World Competition **26(4)**: 541–565, 2003.
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The Proposed New Technology Transfer Block Exemption

Is Europe really better off than with the current regulation?

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This article discusses the legal and economic foundations, as well as the practical implications of the Commission's proposal for a new technology transfer block exemption regulation ("TTBER") and associated Guidelines.

The article concludes that the new TTBER brings desirable flexibility to the assessment of the competitive effects of technology licensing agreements by abolishing the current division of the clauses into four categories of exempted, white, black and grey clauses. The Commission's proposal is also praised for extending the scope of the Regulation to software copyright licences and for exempting some efficiency-enhancing restrictions that currently fall outside of the TTBER. The article, however, adopts a critical stand towards market share ceilings that the new TTBER introduces and criticises the overly stringent approach that the Commission adopts towards licensing between competitors. Finally, the article discusses some implications of the tightening of the rules on territorial restrictions. The article suggests alternatives, which, according to the authors, would lead to a more effective regulatory framework and to more efficient dissemination of new technologies.

The Commission has adopted block exemption regulations for technology licensing to facilitate dissemination of knowledge and maximise the benefits of innovations. The idea behind the block exemption is to automatically exempt certain types of agreements from the scope of Article 81(1) of the EC Treaty, without the need to individually examine the anti- and pro-competitive effects of the restrictive agreement.[1] Licensing agreements that fall within the scope of the block exemption are generally considered to fulfil the criteria set out in Article 81(3) EC and thus regarded as compatible with EC competition law.[2] This is particularly useful with the advent of "modernised" EC competition law, since it will facilitate the tasks of counsel, courts and national competition authorities, which will have to apply Article 81(3) EC directly.

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[1] Article 81(1) of the EC Treaty prohibits agreements between undertakings, if the agreements have the object or effect of restricting competition to an appreciable extent and have, or are likely to have, an effect on trade between EC Member States. The restrictions of competition contained in such agreements are null and void and may give rise to fines, unless (i) they are covered by one of the "block exemption regulations" which automatically exempt certain types of agreements; or (ii) they are notified to and individually exempted by the EC Commission pursuant to Article 81(3) EC. The latter option will fall away as of 1 May 2004, when EC competition law is "modernised". See Regulation 1/2003, [2003] OJ 1/1, 4.1.2003.

[2] In order to qualify for application of Article 81(3) EC, the agreement must be shown to (i) improve the production or distribution; (ii) allow consumers a fair share of the resulting benefits; (iii) not to impose restrictions on the parties that are not indispensable to achieve such benefits; and (iv) not to eliminate competition in the relevant market to a substantial extent.

This article analyses the proposal for a new TTBER, including the proposal to liberalise the exemption, impose market share ceilings, tighten the rules for licensing between competitors, ban certain territorial restrictions that are currently allowed (almost harmonising the TTBER with the Vertical Restraints Block Exemption), and cover software licensing. Although the Commission can be commended for its careful thinking, there is concern that it is inefficient to expand the blacklist and ban certain territorial restrictions just when 10 new Member States join, that the market share ceilings reduce legal certainty because they are too difficult to apply and arguably irrelevant, and that "blacklisting" certain clauses in horizontal licences (such as reciprocal field of use licences) may be unnecessarily restrictive.

I. Background

A. Pro-competitive aspects of technology licensing

Technology licensing contributes to economic development by disseminating innovations and encouraging new entry. This generally leads to more efficient exploitation of the intellectual property. The owner of the intellectual property (IP) may not be able to make the necessary investments to realise the full value of the IP without entering into a licensing agreement with another company possessing complementary assets or capabilities. Licensing also increases the value of IP to consumers (through reduction of costs and introduction of incremental improvements) and to the developers of new technology (by potentially increasing the expected returns from IP).[3] Consequently, intellectual property right (IPR) owners should generally be encouraged (but not forced) to license. This applies also to the cross-licensing between competitors.

It is well recognised that restrictions in the technology licences are in many cases justified to protect the investment of the licensee and prevent free-riding. The different forms of exclusivity (such as territorial restrictions) are examples of provisions designed to increase the incentives of the licensee to invest in the commercialisation and distribution of products embodying the licensed IP.[4]

Restrictions on the licensee may also be reasonably necessary to protect the interests of the licensor (such as field of use limitations). A licence imposing restrictions on the use of the technology is often better than no licence at all, and the ability to include restrictions may be necessary to induce the licensor to disseminate its technology in the first place.

[3] See Annex to the United States Federal Trade Commission and Department of Justice submissions: *Antitrust guidelines for the licensing of intellectual property*, in: *Competition Policy and Innovation*, OECD publication, DAFFE/CLP(98)18, p. 247.

[4] Id.

Restrictions must, however, not go so far as to raise competition concerns. For example, a licensing agreement that divides markets among firms that would have competed on the market using different technologies if no licence had been granted is likely to have anti-competitive effects. A licensing agreement between competitors has the potential to restrict competition by facilitating coordination between them and leading to, e.g. increased prices or reduced output levels.[5] These are examples of situations where competition policy should intervene.[6]

B. STRIKING THE BALANCE BETWEEN EFFECTIVE IP PROTECTION AND COMPETITION

It is now widely recognised that the goals of competition policy, promotion of innovation and intellectual property laws are complementary and mutually reinforcing.[7] All three serve to benefit consumer welfare and an efficient allocation of economic resources.[8] Competition laws are designed to protect competition as the driving force of efficient markets and innovation (indirectly contributing to political freedom and integration). Efficient competition ensures that consumers can benefit from the best quality products at the lowest prices.[9] Intellectual Property Rights ("IPRs") are aimed at creating an incentive to engage in research and development by ensuring a sufficient reward for the innovator.[10] The complementary role of competition laws and IPRs is also recognised in the draft *Guidelines*.[11] In addition, European competition policy is concerned with European integration. This is in contrast to US antitrust law, which concentrates on pure economic assessment.

The new regulation should strike a delicate balance between granting rights broad enough to create incentives for innovation, but at the same time not so broad as to hamper further improvements by competitors.[12] In particular, the TTBER should not be used to correct perceived deficiencies in IP law. New IPRs have been created and are being proposed to address technical and economic developments (e.g. software copyright, software patents, business patents, *sui generis* database rights, semiconductor

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[5] See ibid, at pp. 247-248.

[6] Further examples include e.g. using licensing to leverage IPR to create an advantage outside of the market where the innovation took place, requiring royalty payments for a term that exceeds the life of a patent or in some situations including a provision in the licensing agreement that prohibits a licensee from challenging the validity of a patent. See *Competition Policy and Innovation*, as note 3 above, at p. 9.

[7] See *Commission Evaluation Report on the Transfer of Technology Block Exemption Regulation No. 240/96—Technology Transfer Agreements under Article 81* ("*TTBER Evaluation Report*"), pp. 10-11.

[8] *Competition policy and innovation*, as note 3 above, at p. 7.

[9] K. Mehta and L. Peeperkorn, *Licensing of Intellectual Property under EU Competition Rules: the Review of the Technology Transfer Block Exemption Regulation*, Statement to the FTC/DOJ Hearings on Competition and Intellectual Property Law and Policy in Knowledge-Based Economy, Washington, 22 May 2002, Comparative Law Topics, Session 2: Licensing of Intellectual Property in other Jurisdictions, at p.4.

[10] Id.

[11] See the draft *Guidelines on the Application of Article 81 of the EC Treaty to Technology Transfer Agreements* (the "draft *Guidelines*"), OJ 2003 C 235/17, at para. 7: "both intellectual property rights and competition are necessary to promote innovation and ensure a competitive exploitation thereof."

