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## The New EU Competition Rules for the Assessment of Horizontal Agreements

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# The New EU Competition Rules for the Assessment of Horizontal Agreements

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## I. INTRODUCTION

Following a consultation process of more than two years, the European Commission has now adopted its Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements (the “Horizontal Guidelines”).<sup>2</sup> The new Horizontal Guidelines include a significantly revised chapter on standardization agreements, Chapter 7, an entirely new chapter on information exchanges, as well as numerous other modifications to and refinements of the previous guidelines. The Horizontal Guidelines provide the EC Commission’s new analytical framework for the assessment of most common types of horizontal agreements, including: research and development agreements; joint production agreements; commercialization agreements and standardization agreements that fall outside the two block exemption regulations for specific types of horizontal agreements; the Specialisation block exemption regulation on unilateral and reciprocal specialization agreements and joint production agreements;<sup>3</sup> and the Research and Development block exemption regulation on joint research and exploitation of the results of joint research and development.<sup>4</sup>

As part of its review, the Commission has considerably revised these rules. Overall, the scope of both block exemption regulations has been amended significantly and, while on balance the new rules provide a more liberal, coherent, and user-friendly framework for companies to structure their agreements without losing the benefit of the exemption under Article 101(3) TFEU, the Commission has also taken the opportunity to tighten the rules in a number of important respects. In particular, it has extended the list of hardcore restrictions of the R&D rules and has limited the scope of the Specialisation block exemption regulation in the event the specialization or joint production agreement is entered into between vertically integrated companies and the agreement concerns intermediate products which at least one party uses captively for the production of downstream products. In that case, the new rules provide that the exemption only applies if, in addition to not exceeding a combined market share threshold of 20

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<sup>1</sup> Paul Lugard’s contribution is written in his capacity as Ass. Professor at Law at Tilburg Law and Economics Centre (TILEC). See also his comments on the Commission’s proposals, Paul Lugard, *The EC Commission’s Review of the EU Competition Rules on Horizontal Agreements*, 9(1) CPI ANTITRUST CHRON., September 2010.

<sup>2</sup> 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, available at <http://ec.europa.eu/competition/antitrust/legislation/horizontal.html>.

<sup>3</sup> 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 335/36.

<sup>4</sup> 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 335/43.

percent for the intermediate product, the parties' combined market share on the market for the downstream product does not exceed 20 percent. This new rule is introduced to prevent input foreclosure that would disadvantage downstream competitors.

Significantly, the final legislative texts incorporate many improvements on the drafts that the Commission had published for public consultation in May 2010. In their comments in the September 2010(1) *CPI Antitrust Chronicle* issue on the drafts of the two block exemption regulations and the Horizontal Guidelines, a number of authors identified several significant concerns. In this new issue the same authors evaluate the final text of the horizontal review package, revisit the concerns that they had identified on the basis of the draft texts, and express a much more favorable view.

The Commission must be commended for having been willing to engage in extensive consultations with stakeholders and for having been receptive to many suggestions for improvements. The contribution of Donncadh Woods to this issue of the *CPI Antitrust Chronicle* provides some valuable insights into the main issues that the Commission has been confronted with during the consultation process. CPI is especially appreciative of his contribution.<sup>5</sup>

## II. OVERALL APPRECIATION

While each of the authors in this issue identifies a number of remaining concerns in critical areas, the contributors are supportive of many modifications that the Commission has made to the 2010 drafts.

In particular Richard Taffet, commenting on the Chapter 7 of the Horizontal Guidelines on standardization agreements, concludes that, in contrast to the 2010 draft, the Horizontal Guidelines clearly brings out the dynamic competition-enhancing nature of intellectual property rights and reaffirm that standard setting and IP-related conduct only exceptionally raise anticompetitive concerns that, in any event, require a rigorous assessment before a violation can be established with sufficient certainty.<sup>6</sup> This is despite his observation that the Horizontal Guidelines, particularly paragraphs 263, 308, 321, and 269 still lack coherence in important respects.

