

Deutsche Vereinigung
für gewerblichen Rechtsschutz
und Urheberrecht e.V.

Deutsche Vereinigung für gewerblichen Rechtsschutz und Urheberrecht
Theodor-Heuss-Ring 19-21 • 50668 Köln

European Commission
Directorate General for Competition (DG IV)
Dr. Alexander Schaub
Avenue de Cortenberg/Kortenberglaan 150
1049 BrusselsB ELGIUM

Sitz Berlin
Hauptgeschäftsstelle Köln

50668 Köln, den **10.12.1999**
Theodor-Heuss-Ring 19-21
Telefon (0221) 77 16-151
Telefax (0221) 77 16-205
e-mail: office@grur.de

Ihr Zeichen:

Unser Zeichen:

(Bei der Antwort bitte angeben)

**Legal Opinion on the Block Exemption Regulation for Vertical Agreements and
Concerted Practices
(AmtsBl. C 270/7 dated September 24, 1999)**

Dear Mr. Schaub:

The Deutsche Vereinigung für gewerblichen Rechtsschutz und Urheberrecht e.V. is an association of professionals and academics working in the area of intellectual property and copyright laws including anti-trust law. The association is a non-profit organization. According to its Articles of Association, the purpose of the association is to provide continuing legal education in the area of intellectual property and to support legislative bodies as well as ministerial agencies and institutions in issues of intellectual property.

The comments of the association on the Block Exemption Regulation draft for vertical agreements and concerted practices are as follows:

1. The association already reviewed the draft of the Block Exemption Regulation for vertical agreements during the hearing before the Council's decision pursuant to Article 83 EGV. In view of the numerous criticisms on the main provision of the Block Exemption Regulation, according to which an exemption shall be granted without additional requirements if the relevant market share of the participating companies is not more than 30 percent, the association decided not to give its own opinion at that time. Now that the Council has passed an enabling regulation

pursuant to Article 83 EGV and the Commission has asked again for the opinions of people affected, the association has decided to take the opportunity to express its serious doubts that this provision is suitable.

- a) The provision assumes that market participants who are parties to contracts containing clauses restricting competition and who have market shares above the threshold are far more likely to abuse the situation than those parties to contracts having a market share under the threshold.
 - (1) The practice of the previous Block Exemption Regulation shows that a Block Exemption has only been revoked in three cases. This indicates that the danger of abuse usually does not exist, even with persons having a higher market share.
 - (2) There is no necessary correlation between the market share of a contractual party and the risk of a restriction to competition in a vertical agreement. Cartel law considerations are based on the concrete clauses restricting competition.
 - (3) In the future, companies having strong market shares would be able to enter agreements containing vertical competition restrictions in commercially unimportant cases only if they obtain specific exemptions.
- b) The association doubts whether the Commission's provision will result in easing the burden of the Directorate-General for Competition.
 - (1) In order to avoid economically bad investments, companies with market shares above the threshold will be advised to apply for specific exemptions because their agreements would be invalid (provisionally) (Article 85(2) EGV). From the company's vantage point, it cannot be predicted whether the Commission will use its right to grant a retroactive exemption (Guideline No. 53).
 - (2) Companies will also report their contracts to the Commission because there will be questions on defining the market and therefore questions on the amount of market share.

- c) The use of a market share threshold as a criterion for the exemption is problematic from a legal certainty point of view.
- (1) Defining markets depends on the degree to which goods are homogenous, which is problematic. The market is not constant but variable, which is subject to the influence of the market participators.
 - (2) Defining the subject matter and geography of the relevant market may be problematic. In merger control proceedings, the market definition is controversial in almost every case. The Guidelines' comments on market definition (No. 78 ff.) are extensive and complicated. They will also give as little legal certainty as the Commission's notice concerning defining relevant markets.
 - (3) Even determining the total market volume often poses problems. Participating companies often do not have the necessary data, especially since the exchange of current market data among companies is not permitted.
 - (4) Because in the future the Block Exemption will become effective "automatically", the participating companies will bear the risk of incorrectly defining the market share. Not only manufacturers/suppliers, but also contractual parties will be affected.
 - (5) Previous experience of the EU Commission with defining market shares does not give reason to be optimistic. This is true for the market share of 15 percent in Article 4(2)(3c) of Regulation 17/62 as well as the market share pursuant to No. 9 of the Announcement on Agreements of Little Importance (*Bagatellbekanntmachung*). In creating the Merger Control Regulation, the Commission stated (AmtsBl. 1992 No. C 36/3,4) that the market share criterion will become "hardly more useful in practice and is an unsuitable criterion for defining the regulation's area of applicability". Today, the market share threshold is used in Merger Control Regulation proceedings only as an indication, but does not have any direct legal implication. The Block Exemption Regulation rules which refer to market share, (EWG) No. 17/85 and (EWG) No. 418/85 (market shares of 10 percent or 20 percent), do not have any practical relevance. The Commission

has given up its plans to use the market share criterion in the Block Exemption Regulation "Technology Transfer" (No. 240/96).