[12] See Tom Willard, *Summary*, in: *Competition policy and innovation*, as note 3 above, at p. 455. For examples of limitations in IP protection, see *TTBER Evaluation Report*, as note 7 above, at p. 11, para. 30.

topography rights, rental and lending rights, satellite broadcasting rights, etc.). On the negative side, patent bodies especially in the US, do not properly review patent applications, resulting in the grant of patents for undeserving claims as absurd as the "method of swinging sideways on a swing". Finding the right balance for new IPRs and correcting problems with existing ones is the task of the legislature. Nor should the TTBER be geared to correcting *ad hoc* abuses that can be addressed otherwise.[13] It is true that firms have discovered opportunities such as "patent mining" (systematic review of a firm's activities to file patents for every conceivable innovation, which arguably affects innovation negatively), creation of "patent thickets" (a tangle of overlapping patent claims that is too expensive to cut through, foreclosing competition) or "patent floods". In the context of standards, a few firms have been tempted to set "patent traps" that snap shut when the standard is adopted, to extract royalties from implementers. These problems should be solved by *ad hoc* application of competition law.[14]

Thus, the new TTBER ought to recognise that the growth of importance of IP reflects not systematic abuse, but the fact that our society is becoming more innovation-oriented and more dependent on adding "non-material" value to products and services. Also, technology is becoming more complex, as the pace and cost of development increase.[15] Consequently, we should ensure that the TTBER strikes a balance rather than a blow to the heart of IPRs.

C. IS IP LIKE ANY OTHER PROPERTY?

It has been suggested that for the purpose of the competition analysis, intellectual property ought to be treated like any other property.[16] In our view, however, competition analysis should not disregard some important characteristics of the IPRs that distinguish licences from ordinary vertical agreements such as distribution of physical products:

- The fixed costs of IP development are often greater than the fixed costs sunk by a producer of physical products. To maintain the incentive to invest, the new TTBER should exempt restrictions reasonably necessary to allow the licensor to recover future fixed costs to be sunk in R&D. This is especially relevant for new-economy technologies, which change rapidly and whose product life cycles are short.

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[13] See *TTBER Evaluation Report*, as note 7 above, at para. 58, "If it is assumed that IPR laws are striking the right balance between over- and under-protection of innovators' efforts, such approach [allowing broad freedom for licences between non-competitors] helps to stimulate innovation. *The assumption may however not be correct for all cases*." (emphasis added).

[14] See e.g. Carl Shapiro, *Navigating the patent thicket: cross-licences, patent pools, and standard-setting*, available at <http://faculty.haas.berkeley.edu/shapiro/thicket.pdf>. On standards abuses, see also, Dolmans, *Standards for Standards*, 26 Fordham International Law Journal 1 (2002).

[15] Even the open source community, which often rails against IP, needs IP for its very existence. If no IP protection were available for open source technology, no conditions could be imposed on the GNU licence, and it would not be possible to preserve the integrity of products such as Linux or Java.

[16] Draft *Guidelines*, as note 11 above, at para. 9.

- The risks associated with entering an innovation race are often greater than the risks of manufacturing physical products, especially in markets characterised by network effects before the market has tipped in favour of the IP owner. This argues for allowing the licensor maximum freedom to determine its commercial policy (e.g. by maximum price fixing and ensuring that the licensee concentrates its efforts on development of its core market, if that is needed to reach critical mass quickly).
- Misappropriation of the IPR owner's investment is much easier, calling for greater control over the licensee and over the end-user of products such as software.
- The level of investment required of a licensee may be greater than that of a distributor. This arguably justifies a more liberal approach to intra-technology restrictions than in the Vertical Restraints BER.
- Competition laws ought to promote market structures that do not only benefit consumers through lower prices (emphasis on intra-technology competition) but also through bringing more sophisticated products into the markets.[17] This suggests emphasis on inter-technology competition.

One can question, for these reasons, whether the TTBER should be (to a significant extent) harmonised with the Vertical Restraints BER, as the Commission proposes. The Vertical Restraints BER concentrates on protecting a distributor's investments. A licensee would merit at least equal protection and probably even more. At the same time, however, the Commission should not ignore the R&D investments of a licensor. Consequently, it seems to make sense to allow licensors a greater scope for, for instance, territorial price discrimination than a supplier of physical products, so as to give it an incentive also to license in countries where it can only recover part of its fixed costs. In the end, the consumer in those countries is likely to have greater access to licensed products at a lower price.

II. Reviewing the Current Regulatory Framework for Technology Licensing

Block exemption regulations in the field of technology licensing were first adopted in the mid-80s for patent licensing and know-how licences.[18] These were combined and replaced in 1996 by a unified Technology Transfer Block Exemption Regulation.[19] In December 2001, the Commission adopted a mid-term review followed by a consultation process. This process resulted in a thorough review of the Commission's policies towards technology licensing.

[17] John H. Barton, *Paradigms of intellectual property/competition balances in the information sector*, OECD publication, DAFFE/CLP(98)18, p. 295.

[18] Commission Regulations (EEC) 2349/84 of 23 July 1984, and 556/89 of 30 November 1988.

[19] Commission *Regulation 240/96 on the application of Article 81(3) of the Treaty to certain categories of technology transfer agreements*.

On 1 October 2003, the Commission published a draft for a new TTBER,[20] along with the draft *Guidelines*.[21] The new Regulation will replace the current block exemption and is expected to enter into force on 1 May 2004, at the same time as the accession of new Member States to the EU and the entry into force of Regulation 1/2003 on the Implementation of Article 81 and 82 EC.[22] Until that date, the current block exemption remains in force.[23]

The review of the TTBER forms part of the wider modernisation process including the adoption of the *Vertical Restraints Block Exemption Regulation*,[24] *Guidelines on Horizontal Cooperation Agreements*,[25] Block Exemption Regulations on the applicability of Article 81(3) EC to research and development (R&D)[26] and specialisation agreements,[27] an updated *Notice of Agreements of Minor Importance* (''*De Minimis* Notice''),[28] and finally, *Regulation 1/2003 on the Implementation of Article 81 and 82 EC*.[29] In essence, the idea behind the ongoing reform is to bring the new TTBER into line with this new generation of Regulations and Guidelines, which have moved away from a so-called ''straitjacket'' approach and provided a more flexible analytical framework.[30]

In its Evaluation Report, issued in January 2002, the Commission identified four main categories of concerns concerning the current regulatory framework:

TTBER works as a ''straitjacket''. The old TTBER divides standard clauses in licensing agreements into four categories: (i) exempted clauses; (ii) ''whitelisted clauses'', that generally do not violate Article 81(1) and that can safely be included in the licensing agreement; (iii) ''blacklisted clauses'' that are caught by Article 81(1) and that do not benefit from the block exemption;[31] and finally (iv) ''greylisted clauses'' that are neither exempted nor expressly excluded and the competitive effects of which have to

[20] Draft Commission *Regulation on the Application of Article 81(3) of the Treaty to categories of technology transfer agreements*, OJ 2003 C235/11.

[21] The draft *Guidelines*, as note 11 above, are intended to elaborate the Regulation by providing further guidance on the application of the TTBER and to outline principles for the assessment of technology licences under Article 81 EC in situations where the block exemption does not apply.

[22] This proposed timeframe seems warranted considering that *Regulation 1/2003 on the Implementation of Articles 81 and 82 EC*, which will enter into force on the date of accession of the new Member states into the EU, confers on national courts and authorities increased powers to enforce Articles 81 and 82 EC. One of the objectives behind the reform of the TTBER is to reduce complexity and increase legal certainty, so that national courts and authorities can without difficulty enforce the provisions of the block exemption.

[23] The new TTBER provides for a transitional period for the agreements that have been exempted based on the old TTBER by April 30, 2004. Such agreements continue to benefit from the exemption until 31 October 2005, even if they would not be compatible with the new TTBER.

[24] Commission *Regulation 2790/1999* for vertical agreements.

[25] *Guidelines on the applicability of Article 81 of the EC Treaty to horizontal co-operation agreements*.

[26] Commission *Regulation 2659/2000* for research and development agreements.

[27] Commission *Regulation 2658/2000* for specialisation agreements.

[28] Commission *Notice on agreements of minor importance* which do not appreciably restrict competition under Article 81(1) of the EC Treaty (*de minimis*)

[29] Council *Regulation No 1/2003* on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty.

