

CPI Antitrust Chronicle

February 2011 (1)

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for Production and R&D Agreements
Create a More Coherent Framework
of Assessment and Provide Better
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I. INTRODUCTION

On December 14, 2010, the European Commission adopted revised EU competition rules for production agreements, research and development agreements, and other types of commercial cooperation agreements between competing undertakings. The revised block exemption regulations for research and development agreements (“R&D BER”)² and specialization agreements (“Specialization BER”)³ and the revised Horizontal Guidelines⁴ entered into force on January 1, 2011. They replace the predecessor R&D BER, Specialization BER, and Horizontal Guidelines that were adopted in 2000.⁵

While preserving the existing general approach for assessing such agreements under EU competition law, the revised texts significantly change the predecessor block exemption regulations and Horizontal Guidelines. The final revised texts also incorporate several improvements that stakeholders suggested in their comments on the drafts of the two block exemption regulations and the Horizontal Guidelines that the Commission published for public consultation in May 2010.⁶

Even if not perfect on all accounts, the revised texts overall have to be welcomed as they provide a more coherent and clearer framework for the assessment of R&D and production agreements under EU competition law. They remedy many of the instances of legal uncertainty that arose under the predecessor rules and broaden the scope of the BERs, thus allowing companies more flexibility to structure their cooperation without running the risk of falling outside the safe harbor created by the BERs.

¹ Arnold & Porter LLP. The views expressed are exclusively those of the author and do not necessarily reflect views of Arnold & Porter or its clients.

² Commission Regulation (EU) No 1217/2010 of 14 December 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to certain categories of research and development agreements, 2010 OJ L 335/36.

³ Commission Regulation (EU) No 1218/2010 of 14 December 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to certain categories of specialization agreements, 2010 OJ L 335/43.

⁴ Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements, 2011 OJ C 11/1.

⁵ The revised block exemption regulations are valid for a period of 12 years and expire on December 31, 2022.

⁶ Notably, the revised texts take into account many of the author’s 10 suggestions published in A. Gutermuth, *Revision of the EU Competition Rules on Cooperation in Research & Development and Production: Scope for Further Improvement*, 9(1)CPI ANTITRUST CHRON. (September 2010).

II. OVERVIEW OF THE MAIN CHANGES

The main changes compared to the predecessor R&D BER and Specialization BER are the following:

- The scope of both revised BERs has been significantly broadened so that more varied forms of production and R&D arrangements can benefit from block exemption in the future. Notably, unlike under the May 2010 draft, agreements under which one party finances the R&D work of the other party and R&D agreements that allocate exploitation rights to only one party are included in the scope of the revised R&D BER. Unilateral and reciprocal specialization agreements fall under the revised Specialization BER even if they only provide for a partial (and not a full) cessation of existing production.
- The “access condition” in Article 3(2) of the revised R&D BER, requiring that all parties to an R&D agreement obtain access to the R&D results, has been clarified, thus significantly enhancing legal certainty. Unlike the May 2010 draft, the final revised access condition grants companies a significant degree of leeway to provide financial compensation in return for the granting of access.
- The R&D BER’s list of hardcore restrictions has been simplified and clarified in various respects.
- Active sales restrictions in R&D agreements now can be agreed upon for periods exceeding seven years after product launch.⁷
- Recital 15 of the revised R&D BER clarifies that field-of-use-restrictions are not characterized as hardcore restrictions for the purposes of the revised R&D BER.
- Contractual no-challenge clauses regarding the parties’ intellectual property rights and certain (rare) contractual provisions leading to the non-use of the R&D results are no longer treated as hardcore restrictions in the R&D BER but as “excluded restrictions.”⁸ As such, they are not covered by the R&D BER’s safe harbor but also do not prevent the application of the safe harbor to other parts of the R&D agreement.
- Both revised BERs include a new definition of when a party is considered to be a potential competitor to the other. In short, this is the case if, absent the cooperation agreement, the party can be expected to start supplying competing products within a period of three years in response to a small but permanent price increase.
- The Horizontal Guidelines’ revised chapter on production agreements identifies a new category of production cooperation agreements, referred to as “subcontracting agreements with a view to expanding production.” These agreements cannot fall under the Specialization BER because they are neither unilateral or reciprocal specialization agreements nor joint production agreements, but benefit from a new soft safe harbor created by paragraph 169 of the revised Horizontal Guidelines if the parties’ combined market share does not exceed 20 percent.

⁷ Article 5(c) of the revised R&D BER.

⁸ Article 6 of the revised R&D BER.

