

Electronics Update

Q2 2009

Welcome to the Spring 2009 issue of Bird & Bird's Electronics Newsletter, including articles from around Europe reporting current regulatory, commercial and intellectual property issues affecting the electronics industry. The debate over levies on electronic equipment, reported from Germany in our last issue, is now reaching the courts in Spain as well. The EU-wide environmental protection directives on recycling and constraining materials for use in electronics are under review after their first few years of road testing. And the complex issue of standardisation and its interplay with intellectual property rights is now being scrutinised by the German Supreme Court, whose decision will have a substantial impact for standards setting bodies whichever form of product they relate to.

From now on the newsletter, which has grown rather unwieldy in its volume of material, will be coming out on a quarterly basis rather than annually. We hope this will make it more useful both in terms of accessibility and also currency of information. Please do let us know what you find useful or would prefer to see done differently.

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European Court of Justice decision - *Intel Corporation Inc v CPM United Kingdom Limited*

For many years European national Courts have wrestled with the concept of how broad the protection should be for registered trade marks with a reputation.

A much anticipated decision was handed down on 27 November 2008 by the European Court of Justice (ECJ) providing the most comprehensive guidance on this to date.

The English Court of Appeal had referred several questions to the ECJ regarding the factors necessary to establish whether a later trade mark had taken unfair advantage of or was detrimental to the distinctive character or repute of an earlier trade mark for the purposes of Article 4(4)(a) of the Trade Marks Directive (the "Directive"). The ECJ held that the unique character and huge reputation of a mark like INTEL does not on its own prove the required "link" in the minds of the public between the earlier mark and a later mark, nor that the later mark has taken unfair advantage of or been detrimental to the



earlier mark. The ECJ provided useful guidance on the factors to be taken into account in assessing when there is a "link" and what amounts to unfair advantage and detriment.

Facts

Intel Corporation (**Intel**) is the owner of various national and Community trade marks incorporating the word INTEL, including a UK trade mark registration for the word mark INTEL for, essentially, computers and computer-linked goods and services. The INTEL mark has a huge reputation in the UK for microprocessor products and multimedia and business software.

CPM United Kingdom Ltd is the owner of a UK trade mark registration for the word mark INTELMARK, registered with effect from 31 January 1997 for 'marketing and telemarketing services' in Class 35.

On 31 October 2003 Intel filed at the UK Trade Mark Registry an application for a declaration of invalidity against the registration of the INTELMARK trade mark, claiming that the use of that mark would take unfair advantage of, or be detrimental to, the distinctive character or the repute of the earlier INTEL trade mark within the meaning of section 5(3) of Trade Marks Act 1994 (the UK implementation of Article 4(4) (a) of the Directive).

Intel's application failed, as did its subsequent appeal to the High Court. Intel then appealed to the Court of Appeal,

arguing that both Article 4(4) (a) and Article 5(2) of the Trade Marks Directive seek to protect a proprietor of a trade mark with a reputation against the risk of dilution. It argued that the mere "bringing to mind" of the earlier mark was sufficient to establish a "link" between the earlier and later marks, thus resulting in the invalidity of the later mark. The Court of Appeal referred several questions to the ECJ regarding the factors necessary to establish whether a later trade mark had taken unfair advantage of or was detrimental to the distinctive character or repute of an earlier trade mark for the purposes of Article 4(4) (a).

Decision

Detriment to distinctive character – what does this mean?

The ECJ held that detriment to the distinctive character of the earlier mark (which it noted was also referred to as dilution or blurring) is caused when that mark's ability to identify goods or services as coming from the proprietor of that mark is weakened.

Is the public required to make a connection or "link" between the earlier and later marks?

If the relevant section of the public has not made a "link" between the earlier and later marks, the use of the later mark is unlikely to take unfair advantage of, or be detrimental to, the distinctive character or repute of the earlier mark. However, the

existence of the link, in itself, is not sufficient to establish the required injury under Article 4(4).

Who is the relevant public?

The "relevant public" depends on the type of injury alleged:

- For the purpose of establishing detriment to the distinctive character or repute of the earlier mark it is the average consumers of the goods and services for which the earlier mark is registered;
- For the purpose of establishing unfair advantage, it is the average consumers of the goods or services for which the later mark is registered.

Proof

The owner of the earlier mark must prove that there is either 1) an actual and present injury or 2) a serious risk of such injury.

Establishing a link between the earlier and later marks

Whether there is a link between the earlier mark with a reputation, and the later mark must be assessed globally, taking into account all factors relevant to the circumstances of the case. Factors to be considered include:

- the degree of similarity between the conflicting marks: the more similar the marks, the more likely that there will be a link established;



- the nature of the goods or services for which the conflicting marks were registered, including the degree of closeness or dissimilarity between those goods or services, and the relevant section of the public;
- the strength of the reputation of the earlier mark; for example, if it extends beyond the relevant public for the goods and services for which it was registered, a link may be more likely to be established;
- the degree of the distinctive character of the earlier mark (whether inherent or acquired through use); the stronger the distinctive character, the more likely that there will be a link established; and
- the existence of the likelihood of confusion on the part of the public (although the ECJ noted that the Directive does not require likelihood of confusion).