[30] One of the critical ideas behind the reform was to re-write the TTBER to reflect more sophisticated economic thinking compared to the current BER, which has been criticised as overly formalistic and legalistic.

[31] The inclusion of a ''black clause'' would bring the entire agreement outside the scope of the block exemption.

be analysed case-by-case.[32] This classification of clauses is thought to be formalistic and rigid. This criticism is arguably exaggerated. The TTBER is merely a "safe harbour". It provides useful guidance, but there is no obligation to comply with it. Non-compliant clauses that merit individual exemption can be (and in practice often have been) included.

The TTBER is narrow in scope. The current block exemption is also criticised for being too narrow in scope. It covers only patents (and similar or related IPRs) and know-how, and excludes other IPRs, unless those rights are deemed ancillary to the patent or know-how licence. In a regime where national courts and competition authorities cannot apply Article 81(3) and the Commission adopts very few individual exemptions, this is a problem for licences of copyrights, database rights, trademarks and other IPRs not covered. Further, the old TTBER is limited to agreements between two companies. The Evaluation Report discussed the possibility to extend the scope of the block exemption to multiparty licences and pooling agreements, but the Commission has abandoned this possibility in its new draft.

The TTBER is inconsistent. The existing TTBER has also been criticised for its internal inconsistency. Essentially, the TTBER treats various clauses differently despite their similar effects. Territorial restrictions and customer restrictions, for example, are treated in a different way even though both types of clause serve the purpose of resolving free riding problems, yet have the potential to create foreclosure and market division concerns.

The TTBER is too restrictive. The old TTBER has also been criticised for blacklisting or excluding certain restrictive clauses from the block exemption without valid economic justification. These include, e.g. customer restrictions (blacklisted even though territorial restrictions are partially exempted), non-compete obligations (now considered reasonably necessary to encourage the licensee to dedicate adequate resources to the licensed technology), and tying clauses (which are now considered generally efficiency enhancing if imposed by non-dominant firms).[33]

The TTBER is too liberal? Finally, while regarded as being too restrictive, the existing TTBER is also criticised for exempting agreements containing clauses that according to the Commission might restrict competition. These include (i) ongoing passive sales restrictions protecting territories allocated to other licensees; (ii) active sales restrictions and reciprocal field of use restrictions between competitors; (iii) active sales bans for territories not *exclusively* granted to other licensees; (iv) agreements between parties with a relatively strong market position; and (v) arrangements between competitors, which may cloak collusion.

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[32] For this category of agreements, the TTBER provides for an opposition procedure, whereby the Commission carries out a case-by-case assessment and (within a period of four months) establishes whether the agreement falls within the scope of the TTBER. See Article 4 of the TTBER.

[33] In the old TTBER, tying is subject to opposition procedure and exempted only if tying is considered necessary for technically proper exploitation of the IP or to ensure minimum quality standards.

To an extent, the Commission has succeeded in addressing these concerns and the new TTBER contains some significant improvements compared to its predecessor. Yet the draft—as its stands—arguably contains flaws that would merit reconsideration before the adoption of the new Regulation.

III. Modernisation of the TTBER: What is Going to Change?

A. The most important changes introduced by the new TTBER

The new TTBER will introduce, *inter alia,* the following changes, discussed below in more detail:

- ***Replacing the "straitjacket" with a more flexible framework.*** The new Regulation will no longer contain an exhaustive list of exempted and whitelisted clauses. It will have a limited list of blacklisted and greylisted clauses, while all others will be exempted (including some currently blacklisted clauses);
- ***Extending the scope of the Regulation.*** The new TTBER will be extended to cover software copyright licensing in addition to patent and know-how licences;
- ***Introduction of market share ceilings.*** Agreements between non-competitors will be exempted up to the 30 percent market share ceiling and agreements between competitors up to the 20 percent ceiling.
- ***Treating agreements between competitors more strictly.*** Apart from imposing different market share ceilings, the new TTBER will also impose greater restrictions on licences between competitors than on licences between non-competitors.
- ***Tightening of territorial restrictions.*** Territorial restrictions will only be permitted for exclusively allocated territories, and not exempted between competitors. Bans on passive sales will be further limited.

Even if one agrees that the old TTBER does not provide a sufficiently sophisticated framework for assessing the competitive effects of modern, often complex licensing arrangements, one can doubt that the reform is best carried out by imposing market share ceilings, by tightening some of the rules on territorial restrictions (in particular in horizontal licences even where the licensee is perfectly entitled and able to continue using its own technology), and by imposing greater constraints on the freedom to contract between competitors, as the Commission is proposing. The proposals arguably complicate and restrict the current regulatory framework. This is particularly worrying considering that with modernisation of EC competition rules, national courts will be asked to make difficult economic assessments that they were not expected to make in the past.

IV. Assessment of the Changes Brought About by the New TTBER

This chapter provides an overview of the most significant changes brought about by the new block exemption, namely (i) the replacement of the "straitjacket" with a more flexible and economically oriented framework; (ii) the extension of the scope of the TTBE; (iii) the introduction of market share ceilings; (iv) the more lenient treatment of agreements between non-competitors; (v) tightening of territorial restrictions and (vi) some other changes introduced by the Commission's draft.

A. Replacing the "straitjacket" with a more flexible and economically oriented framework

The current division of the clauses into four categories of exempted, white, black and grey clauses will be reduced to two categories (black and grey).[34] The new TTBER will blacklist certain clauses (Article 4, "hard core restrictions") and completely withhold the block exemption from agreements containing them,[35] and will greylist certain obligations listed in Article 5 (called "conditions"[36]), without withholding the block exemption from the remainder of the agreement. *Guidelines* provide information on exempted and white-listed clauses.[37]

The clauses listed in Article 5 such as non-reciprocal output limitations on a competing licensee, are neither blacklisted nor block exempted. There is no presumption for or against illegality and they require an individual assessment of their pro- and anti-competitive effects. If a greylisted "condition" is found to violate Article 81, it does not prevent the application of the TTBER to the rest of the agreement. Only the clause in question—as opposed to other restrictions—is unenforceable. In other words, the rule of severability applies to restrictions set out in Article 5 but not to restrictions set out in Article 4.[38]

By abolishing the rigid division of clauses into categories of exempted, white, black and grey clauses, the new TTBER brings desirable flexibility to the assessment of the

[34] The Evaluation Reports discussed the possibility of distinguishing between licensing restraints that *relate to the exploitation of the licensed IPR* (e.g. territorial, customer and field of use restraints) and restraints that do *not relate to the exploitation of the licensed IPR* (e.g. non-compete and tying). The Commission did not, however, introduce this distinction into the new TTBER. It is considered difficult to determine whether a restriction actually relates to the use of the licensed IPR. Moreover, such a distinction would add to the formalism of the TTBER, which is exactly what the Commission intends to avoid by the ongoing reform.

[35] The new Article 4 will contain a list of hard-core restraints (such as resale price maintenance or market allocation) and is comparable to the "blacklist" in the old TTBER. If an agreement contains a clause that is categorised as a hard-core restriction, the whole agreement will automatically fall outside the scope of the TTBER.

[36] This is unclear in English, and should probably be called "provisions to be analysed *ad hoc* under Article 81(3) EC".

[37] The elimination of the white list does not necessarily clarify the law. For instance, the uninitiated may read Article 4(2)(b)(ii) as a total prohibition of passive sales bans, even though the *Guidelines* clarify that a passive sales ban may well be permissible. The same applies to Article 4(2)(b) which at first blush does not allow technical field of use and OEM ("captive use") restrictions, which are whitelisted in the *Guidelines* (and in 4(1)(c)(i) and (ii)).

[38] The interplay between the grey and blacklists is not always clear. Article 4(1)(b) might be read to allow non-reciprocal output restrictions on a licensee, whereas Article 5(2) greylists them. It may be useful to insert cross-references.

competitive effects of technology licensing agreements. As a result, companies will be in a position to formulate their licensing agreements to correspond to their commercial needs rather that to the "straitjacket" imposed by the existing regulation.