Similarly, in his contribution, *The Good, the Bad and the Ugly*, Jorge Padilla is appreciative of the acknowledgment that standard setting generally gives rise to efficiencies that benefit consumers.<sup>7</sup> However, he is also concerned that IP holders, wishing to include their (essential) intellectual property in a standard, are, in practical terms, forced to commit to FRAND terms that may on, on balance, not be economically efficient. Padilla and Taffet share a number of important concerns with respect to the methodology that the Horizontal Guidelines lay down to evaluate excessive pricing claims in the IP and standard setting context. In his contribution, Mathew Heim also touches upon this theme and helpfully reminds the reader of a line of well-established case law with respect to the exceptional circumstances in which the exercise of IP

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<sup>5</sup> See Donncadh Woods, *The new EU competition rules for co-operation between competitors of December 2010*, 2(1) CPI ANTITRUST CHRON., February, 2011.

<sup>6</sup> See Richard Taffet, *Further Reflections on the Impact of the EC Horizontal Cooperation Guidelines on Intellectual Property Rights and Innovation*, 2(1) CPI ANTITRUST CHRON., February, 2011.

<sup>7</sup> See Jorge Padilla, *The Good, the Bad, and the Ugly: Comments to the Commission's Horizontal Guidelines—Standardization*, 2(1) CPI ANTITRUST CHRON., February, 2011.

rights may give rise to a finding of abuse under Article 102 TFEU.<sup>8</sup> In passing, he makes the valid point that FRAND commitments potentially also discipline licensees' conduct, and also explores the connection between the Horizontal Guidelines and other areas of EU competition law, in particular the Technology Transfer Guidelines.

In his insightful contribution, Lars Kjølbj expresses his appreciation that the Horizontal Guidelines, in many ways provide an improved analytical framework over the draft Guidelines. However, he signals an important meta-trend with respect to the application of Article 101(1) TFEU by the Commission. While in the past the Commission has shown a willingness to narrow down the scope of that provision to agreements that were, upon proper inspection and analysis, likely to have significant effects on competition, the current Horizontal Guidelines demonstrate a reverse trend by expanding the category of agreements that do not contain hardcore restraints, but that nevertheless have as their object to restrict competition. Kjølbj illustrates this point by analyzing the treatment of joint production agreements in the Horizontal Guidelines and the recent Article 9 decision in the *BA/AA/IB* airline alliance case.

Axel Gutermuth concludes that the revised texts of the Specialisation and Research and Development block exemption regulations are to be welcomed as they provide a more coherent and flexible framework and eliminate many instances of uncertainty that existed under the previous block exemption regulations. His contribution combines analytical rigor with practical insights and contains a concise analysis of the modifications to the previous block exemptions, as well as to the 2010 drafts and identifies a number of missed opportunities.

Finally, Andreas Reindl revisits the complex topic of information exchanges among competitors, a field in which practical guidance is most welcome in light of the Court's judgment in Case C-8/08, *T-Mobile Netherlands*. While the Commission has considered laying down its new policy in a specific block exemption regulation, it concluded that such an approach would not be feasible. Reindl's contribution concentrates on a particularly intricate practical and analytical problem: the distinction between unilateral information disclosures that fall outside Article 101 TFEU and unilateral, "spontaneous," non-reciprocal disclosures of strategic information that, even though market participants do not have an explicit agreement on sharing information, lead to sufficient coordination to meet the "agreement" requirement of Article 101 TFEU. As there has not been one single Court case specifically deciding in which circumstances such unilateral disclosures lead to sufficient coordination under Article 101(1) TFEU, Reindl observes that in this part of the Horizontal Guidelines the Commission enters uncharted waters.

In the second part of his contribution Reindl raises the question whether the analysis underlying the Horizontal Guidelines is exemplary of the "compartmentalization" of European competition law and whether the Horizontal Guidelines display an insufficient focus on general principles that apply across the entire specter of competition law. In this respect he convincingly unveils the diverging regulatory approaches regarding two types of conduct that raise fundamentally similar competitive concerns, namely the potential to increase market power by information exchanges and resale price maintenance.