The fact that, for the average consumer, the later mark calls the earlier mark with a reputation to mind is tantamount to the existence of such a link between the conflicting marks.

Criteria for establishing unfair advantage and/or detriment

The existence of unfair advantage or detriment or a serious likelihood that those will occur in the future must be assessed globally, taking into account all factors relevant to the circumstances of the case.

Even if there is a link between the earlier mark and the later mark in the mind of the consumer, the trade mark owner must still show actual and present injury or a serious likelihood of injury.

What is required in order to satisfy the condition of "detriment to distinctive character"?

Proof that the use of the later mark is or would be detrimental to the distinctive character of the earlier mark requires evidence of a change in the economic behaviour of the average consumer of the goods or services for which the earlier mark was registered consequent on the use of the later mark, or a serious likelihood that such a change will occur in the future. It remains to be seen what kind of evidence will satisfy this criteria.

**Peter Brownlow and Emily Forsyth,
London**

Batteries Directive

EU legislation that aims to protect the environment by ensuring waste batteries are properly collected and recycled is now in force in Europe. The Directive makes producers responsible for the management of batteries once they become waste. Adopted by the European Parliament and Council in 2006, the revised Batteries Directive should be

transposed by Member States into national law. At least seven Member States have notified to the Commission national legislation which fully transposes the Directive.

Peter Ward, London

Software patents in Europe – the next instalment...

The law concerning patents for software-related inventions in Europe has followed a tortuous development with divergent approaches being adopted both in the European Patent Office ("EPO") and in national patent offices and courts (see summary in our **Q2 2008 newsletter**). A recent referral to the EPO Enlarged Board of Appeal has, however, raised hopes that an authoritative decision may be given shortly (this year or next year), clarifying for the future the limits of software patentability in Europe.

Divergent approaches: EPO and national courts (England)

The approaches of the EPO and national courts have diverged in many respects, one of which is described below.

When considering software patentability, the EPO Boards have tended to focus on the "technical contribution" or "technical character" of an invention. The exclusion



from patentability of computer programs "as such" has been interpreted as referring to cases in which the invention has no "technical character" or makes no "technical contribution" to the known art.

The English Court of Appeal, in its decision in *Aerotel v. Telco/Macrossan* ([2007] RPC 7), suggested that it might be adopting a different approach. It adopted a four stage test for assessing patentability which involved checking for a technical contribution after considering excluded subject matter:

- (1) properly construe the claim;
- (2) identify the actual contribution;
- (3) ask whether it falls solely within the excluded subject matter; and
- (4) check whether the contribution is actually technical in nature.

More recently, in an appeal relating to Symbian's application for a patent relating to the mapping of dynamic link libraries in a computer (*Symbian v Comptroller General of Patents* [2008] EWCA Civ 1066), the Court of Appeal has sought to reconcile the two approaches. It observed that there is no reason why the test as to patentability should not turn on whether the contribution can be characterised as "technical". Such an approach may be reconciled with the *Aerotel* four stage test simply by conflating the third and fourth stages so that they are decided together.

The Court of Appeal concluded by finding in favour of Symbian. It could be said that the Symbian instructions "solve a

'technical' problem lying with the computer itself". As a matter of [practical] reality there is more than just a 'better program', there is a faster and more reliable computer."

The next instalment...

In October last year, the President of the EPO referred a point of law – concerning the application of the exclusion of computer programs as such – to the Enlarged Board of Appeal of EPO (case G3/08). The referral raises four questions, one relating to the form of the claims and three relating to where the line should be drawn between those aspects excluded from patentability and those which contribute technical character.

In light of the referral, the UK Intellectual Property Office (UK-IPO) stated that it would not seek to appeal the *Symbian* judgment to the House of Lords. It considered that it would be premature to seek a view from the House of Lords when European practice is likely to be settled shortly by a decision of the EPO's Enlarged Board of Appeal. In the meantime, the UK-IPO issued a Practice Notice (dated 8 December 2008) stating that it would continue to apply the structured approach of *Aerotel/Macrossan* to determine the patentability of a computer program-related invention.

The EPO Enlarged Board of Appeal has invited third parties to file written observations in relation to case G3/08 by the end of April 2009. At least one has

already been filed and it is likely that they will be numerous.

As observed by the UK-IPO, the Enlarged Board of Appeal has the ability to make a definitive statement of EPO practice and as such also carries significant weight in terms of the practice adopted by the UK-IPO and other national Patent Offices within Europe. It is to be hoped that the decision of the Enlarged Board of Appeal in due course does indeed provide the definitive guidance which is sought to clarify the limits of software patentability in Europe.

Anna Duffus, London

The Performing Rights Society launches consultation on code of practice

PRS for Music (formerly the MCPS-PRS Alliance the UK's copyright collecting society for music copyrights) has launched a consultation process open to all interested parties for its proposed new Code of Practice. It is intended to cover all aspects of the PRS' music licensing activities including commitments to service levels, licence payment information and complaint procedures. The consultation period ends on 1 May 2009.