B. Extending the scope of the regulation

I. Extension to software copyright licences

The current block exemption only covers know-how and patent licences. In the new draft, the Commission proposes to extend the new TTBER to cover also software copyright licences. In its Evaluation Report the Commission also considered the possibility of extending the coverage of the block exemption to other types of IPRs (such as trademark and non-software copyright licences). However, the Commission appears to have largely abandoned these plans. Consequently, the new TTBER will not extend the block exemption to cover other types of IPRs such as non-software copyright or trademark licences. In practice this means that pure trademark and copyright licences, such as merchandising agreements, would be excluded, whereas software copyright licences could benefit from the TTBER.

There are several grounds on which to argue that licences of *sui generis* database rights, merchandise licences, and agreements for the use of non-software copyright and related rights (phonographic producers, performing artists, broadcasters/satellite rights, rental rights), and trademarks should also be covered by the TTBER:

- The rationale for including them (i.e. licence enables licensee to provide services or products to consumers) is the same as for technology transfer.
- There would appear to be no fundamental difference between investment in technological innovation and investment in other IP for which there is consumer demand.
- There is little or no need to adjust provisions for such rights (e.g. provisions mirroring moral rights in copyright law would fall outside Article 81 anyway).
- Licences are often mixed, and it is difficult to determine which IP is ancillary and which is the main object of the agreements.
- The Commission argues that performance copyright licences raise issues other than product copyrights, e.g. because exploitation does not result in exhaustion, but if anything that suggests that the Commission should disapply the blacklist, rather than withholding the block exemption.
- The Commission argues that trademark licences raise issues similar to distribution, without however acknowledging that the Vertical Restraints BER does not apply to trademark licences and that trademarks are essentially goodwill carriers, which are often developed at considerable expense.
- Trademark and merchandise licences would tend to have less impact on competition, since even if they are exclusive, competitors can still market

products with identical functionality. It is ironic to exclude the block exemption for such licences and require *ad hoc* analysis, which imposes greater burdens and risks in the case of litigation.

Despite the differences in the purpose, extent, and duration of protection provided under various IPR regimes, competition assessment and principles governing patent, copyright and trade secret, for example, are often similar.[39] This would justify a simple umbrella block exemption regulation, embracing also merchandise (trademark and copyright) licences and agreements for IPRs other than know-how and patents.

2. Exempting previously excluded or blacklisted clauses that can be considered efficiency enhancing

Efficiency-enhancing restraints that are currently presumed illegal or excluded from the scope of the TTBER without a valid economic justification will be brought within the framework of the block exemption. This includes output restrictions and certain customer restrictions between non-competitors,[40] as well as non-compete and tying clauses between competitors and between non-competitors,[41] and all restrictions not specifically blacklisted or greylisted.

C. INTRODUCING MARKET SHARE CEILINGS

Agreements between competitors can benefit from the block exemption only if the *combined* market share of the parties does not exceed 20 percent, whereas agreements between non-competitors can be block exempted only if the market share of *each* of the parties does not exceed 30 percent.[42] The market share ceilings are low, and the ceiling will be quickly reached. This is true especially between the competitors, whose market

[39] See Annex to the United States Federal Trade Commission and Department of Justice submissions: *Antitrust guidelines for the licensing of intellectual property*, in: *Competition Policy and Innovation*, as note 3 above, at p. 246.

[40] On output restrictions, see draft *Guidelines*, as note 11 above, at para. 165, providing that output restrictions between non-competitors are block exempted up to the market share threshold of 30%, provided that the output of other licensees (or the total output of all licensees) is not limited. Output restrictions between competitors are blacklisted with the exception of non-reciprocal output restrictions imposed on the licensee, which are greylisted (see new Article 4(1)(b) and Article 5(2)). As to customer restrictions between non-competitors, Article 4(2)(b) allows bans on active and passive sales to an exclusive customer group reserved for the *licensor* and active sales bans to customer groups reserved for another *licensee*.

[41] See draft *Guidelines*, as note 11 above, at para. 183 (tying) and para. 189 (non-compete obligations). The TTBER should be tough on restrictions that raise barriers to entry or have an exclusionary effect (such as conduct or clauses preventing a licensee from developing competing technology). This does not mean that, for instance, non-compete clauses should be blacklisted. They may in fact be reasonably necessary in "normal" competitive markets to encourage an adequate exploitation of the licensed technology. Exempting them is appropriate, considering that it is possible to attack sequential monopolists under Article 82 if they try to raise barriers to entry.

[42] The draft *Guidelines* discuss the application of Article 81(1) and (3) to agreements above the ceilings.

shares have to be cumulated and whose market shares are not entitled to exceed the ceiling *either* on a relevant technology market, or on a relevant product market.[43]

One can question whether there is a need to impose market share ceilings in the TTBER when it is already clear that Article 82 EC prevails over any block exemption regulation.[44] Another concern is that market shares are backward-looking, whereas analysis on technology and innovative markets should be forward-looking. Yesterday's high market share may not reflect tomorrow's market power, and may be out of date by the time the market share data are available. What matters is not how many firms currently sell products, but how many firms can challenge the licensor's position.[45]

An alternative would be, for example, the adoption of the "technology centre" approach, modelled according to the US Guidelines.[46] The TTBER should arguably not exempt agreements that reduce the available independent poles of research to a number below 4-5 (taking into account not only incumbents, but also credible new entrants).[47]

Perhaps even more serious is that the application of market share ceilings unduly complicates the block exemption and significantly reduces legal certainty. The calculation of market shares is especially difficult if the definition of the market is uncertain, which is a notorious problem especially for innovative products.[48] The problem is compounded because the Commission proposes to analyse ceilings on at least two markets: (i) the market of the product that will be replaced or improved by the licensed technology, and (ii) the market for the technology in which the licensed technology competes. The definition of relevant product markets is difficult enough for

[43] See Article 3(1) of the new TTBER. Compare with Article 3(2) of the new TTBER, providing that in case of an agreement between non-competitors, the market share ceiling cannot be exceeded on the relevant technology and product market.

[44] See Case T-51/89, *Tetra Pak v. Commission*, 1990 ECR II 390, where the Court held Article 82 EC prevails over a block exemption regulation.

[45] See also Evans and Schmalensee, *Some Economic Aspects of Antitrust Analysis in Dynamically Competitive Industries*, NBER Working Paper 8268, May 2001, p. 20, who forcefully argue that market shares provide no indication of the value of intellectual capital, the quality or popularity of tomorrow's products, or the changing nature of markets where the competition takes place. Incumbents holding significant market shares are more constrained by dynamic competition (as opposed to static competition by actual competitors on the market): what is crucial is the threat that another firm will come up with a drastic innovation challenging the incumbent and causing the demand for the incumbent's product to collapse.

[46] Section 4.3 of the *Guidelines*, as note 11 above, provide:

> "In rule of reason cases, if market share data are unavailable or do not accurately represent competitive significance, the following safety zone criteria will apply. Absent extraordinary circumstances, the Agencies will not challenge a restraint in an intellectual property licensing arrangement that may affect competition in a technology market if (1) the restraint is not facially anticompetitive and (2) there are four or more independently controlled technologies in addition to the technologies controlled by the parties to the licensing arrangement that may be substitutable for the licensed technology at a comparable cost to the user."

Identifying (potentially) competing technologies that are commercially viable is likely to be less difficult than defining relevant markets and calculating shares, especially where the application of the relevant technology is uncertain. The technology centre approach is also more appropriate, as it is forward looking, and concentrates on whether the licensor's position can be contested. See e.g. Maurits Dolmans and Anu Piilola, *The New Technology Transfer Block Exemption—Will the New Block Exemption Balance the Goals of Competition and Innovation?*, in ABA IP Law Newsletter, Volume 21, Number 4, at 32.

[47] This should not be equated with a market share ceiling of 20% to 25%. The number of firms includes not only incumbents, but also credible new entrants, whose market share is small but whose promise is significant.

