Competition Policy of EEC

Competition policy, only short time in development, is of growing importance in transferring technology

BY MICHAEL BURNSIDE*

This is an appropriate time and place to consider the competition policy of the European Economic Community. Formal negotiations between Spain and the Community to enable Spain to join are underway. To what extent the competition policy of the Community will be affected by eventual Spanish membership of the Community and to what extent difficulties set by the Community's competition policy will affect those negotiations must be carefully considered. From the public pronouncements I have seen on the negotiations for membership, I am clear that this is the case.

The EEC was brought into being by the Treaty of Rome signed in 1957. The original membership of six was expanded in 1973 by the addition of three new members — the United Kingdom, Eire and Denmark. There have been no additions since then, although it can be expected that Greece will become a member in the not-to-distant future. Membership for Greece and for Spain will present problems which did not exist when the original and first expansion of membership took place. These will arise in various ways and to set the background for an explanation of these problems, I shall give some explanation of how Community competition policy in the licensing field has developed.

The EEC has been in existence for some 20 years and it has been attempting to develop policies which in other "states" have been developed over a much longer period of time.

The first Regulation of Law implementing its antitrust policy is Regulation 17 of 1962. (In EEC parlance the term "Regulation" is equivalent to statute or law). Regulation 17 is the basis of the Community's antitrust policy in that it provides the framework within which it works. It provides in some considerable detail for a notification procedure by which agreements which may be restructive of competition have to be notified to the Commission and a clearance procedure by which the Commission is empowered to notify the parties that the agreement concerned is acceptable.

Scope

The scope of Regulation 17 is much wider and all-embracing than the narrow subject of patent licensing agreements. Within a few months of the passage of Regulation 17/62 the Commission issued an announcement giving an indication of what might be considered to be acceptable practices in relation to patent licensing agreements. This was simply an announcement or a notice and has been commonly called the Christmas Message, because it was issued on December 24th, 1962.

In the 1960s there was little further activity on the part of the Commission with respect to patent license agreement insofar as we are concerned with the type of clauses which are of peculiar interest to specialists in the field.

*Michael Burnside & Partners, London.

There are a number of landmark or basic decisions from the European Court of Justice interpreting the constitutional provisions of the Treaty of Rome and it is now clear tha the important Articles of the Rome Treaty to be considered from the viewpoint of antitrust law are Articles 36, 85, 177 and 222.

As the Community developed, competition policy began to receive greater attention. Starting 1972, the Commission began to issue a yearly report on Competition Policy as an annex to the General Reports on the activities of the Communities for each year. In the introduction to the Second Report on Competition Policy, published in April 1973, the Commission stated as follows:

> "Commission's Competition Policy took on a new dimension during 1972. At a time when the Community is preparing to achieve the gradual approximation of the Member States' economic policies, it is more than ever necessary that the Commission should see to it that fundamental rules of the Treaty are observed, and in particular, that effective competition between undertakings is maintained."

Thus, when the negotiations for the original expansion of the Community took place, competition policy in the industrial field was developing but only at a very slow pace. From the viewpoint of licensing and technology transfer, there was not very much detail to be considered.

The first decision by the Commission dealing with the allowable contents of patent license agreements were only published in 1972, when there were four published decisions. In 1974 and 1975, there were five further decisions which are thought to be relevant although some of these dealt with trademarks.

There have been several further decisions since then and also a draft of a Block Exemption Regulation for Patent License Agreements. Thus, self-evidently any new members of the Community will have to accept a licensing policy in a way that could never have been in the minds of the parties when negotiating the first

expansion of the Community prior to 1973. Moreover, there is a different internal background in Spanish law, with respect to technology transfer agreements from the situation in England, Denmark or Eire.

THE COMMISSION'S LICENSING POLICY

What is this policy which Spain may have to accept? This is very difficult to say. From 1962 industry had been working on the basis of the guidance provided by the Christmas message or Notice of 1962. Between 1972 and 1975, there were about 12 published decisions, but since each decision was given in respect of the specific agreement under consideration, it was not easy to elucidate general principles. Moreover the Christmas message of 1962 had not been withdrawn and some of the decisions were clearly inconsistent with this.