Peter Ward, London



Landmark case on cartel law defence pending before German Federal Supreme Court

On 10 February 2009, the oral hearing took place before the German Federal Supreme Court in a landmark case concerning the relationship between patent law and competition law in general, and the relevance of competition-law-based arguments in patent infringement proceedings in particular.

In 2001, Philips sued a manufacturer of compact discs before the Regional Court Mannheim for alleged infringement of a patent essential to the so called "Orange Book standard" which is the standard for recordable compact discs (CD-R, CD-RW). The defendant argued non-infringement and invalidity and in addition raised the competition law defence. The competition law defence in German patent infringement proceedings is based on the principle that it is against good faith to assert a standard-essential patent by way of a cease and desist claim whilst the patent owner refuses to fulfil his obligation under EU and German competition law to grant a licence under fair, reasonable and non-discriminatory terms and conditions. In the "Orange Book" case the Regional Court Mannheim did not accept the competition law defence and ordered the

defendant to cease and desist. The court doubted whether the competition law defence was admissible but in any event stressed that the defendant had not sufficiently substantiated the preconditions for such a defence, i.e. discrimination and/or abusive licence fees.

The Higher Regional Court Karlsruhe rejected the defendant's appeal. The court was inclined to accept the competition law defence as admissible but just like the first instance, denied that its preconditions were met. The court ruled that discrimination was not substantiated by the defendants and that an abuse of a market dominant position based on excessive licence conditions would only lead to a valid defence if the defendant submits an offer which was so high that any increase in favour of the patentee would be abusive. The court did not allow a second appeal to the Federal Supreme Court but upon the defendants' complaint the Federal Supreme Court accepted the case on basis of its general importance.

Contrary to the Regional Court Mannheim, the Regional Court Düsseldorf clearly accepted the competition law defence in a number of decisions (see separate article in this issue) but there is no specific decision yet of the German Federal Supreme Court. Accordingly, the decision of the Federal Supreme Court in the "Orange Book" case will be of significant importance as to the extent a defendant in patent infringement proceedings is able to defend himself against cease and desist claims on the basis of competition law

without having to initiate separate competition law proceedings against the patent owner.

In the oral hearing which took place on 10 February 2009, the plaintiff's representative argued against the admissibility of the competition law defence by focusing on the argument that patent infringement proceedings would be overloaded and delayed if the competition law defence was accepted. The defendant mainly countered this by stressing that the alleged infringer must be allowed to raise the defence in patent infringement proceedings as there is no realistic possibility to otherwise get access to the patented technology and, thus, to the relevant industry standard. It was stressed that a licence is not available through preliminary injunction proceedings, while proceedings on the merits claiming for a licence could take many years.

The competition senate of the Federal Supreme Court did not give a clear indication if it is inclined to accept or deny admissibility of the defence. However, some specific questions raised by the judges gave the impression that the court is inclined to accept the defence. The decision will be rendered on 6 May 2009. The decision will have a very significant impact on patent infringement proceedings in Germany as far as patents that are essential to important industry standards are concerned. Accordingly, especially from the defendants' point of view, this upcoming decision of the German Federal Supreme Court will have



tremendous impact on the strategy on how to activate EU and German competition law in the most efficient way to defend against cease and desist/patent infringement claims.

Dr Jörg Witting, Düsseldorf

The United Kingdom Intellectual Property Office and China: agreement on streamlining patent and trade mark application procedures.

The Intellectual Property Office (IPO) has announced that the UK and China have signed agreements on patents and trade marks following meetings in February 2009. In anticipation of China becoming the leading patent filing nation by 2012 and in an attempt to reduce the existing worldwide backlog in processing applications, the agreements provide for UK and Chinese patent examiners to make more use of each others' work and reduce duplication in examination procedures. The IPO will also co-operate with the Chinese Trade Mark Office to exchange ideas on best practice and training.

Peter Ward, London

Copyright levies across Europe – German and Spanish decisions

Barcelona - the copyright levy on digital devices: private vs. professional/official use.

On 15 September 2008 the Barcelona Commercial Court of Appeals stayed an action between the major collecting society in Spain (known as SGAE) and Padawan, S.L. to refer a judicial question to the ECJ. Questions referred to the ECJ are always of general interest, but this one is especially important because of the economic implications it may have for manufactures, distributors and resellers of digital devices subject to the copyright levy.

The question raised by the Barcelona Court can be simply stated as: is a professional/official use of a digital device subject to the copyright levy? Responding to this question might not be easy for the ECJ. The Barcelona Court framed its question extensively by requesting that the ECJ also decide upon: i) the nature of copyright levy itself (is it a Community concept that must be harmonised?); ii) the very last ratio of its existence (is the fair compensation set with the aim of keeping the IP rights holder fully compensated?); and iii) the methods to accrue such compensation (is the Spanish system incompatible to such ratio if we apply the copyright levy to all digital devices

irrespective of professional/official use – as opposed to private use?).

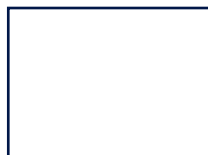
Facts

SGAE commenced a civil action requesting the Court to impose a payment for the copyright levy generated by Padawan, S.L.'s marketing of blank media (DVD-R, DVD-RW, CD-R, CD-RW) and MP3 from September 2002 to September 2004. At first instance, the case resulted in the court granting €16,759.25 plus costs to SGAE.

