

Competition, Dissemination Of Innovation

BY JEAN-FRANÇOIS POISS¹



The new EC block exemption regulation for technology transfer agreements received at LESI conference

On January 31, 1996, following a long consultation process with industry, the Commission of the European Communities adopted its new block exemption regulation on technology transfer agreements. This regulation marks a step forward by the Commission toward the creation of a favorable legal environment for development of technological innovation and its dissemination within the European Union, while ensuring that both healthy competition as well as the achievement of the single market are not affected.

ORIGIN OF THE REGULATION

A certain number of factors, and, in particular, a recognition of the stimulus provided by technology transfer to economic development in today's society is highlighted in the White Paper on Growth, Competitiveness and Employment, has led the Commission to introduce significant simplification to the existing rules governing technology transfer agreements.

These rules were set out in the former regulations (EEC) 2389/84 of July 25, 1984, and (EEC) 1017/88 of July 30, 1988, under which the Commission had already granted block exemptions in pure patent or know-how licenses as well as to mixed patent and know-how licenses. These regulations enabled businesses to avoid having to notify most of their patent or know-how license agreements in order to obtain an exemption from Article 85(1). The rules also enabled the Commission to decide quickly on transfer-how cases by means of an opposition pro-

cedure under which the exemption extended to agreements that include additional restrictions on competition not included in the text of the regulation, on condition that such agreements were notified to the Commission and the Commission did not oppose them within six months of notification.

However, in the Commission stated in its 20th Report on Competition policy, there remained practical difficulties. These were principally related to the detailed character of the two former regulations as well as to the uncertain legal position concerning mixed licenses, which were covered in some manner by both regulations.

The purpose of the new Regulation is to overcome these difficulties. It merges the previous exemption regulations into a single legal instrument enabling business to benefit from a single set of rules for patent licenses, know-how licenses and mixed patent and know-how licenses. The new Regulation recognizes the fact that in practice, mixed agreements play an every more important role in technology transfers.

At the same time, the adoption of the new rules offered the Commission the possibility of broadening the scope of application of the regulation. The previous regulations had in general been considered as useful legal instruments, but they restricted the contractual freedom of the parties. The new Regulation provides for a series of improvements and simplifications and is marked by a more open attitude to provisions that are frequently encountered in practice.

From the outset, given the primary objective of disseminating new technology in a competitive climate in the Community, the Commission considered the various

rules inadequate in that they took no account of undertakings' economic power and the danger that companies with a significant market share could potentially block the implementation of innovations that would compete with their products and processes. You will recall that the Commission, influenced by the *Tetra Pak* case and similar cases,¹ initially favored a solution that would have excluded from the benefit of an automatic exemption, agreements granting territorial exclusivity in favor of a licensee that was part of a close oligopoly of which, at the time the agreement was made, had a market share of at least 40%. After heated discussion with several industry groups (in particular UNICE) and the European Committee of LESI Internationally the Commission decided to adopt a less rigid position and reserve the 40% market share threshold only as a criterion for the possible withdrawal of the benefit of the exemption.

STRUCTURE AND PRINCIPAL PROVISIONS OF REGULATION (EC) 96/27

The structure of the new Regulation follows the usual model with respect to block exemption by creating a distinction between white, black and gray classes. Its principal elements can be summarized as follows:

1. Article 1 sets out the list of obligations that restrict competition and are normally covered by Article 85, paragraph 1, and that are

¹ See the *Tetra Pak* case (DMC) Report - March 95.

² Thierry Dierckx, General, Commission of the European Communities, Brussels, Belgium.

automatically exempted by the Regulation. A license agreement containing such provisions does not have to be notified to the Commission. Article 1 primarily concerns clauses providing for territorial restrictions between parties or licensees/licensees. They are exempted between parties throughout the term of validity of the patent, or for 10 years in the case of know-how agreements and, in particular, between licensees for five years with respect to the prohibition on both active and passive sales.

2. Article 2 sets out a certain number of obligations that are often found in license agreements but that do not generally restrict competition. It provides that, if by reason of a particular economic or legal context, they were to be covered by Article 86, paragraph 1, they should also be covered by the block exemption where are the so-called related-listed clauses. New white clauses were also added in particular, the right for the licensee to terminate the agreement where the licensee doubts the validity of the patent, to terminate the exclusive character of the licensee's rights where the licensee competes and the right of the licensee to reserve the right to avail of the rights conferred by a patent in order to oppose exploitation by the licensee of the technology outside the territory granted to the licensee.