Overall, these changes mean that companies have more flexibility than in the past to structure their agreements according to their commercial needs while preserving the possibility of benefiting from the BERs.

Importantly, the revised R&D BER has not introduced the “disclosure obligation” that was proposed in the May 2010 draft and that would have required the parties to disclose to each other their pre-existing intellectual property rights to the extent relevant for the exploitation of the R&D results. Apparently, stakeholders’ reactions submitted in the public consultation convinced the Commission both that there was no sufficient policy justification for making the application of the R&D BER dependent upon such disclosure and that this requirement would have led to difficult questions of interpretation, thus creating legal uncertainty.⁹

III. AREAS WHERE THE REVISED RULES ARE STRICTER THAN THE PREDECESSOR RULES

Nevertheless, companies should be aware that the revised R&D rules are stricter than the predecessor rules in a number of important respects. Notably:

- Passive customer sales restrictions in R&D agreements are now characterized as hardcore restrictions.¹⁰ Previously, only territorial passive sales restrictions were characterized as hardcore restrictions. The revised R&D rules (unlike the rules on vertical agreements and technology transfer agreements) provide for no exceptions to the treatment of passive sales restrictions as hardcore restrictions.
- The hardcore provisions regarding active and passive sales restrictions have been expanded to also cover restrictions regarding the licensing of technologies that result from the R&D cooperation.¹¹ Previously, only restrictions on the sale of products were characterized as hardcore restrictions.
- The parties are allowed to fix the prices for the products and technologies resulting from the R&D cooperation only if they (i) jointly exploit the R&D results by means of a joint team, organization, or undertaking or (ii) jointly entrust the exploitation to a third party.¹² The wording of Article 5(2)(b) of the predecessor R&D BER was not clear as to whether price-fixing would be allowed also when the parties allocated exploitation rights among themselves.
- As the precise meaning of the access condition in Article 3(2) of the predecessor R&D BER was not clear, it can be expected that several existing R&D agreements will not fully comply with the clarified access requirements set out in Article 3(2) of the revised R&D BER. For example, existing R&D agreements might not give a party access to the final R&D results for purposes of further R&D when the results of the R&D are still exploited by the other party. Such access for R&D purposes is normally necessary for the revised R&D BER to apply.
- The 25 percent market share threshold that determines whether or not the R&D BER applies to agreements between competitors has to be calculated with regard to both

⁹ For further detail, see A. Gutermuth, *supra* note 6 at 4.

¹⁰ Article 5(d) of the revised R&D BER.

¹¹ Article 5(d) and (e) of the revised R&D BER.

¹² Article 5(c) of the revised R&D BER.

product and technology markets.¹³ The market share threshold of the predecessor R&D BER only applied with regard to products that resulted from the R&D cooperation. The market share in technology markets was not relevant.

- In the case of paid-for R&D, which is expressly included in the scope of the revised R&D BER, the 25 percent combined market share threshold has to be calculated not only for the parties to the specific agreement, but cumulatively for the financing party and all other companies with which the financing party has entered into R&D agreements for the same products or technologies.¹⁴

The Specialization BER has become stricter notably in the following respect:

- When the specialization agreement concerns intermediate products that the cooperating parties (partly) use internally for the production of downstream products, the revised Specialization BER can only apply if the parties' combined market share for the intermediate product and for the downstream product does not exceed 20 percent.¹⁵ Previously, the market share threshold only applied at the level of the product that was the subject of the specialization agreement (thus, the intermediate product).

Companies should review their R&D or production agreements for compliance with the revised BERs if their agreements extend beyond the two-year grace period (ending on December 31, 2012) during which the predecessor BERs continue to cover agreements that were in force on December 31, 2010.¹⁶ Such agreements might have to be amended to ensure their validity and enforceability under the revised rules.

The following comments focus on some of the main changes and, in particular, compare the final revised texts with the May 2010 drafts.

IV. RESEARCH AND DEVELOPMENT AGREEMENTS

A. Forms of R&D Cooperation Covered by the R&D BER

The revised R&D BER continues to apply to cooperation agreements concerning “joint research and development” with or without joint exploitation.¹⁷ One possible form of joint R&D continues to be “specialization in R&D,” that is, a situation where the R&D work is “allocated between the parties by way of specialization.”¹⁸

To remedy the uncertainty existing under the predecessor R&D BER as to which forms of cooperation qualify as “specialization in R&D,” the revised R&D BER defines specialization in R&D as occurring when “each of the parties is involved in the research and development activities covered by the research and development agreement and they divide the research and development work between them in any way that they consider most appropriate.”¹⁹ This definition grants the parties broad flexibility to divide the R&D work as they see fit. Notably, this

¹³ Article 4(2) of the revised R&D BER.

