A number of recent cases confirm that disparities remain in how European and US courts tackle conflicts between the competition and intellectual property laws. Companies need to be aware of the impact competition rules can have on the value of their IP, say **Isabel Davies**, **Bruno Lebrun** and **Andreas Stargard** of Howrey

Seeking the right balance to maintain a free market

We are living in dynamic times for the interface between competition laws, intended to promote choice and competitive markets, and the IP laws, encouraging innovation and technology investment leading to improved products and low prices – all to benefit the consumer. Courts in Europe and the US have been far from idle in addressing the IP/antitrust intersection.

Businesses must consider the crossroads of the two bodies of law and develop their approach accordingly, determining how best to commercialize and enforce IP rights, while addressing the potential implications of competition law and its enforcement.

European competition law and IP

EU law recognizes and guarantees national property rights (Article 295, EC Treaty). However, conflicts between IP law and competition law do occur, particularly in the context of compulsory licensing. It is noticeable that cases have mainly arisen at Commission level, in spite of modernization.

Article 81 EC

Article 81(1) prohibits agreements between undertakings that prevent, restrict or distort competition and affect trade between member states. In the IP context, that includes licence agreements limiting the licensee's commercial freedom to sell products that incorporate the licensed IP. Article 81(3) establishes an exception to this prohibition if the agreement confers sufficient benefits to outweigh the anti-competitive effects.

IP agreements and licences can often fall foul of Article 81(1). Examples of anti-competitive clauses include: tying and bundling of products or licences, export bans, price or customer restrictions, no-challenge clauses, or territorial exclusivity grants.

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The main European regulation dealing with the competition aspects of IP licensing is the 2004 Regulation on technology transfer agreements, whose implementation is detailed by Guidelines that may the national courts and competition agencies, which have become the natural enforcers of EC antitrust rules since May 1 2004. That means that the Commission is unlikely to be involved in disputes relating to technology transfer agreements – companies have to assess on their own the compliance of their agreements with antitrust rules.

The new Regulation applies to all technology licence agreements concluded between two parties. These are defined as patent licensing, know-how licensing, software-copyright licensing or mixed licensing agreements (also including copyright in software and designs).

The scope of the new Regulation is defined through a market share threshold. Agreements between competitors with a market share of less than 20% and between non-competitors with less than a 30% market share benefit from the exception in Article 81(3), as long as the agreement does not contain one of the so-called hard-core restrictions. Agreements between parties with market shares in excess of the thresholds of the Block Exemption will not be *per se* illegal, as they are subject to individual assessment. "[T]here is no presumption of illegality of agreements that fall outside the scope of the Block Exemption provided that they do not contain hardcore restrictions of competition". However, they must be carefully assessed to determine whether they could restrict competition.

An agreement is prohibited when it provides hardcore restraints, such as price-fixing, limitation of output, or allocation of markets. Others are blacklisted, such as restrictions on the licensee to use its own technology. Both parties must carry out their own research and development, whether or not in the field covered by the licence. Price restrictions and restrictions on passive sales are also prohibited (the licensee must be able to respond to unsolicited orders from customers in another exclusive territory or customer group; this restriction was authorized for five years under the previous regulation).

If some terms breach Article 81, the agreement is not void (unlike hardcore restrictions), but the restrictions will fall away. They include the non-challenge clauses and the exclusive grant-back or assignment to the licensor of severable improvements or new applications of the licensed technology. Non-exclusive grant-back is not prohibited, and payment of grant-back compensation is irrelevant. The new Regulation authorizes non-compete obligations whereby the licensee is prevented from using competing third-party technologies.

Article 82 EC

Article 82 prohibits the abuse of a dominant position in the EU. IP ownership does not automatically confer a dominant position, but it is possible for an IP right to result in or contribute to a dominant position.

The tension between competition and IP laws becomes evident in cases where the Commission seeks to impose compulsory licences after the holder's withdrawal of or refusal to grant a licence.