- (6) In contrast to the mentioned rules, there is a problem of case load volume where vertical restrictions of competition are involved. Thus the disadvantages from the legal certainty point of view are even more important.
- d) The flanking measures which the Commission has proposed in order to preserve legal certainty will not prove to be sufficient.
- (1) The fact that there is no "presumption" that a contract will not be exempted if a company exceeds the threshold does not relieve companies of their uncertainty.
 - (2) Neither do the transition rules for market share fluctuations (Article 8(2)) remove the legal uncertainty. Market shares for certain products may experience great fluctuations in a short period of time.
 - (3) The Guidelines proposed by the Commission are generally to be welcomed as an aid to interpretation, but this does not change the problem of defining market share.
 - (4) The above-mentioned possibility of granting retroactive exemption (amendment of Article 4(2) of Regulation No. 17) does not remove the risk that a company has for relying on this. If investment is tied to vertical agreements, the participating companies have no other choice but to obtain a specific exemption.
- e) Reservations under the standpoint of legal certainty are especially serious if one considers the effects of the proposed regulation on court proceedings.
- (1) If during court proceedings a petition for specific retroactive exemption is filed, the court will generally stay proceedings because the Commission has exclusive jurisdiction for granting the exemption. According to past experience, one can expect a decision from the Commission to take even a longer period of time. Because the exclusive dealings of the entire agreement is usually of

particular importance, not only the validity of the clause but the validity of the contract is questionable for a longer period of time.

- (2) The court seized does not have its own knowledge on the market share. The court will obtain an expert opinion or information from the EU Commission, which will result in a considerable delay of the proceedings.
 - (3) Under the previous Block Exemption Regulation, the courts were able to decide on the validity of contractual clauses because they only had to decide whether the contractual clause met the requirements of the Block Exemption Regulation which was in effect.
 - (4) Therefore, the majority was correct in voting for broader Block Exemption Regulations without market share upper limits in the first hearing, whereas all variations containing market share thresholds were voted against by, at times, a considerable majority.
- f) The Commission should use the opportunity of holding another hearing to consider alternatives to its concept.
- (1) In Europe, vertical competition restraints have proven to be far less harmful than horizontal competition restraints. Often, exclusivity obligations even have the effect of encouraging competition (example: selective marketing systems).
 - (2) In the United States and in Germany, vertical competition restraints have been removed from the restrictive laws to a much larger extent than in the Commission's draft. In Germany, experience with § 16 GWB, which only provides for an abuse control, has been positive.
 - (3) There are many reasons to subject vertical restraints on competition only to a test of abuse. Even if this were to require an amendment of the primary contractual laws, this variation should be reviewed seriously.
 - (4) Another proposal could be to redraft the existing Block Exemption Regulation. Here, the conditions for its applicability should be considerably simplified, the

list of "black clauses" must be limited to the most important rules, and a limitation of the abuse control (without market share) should be provided.

2. The Guidelines (Nos. 15, 20) correctly do not apply Article 81(1) of the EGV to rules concerning commercial agency agreements which contain risk sharing typical for a commercial agent. Therefore, Articles 3 and 4 of the GVO draft do not affect such agreements. This is especially true for the one-brand commercial agent whose agreement (with the covenant not to compete) also is not already contained in Article 81(1) of the EGV. Number 20 sentence 3 of the Guidelines also states that if the market is compartmentalized by the totality of the agreed competition restraints, Article 81(1) EGV should be applicable; this is a correct statement.
3. Distinguishing between vertical competition restraints and horizontal competition restraints in No. 25 of the Guidelines (in conjunction with Article 1), according to which the regulation does not apply to vertical agreements between competitors, is problematic. The scope of the term "potential competition" is not easy to define in a specific case. For this reason, the present Block Exemption Regulations excluded only agreements between manufacturers of products in competition with each other. This connecting factor has proven to be very useful in practice.
4. There is another distinction which poses problems in vertical agreements which refer to intellectual property rights (trademarks, copyright, and know-how). Agreements concerning such intellectual property rights are covered by the Block Exemption if the relevant provisions are not the "main subject matter" of the agreement.
 - a) Making a distinction between the main subject matter and an ancillary subject matter is not possible in many agreements. According to the wording of Article 1 (3), the relevant provisions are not the main subject matter of the agreement if they directly refer to the performance of the vertical agreement, if they are necessary to the agreement, and if no competition restraints with the same purpose or effect are contained in the agreement, such as vertical restraints which are not exempted by the regulation.