Padawan, S.L. appealed the decision and argued before the Barcelona Court of Appeals that imposing the copyright levy on digital devices without taking consideration of the purpose (whether it be for private or professional/official use) is contrary to the EU Directive 2001/29/CE.

Fair compensation as a Community concept

The Barcelona Court of Appeals is concerned by the wide scope of the copyright levy in Spanish internal regulation. It wants to know whether it can affect the nature of the levy itself, i.e. whether it can establish whether there a relationship exists between the levy and the damage for which the levy is intended to compensate. The Court is doubtful that (i) a levy should be generated where no private copy actually exists (because it considers that professional or official use does not qualify as a copy for levies, so there would be no reason for compensation); and (ii) if the copyright



levy, as it is currently applied, is contrary to EU Directive 2001/29.

In its statements, the Court expressly stated its support of the opinion issued by Internal Markets Commissioner Charlie McCreevy before the EU Parliament on 19 September 2007.

Making express reference to the ECJ ruling on 6 February 2003 (C-245/2000), *Sena*, the Barcelona Court of Appeals wished to know whether the ability of each Member State to establish a private copying exception to copyright infringement should be limited by an harmonised concept for fair compensation. In the *Sena* case¹ the ECJ considered that the concept of equitable remuneration under Article 8.2 of the EU Directive 92/100/EC should be construed following ECJ doctrine in cases *Linster* (C-287/1998, para. 43) and *Yiadam* (C-357/1998, para. 26). In these cases the ECJ ruled that the terms of a provision of Community law which makes no reference to the law of the Member States for the purpose of determining its meaning and scope, must normally be given an autonomous and uniform interpretation throughout the Community. Such interpretation must take into account the context of the provision and the purpose of the legislation in question.

Although the Court of Appeals accepts as starting point that "fair compensation" and "equitable remuneration" are different concepts, it also considers that both are

linked since each remuneration must have a "compensatory nature".

Harmonisation in the respect sought by the Barcelona Court would not affect the Court's understanding of its internal regulations in respect to collecting methods as long as they do not alter the true (and harmonised) nature of the copyright levy.

Although the Advocate General's opinion is expected sooner, the ECJ will not render a decision in less than two years. In the meantime, the collecting societies may encounter some difficulties from manufacturers, importers or resellers who, attending to the circumstances, may choose a third party (consignor) to collect the monies so that they are either released to the collecting societies or revert back to manufacturers, etc. depending on the final opinion. Alternatively they may elect to avoid payment or claim the monies back after payment.

In any event, as different as the internal regulations (in respect of the copyright levy) are, and the eventual impact that this reference to the ECJ may have on the principle of free movement of goods within the EU, the harmonisation of the concept and implications of the copyright levy seems a sensible response.

Fidel Porcuna de la Rosa, Madrid

German Federal Supreme Court - printer levies

In two landmark judgments of 6 December 2007 and 30 January 2008, the German Federal Supreme Court ("FSC") has ruled that the so called "reprographic copyright levy" – implemented by the German legislator to compensate for licence-free copying made with traditional photocopiers – does not apply to single function printers. The levy was applied to multifunctional printers which have a photocopying function under the old German Copyright Act in effect until 31 December 2007, which thus applies to all products manufactured, imported or sold before 31 December 2007.

The rejection of reprographic levies on (single purpose) printers and the expected rejection of reprographic levies on PCs may mark a turning point in the excessive application of reprographic levies on digital devices in Germany. The reasoning of the first judgment also indicates that no reprographic levies apply to PCs under the law applicable until 31 December 2007. However, the application of the so called "audio and video recording copyright levy" – implemented to compensate for licence-free copying made with traditional analogue audio and video recorders – is still a major threat for many digital devices and storage media sold in Germany and elsewhere in the EC (such as PCs, mobile phones with music functions, memory

¹ Paragraph 38.



cards or TV set-top-boxes). In addition, the new German copyright levy regime applicable from 1 January 2008 has reopened the discussion on printer levies.

The copyright law applicable in Germany until 31 December 2007, and the copyright law applicable in some other European jurisdictions, provides for two different levies: an "audio and video recording copyright levy" originally aiming to compensate for private recordings made with analogue audio and video recorders and the respective storage media, and a "reprographic copyright levy" originally aiming to compensate for reprographic copying made with photocopying machines. In most European countries, it is disputed whether copyright levies also apply to modern digital IT and entertainment hardware and storage media (such as PCs, handheld computers, single function printers, multifunctional printers, mobile phones or navigators with music function, MP3 players, TV set-top-boxes, memory cards and USB sticks) and, if so, which levy amounts are applicable. Copyright levies are usually payable by the manufacturers, importers and/or dealers of the devices and media concerned by the levies.