[48] See e.g. Commission *Notice on Market Definition* (9 December 1997), OJ 1997 C 372.

normal products, but can be very complicated in high-technology industries characterized by a high pace of innovation.

The Commission acknowledges the difficulties in defining technology markets and calculating market shares in those markets. To calculate market shares in technology markets the Commission is planning to use the market shares in the product market as a basis. Technology market share would then be calculated on the basis of sales of products incorporating the relevant technology on downstream product markets.[49] The Commission also proposes to avoid reference to separate "innovation markets" in the TTBER due to the difficulties in defining such markets.[50]

These market share ceilings may, however, still be too difficult for national courts to apply in practice. If the defendant in litigation cannot prove that its share is below the ceiling, the court may ignore the block exemption regulation altogether, forcing a more difficult *ad hoc* analysis (with the defendant bearing the burden of proof). For these reasons, it would arguably be better not to subject the application of the TTBER to the *condition precedent* that market shares remain below the ceilings (which creates the risk that the TTBER will be ignored if the market or market share cannot be proven), but to allow the Commission, national competition authorities and courts to *disapply* the TTBER in cases where there is clear evidence that the market is too concentrated and there are not enough poles of technology to ensure sufficient inter-brand competition (a kind of "condition subsequent" resulting in non-applicability).[51] This should avoid litigation inefficiencies and annulment of agreements that in reality merit exemption.

D. Restrictions on agreements between competitors

The Commission's draft distinguishes between agreements concluded between competitors ("horizontal licences") and between non-competitors ("vertical licences").[52] In addition to subjecting competitors to lower market share ceilings, the new TTBER will adopt a less permissive approach towards territorial restrictions imposed on a licensee competing with the licensor, and ban customer restrictions, output limitations,[53] reciprocal field of use restrictions,[54] and maximum resale price maintenance between

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[49] See Article 3(3) of the draft TTBER and the discussion in the *Guidelines*, paras 17-22. Note that the Commission intends to take into account all sales, irrespective of whether the licensed technology is actually incorporated into the product sold. This means technologies that are only used in-house are also taken into consideration. Compare para. 98 of the Commission *Guidelines on Vertical Restraints*, which takes a different approach in this respect.

[50] See draft *Guidelines*, as note 11 above, at para. 22.

[51] This "condition subsequent" approach could also be based on market shares.

[52] Actual and potential competitors are regarded as "competing undertakings" on the product market, whereas (as is proper) only actual competitors are taken into account on the technology market. See Article 1(1)(h) of the draft TTBER.

[53] Non-reciprocal output limitations imposed on the licensee are, however, greylisted (as opposed to blacklisted) between competitors. See Articles 4(1)(b) and 5(2) of the draft TTBER.

[54] Compare Articles 4(1) and 4(2) of the draft TTBER, and see draft *Guidelines*, as note 11 above, at para. 83. Field of use restrictions between competitors qualify for exemption only if they are non-reciprocal and imposed only on the licensee. Both reciprocal and non-reciprocal field of use restrictions on the licensor will be blacklisted. The draft *Guidelines*, however, provide an important exception: symmetrical field of use restrictions between competitors (i.e. both parties can exploit the licensed technology only within the same field(s) of use) are not

competitors. Licensors are further prevented from restricting the licensee's ability to carry out R&D and exploit its own technology, if they are competitors.[55] Between non-competitors such a restriction is not blacklisted, but requires an individual exemption under Article 5.

At first blush, it makes sense to be more lenient towards licensing agreements between non-competitors as opposed to competitors. There is more scope for negative effect on competition in agreements between actual or potential competitors, which may be used to cloak collusion. Nevertheless, one can query whether there is any risk if the licensee is not barred from using its own technology (and it is in practice not uneconomic to do so), and wants a licence to complement its own technology range, or address demand that it does not fully address without the additional licence. Why should a territorial or customer group sales ban between competitors be considered a hard-core restriction, even though (i) non-reciprocal technical field of use restrictions are allowed; (ii) a licensor may have a reason to withhold a licence from a competitor altogether (even more than from a non-competitor) if he cannot limit the licence to a particular market; and (iii) the licensee is not barred from using its own technology? The Commission has not met the burden of proof that such clauses always restrict competition even in the absence of a ban on using competing technology. It may be that they restrict competition in certain cases or often, but not always. Such clauses between competitors should therefore be greylisted,[56] allowing a case-by-case analysis whether the licensee can still in fact use his own technology outside the licensed area. Moreover, greylisting them increases the chance that if the clause is prohibited, the licence itself could still stand. Blacklisting them may have the perverse effect of eliminating the licence altogether, and may have the effect of discouraging licensing and thereby hindering the dissemination of technology.

The definition of a "competitor". It is not always clear when the parties to a licensing agreement will be regarded as "competitors", especially in circumstances where the licensed process or product presents a sweeping breakthrough or where the IPRs owned by the licensor and the licensee are in mutual blocking position.[57] In general, parties should only be considered competitors if without the licence both—

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cont.
blacklisted. Competitors are hence entitled to cross-licence each other for the same field(s) of use. See draft *Guidelines*, para. 83.

[55] This prohibition does not apply, if the restriction is indispensable to prevent the disclosure of the licensed know-how to third parties. See Article 4(1)(d) of the draft TTBER.

[56] This is the approach the old TTBER takes towards reciprocal (field of use and other) restrictions between competitors (unless the parties to the licensing agreement are not subject to any territorial restrictions, in which case the old TTBER applies).

[57] "Sweeping breakthrough" refers to a situation where parties that compete on existing products will no longer compete on future products as innovation of one of the parties leads to a fundamental breakthrough that has the ability to replace completely the existing products. "Mutual blocking position" refers to a situation where the use of one IPR requires access to another IPR. For example, an improvement on a patented machine can be blocked by the owner of the patent on the machine. See e.g. Annex to the United States Federal Trade Commission and Department of Justice submissions: *Antitrust guidelines for the licensing of intellectual property*, in: *Competition Policy and Innovation*, as note 3 above, at p. 247.

actually or potentially—can be expected to (continue to) produce products that belong to the same market as products incorporating the licensed technology.

Sweeping breakthroughs. In case of a "sweeping breakthrough", the parties compete in the product market but are unlikely to do so in the future because the new product will replace existing products. The Evaluation Report indicated that the Commission was planning to treat the licensor and the licensee as non-competitors if the product in question can be considered to represent a sweeping breakthrough. The *Guidelines* acknowledge that in case of a "drastic" innovation, *in some cases* it *may* be *possible* to conclude that parties are non-competitors. However, if it is not obvious that the licensed technology has the effect of replacing licensee's technology by making it obsolete or uncompetitive *at the time of the conclusion of the agreement*, the parties are regarded as competitors.[58]

This makes sense from the point of view of avoiding collusion between actual competitors. The *Guidelines* might usefully make clear that if the parties have reasonable grounds to think that the technology is a "sweeping breakthrough", but are not certain at the time of signature and nevertheless include clauses that are block exempted only between non-competitors, Article 81(3) could be applied with retroactive effect to avoid claims for damages from third parties during the period before the nature of the technology became clear.

This situation may arise also if the processes or products do not represent sweeping breakthroughs, for instance, in case of firms that currently compete in the same product market, but that dedicate their R&D efforts to creating next-generation products that are not close substitutes.[59] The firms would be likely to be considered competitors under the new TTBER, even though they would not compete in the future product market (as they compete in the relevant product market of the current products).

Blocking patents. The *Guidelines* indicate that the Commission is planning to treat the licensor and licensee as non-competitors on the technology market, if the parties own technologies that are in a one-way or two-way blocking position.[60] This makes sense, as does the Commission's recognition (in spite of the *Bayer/Sullhofer* case) that no-challenge clauses are reasonably necessary for settlement agreements (including reciprocal licences to open up mutually blocking positions) and are therefore generally not caught by Article 81(1).[61] There are two concerns, however.

