a preliminary framework for compulsory licensing with the specific policy objectives of enhancing compulsory licensing efficiency in a crisis, improving consistency with other EU crisis-management initiatives, and ensuring an effective compulsory licensing procedure for exports. In requesting feedback on the framework, the Commission emphasized that compulsory licensing will continue to be a *"solution to be used as a last resort when there is a complete breakdown in voluntary cooperation between right holders, third parties such as manufacturers of products and public authorities."*[6]

This suggests that ultimately, the EU is looking to promote access to medicines in a crisis through voluntary licensing of patents by innovators (to

Résumés

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Fiona is the head of the EU Competition & Regulatory Affairs practice in Brussels. She is the former Chief Executive of much of Baker McKenzie's EMEA Region and the former Chair of the Firm's Global Competition and Antitrust Law Practice comprising more than 320 lawyers in over 40 countries. She has remained an active practitioner throughout her various leadership roles with a particular focus on the pharmaceutical and other regulated industries. Fiona has been listed in "The International Who's Who of Competition Lawyers" every year since 2009. Fiona is recognized as a pre-eminent competition practitioner by Chambers that quotes clients as praising her "legal and pragmatic advice" and describing her as "globally minded".
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generic manufacturers), backed up by the threat of a more robust system of EU-wide compulsory licensing. The intention is to keep it a "weapon of last resort" but, despite assurances, it is a signal that IP rights are increasingly vulnerable. This is concerning as a strong and predictable IP regulatory framework is a better guarantee of R&D and manufacturing collaboration in the face of a cross-border public health emergency than the threat of what amounts to expropriation.

Competition law: increased scrutiny of patenting practices

As well as being mindful of the upcoming legislative changes outlined above, companies need to be wary of increasing scrutiny from competition authorities when developing R&D, patent enforcement and commercialization strategies based around the available exclusivities.

Competition authorities can readily establish dominance (markets are regularly defined as narrowly as the molecule level (ATC 5) or the mode of action level (ATC 4)) in order to punish any unilateral conduct they see as an unfair drain on public healthcare budgets. Conduct that delays generic entry by as little as a few months is fair game and can result in high fines. The authorities are also adept at opening investigations and wringing settlements from companies as an effective means of putting an early stop to conduct deemed costly to the public purse.

Back in 2005, the Commission broke new ground ruling that AstraZeneca had abused a dominant position by submitting misleading information to national patent offices to acquire SPCs, and by withdrawing marketing authorizations in markets where patents or SPCs were about to expire to delay generic entry. Recognizing that the withdrawals were permitted by regulation at the time, the European Court of Justice ruled that dominant companies have a special responsibility not to use regulatory procedures to hinder market entry in a way that does not constitute "competition on the merits".

The case was one of the factors that triggered the EU pharmaceutical sector inquiry that ran from 2007-2009 during which time, the Commission embarked on a deep-dive investigation into the "toolbox" of tactics patent holders allegedly employ to thwart generic entry. In the decade that followed, enforcement efforts focused largely on so-called reverse (pay-for-delay) patent settlements. The litigation continues but the European Courts have firmly established that patent dispute settlements will be viewed as hardcore violations of the competition rules where they involve any material "value transfer" to generic manufacturers that cannot be plausibly explained other than by the commercial interests of the parties not to compete.

> **"This suggests that ultimately, the EU is looking to promote access to medicines in a crisis through voluntary licensing of patents by innovators."**

The European Court of Justice has recognized that whilst a patent grant creates a presumption that the patent is valid, that does not equate to a presumption that the generic challenger's product is infringing. Nor does the subject matter of the patent afford protection against actions challenging its validity, especially in relation to secondary patents where the patent protecting the active ingredient of the originator product has expired.

More recently, there has been a wave of competition investigations into alleged abuses of the patent system and of patent litigation processes to unlawfully deter competing generics. In the current political climate, these various investigations signal a willingness to tighten the IP system and to more aggressively pursue alleged abuses going forward. Companies are on notice that extra caution is required.

Following a recent dawn raid, the Swiss competition authority is reportedly cooperating with the Commission looking into blocking tactics – allegations that Novartis acquired certain patents from Genentech with the intention of enforcing them in multi-jurisdiction litigation to protect its psoriasis product Cosentyx from competition.

