THE EU COMMITTEE
OF THE AMERICAN CHAMBER OF COMMERCE IN BELGIUM

Position Paper on the Commission's Review of the Technology Transfer Block Exemption, Regulation 240/96

Executive Summary

The EU Committee welcomes the Commission's proposals to overhaul the TTBE in the short-term. It concurs with the Commission's analysis that the current rules are too narrow in scope and its approach too prescriptive and formalistic. We support the conceptual approach which would treat agreements between non-competitors more generously than agreements between competitors. We agree that consistency with the vertical restraints block exemption is appropriate in relation to restraints not related to the exploitation of the IPRs.

We take issue with the proposal to exclude from the scope of a new block exemption, license agreements where the licensor is dominant. We urge the Commission to publish draft guidelines at the same time it issues a draft regulation for public consultation. In particular, the guidelines should provide as much comfort as possible in relation to issues arising from the various market share thresholds incorporated in the Commission's proposals for change. This is one area which is likely to cause legal uncertainty sufficient to act as a disincentive to technology transfer.

The EU Committee is, in principle, in favor of extending a new regulation to include copyright in software and design rights for as long as such extension does not significantly delay the adoption of a new regime. We are also in favor of developing a more flexible approach to multiparty agreements in guidelines rather than in the block exemption itself so as not to delay the adoption of a more user friendly and flexible block exemption regulation.

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1. INTRODUCTION

The European Commission published a mid-term "Evaluation Report" in December 2001 in which it proposes to replace the technology transfer block exemption ("TTBE") with a less prescriptive regulation covering a wider range of agreements in line with the recent block exemptions on vertical and horizontal agreements. It seems likely that a revised regulation will be on the statute books by 2004, although the TTBE does not expire until 31 March 2006.

The EU Committee welcomes the Commission's proposal to overhaul the TTBE in the short-term.

2. PROPOSED CONCEPTUAL APPROACH

The EU Committee concurs with the analysis that the TTBE is too narrow in scope, its provisions are sometimes unclear, and its approach too prescriptive and formalistic.

The Commission is proposing to distinguish between agreements between competitors and agreements between non-competitors, and between restraints that directly concern the exploitation of the intellectual property rights ("IPRs"), and those which do not.

According to the Commission, a new block exemption would also adopt a more "nuanced" approach to pools, cross-licenses and joint ventures.

<u>2.1 Licenses between Non-Competitors</u>

In relation to agreements between non-competitors, the Commission envisages a regime structured along the following lines:

- Ø restraints related to exploitation of IPRs (e.g., exclusive territorial, customer and field of use restraints) would be covered up to a dominance threshold, assuming the agreement falls within Article 81(1) in the first place

- Ø restraints not related to exploitation of IPRs (e.g., non-compete, tying) would be treated in the same way as in the vertical restraints block exemption which regulates distribution agreements, in other words, they would be subject to a 30% market share threshold

- Ø there would be a limited hardcore list of prohibited restraints focusing on price-fixing and possibly the restriction on passive sales which the TTBE currently permits for a period of five years

- Ø severable restraints may be included subject to conditions (e.g., no challenge clauses, grant-backs of improvements).

The EU Committee supports the overall approach proposed.

A more liberal regime up to a dominance threshold is appropriate for agreements between non-competitors. Consistency with the vertical restraints block exemption is appropriate in relation to restraints not related to the exploitation of the IPRs. As further discussed below, we urge the Commission to take a more liberal approach to no challenge and grant-back clauses.

The Commission proposes to exclude from a revised block exemption, license agreements where the licensor is dominant. Accompanying guidelines would identify licensing situations which do not fall under Article 81(1). The EU Committee strongly urges the Commission to circulate draft Guidelines at the same time as a draft regulation so as to encourage an informed debate on the entirety of the proposed new approach.

Dominant companies ought to be free to avail themselves of the general rules embodied in a revised block exemption. Otherwise, they can be expected to exploit their technology themselves rather than engage in licensing with the risk of challenge, fines, etc., especially given the additional uncertainty that is bound to prevail in the envisaged decentralised enforcement system. As dominant companies are frequently highly innovative, due to their resource base, their exclusion from a revised block exemption would be directly counter to the facilitation of technology transfer in the EU.

2.2 Licenses between Competitors

The Evaluation Report notes that agreements between competitors can result in a cartel-like allocation of markets or customers, especially where an exclusive license is reciprocal or extends to non-licensed competing products. Consequently, the Commission envisages a regime along the following lines:

- Ø a new block exemption would be applicable up to a market share threshold of 25%

- Ø a broader list of hard-core prohibited restraints would include price-fixing, limitation of output or sales, and the allocation of territories or customers.

2.2.1 Definition of "Competitors"

The Commission is proposing to introduce a "more realistic" definition of competitors so that parties to a license will be regarded as being in a vertical relationship, and hence subject to the more generous rules for non-competitors, where:

- the licensor does not exploit the technology itself (i.e., the licensor is only present on the relevant technology market and the licensee is not present on that market)
- the licensor is present on both the technology and product markets, but the licensee is present on neither
- the licensor and licensee produce competing products but the licensed manufacturing process or patented product is such a sweeping breakthrough that there would no longer be any competition between the parties absent the license
- IPRs owned by the licensor and licensee are in a mutually blocking position.