First, the Commission imposes upon parties the obligation to put forward "convincing evidence" that a blocking position actually exists. Relevant evidence

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[58] See draft *Guidelines*, as note 11 above, at para. 26.

[59] David Encaoua and Abraham Hollander, *Competition policy and innovation*, available at http://www.core.ucl.ac.be/GabsHonor/papers/EncaouaHollander.pdf, p.7.

[60] See draft *Guidelines*, as note 11 above, at para. 25. A one-way blocking position refers to a situation where a technology cannot be exploited without infringing upon another technology, whereas two-way blocking position refers to a situation where the holders of blocking IPRs both need to obtain as licence from one another, as neither technology can be exploited without infringing upon the other technology.

[61] See draft *Guidelines*, as note 11 above, at para. 200.

comprises final court judgments and opinions of independent experts.[62] While it is reasonable to expect that the parties need to put forward evidence on the existence of a blocking position, the evidentiary burden should not be raised so high as in practice to force parties to obtain court decisions on the matter, especially when it is possible to establish the existence of blocking patents by less burdensome means. Such an approach would discourage settlements and lead to wasteful litigation.[63]

Second, and perhaps more troublesome, is that the Commission would limit contractual freedom in cross-licenses of blocking patents on the ground that the Commission "considers it very unlikely that in the absence of any particular restraint the agreement would not have been concluded".[64] There may well be reasons to use a patent to keep a third party out, even if that means that the patentee is itself also temporarily kept out of a market blocked by the third party patent pending litigation. This is true, for instance, if the third party would (if licensed) enter into competition in a market where the patentee is not blocked, if the patent periods are not symmetrical, or because the patentee thinks it can win the case and reap monopoly rent. Increasing the costs and opportunity costs of the licence increases the attractiveness of continuing the litigation in an attempt to exclude the other party altogether.

In sum, treating parties with blocking patents as non-competitors follows a sound economic approach and is consistent with actual market conditions. But for the licence, the parties would not compete. Either both patents survive, or one of them survives, excluding at least one party from the market. In *Odin/Metal Box*, a JV case, the Commission recognised that parties that have mutually blocking know-how should not be regarded as competitors.[65] It heralded that case as a sign of the Commission's practical economic approach, and it would be wrong to deviate from that in the *Guidelines*.

E. Tightening of territorial restrictions

The new TTBER will rebalance territorial restrictions, in some cases increasing contractual freedom, while in other cases reducing it. It will contain a short list of "hardcore clauses" that are seen to be seriously restrictive of competition and that by

[62] See draft *Guidelines*, as note 11 above, at para. 25.

[63] The draft *Guidelines* provide, however, that if the parties are not able to provide convincing evidence of the existence of a blocking position, the Commission assumes that holders of substitutable technologies are *potential* competitors on the technology market. (See draft *Guidelines*, as note 11 above, at para. 25). In practice this means that below the market share ceiling, the parties are not in fact considered competitors, as potential competition is not taken into account on the technology market. (See new Article 1(h)). However, the opposite is true when the ceilings are exceeded. (See para. 66 of the draft *Guidelines*, which provides that above the applicable market share threshold, potential competition is taken into account.)

[64] See draft *Guidelines*, as note 11 above, at para. 196 ff, which appear inconsistent with para. 25.

[65] Case IV/32.009, *Elopak/Metal Box—Odin*, Commission decision of 13 July 1990, paras. 24-25. ("Elopak and Metal Box were not competitors, actual or potential, in the relevant product market ... neither party could in the short term enter the market alone as such entry would require a knowledge of the other party's technology which could not be developed without significant and time-consuming investment. Both Metal Box's and Elopak's experience and resources are necessary to develop the new product which will be a combination of their respective technical and commercial know-how").

definition remove the agreement from the scope of the block exemption. To a significant extent, this black list will be harmonised with the Vertical Restraints BER for agreements between non-competitors and with the Joint R&D and Specialisation BERs for agreements between competitors.

On the one hand, compared to the old regulation, the draft TTBER adopts a more lenient approach towards some territorial restrictions between non-competitors. It no longer imposes time constraints on territorial restrictions in know-how licences (which in the old TTBER could not last longer than 10 years from the date the first licensee placed the licensed product on the market).[66] Also, it is now clearer that licence agreements can impose both active and passive sales bans on licensors (which was slightly less clear under Article 1(1)(2) of the old TTBER) and on licensees to protect territory reserved for the licensor (which, again, was slightly less clear under Article 1(1)(3) of the old TTBER).

On the other hand, the draft TTBER also tightens the rules on territorial restrictions: (a) It permits territorial restrictions only between non-competitors. In agreements between competitors, both passive and active sales bans are prohibited. (b) Active sales bans to protect other licensees elsewhere will be permitted only for territories that are exclusively allocated to other licensees (whereas under the old TTBER they are permitted also if the licensee has, for instance, granted semi-exclusivity or co-marketing agreements in the protected territory).[67]

The elimination of the whitelist could create confusion. Article 4(2)(b)(ii) suggests that passive sales restrictions are prohibited altogether to protect other licensees, although the draft *Guidelines* suggest that they would still be allowed for 2 years in agreements with non-competitors.[68] Moreover, the prohibition of active sales bans to protect other non-exclusive licensees might create the impression that the licensees are entitled to exploit the licences technology outside the territory that is licensed to them. The "reservation of rights" clause in Article 2(1)(14) of the old TTBER was clearer.

Tightening the rules on territorial restrictions in particular between competitors even where the licensee continues to be able to use its own technology (i.e., without a non-compete clause), as the Commission proposes, can have unintended side effects. Licensors may, for example, be reluctant to grant licences in new Member States if they cannot during at least a transitional period ensure that the licensee concentrates its

[66] The new TTBER also eliminates the five-year limit on passive sales bans, which used to expire after five years from the first marketing. The draft *Guidelines* (as note 11 above, at para. 93) appear to allow a passive sales ban guaranteeing each licensee a two-year freedom of intra-technology competition, with the two-year period starting to run from the date each individual licensee first puts the licensed product on the market. This new starting date in the draft *Guidelines* is not a liberalization, since even now, Article 81(1) would presumably not apply to a passive sales ban preventing intra-technology competition within the 2-year period.

[67] Territorial restrictions for exclusively allocated territories in agreements between non-competitors continue to be exempted, when imposed on the licensor (who may be banned from active and passive sales) or on the licensee (who may be banned from active sales to protect other licensees). See new Article 4(2)(b).

[68] See draft *Guidelines*, as note 11 above, at para. 93. The draft *Guidelines* provide that the 2-year time limit is triggered on the date when the product incorporating the licensed technology is first put on the market by the licensee *in question*. The old TTBER allows passive sales for the period of five years from the date when the licensed product ids first put on the market by (*any*) one of the licensees. See current Articles 1(1)(6) and 1(2).

efforts on developing the local markets. If the result of a licence in, say, Poland is that Germany is flooded with cheaper products, the licensor will think twice about granting a Polish licence at a royalty that is appropriate for the Polish market. The effect of tightening the exemption for territorial restrictions may be that fewer licences are granted in the new Member States, or that they are granted against higher royalties than local market conditions would support. This is true especially if royalties form a significant percentage of the final price of the product (e.g. software).[69]

The *US Guidelines for the Licensing of Intellectual Property* ("*US Guidelines*") adopt a lenient approach towards intra-brand restraints in licensing agreements, especially when the licensor and licensee are not competitors.[70] The US agencies "*will not require the owner of intellectual property to create [intrabrand] competition in its own technology*".[71] They take the view that competition concerns generally arise only when the licensing agreement harms competition between companies that would have been competitors in the absence of the licence.[72] If the parties are not actual or potential competitors, the licence creates competition where there was none before, and this is beneficial even if the licence imposes restrictions such as exclusivity. Such restrictions therefore cannot be attacked under US antitrust law (absent foreclosure or unless they facilitate collusion by licensees[73]).