Procedurally, licensing in the Community and the need to notify agreements to the authorities follows a different pattern from Spain. Article 85 (1) of the Rome Treaty first says that agreements which distort competition are void. However it then goes on to say in a subsection (3) that if such an agreement contributes to improving the production or distribution of goods or to promoting techincal or economic progress, while allowing consumers a fair share of the resulting benefit, it may be declared exempt from the prohibition of Article 85 (3). Thus, if you have an agreement which does not distort competition, it never has to be registered or notified. If you think there are clauses which may be objectionable, you can notify and ask for negative clearance or exemption.

Because licensing policy has been unclear, licensors and licensees have often not known what clauses in an agreement may cause problems. The Commission has the power under Regulation 19/65 to promulgate a regulation which sets out those clauses in an agreement which will not raise any problems and also those clauses which are objectionable without justification. For years, we have been hoping a draft of this regulation to be proposed by Brussels and this happened late in 1976, when the First Draft of a Block Exemption Regulation for Patent License Agreements was sent to the Member Governments.

Whatever the individual decisions have said, the arguments as to the nature of the Commission's licensing policy have now been brought to a head.

BLOCK EXEMPTION REGULATION FOR PATENT LICENSE AGREEMENTS

There is a large amount of uncertainty as to what are the permissible clauses in a patent license agreement from the viewpoint of Community law. The proposed regulation is supposed to clarify the Commission's policy in this field and since the first draft was produced late in 1976, it has been the subject of heated and often acrimonious debate. We have now had three Preliminary Drafts. The Formal Draft was published in March 1979 and was the subject of a public hearing in Brussels.

Many papers have been written on the Draft Regulation. In a paper of this nature, it is inappropriate and impossible to discuss it in any detail.

The issues in the proposed regulation which have caused the most controversy are:

1. Restrictions on exclusivity of manufacture.
2. Restrictions on a licensor's freedom to impose export sales bans on a licensee.
3. Restrictions on a licensor's freedom to control the use of ancillary know-how.

As compared with the Preliminary Drafts, there is little criticism of the Formal Draft on the controls on exclusive manufacturing licenses. The restrictions on permissible export bans and ancillary know-how are the most controversial.

On export sales bans, broadly the Commission wants to make it difficult for these to be permissible except for small and medium companies. Thus, a clause by which a large English or French licensor agrees not to export to Spain may not generally be permitted. It will require individual justification if Spain becomes a member of the Common Market. While Spain is not a member, the Commission is much less interested because consumers in the Common Market are generally not affected if there is a ban on exports from the Common Market.

Ancillary Know-How

The Commission wants to make it difficult for a licensor to control the use of ancillary know-how once the license agreement has run its full term. This may be changed as it has been strongly criticized on the grounds that it will hinder rather than promote the transfer of technology, if a licensor cannot control the use of his know-how.

The greater part of the Regulation attempts to define what clauses of a patent license agreement are clearly permissible and what clauses are clearly not permissible. These are clauses that can be called the nitty-gritty of many patent license agreements. Thus, as one example, exclusive grant-back clauses for improvement patents are not acceptable but nonexclusive grant-back clauses will be allowed.

In using the term "nonpermissible," I must make it clear that this refers only to the concept that such clauses will not be acceptable without individual approval by the Commission. There is some similarity here with Spanish law.

As far as Spain is concerned any regulation that eventually becomes law can be viewed in two ways. If Spain becomes a member of the Community, it will presumably be, binding law in Spain in whatever form the Treaty of Accession takes. Before, or in the absence of that event, it has some bearing on what type of license agreement may be acceptable between a Spanish company and another company insofar as this can be said to fall within Article 85 of the Rome Treaty. The Commission has made it clear that it believes it has jurisdiction to consider the activities of companies which are located outside the Common Market.

PATENT CONVENTIONS

It is impossible to consider the affect of the licensing policy of the EEC without making some reference to

two Patent Convention which will be generally familiar to most of you. The European Patent Convention or Euro I, which was signed at Munich in 1973, provides for a bundle of National Patents obtained through the European Patent Office. The Common Market Patent Convention of Euro II, which was signed at Luxembourg in 1975, is a convention within a convention. It provides for one patent for the Common Market which will also be obtained through the European Patent Office.