- b) Number 29 lists cases in which the provisions concerning intellectual property rights are the main subject matter of the agreement. The first case mentioned gives the example of a supplier which uses the intellectual property rights of the buyer. Such provisions could, however, be the subject matter of agreements dealing with performance of a cooperation in different production or marketing stages and containing terms under which parties may buy, sell, or resell certain goods or services (definition of vertical relations in Guideline No. 23). In reviewing the entire agreement, such provisions therefore may, depending on the individual case, despite the negative definition in No. 29, be considered to be an "ancillary subject matter" under the first dash of the Guidelines because they are directly tied to performing the main agreement and are necessary.
- c) The second negative distinction in the second dash of No. 29 of the Guidelines does not aid in making a distinction because it only makes general distinctions between the Block Exemption Regulation and agreements pursuant to the Regulation concerning Technology Transfers, the notice on supplier agreements, or regulations under which vertical agreements concluded in connection with horizontal agreements have been exempted. It should be noted that the attempt of Guideline No. 29 to identify provisions which are not the main subject matter of the vertical agreement has not been successful.
- d) In Nos. 30-36, the Guidelines attempt to describe provisions concerning intellectual property rights (in particular trademarks, copyrights, know-how) which are to be deemed directly tied to vertical agreements and necessary. This definition also does not appear to be adequate.
- (1) A trademark license (the Guidelines incorrectly use the term "Warenzeichenlizenz") is not "usually necessary" for the distributor to distribute goods or services. Once the designated goods are brought on the market within the Community, the trademark right is exhausted. The distributor does not need a license for resale or advertising. Apart from this editing mistake, a problem could arise in a case in which the license is the main subject matter of the agreement as well as the case in which the trademark license is only of a subsidiary, supplemental character. This also shows that the distinction

between the main subject matter and the "ancillary subject matter" cannot be made in many cases and does not conform to the rule of legal certainty.

- (2) In Guideline No. 32, an example of the case is given in which the retailer has an obligation to resell only under the condition that the buyer has an obligation not to infringe copyright. Because in this example (No. 32) the existence of a copyright is assumed, by virtue of this fact alone the case does not fall under Article 81(1) EV, as is correctly implied in No. 32. Therefore this is not an appropriate example for distinguishing between main subject matter and "ancillary subject matter".
- (3) The obligation of the retailer to place the users of software under the obligation to observe the manufacturer's conditions for use upon opening the packet must be distinguished from the case in which the manufacturer has "rights to software" and such cases in which the software is not protected. Number 33 of the Guidelines seems to assume the first case. The same is true for No. 32. If the manufacturer does not have exclusive rights to the software (ability and boundaries of software protection have for the most part not been clarified), the problem arises to what extent the contractual agreements provide protection which corresponds to intellectual property rights. First, one cannot say that such contractual conditions between the manufacturer and retailer only concern "ancillary subject matter". Second, there is the question whether by including this under the Block Exemption Regulation an exemption should also be granted in the latter cases, where the software manufacturers do not have any exclusivity rights except as provided for in the contractual agreements.
- (4) Number 34 of the Guidelines concerns hardware in which copyright protected software is included. Here, our comments on No. 32 of the Guidelines apply.
- (5) The inappropriateness of distinguishing between "main subject matter" and "ancillary subject matter" is best seen in an example of an agreement giving know-how to the buyer for marketing purposes (franchise agreements). Here, the use of intellectual property rights (trademarks, company designations, know-how) are not ancillary subject matters but the main subject matter of the agreement. There is no question that the marketing-franchise agreements

which until now fall under the regulation (EWG) No. 4087/88 should be included in the Block Exemption Regulation. However, making a distinction between a main subject matter and an "ancillary subject matter" will not lead to this result; instead, it appears that an express provision for franchise agreements needs to be included in the regulation text itself (not only in the Guidelines).

Gloy
President

Loschelder
Secretary General