3. Article 3 sets out the "black list" of clauses or restrictions whose presence in an agreement prevents the grant of a block exemption (price limitations, restrictions on competition, restrictions on clientele between competing manufacturers, restrictions on the extent of exploitation, an obligation on the licensee to bring improvements to the technology, territorial restrictions in respect of the exempted period). In order to facilitate technology transfers the black list has been significantly reduced — almost by half — in comparison with the two former regulations. The black-listed clauses that have been eliminated have not, however, been transferred to the white list. They have been moved to the opposition procedure, as is the case specifically, for the nonchallenge

clauses and for the tie-in obligations that are not necessary for exploitation of the transferred technology.

4. Article 8 requires that agreements notified to the Commission that contain gray clauses, be subject to an opposition procedure. Gray clauses are restrictions on competition not referred to in Articles 1 and 2 and that are also not covered by Article 3. In order to make the procedure more efficient, the time within which the Commission must intervene has been shortened from six to four months. Moreover, in the 28th recital to the regulation, the Commission has stated that instead of all the documentation required by Form A/B, it requires only notification of the text of the agreement and an estimate of the market. Therefore, the notification will be considered as having been validly made at the date of such communication, even if the Commission, in the light of the particular circumstances, requires additional information after this date.

Even though the Regulation no longer provides for a market share threshold beyond which the relevant license agreements would have to be notified, the existence of significant market share will be particularly important in the context of possible withdrawal of the exemption. In accordance with the provisions of Article 7, paragraph 1 of the Regulation, the Commission will attach particular importance, in assessing conditions of competition, to situations in which the licensee's market share exceeds a threshold of 40% of the total market for the licensed products and all products or services that the consumer considers as being interchangeable or substitutable by reason of their properties, price and use.

The United States authorities also attach particular significance to situations in which a licensee has a strong market share. The Department of Justice has intervened in the past in order to force the licensee to grant nonexclusive licenses instead of a single exclusive license (see the *Sea-Johnson* case). The Antitrust Guidelines for intellectual property licenses highlight the anticompetitive risks associated with the grant of exclusive licenses in

concentrated markets or in favor of licensees holding significant market share. The 13th example of those guidelines specifically refers to the case where a license is granted for the manufacture and distribution of a patented pharmaceutical substance in favor of a business that already offers the only remedy on the market for treating the same illness. Even though such license was not formally exclusive, the patent holder has refused to grant other licensees on reasonable conditions.

The importance of the market share threshold should not be exaggerated. It is only one indicator, among others, of the existence of market power and does not itself lead to the conclusion that there exists possible abuse of such power. In addition, if the Commission were to initiate proceedings, in particular on the basis of a complaint, the parties would, prior to any possible decision to withdraw the exemption, have the benefit of all procedural rights available in case of examination of individual cases (such as communication of the complaint, access to the file and the possibility of an oral hearing).

RESULTS OF EXPERT STUDIES

In order to have an exact idea of the numbers and types of exclusive licenses, the Commission asked three experts, British, French and German, to carry out studies in their respective countries based on a representative sample of licensees and licensors. In particular, the idea was to evaluate the annual flow of exclusive licenses for which the licensee's market share was above the 40% threshold.

There were difficulties in obtaining detailed data, by reason of a certain foreseeable reluctance on the part of business to divulge information on their license agreements, to which must be added the difficulty linked to the determination of the relevant market. The studies, nevertheless, permitted identification of the sectors where the risk of concentration of technological protection is highest as well as confirming that the annual flow of licenses above the 40% mark is limited (about 30 per year for the French

study, whose results seem to be the most reliable). Another interesting result was that the pharmaceutical and biotechnology sectors seem to be the most likely sectors of an in-competitive risk.

CONCLUSION

In ending my speech, I would like to make the following observation: At the dawn of the third millennium our world dreams of conquering the vital importance of innovation in products and processes for economic development. In

the Commission's view, the industrial progress in the European Union is inextricably linked to the dynamism of its businesses in the conception of new technologies. For this purpose, the Commission has launched various international cooperation programs in the area of research, such as Esprit, Drive and Brins, and a significant portion of the Community's budget is devoted to them. Simplification of technology transfers, in the context of the rules on competition, is an important addition to these actions.

Of course, the new Regulation is not revolutionary, but it appears to be a significant improvement on the existing situation. The new Regulation abolishes the disparities that existed between the patent license regulation and the regulation of transfers of know-how. It eliminates, as transfers to the opposite procedure, several clauses from the old regulation that prevented the block exemption being obtained and, in order to attach greater respect to the freedom of parties to contract, it provides for new acceptable clauses.