Any new member of the Community is required (Art. 95 (3)) to accede to the Common Market Patent Convention. It is not possible to adhere to the Second Convention without first becoming a member of the European Patent Convention. Thus, I would anticipate that Spain will be, at the very least, urged to undertake at an early date, to sign and become a member of the European Patent Organization so that she will be in a position to ratify the Common Market Patent Convention at the appropriate time. This convention is thought to be of considerable importance in promoting the economic integration of the Common Market. It has a political aim. It is hoped that it will help to break down the barriers to free trade between the Member States.

The significance of Article 43 (2) has been hotly debated in European industry circles. Indeed, the very wording was the subject of considerable argument at the Luxembourg conference where the convention was signed and a comprehensive account of these discussions will be found in an article by Dr. Albrechtskirchinger (see International Review of Industrial Property and Copyright Law 7. IIC 447 (1976)). There has been much discussion of what is meant by "express consent" and the significance of Article 93, which reads as follows:

> No provision of this Convention may be invoked against the application of any provision of the Treaty establishing the European Economic Community.

In the Fifth Report on Competition Policy (page 22) the Commission has already stated that it does not accept Article 43 (2) and that it will be for the Court of Justice to resolve this difficulty. In other words, we may have a situation in which the Commission is saying that in view of Article 93, Article 43 is inconsistent with the Rome Treaty.

Express Consent

This argument has been very much concerned with what is meant by the express consent of the licensor and what meaning can be attached to the phrase "implied consent". The importance of the argument is concerned with the permissibility of intra-European export bans imposed on a licensee or licensor.

Will the Common Market Patent Convention ever come into force? Originally it was hoped that both conventions would start at the same time. This was early realized to be impractical. On signing the CMP, the governments restricted themselves to a Declaration.

Upon signing the Community Patent Convention, they declared that they intend to seek ratification of the convention as soon as possible so as to minimize the interval between entry into force of the convention and of the European Patent Convention. This declaration of intent has certainly not been realized. Denmark has not even ratified Euro I.

Greece may shortly join the Common Market. Article III of the Treaty of Accession calls for Greece to take measures to implement agreements already made between the Member States, but no time limit is imposed. As Greece has not yet ratified Euro I, its early adhesion to the Euro II appears unlikely. Thus, I conclude that early ratification of the Common Market Patent Convention is hypothetical. As the Community increases in size, unanimous actions are becoming increasingly difficult. For practical purposes you may now disregard it.

It is not for me to speculate or advise on the desirability of Spain acceding to Euro I. It may call for a change in Spanish Patent Law. I have a greater hesitancy in commenting on the advantages to Spain of the Common Market Patent Convention. Both conventions have taken a long time to settle and in so doing priorities have been reversed. The driving force behind the European Patent Convention was that it was a necessary preliminary for a Common Market Patent Convention. In the end result, we have a procedure for obtaining centrally a bundle of National Patents, but no means as yet for obtaining one patent for the Common Market.

The Spanish background to the subject is different from that of any of the present members of the Common Market. Some of the present members have government departments and/or laws which exercise controls over anticompetitive activities of companies, both domestic and foreign. This is antitrust law. It is one of the primary functions of D.G. IV, the Competition Directorate-General of the Commission.

However, Spain has a law which is primarily concerned to control the transfer of technology from foreign licensing to Spanish licensees — Decree Regulating the Transfer of Technology in Spain (Sept. 21st, 1973). This provides for a resgistration procedure.

Once the contract is approved, it is a confidential document and not on a public Register. Following the precedents set when the Community was first enlarged in 1973, it can be assumed that there will be a short transitional period in which such agreements will have to be notified to the Commission or modified so as not to require notification. The Commission will have certain powers to require the appropriate Spanish Government Department to notify them of any agreements which may indicate a violation of the Rome Treaty as interpreted by the Commission in its antipolicy. Where will this lead to? I do not know.

It may well be that agreements with present Common Market members will be discovered, which will cause considerable problems to the non-Spanish licensor? Having looked at the Spanish law, I can see that many of the clauses which are indicated as being objectionable are looked at by the Commission in the same way.

The two principal areas where there may be trouble are export bans and freedom to use know-how after the contract has terminated. The relevant section of the Order Regulation, the Registration of Contracts for the Transfer of Technology (Dec. 5th, 1973), is Section 3.