### **III. THE IMPACT ASSESSMENT OF THE DRAFT HORIZONTAL GUIDELINES AND BLOCK EXEMPTION REGULATIONS**

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<sup>8</sup> See Mathew Heim, *Some Observations on the Treatment of Standardization Agreements in the EC Guidelines on Horizontal Cooperation Agreements*, CPI ANTITRUST CHRON., February, 2011.

Following the publication of the 2010 draft texts DG COMP conducted an Impact Assessment of its policy proposals and submitted its report to the Commission's Impact Assessment Board for review. The interim and final reports of the Impact Assessment Board contain valuable insights into the principal issues that the Commission identified and the pros and cons of the various policy options that it considered to remedy the perceived issues.<sup>9</sup> While the Impact Assessment procedure does not seem ideally suited for a critical, in-depth, independent appraisal of "proper" rulemaking in the field of antitrust policy and, perhaps, gives the lead Commission services a large degree of leeway in directing the attention to specific subjects, it does seem to have disciplined the internal procedure and deliberations within DG COMP that eventually led up to the new legislative texts.<sup>10</sup> The report submitted by DG COMP to the Impact Assessment Board also elucidates in various respects the final texts.

The Impact Assessment procedure is part of the Smart Regulation initiative and is intended to help the Commission make evidence-informed decisions, to design better policies, to take account of the expertise of external stakeholders, and to explain the costs, benefits, and rationales for its actions in a transparent manner. The Impact Assessment Board was set up in 2006 to review Impact Assessments that are carried out by the lead Commission service in accordance with Commission-wide guidelines. The Secretariat-General, in discussion with the lead services, decides which legislative initiatives should undergo an impact assessment. The Impact Assessment Board issued a first report on October 8, 2010, followed by a final report on December 14, 2010.<sup>11</sup>

The Impact Assessment Report notes both that horizontal co-operation is a prevalent behavior for innovating firms and also that, based on the Community Innovation Survey, approximately one-third of the innovating firms cooperate with other firms, while about fifty percent are involved in horizontal cooperation.<sup>12</sup> The methodology applied in the Report centers around a limited number of defined problems and a number of policy options. The main part of the assessment discusses the merits of the respective options on the basis of two main criteria, i.e. the impact on competition (and consumers) and on compliance costs borne by companies. Remarkably, the Report only includes rudimentary wording on the impact of the identified options on innovation and research.<sup>13</sup>

The Report discusses four specific problems of which two relate to standardization (*ex ante* disclosure of IPR and *ex ante* disclosure of most restrictive licensing terms), one to information exchanges, and one to the block exemption regulation on specialization agreements (introduction of a second market-share threshold for intermediate products).

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<sup>9</sup> See Impact Assessment Accompanying document to the Communication from the Commission Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements available at [http://ec.europa.eu/governance/impact/ia\\_carried\\_out/cia\\_2010\\_en.htm#comp](http://ec.europa.eu/governance/impact/ia_carried_out/cia_2010_en.htm#comp)

<sup>10</sup> The Impact Assessment Report itself notes also the difficulties associated with the provision of reliable quantitative data on the positive or negative impacts of the proposed policy options. As a result the Impact Assessment Board has chosen to confine itself to outlining the expected qualitative. *Id.* ¶ 8.

<sup>11</sup> See, *supra*, note 9.

<sup>12</sup> With regard to intellectual property rights the report refers to the steep increase of patent applications and indications that in the ICT industry between the eighties and 2004 approximately 70,000 standards have been developed, while each year about 3000 new ICT specifications appear. The report also refers to estimates of the number of standard-setting organisations worldwide (674 and 224).

<sup>13</sup> See in relation to *ex ante* disclosures of IPR, *supra* note 9 ¶¶ 84 and 85.

