LICENSING (TECHNOLOGY TRANSFER): COMMISSION REPORT

Subject: Licensing
Patent licensing
Know-how licensing
Intellectual property

Industry: All industries

Source: Commission Statement IP/02/14, dated 7 January 2002

(Note. This is a timely report on the effectiveness of the Block Exemption Regulation governing technology licensing agreements. The Regulation represented an advance on its predecessor, in that it extended the scope of the exemption to mixed intellectual property licenses. But it did not go far enough. In addition, it reflected an approach to licensing bases on somewhat formal views on competition policy and not sufficiently on economic considerations. It is a complex Regulation; and some of its provisions are manifestly extraneous to the process of licensing as such. The Commission's report recognizes these limitations and invites comments on the possible ways of improving the scope and content of the Regulation.)

Evaluation of the Regulation

The Commission has adopted a report evaluating the functioning of Regulation EC/240/96, which sets out the competition rules for the application of Article 81(3) to technology transfer agreements. This is an important policy area, as the economic development of the Community and its ability to draw abreast of its competitors in the rest of the world depend on the capacity of industry to devise new technologies and to disseminate them on a large scale. Competition is one of the main driving forces of innovation; and it is therefore important to find the right balance between protecting competition and protecting intellectual property rights. The evaluation report adopted by the Commission raises issues such as the treatment of software licensing agreements and licensing pools which have become increasingly important for the development and dissemination of new technologies. In its report the Commission is asking for comments on its competition policy approach to licensing agreements. After discussion on the report with industry, consumer associations and other interested parties the Commission may propose new competition rules for the application of Article 81 to licensing agreements in the second half of the year 2002.

Article 81(1) of the EC Treaty prohibits agreements which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market. Under Article 81(3) an anti-competitive agreement may be exempted from the prohibition of Article 81(1) if the positive effects brought about by the agreement outweigh its negative effects. The Commission can block exempt categories of agreements of

the same nature and has done so in 1996 for certain licensing agreements by adopting the technology transfer block exemption Regulation 240/96 (hereafter the TTBE) which covers the licensing of patent and know-how rights.

The report provides a critical analysis of the application and the policy approach underpinning the TTBE. It discusses the problems arising in the context of licences of intellectual property rights (hereafter IPRs) and acknowledges the complementary role of competition and innovation policies. It also contains a comparison between the competition policy approach to licensing of IPRs in the Community and in the US. It stresses the need to adapt the TTBE to ensure consistency with the new Commission block exemptions concerning distribution agreements, as well as R&D and specialisation agreements. Both of which are based on a more economic approach.

Basic findings of the Report

Before adopting its report, the Commission carried out a preliminary fact-finding that has shown that industry would be favourable to a review of the TTBE and insists on the need to proceed with a simplification and clarification of the current rules. The report finds that the TTBE uses criteria relating more to the form of the agreement than the actual effects on the market. The TTBE has in fact four main shortcomings. Firstly, the TTBE is too prescriptive and seems to work as a straitjacket, which may discourage efficient transactions and hamper dissemination of new technologies. Secondly, the TTBE only covers certain patent and know-how licensing agreements. This narrow scope of application of the TTBE seems increasingly inadequate to deal with the complexity of modern licensing arrangements, such as pooling arrangements, software licenses involving copyright and so on. Thirdly, a number of restraints are currently presumed illegal or excluded from the block exemption without a good economic justification. This concerns in particular certain restrictions extending beyond the scope of the licensed IPR (for example, non-compete obligations and tying). In terms of economic analysis, such restraints may be efficiency enhancing or anti-competitive depending on the competitive relationship between the parties, the market structure and the parties' market power. Fourthly, by concentrating on the form of the agreement the TTBE extends the benefit of the block exemption to situations which cannot always be presumed to fulfil the conditions of Article 81(3), either because the contracting parties are competitors or because they hold a strong position on the market. For instance, the grant of an exclusive license can have serious foreclosure effects when an exclusive license granted to a dominant producer prevents other companies gaining access to technology that might foster their market entry.

Some issues for discussion

The report invites comments on a number of issues. One is the question whether the scope of the TTBE, which applies only to patents and know-how should be widened to cover also copyright, design rights and trademarks. This issue is of particular importance for a number of sectors, including the software industry,

which depends upon a chain of copyright licences for manufacture and distribution.

A second question is whether the TTBE should also cover licensing agreements between more than two companies such as licensing pools. Such arrangements have become increasingly important for industry, given the growing complexity of new technologies. In this respect, it can be observed that multi-party licences may be efficiency enhancing and pro-competitive, in particular where without all the patents contributed to the pool the exploitation of the new technology would not be possible. However, multi-party licenses may also have serious anti-competitive effects, especially when the agreement covers competitive technologies or where it requires the members to grant licences to each other for current and future technology at minimal cost or on an exclusive basis. In such circumstances, multiparty agreements may disguise a cartel, lead to foreclosure or reduce the parties' incentives to engage in R&D thereby delaying innovation.

A third question concerns the possibility of a more lenient approach to licensing agreements between non-competitors. It is generally acknowledged that if the parties to an agreement are in a vertical relationship, and are therefore not competitors, exclusive licences are generally efficiency enhancing and pro-competitive. For instance, if the IPR holder does not have the assets for the production or distribution of the licensed products, it is more efficient to license to someone who does have these assets. The exclusivity may be necessary to protect the licensee against free riding on his investments or to create the necessary incentives for both parties to invest in further improvements.

A fourth question concerns the possibility of a more prudent approach to licensing agreements between competitors. Agreements between competitors may give rise to a number of competition concerns if the licence prevents competition that could have taken place between the licensor and the licensee absent the licence. On the one hand, exclusive licences will often lead to market sharing through the allocation of territories or customers, especially when the licence is reciprocal or the exclusivity extends also into non-licensed competing products. Production quotas agreed in licensing agreements between competitors may easily lead to a straightforward output restriction. On the other hand, under certain conditions, in particular in the case of licensing to a joint venture and in case of non-reciprocal licensing, the exclusivity may not only lead to a loss of inter-brand competition but also to efficiencies. To assess whether the negative effects on competition may be outweighed by the efficiencies, the market power of the parties and the structure of the markets affected by the agreement need to be taken into account.

Publication of the Report

The report will be published and is already available on the internet, as follows.
http://europa.eu.int/comm/competition/antitrust/technology_transfer/
Comments on the report have to be sent to the Commission by 26 April 2002. ■