The last two scenarios are viewed as horizontal relationships under the current TTBE.

A narrower definition of "competitors" is appropriate. We would however welcome further guidance and practical examples on what the Commission considers would be a "sweeping breakthrough" or a "mutually blocking position". A great many patents concern incremental improvements to existing products/technologies; presumably improvements made by a licensee in an otherwise vertical agreement will not re-qualify that relationship as horizontal. For example, a licensee might suggest improvements to a licensed product in relation to a specific application. The improved product might qualify for patent protection only in relation to that application, perhaps entitling the licensee to joint ownership of the new patent. How would such a relationship be qualified?

2.2.2 25% Market-Share Threshold

Past attempts to introduce market share thresholds in the TTBE have been opposed due to the difficulty in defining the relevant market when it comes to innovation markets. These concerns remain valid today.

In this respect, the Evaluation Report notes that market definition difficulties are unlikely to arise where the IPR concerns only a small improvement on existing technologies or products, since the relevant market will be the existing technology or product markets affected.

However, where the IPR concerns a major improvement or breakthrough on existing technologies or products, the Report merely states that "it has to be investigated" whether the analysis may require the delineation of markets for R&D (innovation markets) and whether other indicators of market power could be used.

A 25% market-share ceiling will inevitably give rise to much legal uncertainty unless the Commission provides very clear guidance on how markets are to be identified and market-share quantified. In technology markets, is market share to be measured as a percentage of total licensing income? How does one measure potential competition? Defining innovation markets often requires evidence that is not in the public domain. These types of issues must be addressed in some detail if a new block exemption regime is to provide sufficient legal certainty as a necessary incentive to license.

2.2.3 Prohibited Restraints

The EU Committee urges the Commission to adopt a more nuanced approach in relation to the restraints that would not be permitted in agreements between competitors. If a licensor falls below the 25% market-share, if the agreement is non-reciprocal, and if the licensee is not restricted in terms of what it can do with its own technology, it is not clear why output restraints and territorial/customer restrictions should be blacklisted. In such circumstances, if licenses between competitors risked giving rise to coordination, for example, in an oligopolistic market, the Commission would be free to withdraw the benefit of the block exemption.

2.3 Multiparty Licenses, Cross-Licensing, Pools and Joint Ventures

Multiparty license programs, pools and license packages are excluded from the TTBE. Yet the Evaluation Report recognizes that they are likely to be pro-competitive when between non-competing undertakings, especially when they cover only essential IPRs.

The Evaluation Report promises a more coherent set of rules distinguishing between such arrangements depending on whether the parties are competitors or non-competitors. However, unfortunately, there is little detail in the Evaluation Report as how to such agreements would be regulated. The EU Committee supports a more generous approach to agreements between non-competitors.

Inclusion of multiparty license agreements in a block exemption will require Council amendment of Regulation 19 which is likely to delay adoption of a new regulation by a year. The alternative is to cover multiparty licenses only in explanatory guidelines. The EU Committee takes the view that the adoption of a new block exemption which no longer contains the artificial constraints that currently act as a disincentive to technology transfer should be an urgent priority. For this reason, the EU Committee would support a block exemption covering only bilateral agreements, provided the Commission were to publish draft Guidelines for consultation well in advance of the new regime's entry into force. The Guidelines should provide for a reasonable level of legal certainty.

In relation to joint ventures between competitors, the TTBE covers licensing up to a 20% market share if the joint venture is limited to production and 10% if it includes distribution. These thresholds are likely to be revised upwards to reflect the higher thresholds of the new specialization and R&D block exemptions and this is welcomed.

2.4 Broader Range of IPRs

A new block exemption could be extended beyond patents and know-how to include other IPRs such as copyright in software and design rights. In particular, the Evaluation Report highlights the current uncertainty surrounding software licenses.

The EU Committee is of the view that a new block exemption could usefully include copyright in software and design rights, for as long as this does not unduly delay the adoption of the new TTBE. We are concerned that any further extension to include copyright in content, trademarks etc. could result in an overly complex block exemption regulation.

3. MARKET SHARE THRESHOLDS

The Evaluation Report is silent on the practical effects of the proposed multiple market share thresholds. Under the new regime, it appears that those drafting and negotiating licences would have to have regard to the following potentially applicable market share thresholds:

10%	-	vertical de minimis
15%	-	horizontal de minimis
20%/25%	-	specialisation/R&D/joint venture licences
25%	-	licences between competitors
30%	-	clauses unrelated to IPR exploitation
dominance	-	no exemption

The EU Committee stresses that the proliferation of market share thresholds which are inherently difficult to apply in any but the most straightforward of cases, significantly reduces clarity and legal certainty and will increase the cost and duration of licensing negotiations.

This may undermine the incentive to innovate and to disseminate innovation which is stated to underlie the review exercise and likely replacement of the existing regime.

4. SPECIFIC RESTRAINTS

4.1 Exclusivity Issues

To the extent that non-exclusive licenses are capable of falling within Article 81(1), they are likely to be included in the scope of a revised block exemption. The EU Committee welcomes this proposal.