The Report makes clear that the policy options that the Commission considered with respect to the treatment of information exchange were limited to the questions whether or not a specific chapter on information exchanges should or should not be included in the Horizontal Guidelines; laying the new Commission's policy in this area down in a separate block exemption regulation was not deemed feasible.<sup>14</sup> The Report notes that in light of the need for comprehensive Commission guidance, as reflected by unanimous demands of stakeholders and national competition agencies, it is preferable to include a chapter on this type of conduct in the future guidelines. This is hardly surprising. The Report states that providing guidance will strengthen enforcement in high-risk areas, particularly in the event of exchanges of individualized future intentions on prices and quantities, while at the same time encouraging pro-competitive information exchanges. The new chapter is also thought to increase legal certainty, particularly for SMEs and reduce their compliance costs.

With respect to the risk of input foreclosure under the Specialization block exemption regulation in the event of captive users, the Commission faced a similarly simple choice: retaining the existing regime or introducing a second market-share threshold of 20 percent for the parties' downstream product. Eventually, it opted for the introduction of that threshold, because the new rule would eliminate the identified problem and would not lead to significant higher compliance costs. The Commission believes that, even though some companies that wish to avail themselves would have to assess their market shares on one or more downstream markets, many of those (vertically integrated) firms would already do so under the existing block exemption regulation to rule out the risk of a withdrawal of the exemption, or would already have a good understanding of their market shares on downstream markets.

This argument is somewhat curious. Indeed, if companies would already self-assess the risk of foreclosure in light of possible foreclosure risks, how large would the identified problem then be? The Report is unfortunately silent on this issue.<sup>15</sup> As a result, it is impossible to opine on the merits of the revised Article 3 of the Specialisation block exemption regulation with any reasonable degree of certainty.

With regard to the *ex ante* disclosure of most restrictive licensing terms in the context of standardization, the Commission considered four policy options: (i) making the *ex ante* disclosure of most restrictive licensing terms a necessary condition for compliance with Article 101(1) and (3), (ii) making those terms part of the safe harbor, (iii) making clear that those provisions, in principle, are not infringing, and (iv) not providing any guidance. The objective of *ex ante* disclosure of most restrictive licensing terms is to allow the standard setting organization to make an informed choice on the inclusion of a specific technological solution in a standard, thereby taking account of both technical and commercial considerations.

Somewhat surprisingly, while the Commission seems to have been of the opinion that early disclosure would be most beneficial for competition by providing for more information on the technological solutions at a time that the standard setting organization may still adapt its choice, it finally concludes that it would be preferable to merely stipulate that early disclosure regimes are not competitive (option iii). The reason is the lack of empirical evidence on how *ex ante* regimes function, combined with suggestions made by commentators that *ex ante* disclosure

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<sup>14</sup> *Id.*, ¶¶ 67.

<sup>15</sup> *Id.*, ¶ 55.



may not always result in more competitive pricing. This could particularly be so in industries with very complex technologies and where the technology and standards are simultaneously developed. The Commission appreciates that, in those cases, the uncertainty surrounding which patents will eventually read on the standard might not lead to lower prices and not allow for an efficient process of competition between technologies. Moreover, this approach would provide the necessary comfort for standard setting organizations to experiment with systems of *ex ante* disclosures, without creating a straightjacket or unduly incentivizing their use. Furthermore, the Commission does not expect compliance costs to rise.

It is submitted that the chosen approach is well-balanced. While there were clear indications that the Commission initially favored early disclosure systems, it has, upon reflection, decided that there was insufficient evidence that that policy option would, on balance, be efficient in the vast majority of cases. This is to be welcomed, especially in dynamic, high-tech sectors, where (successive) standards are often developed at a high pace.

Finally, the Commission considered a number of policy options in relation to the *ex ante* disclosure of intellectual property rights. These disclosure policies allow for members of the standard setting organization to obtain an early understanding of the (“essential”) IPR that might read on the standard under development. This, in turn, allows the standard setting organization to either request a (FRAND) licensing commitment from the IPR holder, or to try to work around that particular solution. IPR disclosures are also intended to avoid future “hold-up” problems. The Commission has considered three options: (i) making disclosure mandatory in the sense that such disclosure would be a necessary condition for compliance with Articles 101(1) and (3), (ii) requiring IPR disclosure in order to benefit from the safe harbor, and (iii) not requiring IPR disclosure in order to benefit from the exemption under Article 101(3), but instead provide an effect based guidance.

