

# The New European Union Technology Transfer Block Exemption



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New rules now apply to patent and knowhow licensing in the European Union. On January 31, 1996, the European Commission issued a "Technology Transfer Block Exemption," which is a Regulation granting a block exemption from Article 85 of the Treaty of Rome for certain categories of technology transfer agreements. The Technology Transfer Block Exemption took effect on April 1, 1996.

This Block Exemption replaces and consolidates the formerly separate block exemptions for patent licensing and knowhow licensing, including agreements containing mixed or ancillary intellectual property rights. (There is no block exemption covering pure copyright licenses, but the Technology Transfer Block Exemption can be a source of authority by analogy so long as unique aspects of copyright law are taken into account.) The Technology Transfer Block Exemption makes important changes in EU competition law and, for various reasons, is a far more significant document than the analogous Intellectual Property Licensing Guidelines recently issued by the U.S. Department of Justice and the Federal Trade Commission. In addition, several critical differences with U.S. law remain.

A block exemption is a less-than-perfect solution to an intractable problem posed by EU competition law. The problem is that Article 85(1) — one of the two main provisions of EU competition law — is applied very broadly and covers many types of agreements that merely restrict the eco-

nomie freedom of the parties even if they are procompetitive. Generally speaking, such an agreement is null and void and can subject the parties to fines unless it is notified to the European Commission and found to:

- improve the production or distribution of goods or promote technical or economic progress;
- accord consumers a fair share of the benefits;
- be indispensable to the accomplishment of these goals; and
- raise no possibility of eliminating substantial competition.

Notification to the Commission is an expensive and time-consuming procedure that is simply not a viable alternative for many licensing transactions.

The Commission issues block exemptions in order to define certain categories of agreements that are exempt without individual notification. The Commission has issued block exemptions covering, among other subjects, exclusive distribution, exclusive purchasing and franchising.

In general, the Technology Transfer Block Exemption's changes reflect a more lenient approach toward numerous clauses traditionally viewed as raising EU competition law issues. The types of clauses addressed by the Block Exemption can be broken down into four color-coded categories, e.g., white = permissible, black = prohibited.

1. *The "White" List* includes clauses that generally fall under Article 85(1) but that are exempted by the Block Exemption. Significant examples of permissible clauses include restrictions:

- on the licensor's ability to license or exploit the technology within the licensee's territory;
- on the licensee's ability either to exploit the technology within the

licensor's territory or to manufacture or use the licensed product or process within territories licensed to others;

- on the licensee's ability to pursue an active marketing policy in other territories; and
- on the licensee's ability to accept unsolicited orders from other territories.

The permissible duration for each type of clause is either five years, ten years or the life of a licensed patent, depending upon the clause and the mix of intellectual property involved. There are many other clauses on the White List.

2. *The "Whiter than White" List* includes clauses that generally do not fall under Article 85(1), but that would be exempted if they did so in a particular situation. Some of the more significant examples on this nonexhaustive list include:

- grantback requirements that are mutual and non-exclusive (unless improvements are not severable from the basic technology);
- minimum quality specifications, including requiring the purchase of additional goods necessary for the proper exploitation of the licensed technology;
- royalty payment schedules extending beyond the duration of the licensed property where necessary to facilitate payment;
- field of use restrictions;
- minimum royalty or quantity requirements;
- most-favored-nations clauses; and
- rights to terminate in the event of a challenge to patent validity or knowhow substantiality and necessity of use.

Many other clauses are actually (and potentially) on this list.

3. *The "Black" List* includes clauses that preclude the application of the Block Exemption to the entire agreement. This list was reduced substantially by the new Block Exemption. The remaining prohibited clauses are:

- pricing restrictions;

- direct restrictions on competition other than those otherwise exempted;
- requirements, without objective justification, that a party refuse to fill orders placed within a territory by customers who would market the product in other EU territories;
- requirements, without objective justification, that a party make it difficult for customers to obtain goods from other territories;
- customer restrictions within the same field of use where the parties were competitors prior to entering the license;
- maximum quantity restrictions, except under very limited circumstances;
- grantback assignment requirements; and
- exclusivity provisions exceeding the permissible duration set forth on the White List.

4. *The “Gray” List* includes clauses generally restrictive of competition but that might be exempted upon notification to the Commission. Examples include:

- the tying of unnecessary goods and services; and
- outright prohibition of challenges to patent validity or knowhow secrecy and substantiality.

The Block Exemption does not apply to several categories of licenses. Two examples are reciprocal licenses between competitors and patent or knowhow pools, unless there are no territorial restrictions within the European Union. Another is an agreement between competitors holding interests in a joint venture (or between one of them and the joint venture), unless the combined market shares are not more than 20 percent in the case of a production license or 10 percent in the case of a production and distribution license.

Agreements with potentially restrictive clauses (not on the Black List) may be notified and deemed to be covered if the Commission expresses no opposition within four months (down from six months). This procedure is far less costly than individual notification but only time will tell whether it is a significant option for many transactions, and whether the Commission will be flexible in its approach or adequately take individual circumstances into account.

Parties engaged in licensing transactions involving high market shares must be wary for other reasons as well. Most significantly, the Technology Transfer Block Exemption only applies to Article 85, and does not provide an exemption from Article 86 — the second main provision of EU competition law. Article 86 prohibits the abuse of a dominant position. Firms have been found to be dominant with market shares as low as 40 percent, and a wide range of business

practices and contractual provisions have been found to be abusive.

The Technology Transfer Block Exemption may be withdrawn where a strong market position threatens competition and the Commission will carefully scrutinize agreements involving more than 40 percent of the relevant market. (The Block Exemption also might be withdrawn for refusal to sell into other territories, or to customers who would do so, without objectively justified reasons.) Fortunately, the Commission dropped a controversial proposal to automatically deny the benefit of the Block Exemption if the combined market share of the parties was above 40 percent. The Commission nonetheless recommends notification for exclusive licenses involving market shares in excess of 40 percent.

In sum, the Technology Transfer Block Exemption is, at best, only a mixed success. On the one hand, it eliminates former inconsistencies in the patent and knowhow licensing block exemptions, provides greater certainty as to the enforceability of certain clauses and liberalizes the EU Commission’s approach in key areas. On the other hand, it preserves the Commission’s rigid approach to certain clauses and offers only limited alternatives for testing their enforceability in the context of particular licensing transactions. Thus, parties engaged in licensing transactions in the European Union will have to carefully scrutinize their agreements under EU competition law. 