¹⁴ Article 4(2)(b) of the revised R&D BER.

¹⁵ Article 3 and 1(1)(i) of the revised Specialization BER.

¹⁶ Article 6 of the revised Specialization BER and Article 8 of the revised R&D BER.

¹⁷ Article 1(1)(a)(i)-(iii) of the revised R&D BER.

¹⁸ Article 1(1)(m)(iii) of the revised R&D BER.

¹⁹ Article 1(1)(n) of the revised R&D BER.

definition is significantly broader than the definition proposed in the May 2010 draft, which required that each party “focuses on a distinct area of the research and development.”²⁰

Importantly, the revised R&D BER also applies to so-called “paid-for” R&D, which occurs when one party (the “financing party”) does not carry out any of the R&D activities itself but finances the R&D work of the other party.²¹ Paid-for R&D does not fall under the definition of joint R&D, but constitutes a separate type of agreement covered by the revised R&D BER. While it was unclear whether or not the predecessor R&D BER applied to scenarios of paid-for R&D, the May 2010 draft R&D BER explicitly excluded this possibility.²²

The inclusion of paid-for R&D in the revised R&D BER, and the more flexible definition of joint R&D by means of specialization in R&D, are to be welcomed. These changes make the BER accessible to a broader range of agreements and make it unnecessary for companies to design artificial forms of R&D cooperation just to bring their cooperation under the framework of the R&D BER.

B. Forms of Joint Exploitation of the R&D Results Covered by the R&D BER

As under the predecessor R&D BER, joint exploitation of R&D results can occur by means of joint teams, organizations or undertakings, joint entrustment of the exploitation to a third party, and by specialization in exploitation.²³

Article 1(1)(o) of the revised R&D BER introduces a new definition of “specialization in the context of exploitation.”²⁴ Importantly, the new definition includes arrangements under which the exploitation rights are allocated to only one of the parties. Unlike under the May 2010 draft, it is not necessary that each party be granted exploitation rights in the internal market.²⁵ Arguably, the revised R&D BER is not different in this respect from the predecessor R&D BER, but the fact that the revised R&D BER explicitly recognizes that it applies to situations of exploitation by only one party enhances legal certainty.

C. Access Condition

The predecessor R&D BER could only apply if each party had “access to the results of the joint research and development for purposes of further research or exploitation.”²⁶ This wording led to several difficult questions of interpretation.

The revised R&D BER clarifies the access condition in several important ways. Notably, the amended wording of Article 3(2) makes clear that access, which is now referred to as “full” access, only has to be granted to “final results” of the R&D cooperation (and thus not to

²⁰ See A. Gutermuth, *supra* note 6 at 2.

²¹ Article 1(1)(a)(iv)-(vi), Article 1(1)(p) and Article 1(1)(q) of the revised R&D BER.

²² See A. Gutermuth, *supra* note 6 at 3.

²³ Article 1(1)(m) of the revised R&D BER.

²⁴ Article 1(1)(o) of the revised R&D BER states: “‘specialisation in the context of exploitation’ means that the parties allocate between them individual tasks such as production or distribution, or impose restrictions upon each other regarding the exploitation of the results such as restrictions in relation to certain territories, customers or fields of use; this includes a scenario where only one party produces and distributes the contract products on the basis of an exclusive license granted by the other parties.”

²⁵ Article 13 No. 13 of the draft revised R&D BER required that each party “carry out some of the exploitation of the results in the internal market.” See also A. Gutermuth, *supra* note 6 at 3.

²⁶ Article 3(2) of the predecessor R&D BER.

intermediate results, although it may be difficult to determine in practice when a R&D result is a “final” result) and that access rights for purposes of exploitation can be limited to the extent that the parties engage in joint exploitation. Importantly, however, access for the purposes of further R&D must be granted once final R&D results have been obtained, even if joint exploitation occurs afterwards. In practice, this means that many R&D agreements will have to foresee a staggered approach to access to the R&D results by the non-exploiting party.

Article 3(2) of the revised R&D BER does not include the—controversial²⁷ — requirement suggested in the Commission’s May 2010 draft that the parties must have “equal” access to the R&D results. Instead, Article 3(2) of the revised R&D BER clarifies that the agreement can “foresee that the parties compensate each other for giving access to the results” although “the compensation must not be so high as to effectively impede such access.” Again, this is an area where the final revised R&D BER has improved compared to the May 2010 draft,²⁸ although it may be difficult to determine in practice under which circumstances a specific level of compensation “effectively impedes” access.