In *Magill* (*RTE and ITP v Commission, 1995*), the ECJ first held that a refusal to grant a licence is not an abuse, even if the licence-holder is in a dominant position. However, it also stated that, in "exceptional circumstances", the exercise of an exclusive right by the owner could involve abusive conduct. The scope of these exceptional circumstances remains controversial.

In *IMS* (*IMS Health GmbH v NDC Health GmbH*, 2004), the ECJ attempted to clarify these circumstances. IMS provides data on regional sales of pharmaceutical products in Germany. It had developed a brick structure that became standard for presenting sales. In its preliminary ruling, the ECJ decided that, in this case, the refusal to grant a licence on the copyright of this structure, indispensable for providing pharmaceutical sales data, could constitute an abuse of a dominant position if the following conditions are fulfilled:

> "The undertaking which requested the license intends to offer, on the market for the supply of the data in question, new products or services not offered by the copyright owner and for which there is a potential consumer demand;
> The refusal is not justified by objective considerations;
> The refusal is such as to reserve to the copyright owner the market for the supply of data on sales of pharmaceutical products in the Member States concerned by eliminating all competition on the market."

This judgment clarifies when a refusal to license can become an abuse and when a licence can be imposed on the IP owner. But this may prove difficult in practice. For example, the undertaking requesting the licence must "intend" to offer a "new" product. It may be difficult to define what constitutes the novelty of a product or the extent to which that "new" product competes with the existing product of the IP owners. The mere fact that the undertaking requesting the licence must so "intend" may be controversial. The request for a licence may be based on one product, which the undertaking may not be able to produce, and still use the licence for producing another product that could not be "new". There is still a lot of room for interpretation.

The Court of First Instance may use the appeal of the *Microsoft* decision to clarify how to apply the *IMS* test. On March 24 2004, the Commission fined Microsoft €497 million for abusing a dominant position. The main issues are access of the interoperability information necessary to compete with Microsoft on the workgroup server market and Microsoft's automatic inclusion of its Windows Media Player into PC operating systems. Only the first issue questions more specifically the relationship between IP and antitrust, as recognized by the Commission in its decision: "it cannot be excluded that ordering Microsoft to disclose such specifications and allow such use of them by the third parties restricts the exercise of Microsoft's intellectual property right."

The Commission emphasized that the refusal to grant a licence cannot generally constitute an abuse of a dominant position, but may do so in "exceptional circumstances". It noted that Microsoft was "the *de facto* standard operating system product for client PCs", and was dominant for workgroup server operating systems. The two markets are closely linked due to interoperability requirements. In refusing to provide full interoperability information, in particular to Sun Microsystems, Microsoft encumbered others to interoperate with Windows, restricting competition in the workgroup server operating systems market.

The Commission found the refusal was part of a general conduct pattern whereby Microsoft exploited a range of privileged connections between its dominant PC operating systems and its workgroup server operating system. It concluded that the refusal to disclose interoperability information limited technical development on the market and was harming consumers; it required Microsoft to disclose interface documentation and to conclude licences on fair and reasonable terms.

Microsoft appealed the decision to the CFI, which will have to consider the Commission's position in light of the test in *IMS*. In particular, the Court will have to decide whether interoperability is necessary to issue a "new product" as defined in *IMS*.

Briefly after *IMS*, the ECJ missed an opportunity to clarify the year-old question regarding the conditions under which the refusal by a dominant company to supply in full wholesalers' orders to control parallel trade is illegal. In *Syfait v GlaxoSmithKline*, a wholesaler in Greece complained before the Greek competition authority against GlaxoSmithKline's refusal fully to supply its orders. Unfortunately, the ECJ declined jurisdiction, because the Greek national competition authority is not a "court" and therefore not entitled to request a preliminary ruling.

