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Upcoming Reform of the Technology Transfer Block Exemption - Important Developments for Companies Involved in Licensing Activities

In January 2002, the Commission issued a detailed “[Evaluation Report](#)” on the Transfer of Technology Block Exemption (the “TTBE”), running to some 42 pages.¹ After a one-year “reflection” period, the stage now appears to be set for significant impetus in the reform process. An official proposal for a new Block Exemption and related IP Guidelines and the opening of public consultations is expected in early summer 2003. In order to prepare companies for another major reform in EC competition law, we thought it might be useful to outline the current state-of-play and highlight potential future developments in this important area.

The Evaluation Report was based on the Commission’s own assessment as to what needs to be reviewed and responses to a Commission questionnaire during the previous year. It also referred to comparative approaches, notably the US Guidelines on Intellectual Property. In response to the Commission’s invitation to comment on the Evaluation Report, more than 30 entities have submitted comments, which the Commission has published on its website together with a summary.

It appears likely that a revised regulation will be on the statute books in 2004, although the TTBE does not formally expire until 31 March 2006. The new TTBE will most probably shift to a pure “black” list approach and put special emphasis on distinguishing agreements depending on whether they have been entered into by competitors or not. Controversially, in all likelihood it will also introduce a system of market share thresholds, probably excluding from its scope agreements entered into by dominant companies. Even companies with market shares under 30% may find themselves required to review and adjust their existing licensing arrangements.

All companies which are involved in IP licensing agreements, either as a licensor or licensee, should therefore carefully observe EU developments in this field, especially since the new legislation will also affect license agreements already in force.

The current TTBE²

The [current TTBE](#) provides a regime for the block exemption from Article 81(1) EC of pure or mixed patent and know-how licenses. Licenses under other intellectual property rights (copyright, trademarks, design rights) are covered only when ancillary to such patent and know-how licenses. The current TTBE exclusively covers agreements entered into by two parties and does not extend its scope to multiparty licenses or pooling agreements.

¹ Commission Evaluation Report on the Transfer of Technology Block Exemption Regulation 240/96 - Technology Transfer Agreements under Article 81. See also [Commission Press Release IP/02/14](#), of 7 January 2002.

² Commission Regulation (EC) No 240/96 of 31 January 1996 on the application of Article [85(3)] of the Treaty to certain categories of technology transfer agreements, 1996 O.J. L31/2.

The current TTBE contains: (i) “black-listed” clauses that might make the whole license agreement void, for instance clauses relating to price restrictions, consumer restrictions, certain types of non-compete restrictions, and tying the licensee to further licenses; (ii) permitted clauses whose legality is clarified by them being expressly mentioned in the block exemption (the “white list”); and (iii) clauses which might be permitted but need to be cleared by the Commission on a case-by-case basis via a built-in notification procedure (the “grey list”).

Further, the current TTBE is form-based and follows a legalistic rather than an economics-based approach. Contrary to more recent block exemptions, the TTBE applies regardless of market shares and may exempt agreements entered into by dominant undertakings. The Commission is, however, entitled to withdraw the benefit of the TTBE on a case-by-case basis. Such right of withdrawal may be exercised in particular when the licensee’s market share exceeds 40%.

The Commission’s motivation for change and the comments submitted

Enhancing clarity and coherence. The Commission has indicated that it is aiming to make the TTBE rules simpler, clearer and more coherent — an aim which third party submissions on the Evaluation Report unanimously support.

In line with those aims, the stated objectives of the reform are (i) to encourage the dissemination of technical knowledge in the Community; (ii) to generate effective competition and technical progress; and (iii) to create a favorable legal environment for investments. These aims are to be accomplished within the new modernization and decentralization framework.

Covering a wider range of IP. The Commission is considering widening the scope of the TTBE further so that, as with the Vertical Restraints Block Exemption, there would be an “umbrella” type of block exemption for IP rights, including copyright (including rights in software), design rights and perhaps trademarks.

Coverage of software licensing agreements appears to be widely supported by submissions to the Commission. Opinions diverge as to whether the scope should be extended more generally to cover all IPRs, in particular copyright, trademarks and design rights. Some emphasize that this would increase legal certainty (as the applicable principles would be the same for all or most IPRs), and remove the difficulty in assessing whether an IPR is really ancillary to patent or know-how licensing agreements (and therefore covered by the current TTBE). On the other hand, a number of submissions stress that the different IPRs involve different antitrust concerns that should not be lumped together.

Bringing the TTBE structure in line with the modernization process. The Commission aims to remove the “grey list” of “arguably restrictive” clauses that, at present, are to be notified to the Commission under a so-called “opposition procedure”. (Under this procedure agreements are deemed cleared if not opposed by the Commission within four months.) Once notification is abolished, as will occur from May 2004, the procedure will not be available (unless some transitional exception is made). Essentially, such clauses therefore have to be reviewed to determine whether they should be fully exempt under the new TTBE or not. Furthermore, the Commission might be tempted to re-examine the current balance between *intra-brand* and *inter-brand competition* in the TTBE. In practical terms, this could mean, for instance, aligning the restriction on passive sales between licensees (for the first five years from when a product is put on the market in the EU by a licensee), with the

ordinary active/passive rules in distribution, where a restriction on passive sales is black-listed.³

Envisaging an “economics-based” approach. The Commission has questioned the rationale of some policy determinations taken in the current TTBE and suggested that they may need updating. As is the case now with vertical and horizontal restraints, the Commission envisages a move from a legalistic into a more “economics-based” approach, focusing on the competitive relationship between the parties, their market share and the nature of the restriction concerning IP rights. Detailed IP Guidelines are envisaged to ease the transition to the future TTBE and enhance legal certainty.