1. FSC decision on single function printer levies

The decision, given in a test case between Hewlett-Packard and the German collecting society, VG Wort, is that no reprographic copyright levies and, thereby, no copyright levies at all apply to single

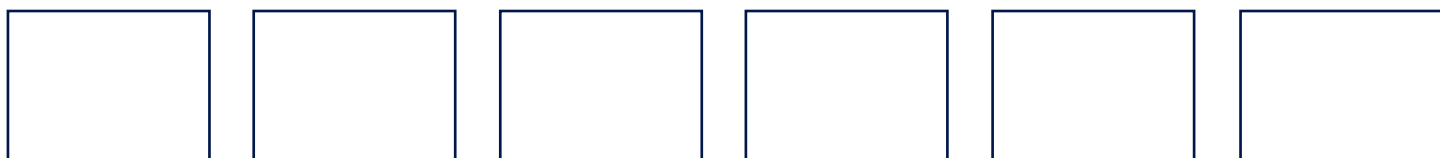
function printers under the German Copyright Act applicable until 31 December 2007 (judgment of 6 December 2007, ref. no. I ZR 94/05). This decision is of major economic importance. The collecting societies claimed reprographic levies of €10 to €300 (depending on the printing speed) for each single function printer sold between 2001 and 2007. In total, the judgment saved the printer industry several hundred millions of Euros.

In its reasoning, the FSC stated that single function printers can only be used for "reprographic" copying if used together with a PC and a scanner in a similar manner as a traditional photocopier. However, in this scenario only the scanner is subject to the reprographic levy (cf. judgment of the FSC of 5 July 2001, ref. no. I ZR 335/98, regarding copyright levies on scanners). In all other cases, there is no reprographic, but only digital copying. The FSC argued that the situation of digital copying cannot be compared with reprographic copying (in particular with respect to the harm which right holders suffer). Copying of books, magazines and other hardcopy text and picture works by photocopiers are normally not permitted by right holders, but cannot be prevented by them. However, the print-out of digital works is often expressly licensed or, by publishing the works without any copy protection, impliedly allowed by the right holders. In case of an express or implied licence, no copyright levies apply. Therefore, the FSC decided that single function printers cannot be compared with

traditional photocopiers and are thus not subject to the "reprographic copyright levy".

These arguments used by the FSC in its judgment of 6 December apply equally to the question of whether PCs are subject to reprographic levies. PCs can be used for reprographic copying together with a scanner (where only the scanner is subject to the levy). In cases of digital copying, the arguments set out with respect to printers are just as valid with respect to PCs. Thus, it is expected that in proceedings on the point now pending the FSC will reject the application of reprographic levies on PCs. The collecting societies claim a reprographic levy of €30 per PC put onto the market in Germany (irrespective of price and PC capacities) and the economic importance of this decision is as high as the importance of the single function printer decision. The judgment of the FSC is expected to be rendered in autumn of this year.

Finally, it should be noted that the collecting society is considering filing a constitutional complaint before the German Constitutional Court against the judgment of the FSC in the single function printer case. The chance that such a constitutional complaint is successful is rather low, but can not be absolutely excluded at the outset. It may take a couple of years until the Constitutional Court renders its decision.



2. FSC decision on multifunctional printer levies

The FSC has further decided that the multifunctional printers marketed by Hewlett-Packard until 31 December 2001, which can photocopy, are subject to the same reprographic levy amounts as traditional photocopiers under the German Copyright Act applicable until 31 December 2007 (judgment of 30 January 2008, ref. no. I ZR 131/05). These amounts are high (€76.70 to €613.56 for multifunctional printers which can make colored copies). They exceed the manufacturer's margins by far in the years until 2001 and even exceed the end-user purchase prices of low-end ink-jet multifunctional printers today. Therefore, Hewlett-Packard may consider filing a constitutional complaint before the German Constitutional Court against the judgment of the FSC.

The reasoning of the judgment has not been issued. In its press release, the FSC stated that it is bound in principle by the legislator's decision to set concrete statutory tariffs for all devices which enable acts of reprographic copying. In the oral hearing, the FSC acknowledged that the statutory tariffs are too high in light of the decreasing device prices and the changed use of such devices. The FSC expressly said that it was a "mortal sin" of the legislator to introduce inflexible fixed tariffs. However, both in the oral hearing and in the press release, the FSC argued that a court can only deviate from statutory tariffs in very extreme cases. The

FSC stated that such an extreme scenario was not presented in the case at hand.

Therefore, it is not yet clear whether the FSC holds the opinion that the full photocopier levy amounts also apply after 31 December 2001 when device prices dramatically decreased. The industry and the collecting societies hope that the reasoning of the judgment (which is expected to be issued within the next few months) will give unambiguous indications for the application of the reprographic levy to multifunctional printers also after 31 December 2001. However, it is not sure that the reasoning of the judgment will contain such clear guidance for the years following 2001 since that was not the question before the court.

Outlook

The two recent decisions of the FSC only deal with reprographic levies under the old law. Nevertheless, they give certain indications with respect to the disputed application of the audio and video recording levy to PCs, mobile phones with music functions and mobile phone memory cards under the old German Copyright Act applicable until 31 December 2007 and even some indications for the applications of levies under the new law applicable from 1 January 2008. In particular, the arguments of the FSC regarding the differences between analogue and digital copying suggest that the levy amounts for digital devices and storage media must be substantially lower than the amounts set out for reprographic

copying devices, analogue audio and video copying devices and storage media under the old law.