Advocate General Jacobs opined that a pharmaceutical manufacturer does not *per se* abuse its dominant position by refusing to supply in full wholesalers' orders, even if aimed at limiting exports. Jacobs noted that all European countries influence the price of pharmaceutical products in their territory, creating opportunities for parallel trade. By attempting to prevent parallel imports, pharmaceutical companies are trying to avoid the consequence of an EU-wide application of the low prices imposed upon them in some member states. In Jacobs' view, unlimited parallel trade in the pharmaceutical industry would eventually harm this industry where research and development are crucial.

Wholesalers in the pharmaceutical industry are obliged to ensure appropriate and continuous supplies to cover the needs of member states' patients. This obligation casts doubt on the reasonableness and proportionality of requiring manufacturers to supply wholesalers in low-price member states when they intend to export the products to high-price states. Jacobs observed that not the end-consumers but the traders benefit from parallel trade, because the product price is defined by the state. While he stressed that this was "highly specific" to the pharmaceutical industry, the *Syfait* arguments can be extended to other sectors.

On June 15 2005, the Commission fined AstraZeneca €60 million for breaching Article 82 by misusing the patent system and the procedures for marketing pharmaceuticals to delay the market entry for generic competitors to its drug Losec. It is the first time the Commission has decided that the abusive use of patent and regulatory procedures could constitute a breach of Article 82. AstraZeneca abused its dominant position because it made misrepresentations to national patent offices to obtain undue additional five-year extensions of its Losec patent, thereby delaying the entry of competing generics, and because it requested national medicine agencies to withdraw authorization for Losec capsules, and instead to authorize the new tablet form.

The US situation

Federal Circuit law governs all antitrust claims as long as they are related to the patent. The Circuit deems itself to be in the best position to impose and maintain uniformity of the patent laws. Pleading an antitrust case generally requires a fairly low standard: the facts must "at least outline or adumbrate" a violation, otherwise the plaintiff "will get nowhere merely by dressing them up in the language of antitrust" (*Rutman Wine v E&J Gallo*, 9th Circuit 1987).

Until recently, one had to allege all requisite elements of a substantive antitrust claim (such as antitrust injury or market power), but this has potentially changed with the Federal Circuit's recent *Illinois Tool Works v Independent Ink* opinion, holding that proof of market power in a patent tying case

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is no longer required. The most common antitrust claims in IP-related cases remain the tying of IP-protected goods to other goods; fraud in the procurement of the IP right (*Walker-Process* actions); the patent misuse defence (the illicit and anti-competitive enlargement of the patent's scope); challenges to mergers under § 7 of the Clayton Act, due to the parties' unique IP assets; discriminatory licensing or pricing under the Robinson-Patman Act; the foreclosure of a competitor's use of IP assets in furtherance of a Sherman Act § 1 boycott or cartel, or their use in aid of monopolization illegal under § 2; and sham patent litigation.

The right balance

Eight years ago, Joel Klein, former assistant attorney general at the DOJ Antitrust Division, observed in front of the AIPLA that, "the intersection of antitrust law and intellectual property has become a major agenda item for the Antitrust Division." Today, this often invoked intersection has grown from a rural four-way stop to a major highway's cloverleaf interchange: the courts no longer hear only the notorious *Walker-Process* or patent-misuse defences in patent infringement actions, so habitually charged "in almost every major patent case" that they have "become an absolute plague" (*Burlington Industries v Dayco Corp,* Federal Circuit 1988).

The courts, together with the agencies, have taken affirmative steps to improve previously undeveloped areas. Both businesses and IP practitioners benefit from the added guidance. For instance, according to the DOJ, "by far most cross-licences and pools are, on balance, procompetitive," and the agencies' joint Collaboration Guidelines delineate a way for competitors to engage in pro-competitive joint-venture R&D efforts, allowing companies to estimate the attendant antitrust risks more precisely. They prohibit all price or output fixing, bid rigging, or division of markets among JV partners. All other conduct falls under either the rules laid out in the Horizontal Merger Guidelines or is analyzed under the classic antitrust Rule of Reason. The agencies believe that pro-competitive efficiency gains arise from the type of collaboration that combines different capabilities or resources, and favour sunset provisions that ensure effective competition thereafter. If an IP "cross-license is between firms that are competitors, whether in producing goods or services, licensing intellectual property, or in R&D, our antitrust antennae go out".