For the purposes of the provisions of Section 5 of Decree 2343/1973, the Ministry of Industry, or, where appropriate, the ministry competent by reason of the

subject matter covered by the contract, shall make a general appraisal of the situation in the sector concerned and of the characteristics of the process and product to which the technology covered by the contract relates having regard to the rights and obligations given to the parties by the contract.

In making such general appraisal, the following conditions or aspects of the contract shall, among others, be considered unfavorable:

1. Prohibitions, restrictive conditions, or limitations on the use of the transferee's own technology, or on his acquisition of technology from other sources, or on the use of nonpatented know-how after the expiry of the contract; restrictive conditions, or limitations on efforts by the transferee to conduct his own research, introduce innovations or proceed to technological developments, or provisions counteracting the aforesaid efforts if made.

2. Provisions whereby the transferee is required to assign patents, improvements or innovations introduced or developed by him on the basis of the technology acquired under the contract.

3. Provisions for the transfer of technology in the form of a "package deal," including parts or elements which are unnecessary or for which supplies of equivalent quality and reliability are manifestly available from Spanish industry, provided that the said parts and elements are technically separable from whatever else the contract transfers.

4. Provisions for the transfer of technology which is wholly or partly inadequate by reason of obsolesence, insufficient competitiveness or other similar reasons, or provisions imposing quality specifications or measures standardizing quality which are incompatible with the standards laid down by Spanish legislation, except in cases in which the product is mainly intended for markets in which such standards and qualities are necessary.

5. Prohibitions on, excessive limitations as to the geographical range of, or the omission of an express authority for exports in specific areas by the transferee; and provisions requiring the transferee to purchase raw materials or components or other intermediate goods or equipment from the transferor or from suppliers stipulated in the contract.

6. Provisions requiring minimum levels of activity or limiting the transferee's freedom to decide his working methods in respect of levels, models, competitive articles, prices and periods of delivery, or giving the transferor the unilateral right to fix the prices of the goods produced by the transferee.

7. Provisions favorable to the transferor's interest on the sale of the goods produced by the transferee in the Spanish market; provisions imposing on the transferee an exclusive relationship with the transferor, or requiring the transferee to use marks registered in Spain by the transferor.

8. Provision imposing on the transferee the obligation to supply to the transferor or to stipulated third parties the goods produced with the aid of the technology transferred in circumstances contrary to the interests of the Spanish economy.

9. Provisions giving the transferor the right, not previously acquired by other means, to intervene in, control or impose conditions on the management of the tranferee's undertaking or his plans for expansion or diversification.

10. Provision requiring payments substantially higher than those normally prevailing on the market in similar situations, or minimum returns when the payments are based on rates proportional to the various levels of activity.

11. Provisions fixing payments in the form of rates proportional to the level of production without deduction the value of imported products or components incorporated in the production process to which the acquired technology is applied; and provisions which do not exclude the invoicing of lines of production not affected by the acquired technology.

12. Provisions imposing payments based on rates proportional to the transferee's level of activity when the transferee is a subsidiary of the transferor and the transferor holds more than 50% of the transferee's capital stock, or when the transferor of technology supplies raw materials or intermediate products used in the process to an amount equal to more than 30% of the total cost of the product, or when the transferee is a consultancy or engineering firm, unless in the latter case the technology transferred relates to a process for activities in which the process is constantly applied.

13. Overpricing (differences between the prices stipulated in the contract and those charged on the international market by the supplier or his principal competitors) of supplies, materials or pieces of equipment associated with the process to which the transferred technology applies, which are furnished by the transferor or by suppliers stipulated in the contract.

14. Provisions for the duration, either too long or too short, of the contract or of its direct consequences; provisions whereby the duration of the contract is automatically extended; and provisions which impose payments for a period longer than the period of validity of the patents involved.

15. Provisions to the effect that a foreign-language version of a contract which has been signed in other languages as well as Spanish shall be the authoritative one for the purposes of interpretation.

CONCLUSION

The competition policy of the Commission in the industrial field is one of the areas of Community activity which is becoming increasingly and rapidly effective. Five years in the development of an antitrust policy is a very short time and when one looks at the changes that have taken place since 1973, when the Community was first expanded they are considerable. Agricultural policy and the freedom of movement of labor may occupy the headlines but to those of us concerned with industry and the transfer of technology, competition policy may be much more important.