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New Technology Transfer Agreements Regime to kick in from 1 May: caution needed for the few areas that have changed

After two public consultations in 2011 and 2013, and reportedly much internal debate, the European Commission's new regime for the assessment of technology transfer agreements under EU competition law, which was adopted last month, will enter into force on 1 May 2014. As a reminder, these agreements involve the licensing of technology (e.g. patents, know-how or software) for the production of goods and services, between two or more competing or non-competing parties.

The new Technology Transfer Block Exemption Regulation ("TTBER") and Technology Transfer Agreements Guidelines (the "Guidelines") largely mirror their predecessors and do not bring about many changes compared to the current regime. In particular, the safe harbour is maintained where the parties to the agreement have a combined market share below 30% (for non-competitors) and 20% (for competitors), except where the agreement includes so-called hard-core restrictions. However, there are a few interesting changes. The main ones relate to patent settlements (a controversial extension of the principles applied by the Commission in the pharmaceutical sector), technology pools and the exclusion of certain clauses from the benefit of the block exemption regulation. So there is a certain hardening of the position of the Commission.

Settlement agreements potentially caught by Article 101(1)

In comparison with the 2004 guidelines, the new guidelines introduce several changes to the assessment of settlement agreements. No doubt this responds to the desire to provide support for DG Competition's ("DG Comp") recent monitoring reports and enforcement actions against patent settlement agreements in the pharmaceutical sector. However, the guidelines lack clarity on this issue and appear incoherent with other documents published by DG Comp. They are likely to inject much uncertainty in the resolution of IP disputes.

The new rules on settlements apply across sectors and IP instruments. Any company active in an IP-intensive industry will therefore have to carefully consider the way it settles disputes to avoid antitrust liability and/or seeing its settlement challenged in court by its counterpart on the basis of competition rules.

The guidelines now include a section referring to "pay-for-restriction" or "pay-

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for-delay" settlements, said to consist of settlements based on a "value transfer" from one party in return for a limitation on the entry and/or expansion on the market of another party. The term "value transfer" is not defined and the only available guidance (at least so far) is in DG Comp's monitoring reports on patent settlements in the pharmaceutical sector in Europe.[1] In these reports, "value transfer" is defined – without limitation – as including monetary payments, distribution agreements, side deals in which a commercial benefit is granted to the patent challenger, licences, etc. Such a broad definition makes it particularly difficult to know when an agreement will be tagged "pay-for-restriction or delay" and hence be viewed as potentially anticompetitive.

According to the guidelines, when a settlement including the licensing of a technology right leads to a launch delay or limited ability for the licensee to launch the product, the agreement may be anticompetitive.[2] It is unclear what "limited ability" covers and, again, the only guidance is in DG Comp's patent settlement monitoring reports, which provide that a *licence in itself* limits the ability of the patent challenger to market its product, unless it allows for immediate entry and is royalty-free. A settlement with any other form of licence may therefore be caught by Article 101(1). It is hard to reconcile this conclusion with the statement, three paragraphs above, that settling by means of a licence is generally not caught by Article 101(1) where it is possible that the licensee could be excluded from the market (for example if it loses the litigation)[3] – a statement which makes good sense.

Also worrisome is the treatment of non-challenge clauses in settlement agreements. The 2004 guidelines provided that such clauses were generally considered to fall outside Article 101(1), since it is inherent in settlement agreements that the parties agree not to challenge the IP rights covered by the agreement. The new guidelines confirm this general principle, but go on to add some exceptions to it.

- First, referring to the *AstraZeneca* case[4], the Guidelines indicate that a non-challenge clause may infringe Article 101(1) where the IP right concerned was granted on the basis of incorrect or misleading information (§243). Such an exception may however be difficult to apply in practice: at what point does information become incorrect? Is a declaration that no prior art exists incorrect if prior art is later discovered? This exception would preferably have been limited to situations where the patentee *knowingly* submitted incorrect or misleading information.[5] It is also questionable to transpose the *AstraZeneca* case law, which relates to unilateral conduct under Article 102, to agreements between undertakings. At the very least, if the party challenging the patent does not know that the patent was obtained on the basis of incorrect or misleading information, it should not be exposed to fines even if the agreement is found to be contrary to article 101 by a competition authority. Contractual representations & warranties and indemnity clauses in the settlement agreement will be important to protect the patent challenger against risks of fines and liability in case the patent holder obtained the patent through fraud.

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1 The four reports to date are available here: http://ec.europa.eu/competition/sectors/pharmaceuticals/inquiry/. For an analysis of these reports by White & Case, see: http://www.whitecase.com/alerts-12202013/

2 See Guidelines, para 239.

3 *Ibid*, para 236.