It is submitted that the same approach should apply under EC law. According to the Court of Justice–

> "It is necessary first to consider the precise purpose of the agreement in the economic context ... Where an analysis ... does not reveal the effect on competition to be sufficiently deleterious, the consequences of the agreement should then be considered, and for it to be caught by the prohibition it is then necessary to find that those factors are present which show that competition has in fact been prevented or restricted or distorted to an appreciable extent. The competition must be understood within the actual context *in which it would occur in the absence of the agreement in dispute*." [74]

The guidelines, however, propose an additional test: an objective assessment of "whether a less restrictive agreement would have been concluded" in the absence of the restriction. They therefore impose bans on territorial restrictions between competitors that the old TTBER does not impose. EC competition policy appears to attach greater importance to intra-brand restrictions and territorial restrictions in particular.[75]

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[69] See above, where we argue that a licensee would merit at least equal protection and probably even more than a distributor of a tangible product.

[70] K. Mehta and L. Peeperkorn, as note 9 above, at p. 6.

[71] *Antitrust Guidelines for the Licensing of Intellectual Property*, US Department of Justice and the Federal Trade Commission, April 1995, available at: <http://www.usdoj.gov/atr/public/guidelines/ipguide.htm>, at section 3.1. See also Section 2.3 (example 1) and 3.3.

[72] Ibid, at 2.3 (example 1), 3.1 and 3.3.

[73] Ibid, at section 4.1.1.

[74] Case 56-65, *Société Technique Minière (L.T.M.) v. Maschinenbau Ulm GmbH (M.B.U.),* [1966] ECR English special edition, p. 235 (emphasis added).

[75] *TTBER Evaluation Report*, as note 7 above, at para. 55, p. 17 ("It is considered important to protect intra-brand competition as distribution costs make up a substantial part of the end-price of most products and competition between distributors may help to reduce these costs.").

This approach can be questioned. A clause should be blacklisted only if the Commission has met the burden of proof that the restriction almost always limits competition and the parties would always have entered into a licence even without the restriction. First, an objective assessment of "whether a less restrictive agreement would have been concluded" arguably amounts to speculation and gives the Commission a chance to second-guess the market.[76] It is possible that absent the licence, no agreement would have been concluded at all. Second, while vigorous intra-brand competition may well reduce distribution costs,[77] distribution costs are relatively less significant in highly innovative industries compared to the costs associated with R&D activities. This justified a more liberal approach than in the *Vertical Restraints Block Exemption*. Third, emphasising territorial integration could have unintended side effects. Such side effects are plausible especially if the TTBER is to be tightened precisely when the new Member States join the common market. Territorial restrictions serve not only to protect against free riding, but (especially if high costs are sunk in R&D) also allow the licensor to license its technology in the first place.[78] One can reasonably ask whether the focus of the competition assessment should not shift towards protecting dynamic inter-brand competition especially in innovation industries. One solution may be to greylist territorial restrictions between competitors, and blacklist them only where the territorial restriction is combined with a ban on using competing technology.

F. Other changes introduced by the new TTBE

1. *Re-defining "know-how"*

The draft TTBER brings changes to the definition of "know-how". For the purpose of the application of the TTBER, "know-how" means a body of technical information that is *secret*, *substantial,* and *identified* in any appropriate form. Under the current Regulation, to be substantial, the know-how must include information that is "useful", i.e. know-how must be is capable of improving the competitive position of the licensee.[79] The new TTBER, however, defines substantial as "indispensable" for the manufacture or provision of the contract product.[80]

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[76] Draft *Guidelines*, as note 11 above, at para. 14 (b): "Claims that in the absence of a restriction, the supplier would have resorted to vertical integration are not sufficient. . . . The initial choice to rely on co-operation rather that vertical integration anyhow already generally indicates that vertical integration was not practicable". This can be criticised in that it compares the situation not with that which would have existed in the absence of the restriction (which depends on the parties' assessment of the costs and benefits of the specific restriction and the alternative arrangements), but with what the Commission thinks generally should exist in the absence of the restriction.

[77] This argument is made in defence of focusing on "intra-brand" restrictions by K. Mehta and L. Peeperkorn in: *Licensing of intellectual property under EU competition rules: the review of the technology transfer block exemption regulation*, p. 6.

[78] See also *Joint Comments of the American Bar Association's Section of Antitrust Law, Section of International Law and Practice and Section of Intellectual Property Law on the Commission Evaluation Report on the Transfer of Technology Block Exemption Regulation No. 240/96*, p. 28–29.

[79] See Article 10(3) in the old TTBER.

[80] See Article 1(g) of the new draft TTBER.

A significantly "greater degree of substantiality" is required for know-how agreements to benefit from the new TTBER, if the information in question has to be *indispensable* as opposed to merely *useful*. This may have an effect of narrowing down the scope of the TTBER, without any apparent justification. Why should the block exemption not be available to licences of more efficient know how that is not strictly speaking essential, or the disclosure of which saves substantial lead time? How much lead time is needed before know-how is "indispensable"? How are parties supposed to know whether internal development will in fact result in a viable alternative? In addition, know-how is by definition confidential, and how can parties be certain that know-how is "essential" if they are not aware of future or existing alternatives that might exist elsewhere? Considering that the block exemption will be completely withheld, this criterion is bound to introduce very significant uncertainty, discouraging licensing.

If the Commission actually intends to adopt a stricter approach to know-how licences as the new definition indicates, it should at the very least include clear guidance on the application of this new notion into the *Guidelines*—and it is submitted that its will be difficult and unjustifiable to draw the line there. However, the *Guidelines*—as they stand—contain no information that would clarify the position the Commission intends to take in this respect.

2. *Exemption of grant-back obligations*

A grant back obligation refers to a requirement to assign to the licensor or grant him an exclusive licence to (severable or non-severable) improvements of the licensed technology. The new TTBER will exempt obligations to grant an *exclusive* licence to *non-severable* improvements.[81] It remains unclear why assignments of non-severable improvements (which are greylisted) are treated differently from exclusive grant-back licences of such improvements (which are allowed). Regarding *severable* improvements, an *exclusive* grant back obligation is no longer blacklisted, but requires an individual analysis under Article 5(1)(a). An individual examination is also required for an obligation imposed on the licensee to assign the rights to improvements to the licensor.[82]

Non-exclusive grant back obligation is also covered by the new TTBER when the obligation is *non-reciprocal*, i.e. only imposed on the licensee.[83]

3. *Validity no-challenge clauses continue to require an individual exemption*

Non-challenge clauses are obligations imposed on the licensee requiring them not to challenge the validity of the licensor's IPRs. Validity and essentiality challenge

[81] See Article 5(1)(a) and draft *Guidelines*, as note 11 above, at para. 99.
[82] See new Article 5(1)(b).
[83] See new Articles 5(1)(a) and (b), and draft *Guidelines*, as note 11 above, at para. 99.

clauses will not be blacklisted nor exempted in the new TTBER, but assessed individually under Article 5(1)(c). The licensor is, however, entitled to terminate the licence if the licensee challenges the validity of the licensed IPR.[84] In the current Regulation, no-challenge clauses are greylisted and hence subject to the opposition procedure, without prejudice to the licensor's right to terminate the licence in case the validity is challenged.[85] The draft *Guidelines* now recognise that no-challenge clauses are ancillary to IP litigation settlement agreements, and should therefore be exempted if settlement is designed to end good-faith litigation (i.e. where the IP is not patently invalid).[86]

G. Multiparty licences and patent pools

The old TTBER only regulates bilateral technology transfer agreements. Initially, the Commission considered extending the TTBER to cover multiparty licensing such as patent pools. As the Commission is currently only empowered to regulate *bilateral* technology transfer agreements, the extending of the block exemption to cover multiparty licensing would require authorisation by the Council. The draft TTBER makes clear that the Commission has abandoned the idea of bringing multiparty agreements within the scope of the TTBER. The exclusion of the multiparty licences can be explained, *inter alia*, by following reasons:

- The cooperation of Council and Parliament would be required, and the need for a Council regulation would delay the adoption of the TTBE;
- Multiparty licensing rules in the TTBER would be of limited added value since typically patent pools have high market shares and would fall outside the block exemption;
- Patent pools meeting conditions of recent cases are not caught by Article 81 anyway (if limited to essential and complementary patents, open, non-exclusive, and licensing on fair, reasonable and non-discriminatory ("FRAND") terms)
- Pools not meeting these conditions may lead to foreclosure and facilitate collusion and therefore require *ad hoc* analysis
- An inclusion of multiparty licences would complicate the TTBER.