In the European Union, the situation on copyright levies substantially differs in the individual Member States. Whereas some countries such as the United Kingdom or Ireland have no copyright levies at all and further countries such as the Scandinavian States and Greece do not apply levies to multipurpose devices such as PCs and mobile phones, collecting societies in other countries such as Germany, France, Spain and Hungary currently request levies even on mobile phones with music functions, memory cards and/or PCs.

An earlier initiative of EC Internal Markets Commissioner Charlie McCreevy to harmonise copyright levies was stopped after political pressure from certain Member States in December 2006. McCreevy and the commission re-launched the consultation process on "Private Copying Levies" on 14 February 2008. The re-launch raises hope for harmonisation and for the introduction of clear EC limits to the excessive application of levies in certain Member States.

If the initiative for harmonisation is successful, it will still take some years until the respective decisions have been implemented by the Member States and an agreement on the European level is reached. Accordingly, the uncertainty and inequality will remain for several years yet.

Fabian Niemann, Frankfurt



United Kingdom Government publishes interim report on Digital Britain

The UK Government's Department for Culture, Media and Sport and Department for Business, Enterprise and Regulatory Reform has published an interim report entitled *Digital Britain*. The report addresses proposals relating to subjects such as future fixed and mobile next-generation networks, universal access to broadband internet services, the creation of a second public service broadcaster, the reform of wireless radio spectrum holdings, and the status and delivery of digital services and digital content. One aim of the Government's *Digital Britain* action plan is to have universal access to broadband services by 2012.

Peter Ward, London

E-signatures and E-identification Action Plan

The European Commission has published an action plan to establish a framework supporting electronic signatures and identification. This has been welcomed following a perceived lack of progress in the field since the Electronic Signatures Directive in 1999.

Peter Ward, London

Local judgment with an international economic approach - new German case law on the FRAND defence in patent litigation

With a series of decisions of 11 September 2008, the highly regarded Regional Court Düsseldorf has further specified the so-called FRAND defence in an international patent case in the Electronics sector.

For some years, the competent patent infringement chambers of the Regional Court Düsseldorf have accepted the competition law objection as an admissible defence in patent infringement proceedings. According to this standing

case law, the defendant in a patent infringement proceeding can defend himself by stating that the enforcement of patent infringement claims would be an abuse of the law pursuant to § 242 BGB (German Civil Code), because the patentee is obliged to grant him a licence to the infringed patent under the rules of competition law (cf. Regional Court Düsseldorf, in: InstGE 7, 70 et seq. – Videosignal-Codierung I). This defence particularly applies to cases where the patentee is required to grant the defendant a fair, reasonable and non-discriminatory (so-called FRAND) licence on basis of contractual claims (e.g. obligation to grant FRAND licences in standardisation agreements) or the law (e.g. Art. 81, 82 ECA). In its landmark decision Siemens vs. Amoi (Regional Court Düsseldorf, decision of 13 February 2007, 4a O 124/05) the Regional Court Düsseldorf was the first reported court to dismiss a patent infringement action solely for this reason.

In the present case several licensors of the MPEG LA LLC patent pool had sued a Danish DVD replication company and some of its subsidiaries and directors for patent infringement in Germany and Denmark. MPEG LA grants licences for a number of patents that are, according to its own view, essential for the use of the MPEG-2 ISO standard for transmission and storage of video signals. MPEG-2 is a very successful standard that is used e.g. in DVD video systems, set-top-boxes, DVB-T devices, personal computers etc. So far 25



licensors have contributed about 800 patents in 57 countries to the MPEG-2 patent pool. Presently, more than 1,400 licensees are licensed worldwide under the MPEG-2 standard agreement offered by MPEG LA.

The DVD replication company's group produced DVDs in Denmark and distributed these for the most part in Scandinavia, but also in small numbers in Germany through its German subsidiary. After being sued in Germany by the MPEG LA licensors the company requested a standard licence from MPEG LA, but limited to the territory of Federal Republic of Germany. The German subsidiary had asked for a worldwide standard licence. MPEG LA had refused to grant any regional licences, arguing that this would disregard the major Scandinavian sales. These sales, however, were the subject of a parallel patent infringement action pending in Denmark.

The Defendants raised the competition law licence objection stating, as its reason, that MPEG LA has refused to grant the requested licence for Germany. The Defendants alleged that by an abuse of the German legal system the Claimants were attempting to force Defendants into a worldwide licence for all patents licensed by the MPEG LA, some of which were not subject of the German litigation.

The court found that a patent pool licence offer of the patent owners participating in the standard is, however, per se not a competition law infringement because the

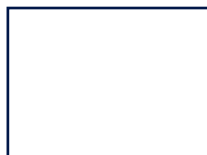
European Commission, in its "Guidelines on the application of Article 81 of the EC Treaty to technology transfer agreements", does not articulate any fundamental reservations with respect to technology pools. This is true even if they – de facto or de jure – support an already existing industry standard (paragraphs 210-211).

If the patent owner is in principle willing to grant a licence, there would only be one question under competition law. The question would be whether its licensing practice is discriminatory (because those asking for a licence are treated differently without a substantial reason); or whether it asks for unjustified royalties (so called exploitation abuse). Thus the court concluded that the Claimants could choose whether to offer individual licences or a patent pool licence, as long as they do not categorically refuse to conclude a licence agreement.