Recent developments

Recent US developments are, most notably, the Federal Circuit's radical approach in *Illinois Tool Works* to the question whether patent ownership automatically creates market power for purposes of an antitrust tying claim. The Supreme Court has now granted *certiorari*, and the FTC and DOJ recently decided to file an *amicus* brief urging reversal of the decision, seeking to retain the *status quo* of the classic rule that every element of an antitrust offence – including market power in the tying product market – must be *proven* and cannot be presumed, be it by a careless plaintiff or the stroke of a Federal Circuit judge's pen in a landmark ruling.

Less well-known and not as far-reaching is *Applera Corp/Roche Molecular v MJ Research*, a 2004 Federal District Court decision. It is a fitting example of the modern antitrust-IP interplay at work in a civil business dispute. The court granted summary judgment for the patentee-plaintiffs. The subject matter was complex, relating to DNA polymerase chain reaction and thermal cycler instrument technology, purportedly violating plaintiffs' patents. MJR counterclaimed that the plaintiffs licensed and enforced their patents anti-competitively, alleging a horizontal hub-and-spoke conspiracy.

The court bifurcated the trial, hearing infringement issues first and antitrust claims second. A month before the jury's $19.8 million infringement verdict and the court's subsequent denial of MJR's antitrust claims, however, the defendant went into bankruptcy. The court held that MJR not only lacked cognizable antitrust injury and thus standing, but also that plaintiffs' licensing program did not constitute horizontal price fixing and did not extend the lawful scope of the patent grant. The evidence failed to show a fixed market price, instead indicating a wide range of retail prices for the cylinders.

Applera shows that price-fixing claims based on IP licensing must be based on more than mere 1) evidence of improper motive, 2) imposition of a licensing fee covering only the patented technology, 3) multiple licensing, which is not a *per se* antitrust violation, or 4) most-favoured-nations (or -licensee) clauses. The latter are especially benign when they provide licensees with lower royalty rates, as the licensor may engage in subsequent negotiations leading to lower licence fees, as the opinion observes. It also re-emphasizes US patent owners' broader antitrust immunities compared to non-patentees' conduct, and shows the mixed results with which infringement defendants try to extend the reach of Sherman § 1 as it relates to agreements by patentees.

Recommended strategies

Companies need to be aware of the antitrust angle when acquiring, enforcing or licensing IP rights.

In the EU, on the one hand, a decision like *Microsoft* indicates that the Commission may take a strong stance against IP rights owners (which could be confirmed by the decision in *AstraZeneca)*. On the other hand, the new Guidelines on technology transfer indicate that the Commission is very much aware of the need to maintain a balance between the reward of innovation and the good functioning of the market through competition: IP rights "promote dynamic competition by encouraging undertakings to invest in developing new and improved products and processors. So does competition by putting pressure on undertakings to innovate. Therefore, both ... are necessary to promote innovation and ensure a competitive exploitation thereof."

Businesses involved in technology licensing need to take particular account of the new Regulation on transfer of technologies when negotiating new licences and should review their existing arrangements for compliance. Companies also need to consider the effects of parallel imports, including whether price differentials between member states are justified, and to which extent they motivate parallel imports.

In both the US and the EU, it is recognized that competition and IP laws are complementary (both are centred on the innovation process and the expansion of economic activity). The US imposes fewer limitations on the commercialization of IP rights than the EU, and there is a noticeable tension between the competition and IP regimes in the area of compulsory licensing. Changes to competition and IP laws are occurring on both sides of the Atlantic to enhance and strengthen coherence between the two regimes and there is a growing convergence between EU and US competition policy towards licensing agreements.