- **Distinction between competitors and non-competitors.** Above all, the Commission suggests that a distinction should be made depending on whether licenses are *between competitors* or *between non-competitors*. The Commission acknowledges that it is especially difficult to decide who is a “competitor” in the IP licensing context given the potential markets concerned (R&D/innovation, technology and product markets), and suggests that the definition of who is a competitor should be more realistic (and narrow).⁴ According to the Commission, the nature of competition between a licensor and licensee might also change in cases where both parties are in a mutual blocking position and where the licensed process or product represents such a “sweeping breakthrough” that, without the agreement, the licensee would no longer be a competitor at all.⁵

There is general consensus among the submissions that the competitive assessment of license agreements depends very much on the distinction between competitors and non-competitors, and that licensing between non-competitors should be assessed more leniently. Many submissions also ask that the Commission clarify in its final proposal when an innovation will be considered a “sweeping breakthrough”, so that existing technologies can no longer be considered real substitutes.

- **Market share ceilings.** The Commission strongly suggests that there should be market share ceilings in the revised TTBE. Agreements falling outside the scope of the TTBE (e.g., involving market power) would be dealt with in related IP Guidelines and, after the [Modernization Regulation](#) enters into force in May 2004, could not be notified en masse.⁶ The Commission proposes limiting automatic exemption to a 25% market share for licensing agreements between competitors, 30% market share for licensing between non-competitors when it concerns restrictions that do not relate to the exploitation of the IPR, and a dominance threshold when the restrictions do relate to the exploitation of the IPR.

Reactions by the business and legal community to these proposals appear to be mixed. Some argue that it is usually too difficult to define markets, as licenses may concern new products or innovative technologies with unclear function and demand. Since market shares in IP-related markets may often be high without implying real market power, the use of market share thresholds could stifle licensing and innovation. However, many submissions appear to be in favor of market share

³ Evaluation Report, para. 141.

⁴ Evaluation Report, para. 43, para. 125 and para. 130.

⁵ Evaluation Report, para. 130(c).

⁶ Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, 2003 O.J. L1/1.

ceilings and many even agree to those suggested by the Commission as long as the IP Guidelines provide certainty regarding how the markets will be defined.

- **Nature of restrictions.** Restrictions concerning the exploitation of IP rights would include territorial, customer, output and price restrictions. Restrictions *going beyond* exploitation of licensed IP rights would include non-compete obligations, tying, grant backs and no-challenge clauses.

The comments as to the specific way such restrictions should be treated are very detailed and reveal a variety of often diametrically opposed views. For instance, submissions regarding no-challenge clauses (currently considered to be a “grey clause” under the TTBE) are split. Some submissions argue against exemption, while others favor a review of the policy, especially for no-challenge clauses in the case of an amicable settlement of a pending IP lawsuit. Some also argue that the exploitation criterion is too complex in practice.

A more permissive approach. The Commission leans towards favoring a more permissive approach to restrictions when parties lack market power or are in a vertical relationship. Also, in line with the “new style” approach to block exemptions, the “white” list of clauses would be abolished, leaving just the “black” list.

There is also discussion as to the efficiencies involved in IP-related restrictions (as opposed to a focus on form), which would be linked to a market power assessment in order to see if there is sufficient competition to pull efficiency benefits through to customers. The issue as to whether the 10-year limitation for exclusive licenses of know-how is adequate (considering that such time-limitations are not included in the vertical restraints block exemption) is also expressly referred to in the Evaluation Report. Last, the Commission is also considering exempting non-exclusive licenses since they, in principle, do not have any foreclosure effects. Reactions to this more permissive approach are in general overwhelmingly positive.

Multi-party licenses and patent pools. The Commission is concerned that only bilateral licenses are covered by the TTBE and is now considering whether *multi-party licensing pools* and other *cross-licensing* arrangements could also be considered favorably and be block exempted. The Commission also pays attention to the use of patent pools to unblock conflicting IP positions and to create a new industry standard — also noting the increased use of package-licensing programs, technology pools and cross-licensing. On the other hand, the current Council Regulation 19/65 (enabling the Commission to adopt block exemptions) does not entitle the Commission to block-exempt multi-party agreements so this would have to be amended to bring multi-party licenses into the new block exemption.

Not surprisingly, opinions are split. Most voices plead for the coverage of multi-party licensing by a future block exemption regulation, although only below a rather low market share threshold and/or limited to situations of complementary or blocking IPRs. Some submissions speak out against coverage of this complex issue by the block exemption itself and plead for IP Guidelines to address the matter, including patent pools for standard setting. Many are also concerned that express provisions in the revised block exemption for multi-party licensing could result in significant delay — until there is a respective amendment of Council Regulation 19/65 - and therefore prefer that a more modern approach be reflected in IP Guidelines.

This Bulletin has been prepared by *John Ratliff* and *Michael Goldmann*. If you have any questions about the reform of the TTBE or any other EU law matter, please do not hesitate to contact them, our IP specialists *Rajeshree Bhojnani* in London and *Klaus Schubert* in Berlin, or any of the lawyers listed below.

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