4 Case C-457/10 P, *AstraZeneca v. Commission*, [2012] ECR, not yet published.

5 As was suggested in the public consultation by the American Chamber of Commerce: http://ec.europa.eu/competition/consultations/2013_technology_transfer/amcham_eu_en.pdf

- Second, non-challenge clauses may be scrutinised if the licensor "*besides licensing the technology rights, induces financially or otherwise*, *the licensee to agree not to challenge the validity of the technology rights"*.[6] This exception is of concern, as it is not very clear what provisions in a settlement agreement will be seen as an "inducement" (potentially any concession from the licensor to the licensee can be seen as an inducement). The wording "*besides licensing the technology rights*" was added after the public consultation and seems to indicate that a licence alone will not be viewed as an illegal inducement. This is obviously welcome, as settling a patent dispute by means of a licence is most common and should not be seen as suspect. However, such interpretation cannot fully be reconciled with DG Comp's patent monitoring reports in the pharmaceutical sector which consider a licence *itself* as an inducement/value transfer that could render a non-challenge clause illegal. More clarity on this point would therefore be welcome.

- Third, a non-challenge clause in a settlement agreement will also be scrutinised if the licensed right covers a "necessary input" for the licensee's production.[7] This exception, which was added after the public consultation, seems to imply that the legality of a non-challenge clause will depend on how important the right is for the licensee. This could be worrisome as one may question the usefulness of a settlement that offers no guarantee to the licensor that its IP right will not be challenged the next day. In addition, it opens up the possibility of tricky disputes over whether an IP right is a "necessary input" to the licensee.

Last, one may regret that the Commission does not provide any guidance on the conditions under which a settlement agreement found to be caught by Article 101(1) may satisfy the conditions of Article 101(3).

Overall, whereas the Guidelines repeat that settlements are in principle legitimate, they introduce several exceptions that are unclear and sometimes incoherent with DG Comp's positions in the pharmaceutical sector. This could lead to uncertainty in the settlement of disputes in IP-intensive industries.

Other notable changes

The other notable changes of the new regime are perhaps slightly less controversial, though some might still create problems for businesses in practice.

First, passive sales restrictions between licensees will no longer be covered by the safe harbour of the new TTBER. Under the old rules, the safe harbour was available for an initial period of two years. These restrictions will now need to be assessed on a case-by-case basis. In practice, the removal of the two-year period may have negative repercussions for businesses' incentives to conclude licensing agreements in sectors where significant investments are needed to move in, develop and market new product markets.

Second, the benefit of the block exemption will no longer apply to any exclusive grant-backs. These oblige licensees to license back to licensors exclusively (precluding even their own use) improvements to licensed technologies. Until now, the TTBER rules distinguished between severable and non-severable improvements, with only exclusive grant-backs relating to severable improvements excluded from the safe harbour. All grant-backs will

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6 See Guidelines, para 243.

7 *Ibid*.

now be subject to individual assessment, and may need to be looked at under Article 101(3). This change introduces unwelcome certainty to a popular clause in IP licenses.

Third, termination clauses allowing licensors to terminate agreements when licensees challenge the validity of the licensed technology will no longer be block exempted in non-exclusive licensing agreements. This change may negatively affect licensors' willingness to grant licences to avoid disputes altogether. The Commission's rationale here is that licensees are in the best position to assess whether an IP right is invalid and should therefore be able to challenge it if it represents an unnecessary restriction to competition. Such clauses will nevertheless continue to be block exempted in exclusive licensing agreements, provided the other conditions of the safe harbour (e.g., the market thresholds) are present. Indeed, the Commission takes the view that, in exclusive licensing agreements, termination clauses are usually less likely to cause competition concerns as licensors may sometimes be more dependent on licensees as their only source of income (e.g., if royalty payment structures rely on production with the licensed technology rights).

Next, the new Guidelines also contain a separate section on technology pools between two or more parties (e.g., patent pools). According to the Guidelines, any competition assessment concerning technology pools should focus on two crucial distinctions: the complementarity (as opposed to the substitutability) of the technologies included in the pool, as well as their essential (versus non-essential) character. As a rule of thumb, it is likely that the bringing together in a pool of significant substitute and non-essential technologies (i.e., not necessary for the relevant "package" standard or technology to work) will fall foul of Article 101 TFEU as licensees may no longer benefit from a real choice between different competing technologies. These distinctions between essential and non-essential and substitute and complementary are fine ones. These hard rules may be difficult to apply in practice. Another interesting feature is that the Guidelines now provide for a comprehensive safe harbour covering the creation and operation of technology pools, as well as their subsequent licensing out.

Finally, it is also worth mentioning that the Commission dropped its initial proposal to introduce a lower market share threshold of 20% for certain licensing agreements between non-competitors (i.e., in exceptional situations where licensees own a captively-used technology for in-house production only, which is substitutable for the licensed technology). Most likely because of the strong reactions from stakeholders that this would create legal uncertainty, the Commission finally decided to keep the higher, more beneficial 30% market share threshold for all non-competitor agreements.

The revised rules will enter into force on 1 May 2014 and are due to expire on 30 April 2026. For more information, the new TTBER and Guidelines may be accessed at:

http://ec.europa.eu/competition/antitrust/legislation/technology_transfer_regulation_en.pdf

http://ec.europa.eu/competition/antitrust/legislation/technology_transfer_guidelines_en.pdf