D. List of Hardcore Restrictions

The substance of the list of hardcore restrictions in Article 5 of the revised R&D BER has not significantly changed compared to the May 2010 draft, although its structure has become more complex to reflect the broadened scope of the revised R&D BER. Significant changes to the list of hardcore restrictions compared to the list included in the predecessor R&D BER have been identified in Sections II and III above. Overall, the revised list of hardcore restrictions is more coherent and offers a higher degree of legal certainty.

V. PRODUCTION AGREEMENTS

The final text of the revised Specialization BER is largely in line with the May 2010 draft and brings about the following main changes compared to the predecessor BER:

- The characteristics of unilateral and reciprocal specialization agreements have been harmonized and now require in essence that: (i) the parties must be active on the same product market (but not necessarily on the same geographic market); (ii) one party agrees to fully or partly cease production of the products in question or to refrain from producing such products in the future and to source them from the other party; and (iii) the other party agrees to produce the products and supply them to the first party.²⁹
- Importantly, it is no longer necessary for the parties to fully cease existing production in order for their agreement to qualify as a unilateral or reciprocal specialization agreement. It is sufficient to partly cease production. This change is of significant importance for the practical relevance of the Specialization BER, as situations of partial cessation of production occur very frequently; for example, the closure of an outdated production plant by a company that operates several production plants. Recital 7 of the revised

²⁷ See A. Gutermuth, *supra* note 6 at 4.

²⁸ It should be noted that the revised Horizontal Guidelines retain the explanations of the predecessor Horizontal Guidelines on the assessment of R&D outsourcing agreements (paragraph 131 of the revised Horizontal Guidelines) and exclusive access rights that are required in light of risks and investments made to exploit R&D results (¶140 of the revised Horizontal Guidelines).

²⁹ Article 1(1)(b) and (c) of the revised Specialization BER.

Specialization BER now also specifies³⁰ that the parties do not have to agree on a reduction of their existing production capacity in order to “partly cease production.” A reduction of existing production volumes is sufficient.³¹

- If the specialization agreement concerns intermediate products that one or more of the parties fully or partly use captively for the production of downstream products, the 20 percent combined market share threshold set in Article 3 of the revised Specialization BER must not be exceeded with regard to both the intermediate and the downstream product market.³² Under the predecessor Specialization BER, only the market share on the intermediate market was relevant in such situations.
- The BER can apply to all three forms of specialization (unilateral specialization, reciprocal specialization, and joint production) even if the agreement provides for joint distribution by the parties through a joint team, organization, or undertaking or by means of a third party distributor appointed by the parties.³³ Arguably, the predecessor Specialization BER applied to agreements that included joint distribution only if the specialization occurred in the form of joint production, while unilateral and reciprocal specialization agreements arguably were not covered by the predecessor BER if they provided for joint distribution.

Overall, the revised Specialization BER has become more flexible and will be of greater practical relevance to companies in the future. The revisions have also remedied several important questions regarding the correct interpretation of the predecessor Specialization BER and, overall, offer a more coherent framework.

Unfortunately, the Commission did not define when parties can be considered to “produce certain products jointly” so that the agreement qualifies as a joint production agreement under Article 1(1)(d) of the revised Specialization BER, notably distinguishing it from the new category of “subcontracting agreements for purposes of expanding production,” which do not fall under the Specialization BER. This will remain an important area of legal uncertainty, although subcontracting agreements for purposes of expanding production now can benefit from a soft safe harbor created by paragraph 169 of the revised Horizontal Guidelines. It is also regrettable that the revised Horizontal Guidelines include little improvement regarding the individual assessment of production agreements under Article 101 TFEU as far as the counter-factual and commonality of costs are concerned.³⁴

³⁰ See A. Gutermuth, “*supra* note 6 at 6.

³¹ It appears to follow from Article 1(1)(g) of the revised Specialization R&D BER that “production” in this sense does not have to be the parties’ own production but can be product volumes previously sourced by the parties from third parties under subcontracting agreements. It is also important to note that Recital 7 of the revised Specialization BER specifies that, to qualify as joint production agreement within the meaning of its Article 1(1)(d), it is not necessary that the agreement foresees the reduction of the parties’ individual pre-existing production activities.

³² Article 3 with Article 1(1)(i) of the revised Specialization BER.

³³ As under the predecessor Specialization BER, the appointed third party must not be a competing undertaking (Article 1(1)(q)(ii) of the revised Specialization BER).

³⁴ On these issues, see A. Gutermuth, “*supra* note 6, 6-7.