The Commission addresses technology pools in the draft *Guidelines*.[87] The *Guidelines* provide, for example, that patent pools typically raise no issues if (i) the patents are essential and complementary (as opposed to substitutes), (ii) the licence-in and licence-out are non-exclusive, (iii) access is non-discriminatory, and (iv) the technology is licensed on FRAND terms. The *Guidelines* acknowledge the pro-

[84] See draft *Guidelines*, as note 11 above, at para. 104.
[85] See Article 4(2)(b) in the old TTBER.
[86] See draft *Guidelines*, as note 11 above, at para. 200, and the discussion, above, in connection with blocking patents.
[87] See draft *Guidelines*, as note 11 above, at paras 202–228.

competitive elements of technology pools, e.g. the fact that the creation of a pool allows for one-stop licensing and reduces transaction costs as a result. Technology pools may, however, in some instances be restrictive of competition. The pooling of technologies may reduce competition between parties and (especially when the pool is composed of substitute technologies, which is only rarely allowed) amount to collective tying and to a price fixing cartel. Patent pools also have the potential of foreclosing alternative technologies.

The draft *Guidelines* contain a useful basic framework for the assessment of individual restraints that commonly appear in technology pools. However, the *Guidelines* could also usefully include e.g. the following:[88]

- An indication that the Commission will seek compulsory licence under Article 82 against any firm that sets a patent trap for a standard for instance, if a company has encouraged the development of a standard without disclosing that it owns a patent or other IP right that is essential to the standard.
- Members of a standard setting body contemplating a patent pool should be allowed to engage in price/quality comparisons between technologies that compete for inclusion in the standard.
- In cases where no such *ex ante* competition took place, the members of standard patent pools should not be allowed to obtain injunctions against potential licensees who are willing to license on FRAND terms but dispute that the terms demanded by the pool are FRAND, or dispute the validity or ownership of the patent.
- A generous approach to multiparty licensing is warranted: (i) between non-competitors; (ii) between parties with small market shares; (iii) for a short initial period to facilitate start-up; and (iv) if parties agree to disclose all the relevant technology to third parties and allow open access on a non-discriminatory basis (the open standards approach).

H. Conclusion of the Changes Brought About by the New TTBER

The following chart illustrates the changes that the new block exemption will introduce to the current regulatory framework:

[88] For further discussion and recommendations that could be included in the *Guidelines* to deal with issues such as patent traps and excessive royalties, see Dolmans, as note 14 above, at p. 163.

THE BALANCE

MORE RESTRICTIVE THAN OLD TTBER	NEUTRAL	MORE LIBERAL THAN OLD TTBER
Market share ceilings	White list moved to *Guidelines* (although that reduces clarity in some cases)	Extension to copyright and neighbouring rights for software (but not other IPRs)
Territorial restrictions not exempted between competitors	Elimination of opposition procedure for the grey list	Unlimited (non-exhaustive) list of exempted clauses
Active sales ban only exempted to protect territories *exclusively* allocated to other licensees	No coverage for multiparty agreements and pools	Passive sales ban allowed between non-competitors to protect territories or customers reserved *exclusively* to licensor
Passive sales ban excluded (except between non-competitors to protect territories or customers reserved exclusively for the licensor)	Validity no-challenge clauses continue to require an individual exemption	Elimination of time limits for active sales restrictions in know-how licences between non-competitors
Between competitors, all reciprocal field of use restrictions (except where symmetrical) and non-reciprocal field of use restrictions on the licensor blacklisted (as opposed to greylisted)		Exemption of all non-compete and tying
Second-source limitations between competitors blacklisted		Exemption of customer (active sales) and output restrictions between non-competitors
To be exempted, know-how has to be "indispensable" (as opposed to "useful")		Exemption of grant-back licence obligations (except exclusive grantbacks of severable improvements), even when non-reciprocal
Possibility to withdraw block exemption with general effect in case of parallel networks with more than 50% share		Quantity limitations on non-competing licensee greylisted and no longer blacklisted
More restrictive treatment of cross-licences		

V. Conclusion

A. Benefits brought about by the new TTBER

By abolishing the exhaustive lists of exempted and whitelisted clauses, and introducing a non-exhaustive block exemption, the new TTBER brings flexibility to the assessment of the competitive effects of technology licensing agreements. Broadening the scope of the Regulation to cover software copyright licences is also a

positive (yet arguably insufficient) adjustment to the old TTBER.[89] The new TTBER will also follow a more sound economic approach by exempting some efficiency-enhancing restrictions that currently fall outside of the Regulation, such as non-compete and tying clauses between competitors and non-competitors and customer and output restrictions between non-competitors.

B. The Criticism of the Proposed New TTBERs

1. *The market share ceilings add unnecessary complexity*

Despite the benefits discussed above, the new draft TTBER also contributes to an increasingly complex and restrictive regulatory framework, in particular by imposing market share ceilings and by tightening the rules on territorial restrictions. The inclusion of market share thresholds always requires complex economic assessments. The calculation of market shares is particularly difficult when the definition of market is uncertain or markets are innovative. It is also doubtful whether national courts are capable of making such difficult economic assessments. This contributes to legal uncertainty and thereby compromises one of the central objectives of the reform. In addition, the reliance on market shares is questionable, considering that a high market share in a market characterised by a high pace of innovation may not be at all indicative of actual market power. Instead of imposing market share ceilings as a condition precedent for application of the TTBER, the new TTBER should provide for disapplication of the block exemption if it is proven that there are insufficient poles of research and insufficient inter-brand competition.

2. *The approach towards licences between competitors is unnecessarily stringent*

It makes sense to be more lenient towards licensing agreements between non-competitors as opposed to competitors. However, the Commission has not met the burden of proof that the restrictions in Article 4(1)(c) are always bad for competition. Customer, territorial, and reciprocal field of use restrictions on competitors should be blacklisted only where the licensee also accepts a ban on the use of competing technology. When the licensee is entitled to continue to use its own technology without restriction, they should be greylisted. Further, the market share ceiling of 20 percent is low and easily reached given the accumulation of market shares of competitors.

[89] The Commission could have gone further in expanding the scope of the TTBER. There appears to be no fundamental difference between investment in technological innovation and investment in other IP for which there is consumer demand. This would justify a simple umbrella block exemption regulation, embracing also IPRs other than know-how and patent licences currently covered by TTBER, and software copyright licences, as envisioned in the draft TTBER.

3. Tightening rules on territorial restrictions may backfire

Licensors ought to be entitled to price discriminate between territories, irrespective of whether the territory is exclusively allocated to the licensor or to a licensee. Otherwise they may be reluctant to license in Member States where prices are low, or refuse to lower royalties to a level that the local market can bear. This is particularly relevant with the accession of new Member States. The Commission's proposals to exclude active and passive sales bans completely between competitors (even in unilateral licences where the licensee can continue using its own technology), to reduce the duration of passive sales bans between non-competitors, and to allow active sales bans only into territories exclusively licensed to other licensees, could backfire. They make it more difficult for licensors to recover fixed costs of R&D. The result could be reduced licensing in the new Member States, or an increase of royalties from the current to the Western-European level. This is another reason to greylist the restrictions in Article 4(1)(c) where the licensee continues to use its own technology.

The new TTBER should reflect the fundamental premise that, as a general rule, IPR owners should be encouraged but not forced to license. A licence imposing restrictions to the use of the licence is better than no licence at all, and the ability to include restrictions may be necessary to induce the licensor to disseminate its technology in the first place.