

Technology Transfer In Europe: The Business Impact Of The EU Regulation

By Dr. Winfried Büttner*

I. Introduction

On April 7, 2004, the European Commission adopted a new block exemption regulation with respect to Technology Transfer Agreements (TTBER). The TTBER replaces the existing Regulation 240/96 and sets out a new regulatory framework for applying competition policy to the licensing of patents, know-how and software copyrights. It contains extensive changes and is part of the fundamental revision of the Commission's rules for safeguarding competition, which has a particular focus on a more economic-based approach in the assessment of agreements. It entered into force on May 1, 2004, at the same date when the new regulation on the implementation of the rules on competition 1/2003 became effective. The TTBER is accompanied by detailed guidelines that shall assist market participants in the assessment of restrictive agreements, in particular when they fall outside the scope of the TTBER.

The need for a new block exemption regulation has been caused by the general modernisation of the competition law at the European level, driven by the expansion of the European Union to 25 member states. The resulting administrative burden of enforcement and the individual notification system would have endangered the effectiveness of community law and the working capacity of the European Commission had it remained in place.

As a result, the system of individual exemptions is now replaced in its entirety by a system of legal exceptions through block exemption regulations and the individual assessment of restrictions of competition by the parties in case the block exemption regulations do not apply. The block exemption regulations provide a "safe harbour." Agreements or restrictions that do not fall in the scope are not per se illegal, but still can be assessed under Article 81 Section 3 EC Treaty. However, parties do not have the option anymore to seek formal approval for clauses that might be in compliance with the prerequisites of Article 81 Section 3 EC Treaty. Today, they need to assess the respective agreements on their own, thereby also assuming the risk of misjudgment.

The new TTBER entered into force on May 1, 2004, and will remain in force until April 30, 2014. For a transitional period that will end on March 31, 2006, agreements that were already in force prior to May

1, 2004, and exempted from Article 81 Section 1 EC Treaty under the old Regulation 240/96, but not under the new regulation, will remain unaffected. Since the preceding regulation was intended to remain in force until March 31, 2006, this transition period, that in earlier drafts was initially meant to be shorter, provides legal certainty for agreements that were concluded in the view that regulation 240/96 will remain in force until March 31, 2005.

II. Balance Between IP Protection and Competition

Technology licensing contributes to economic and technological development by spreading innovations and encouraging new market entry. This generally leads to more efficient exploitation of the intellectual property. The owner of the IP may not be able to make the necessary investments to realize the full value of the IP without entering into a licensing agreement with another company possessing complementary assets or capabilities.

It is well recognized that restrictions in technology license agreements are in many cases justified to protect the investment of the licensee and to prevent free riding. Restrictions on the licensee may also be necessary to protect the interests of the licensor. A license imposing restrictions on the use of the technology is often the better alternative for competition and innovation than no license at all, and the possibility to include restrictions may be necessary to induce the licensor to share its technology with other market participants at all.

Restrictions may, however, not go as far as to raise competition concerns. For example, a licence agreement that divides markets among companies that would have competed in the market using different technologies if no license had been granted is likely to have negative competition effects.

It is now widely recognized that the goals of competition policy, promotion of innovation and intellectual property laws are complimentary and mutually reinforcing. They all serve consumer benefit and welfare, technological innovation and an efficient allocation of economic resources. Competition laws are designed to protect competition as the driving force of efficient markets and innovation. Efficient competition ensures that its consumers can benefit from the best quality products at fair prices. IPRs are aimed at creating an incentive to engage in research and development by ensuring a sufficient reward for the innovator.

It is therefore the task of the legal framework to find a balance between granting rights broad enough to create incentives for innovation, and at the same time narrow enough as to hamper further improvements by competitors.

III. General Principles of the New Regulation

The predecessor of the new regulation, Regulation 240/96, was rather form-based and followed a legalistic approach, primarily referring to the terms contained within the licensing agreement. It relied on the assumption that any restriction that overstepped the boundaries of the subject matter of a patent is potentially caught by the prohibition of cartels in Article 81 Section 1 EC Treaty. Article 2 of the regulation set down a list of clauses that generally would not violate Art. 81 Section 1 EC Treaty; the legality of which was clarified and also exempted in the event that under particular circumstances, those clauses would fall within the scope of Article 81 Section 1 EC Treaty (so called “white list”). Article 3 of the regulation listed a number of licensing clauses that would violate Article 81 Section 1 EC Treaty; the inclusion of which would have taken the entire agreement outside the scope of the block exemption (so called “black list”). Article 4 of the regulation dealt with clauses that were neither exempted nor expressly excluded; the assessment of which required a case-by-case analysis (so called “grey list”).

This system of regulation 240/96 was subject to substantial criticism. Critics focused on the form-based framework which imposed a legal “straitjacket” on the parties. Regulation 240/96 was also criticized for its legalistic approach, geared to the mere wording of a licensing contract rather than the economic context. Furthermore, Regulation 240/96 was considered to be incompatible with the recent reforms of European-competition rules. On the one hand in recent block exemption regulations, the Commission took a more effects-based approach. On the other hand, with the new Regulation 1/2003 and the abolition of the notification system, the opposition procedure provided for in Article 4 of Regulation 240/96 had to be repealed.