The European Commission has recently charged Teva with misuse of the patent system and disparagement of a rival multiple sclerosis medicine to its blockbuster Copaxone in seven EU Member States. Teva is alleged to have artificially extended patent protection after the original active pharmaceutical ingredient patent expired, by systematically filing and withdrawing secondary patents, thereby forcing its generic competitors to file new lengthy legal challenges each time – a tactic the Commission has emotively labelled the "divisionals game".[7] The theory of harm is that by filing for divisional patents, Teva artificially prolonged legal uncertainty for generics to its benefit.

In October 2022, MSD was fined €39m by the Spanish competition authority for having pursued allegedly unjustified patent litigation to delay the entry of a rival generic contraceptive ring. In initiating a pre-trial discovery mechanism designed to help establish the likelihood of infringement, MSD was found to have used the process to artificially create doubt about a patent infringement to create a base for successfully seeking injunctive relief (that halted the rival's sole manufacturing site for two and a half months for the Spanish market).

There appears to have been a number of irregularities in the initial discovery and injunctive relief proceedings and MSD was faulted for failing to engage with the defendant and for a lack of transparency in the information it provided to the court. But the decision is harsh in concluding that MSD had engaged in an

[7] Divisionals do not extend the period of patent protection - they expire at the same time as the parent patent. There are many scenarios where it is entirely legitimate to file for a divisional patent, for example, where it is not necessarily known at the original filing date which specific inventive embodiments will become a commercial product, or where there is a commercial development opportunity that would benefit from the certainty of grant of a narrower patent for a specific licensed field of use.

"irresponsible" use of patent litigation procedures that amounted to sham litigation. The bar to establish sham litigation has been set high by the European Courts since access to justice is a fundamental human right. The legal test requires that (1) the action could not reasonably be considered as an attempt to establish the patent holder's rights but served only to harass a rival, and (2) the action is conceived in the framework of a plan whose goal is to eliminate competition.

Equally troubling is the finding that MSD's decision to allow the main litigation to lapse some months after the patent expired (at which point the abuse is deemed to have ended) was a separate misuse of the injunctive relief process. The Spanish authority is saying that because injunctive relief is intended to preserve the patent holder's rights so as to ensure the effectiveness of the main proceedings, the fact that the patent holder subsequently halts the main proceedings casts a pall over its intentions in seeking injunctive relief in the first place. There can be many valid reasons to end expensive litigation at any point in the process - as new facts come to light, as management priorities change, as the parties discuss settlement, etc. The risk of any such decision infringing the competition rules because injunctive relief was sought at the outset could have the perverse effect of protracted unnecessary litigation continuing.

Also alarming is the fact that the fine was increased by a "deterrent factor" because the Spanish authority considered that it is "especially costly and problematic for competitors to demonstrate the unjustified nature of the litigation constituting the infraction, given the technical and legal specificity of patent infringement procedures".

The aim is no doubt to create a chilling effect on any patent litigation that may delay generic entry and it may be years before these findings are ultimately challenged on appeal. Left unchecked, the Spanish authority's decision places a considerable burden on companies contemplating patent filing and patent litigation strategies. It will require close monitoring and control of all related internal and external correspondence and exchanges, and solid contemporaneous documentation of the internal decision-making processes to avoid allegations of abuse.

Conclusion

The pending EU legislative changes risk scaling back established IP and regulatory exclusivities unless manufacturers are willing to launch in all Member States within two years. This approach entails greater administrative complexity and cost with no guarantee of being able to maintain current levels of protection, and no guarantee that patient accessibility will materially improve. Pricing and reimbursement approval is the sole competence of Member States some of which do not have the capacity (nor the will from a budgetary perspective) to process many more applications. There can be no quick fix from an EU legislative perspective to what are essentially fundamental macro-economic and policy choices at the Member State level.

> **"2023 will see the reshaping of the established incentives landscape for innovators that will impact both their R&D and patent strategies."**

The changing legislative environment should be understood against a backdrop of increased scrutiny from the competition authorities focused on ensuring that the patent system is not used to delay generic market entry in pursuit of the overarching policy objective of improving the access and affordability of medicines across the EU.

2023 will see the reshaping of the established incentives landscape for innovators that will impact their R&D and patent strategies alongside their commercialization and enforcement strategies. A multidisciplinary effort will be required from IP, regulatory and competition teams within companies in support of a more cautious and holistic approach to mitigate the associated risks from the new political and legal environment.

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