In addition to these options the court did not see a reason to adopt the third possible solution of a "territorial pool licence". Such a licence would perhaps be relevant when a worldwide licence seems unreasonably broad to a customer in view of his sales territory, he might limit himself to obtaining individual licences for the countries of his sales territory. However, this had not been done. The court found that the Defendants acted contradictorily when demanding modifications of the standard-pool licence agreement that could have been realised by means of individual licences.

The court further argued that the Claimants and MPEG LA are not forced to offer a territorial pool licence because the rule of equal treatment forbids Claimants to treat different licensees unequally without any justifying reason. As MPEG LA has not so far granted modifications comparable to those requested, the Defendants could not request such a licence on the basis of discrimination. The court points out that DVDs are "volatile goods" where the export to non-licensed countries has no practical obstacles. Therefore, a territorial licence as requested by the Defendants would involve a hardly controllable risk of abuse. The Claimant would therefore be allowed to generalise when offering a pool licence agreement in order to meet this abstract risk of abuse.

The court went on to state that the Claimants were justified in refusing the specific request of the German subsidiary on the grounds that the Defendant's group owed a considerable amount of royalties to the MPEG LA because of past patent infringements. The Claimants could not be expected to grant a standard licence agreement – in addition one that is only for a subsidiary of a corporate group – without a provision in the licence agreement specifying the extent to which royalties have to be paid additionally for past patent infringements. Otherwise, the owners of the proprietary rights would be in danger that other (potential) licensees could be motivated to use their technology without obtaining a licence and to then



show willingness to take a licence only after the discovery of the infringing activities.

The court found that there is a danger that if the Claimants had an obligation to grant an individual licence to a single subsidiary, corporate groups would be tempted to avoid the obligation to pay royalties for past infringing activities by forming new subsidiaries. Past patent infringements by several companies of a group justify the ambition of the patentees to conclude cumulative licence agreements with all companies belonging to the corporate group that are active in the corresponding field of business with retrospective effect, thereby including any missing royalties of all companies belonging to the corporate group. Last but not least, this request would be justified also with respect to the principle of the obligation to treat all licensees equally: law-abiding licensees would be discriminated against significantly if their competitors were permitted to undercut them in price because they had been economically strengthened by saving past royalties.. In the view of the court this would generate a danger of distortion of competition within the market.

With this decision, the Regional Court Düsseldorf has clearly strengthened the position of owners of standard essential patents as potential licensees are not able anymore to benefit on the one hand from a pool licence and to limit on the other

hand territory of the licence. But the decision also shows a generous view of the Court on international licence practice. Interestingly, it allows patentees to force potential infringers into global licences with an action in only one country. Thus, it could avoid costly parallel litigation. The Defendant, however, loses the option to use the many opportunities of the national driven European patent court system. And this system is typically considered and used by patentees when taking action in the appropriate forum.

Christian Harmsen, Düsseldorf

European Council adopts a Common Position over amendments to the E-Privacy Directive

The European Council has adopted a Common Position on the amended proposal for changes to the E-Privacy Directive (2002/58/EC). The Common Position builds on proposals developed by the European Commission during 2008. The Council proposes further revisions to the data security breach notification system proposed by the Commission, to the right of providers to use traffic data for network and information security purposes, and the right of natural and

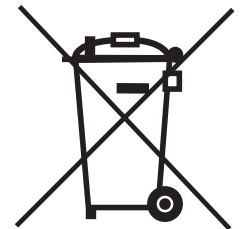
legal persons to bring legal actions against third parties for infringement of the E-Privacy Directive. The Common Position will now go to the European Parliament for second reading after further scrutiny in committee.

Peter Ward, London

Have electrical and electronic products been cleaned up?/how green is your EEE?

Recognise the symbol?

As consumers we are all now familiar with the "crossed-out" wheelie bin symbol which appears on all electrical and electronic goods



put on sale since 13 August 2005 and which will also identifies the producer.

But many consumers will not be aware what this really means vis à vis the obligations of the retailer from which they have bought the product or how the manufacturer of that product is affected.

There has been much discussion by manufacturers as to whether their products are covered or not by the WEEE¹

¹ Directive 2002/96/EC on Waste Electrical and Electronic Equipment



Directive (which sets minimum collection, recycling and recovery targets to reduce the quantity of waste discarded – see table at end of this article as to current product categories and targets) and RoHS² Directive (which restricts the use of certain hazardous substances in equipment) and interpretation issues, for example for the exclusion of fixed installations or whether electricity is needed for the primary function of the equipment³. Nevertheless, there has, in the UK at least, been very limited litigation as a result of this legislation. There have also been major concerns as to how the collection and recycling obligations would be financed. The latter was one of the main reasons the UK was late in implementing the two Directives. This contrasts with the number of prosecutions that have been brought in the UK over the disposal of waste in general in breach of the waste management regulations, now the Environmental Permitting Regulations 2007.