With the new regulation, the Commission made the competitive relationship of the parties and their market shares the two major parameters of the block exemption. The legal framework for agreements between competitors is now different than one for agreements between non-competing companies.

Furthermore, the regulation now offers a general block exemption (“safe harbour”) for technology transfer agreements only below certain market share thresholds by introducing market share ceilings, the introduction of which was highly criticised by many companies in the consultation process.

The TTBER still includes a list of hard-core restrictions (“black list”), but not a list of permissible measures any more (“white list”). The concept of the new regulation is therefore in line with other recent block exemption regulations, such as the block exemption regulation for vertical agreements, for research and development agreements or for specialisation agreements.

IV. Analysis of Various Important New Provisions

1. Inclusion of Software Licensing Agreement

The analysis of software licensing agreements has always been a difficult task due to the fact that they often fall in the grey zone between vertical supply relationships (block exemption regulation on vertical agreements) and technology transfer agreements. A special software license block exemption regulation never came into force.

The new TTBER now explicitly includes software license agreements in the definition of “technology transfer agreements” (Article 1 Nr. 1 b), thereby contributing to legal certainty in the field of software licenses.

2. Market Share Ceilings

As a prerequisite of the application of the block exemption regulation, Article 3 of the new TTBER provides for market share ceilings.

Agreements between competing undertakings are generally exempted if the combined market share of the parties does not exceed 20% of the relevant technology and product market. Where the contracting parties are not competing, a block exemption is generally granted on conditions that the market share of each of the parties does not exceed 30% of the relevant technology and product market.

The concrete market share ceiling shall bring the TTBER in line with other revised block exemption regulations (e.g. block exemption regulation on vertical agreements) and the legal framework for technology transfer in the U.S. (U.S. guidelines for the licensing of IP).

From a practical point of view, the application of market share ceilings unduly complicates the block exemption and seriously reduces legal certainty. The definition of relevant markets is already difficult for normal products, but can be extremely complicated in

**Professor, Dr. Büttner, Honorary Professor at the University of German Armed Forces, Munich. Responsible for Corporate and Intellectual Properties and Functions at Siemens, AG in Munich, Germany.*

high technology industries characterised by high pace of innovation. In addition, the TTBER requires analysing ceilings in at least two markets:

- the market of the product that will be replaced or improved by the license technology, and
- the market for the technology in which the license technology competes.

The difficulties associated with market share ceilings have increased after May 1, 2004, when Regulation 1/2003 came into force. The national courts that are called upon to decide on enforceability of licenses may not be well equipped to define markets and calculate market shares, and may be forced to ignore the TTBER if the relevant market data is unavailable.

On the other hand, the guidelines make clear that agreements that do fall outside of the scope of the TTBER are not considered to be illegal. As long as the agreement does not include hard-core restrictions listed in Article 4, and as long as there are four or more competing technologies available on the market, the agreement should not raise competitive concerns. We see here an important step towards the legality of restrictions in general that do not constitute hard-core restrictions.

3. Distinction Between Competitors and Non-Competitors

The regulation provides for a distinction between horizontal and vertical licenses with respect to market share ceilings and hard-core restrictions. This is generally a valid approach, since there is more scope for a negative effect on competition in agreements between actual or potential competitors than in those between non-competitors. However, problems arise in this context. It is not always clear when the parties to a licensing agreement will be regarded as competitors, in particular where the license product presents a sweeping breakthrough or where the IPRs owned by the licensor and the licensee are in a mutual blocking position.

Besides, the old Regulation 240/96 did not generally make this distinction and worked very well in that respect in practise.

4. Non-Assertion of Patents (NAP)

In Regulation 240/96, the obligation of the licensee not to assert the validity of patents of the licensor were treated as so called grey clauses. This meant that the parties had to undergo the “opposition procedure” under which they had to notify the Commission of the provision. It was treated as exempted if the Commission did not oppose the clause within a period of four months. The new regulation only contributes little to legal certainty in that respect by abolishing the opposition procedure, but by including the NAP clauses in the list of restrictions that are not exempted but which do not cause the agreement to fall out of the block exemption in its entirety. As a result, the validity of NAP clauses in specific cases remains unclear.

5. Hard-core Restrictions

In order to benefit from the exemption, the parties definitely must avoid imposing any of the regulation’s hard-core restrictions. The same applies for the individual assessment of an agreement that falls outside the scope of application of the TTBER.

It is generally accepted that the competition risk is greater for licensing between competitors than between non-competitors. As a result, Article 4 provides for different sets of hard-core restrictions, thereby making the identification of the parties as competitors or non-competitors a key decision.

In the context of competitors, it is also accepted that the competition risk is greater for reciprocal licensing than for non-reciprocal licensing. As a result, the TTBER prohibits certain restrictions in reciprocal agreements between competitors that are accepted in unilateral license agreements.

V. Summary and Conclusion

Despite the imperfections that I pointed out earlier, the new TTBER is a significant step in the European Commission’s effort to modernize the European competition law by adapting it to the economic realities. The TTBER provides for a sound legal framework, and the approach of abolishing “white lists” gives the companies flexibility in the use of technology transfer agreements. In addition, it leads to a further convergence between EU law and U.S. law. ■