The Commission felt that a case-by-case assessment whether IPR (non-) disclosure policies of a standard setting organization would violate Article 101(1) and (3) would have the advantage of allowing for competition among various models of IPR disclosure, but would sufficiently incentivize companies and organizations to adopt IPR disclosure obligations. The alternative option, i.e. stipulating that the lack of clear IPR disclosure rules would, by definition, infringe Article 101(1) and not meet the conditions of Article 101(3), would be too stringent as it would disadvantage “participation” models whereby IP holders agree upfront that they would license future essential IP on FRAND or royalty terms.

The Commission seems to have been of the view that these types of IP systems are particularly applicable in situations where standards are developed within a short period of time, thereby allowing the quick proliferation of new or better products to consumers.<sup>16</sup> The cost of compliance for companies that wish to comply with an IPR disclosure regime would potentially be significant, but are mitigated by the fact that such rules would—as mandated by the Commission—not include costly patent searches, but are merely an obligation to use reasonable efforts to identify essential IPR.

It remains to be seen whether the Commission’s explicit wish—as expressed in the Impact Assessment Report—to not unduly disadvantage systems that do not contain mandatory IPR disclosure rules but, instead, up-front promises to license essential IPR, is adequately reflected in

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<sup>16</sup> *Id.*, p. 24.

the Horizontal Guidelines. Paragraph 281 provides that an IPR disclosure policy is a necessary condition for avoiding the application of Article 101(1). However, the Guidelines are less than crystal clear with regard to the conditions under which participation models meet the conditions of Article 101(3). Moreover, example 2 of paragraph 316, while not discussing up-front licensing requirements, supports the position that standard setting arrangements that lack clear IPR disclosure rules are unlikely to meet the Article 101(3) criteria. As a result, it seems that participation models, while relatively favorably looked upon in the Impact Assessment Report, are relatively ill-treated under the Horizontal Guidelines.

#### IV. A FEW CONCLUDING REFLECTIONS

The new rules provide an improved and much clearer framework. Nonetheless, there are a number of issues that may raise concern.

1. As Lars Kjølby points out in his contribution to this issue of *CPI Antitrust Chronicle*, the Horizontal Guidelines demonstrate a reverse trend by expanding the category of agreements that do not contain hardcore restraints but, nevertheless, have as their object to restrict competition.
2. The provisions with respect to FRAND commitments included in the standardization chapter tend to blur the distinction between Articles 101 and 102 by importing Article 102 considerations in the application of Article 101.
3. The FRAND provisions with regard to the establishment of whether royalties are not unfair (paragraphs 284 and 285) appear overly prescriptive and might have inefficient consequences in practice.
4. The treatment of standard setting arrangements under Article 101 (3) that do not incorporate IPR disclosure rules is unclear.
5. The statements that, by their nature, standards should not include “all possible specifications or technologies” and “should cover no more than is necessary to ensure their aims” (paragraphs 306 and 307) may create significant uncertainty as to the compatibility of the underlying standard setting arrangements with Article 101(3).
6. As Andreas Reindl explains in his contribution to this issue of *CPI Antitrust Chronicle*, the Commission’s new policy with regard to unilateral disclosure of strategic information to competitors has not been tested by the Court and may therefore give rise to disputes.
7. While it is undisputed that the new regime has an important impact on innovation, it is striking that the notion of innovation and the various shapes it may take, itself, is ill-articulated. In particular, the Horizontal Guidelines remain largely silent on the question of which type of innovation (breakthrough innovation, incremental innovation) merits protection. Overall, the Horizontal Guidelines seem to be slightly biased towards stimulating follow-on innovation, at times at the risk of discouraging “original” innovation. It would be helpful if the Commission would more clearly articulate its vision in the future.