The TTBE permits exclusive know-how licenses up to a maximum duration of 10 years, even if the original know-how is improved during this period. The Evaluation Report suggests alignment with the vertical restraints block exemption where ancillary licenses of know-how are exempted without any duration limit. The EU Committee would welcome the deletion of this arbitrary duration limit from the TTBE.

The TTBE permits territorial exclusivity but excludes field of use exclusivity. However, territorial exclusivity coupled with a field of use is permitted. Customer allocation is black-listed in an agreement between competitors, and grey-listed in an agreement between non-competitors. The Evaluation Report recognises that these distinctions are unjustified since exclusivity provisions have similar effects regardless of whether they are linked to a territory, customer group or field of use.

The EU Committee supports the Commission's proposal to include territorial and customer restrictions in agreements between non-competitors within the scope of a new block exemption to the extent they fall within Article 81(1).

The Evaluation Report states that the TTBE does not address foreclosure and interbrand competition problems resulting from exclusive licenses between competitors. The block exemption is likely to be amended to prohibit exclusivity restraints in agreements between competitors. As mentioned at Section 2.2.3 above, the EU Committee urges the Commission to take a more liberal view of such agreements provided certain conditions are met.

4.2 Output Restrictions and Site Licenses

The TTBE permits field of use restraints, "own use licenses" and "second supplier licenses". Quantity restraints are otherwise blacklisted.

The Evaluation Report points out that site licenses are problematic where the license is limited to a plant with a specified nameplate capacity amounting to an output restriction. The Commission asks whether such output restraints should be treated differently depending on whether the agreement is between competitors or not.

Site licenses are a common phenomenon in the petrochemical and refining sectors and are often concluded between competing companies. In industries where the location of sites is regulated by geographical and environmental regulatory factors and where licenses represent long-term commitments and major investments, licensors must be able to continue to impose restrictions in site licenses if this way of doing business is to continue.

See our comments on agreements between competitors at 2.2.3 above.

4.3 Non-Compete Obligations

The TTBE prohibits non-compete obligations, although the licensor may terminate exclusivity and stop licensing improvements to a licensee that begins to compete.

In line with the vertical restraints block exemption, the Evaluation Report contemplates permitting an obligation on the licensee not to use a competing technology or use or sell competing goods in agreements between non-competitors below a 30% market share threshold, except perhaps if the restraint extends to R&D since this would indicate that the parties may in fact be competitors.

The EU Committee welcomes this approach. However, it believes that below a 30% threshold, the non-compete should be valid for the entire term of the license agreement. The limitation at Article 5(a) of the vertical restraints block exemption which requires a non-compete obligation to be expressly renewed every 5 years, would not be appropriate in a licensing context.

4.4 Tying

The TTBE grey-lists tying unless it is necessary for a technically proper exploitation of the licensed technology.

The vertical restraints block exemption permits tying up to a threshold of 30%. The Commission asks for comments on whether this approach would also be appropriate in the context of a revised TTBE.

The EU Committee is of the view that an approach in line with the vertical restraints block exemption is appropriate.

4.5 Grant-Backs

The TTBE excludes non-reciprocal or exclusive grantbacks for severable improvements. The Evaluation Report queries whether it is necessary to exclude non-reciprocal and certain exclusive obligations from a new block exemption.

The EU Committee is of the view that where a licensor's technology has multiple uses and is licensed to multiple licensees for exploitation in separate fields of use, the licensor's management of such licenses – and the dissemination of improvements to licensees – would be greatly facilitated if improvements were assigned to the licensor. At the very least, the licensor should be able to require the licensee to grant it a non-reciprocal exclusive license for non-severable improvements for an unlimited period in time, and non-reciprocal but non-exclusive license for severable improvements.

4.6 No-Challenge Clauses

No challenge clauses are currently grey-listed, although termination is possible if the licensee challenges the validity of the licensed IPRs. The recent R&D block exemption also excludes no-challenge clauses from its scope but also allows for termination in the event of challenge.

The Evaluation Report recognizes that no challenge clauses can facilitate the dissemination of technology, especially where the licensor is the smaller party and fears that the licensee would challenge the validity of its patent or the confidentiality of its know-how once divulged.

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The EU Committee is of the view that no-challenge clauses would give smaller licensors a greater level of comfort and could contribute to the greater dissemination of new technologies. Below a dominance level, such restriction should be permitted.

This appears to be in line with the U.S. licensing guidelines which recognise that the fact that IPRs may in some cases be misappropriated more easily then other forms of property may justify the use of some restrictions that may be anti-competitive in other contexts.

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The EU Committee welcomes the Evaluation Report and looks forward to a continued dialogue with the Commission on the form and scope of a new licensing regime.

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The EU Committee of the American Chamber of Commerce is keen to contribute to a constructive dialogue on this important issue. We would be delighted to provide additional material should you require any clarification or further information. The EU Committee is the key organization in Europe representing the views of European companies of American parentage. Its member companies are drawn from a broad cross-section of the European business community and typically are present in most Member States of the European Union

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