This is also surprising, as the European Commission has confirmed that the two Directives have not been as successful as it had hoped in encouraging the collection and recycling of waste electrical and electronic equipment or in ensuring certain substances are not contained in

such products. In addition the lack of harmonisation in their implementation and market surveillance between EU Member States has been an issue.

So, almost 5 years after the WEEE Directive entered into force, 6 years in the case of RoHS Directive, the Commission has published proposals⁴ as to revisions to be introduced in an attempt to improve, simplify and also harmonise these rules with other EU legislation (for example the REACH⁵ regulation). The aim is that the original objectives of reducing the impact on the environment of our increasing reliance on electrical and electronic equipment and protecting human health can be met.

Have the Directives been successful?

The Commission has stated that currently only about a third of waste electrical and electronic equipment is reported as being treated in accordance with the WEEE Directive. This means, therefore, that two-thirds is still going to landfill, either in or outside the EU. Illegal trade of electrical waste to non-EU countries is also still widespread. In addition the EU has confirmed that many electrical and electronic products are not complying with

the substance restrictions set out in the RoHS Directive, partly due to enforcement difficulties.

The EU figures reveal that, in weight terms, each year the equivalent of 80% of the EEE put on the market the previous year becomes waste. Of this 80%

- 26% is reported as properly collected and treated;
- 2% is reused;
- 10% is landfilled; and
- 42% is separately collected but not accounted for

As a result, the environmental and health risks posed by these products continues to be a concern, and so the sector can expect to face greater monitoring and checking by the regulators than has been the case to date. A producer⁶ of such products will, as a result, need to be even more vigilant as to the components it is using, the raw materials it buys or equipment which it rebrands and sells on, and will need to make sure it has robust contractual provisions in place with its suppliers and verifying procedures within its own manufacturing facilities. R&D, innovation and design will continue to have a key, and probably greater, role as more and more substances are determined as posing an

² Directive 2002/95/EC on the Restriction of the Use of Certain Hazardous Substances in Electrical and Electronic Equipment.

³ Electrical and Electronic Equipment ("EEE") means equipment which is dependant on electric currents or electromagnetic field in order to work properly.

⁴ On 3 December 2008.

⁵ EC1907/2006: The Registration, Evaluation, Authorisation and

Restriction of Chemical Substances.

⁶ This is defined as any person who:

(i) manufactures and sells EEE under its own brand name;

(ii) resells under its own brand equipment produced by other suppliers;

(iii) imports or exports EEE on a professional basis into a Member State.



unacceptable risk to the environment and human health and temporary exemptions for substances are removed.

Proposals to amend the RoHS Directive

(i) What is banned?

The ban imposed by the RoHS Directive as to the use of four heavy metals⁷ (lead, cadmium, mercury, hexavalent chromium) and two brominated flame retardants (PBBs and PBDEs) in EEE was put in place to increase the protection of human health and to aid the recovery, re-use or recycling and environmentally-sound disposal of waste electrical and electronic products. This has already led to changes in design and increased awareness of product composition and the toxicity of substances.

The list of banned substances is to remain the same, but **four new substances** are identified for priority assessment (all being included in the Candidate List as Substances of Very High Concern under the REACH regulation) and a mechanism is to be introduced for new substance bans in line with the REACH requirements to ensure coherence. Current substance exemptions instead of being subject to a four year review will have a four year maximum exemption, although there will be an ability to request a renewal. New criteria have also been added to cover the availability and reliability of substitutes and an assessment of the socio-economic impact.

(ii) Scope – what products are caught

As already mentioned, a lot of time has also been spent by producers trying to determine whether or not their products fell within the scope of the RoHS Directive. As a result, the modifications will clarify the scope and the definitions and include a binding list of products that are caught, rather than by reference to the annex to the WEEE Directive – see table below. Two new annexes have been added, the first describes the broad product categories and the second is a binding product list within each category. This clarification will be welcomed as the uncertainty of interpretation by individual Member States and also producers has been a concern. A vast range of products that use electricity, both small and large household appliances, IT and telecommunications equipment and consumer goods are already covered but **medical devices and control and monitoring instruments** were not included (mainly due to concerns as to the reliability of lead-free solder), although they were caught by the WEEE Directive. RoHS, as amended, will now include these categories, albeit in a staged manner, commencing in 2014 and running through to 2017. Military equipment is now specifically excluded from RoHS Directive.

(iii) Placing on the market

A further amendment to the RoHS Directive makes it clear that 'placing on the

market' means the 'Community market' to ensure Member States do not interpret this as their own domestic national market.

(iv) Can you still use your spare parts?

Further clarification is given to the use of spare parts with the permission to use non-compliant spare parts being extended to equipment which benefits from an exemption when placed on the market. This change has been brought in to prevent the premature withdrawal of equipment from use.

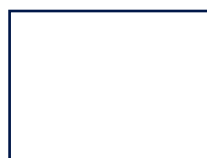
(v) Will enforcement become tougher?

Spotting and removing non-compliant products from the market has not been easy and differences between the methods of Member States as to enforcement has caused problems. As a result, the modifications proposed include introducing all the relevant provisions already used in the EU's Marketing of Products⁸ package with the hope that this will bring better and harmonised market surveillance methods and mechanisms for assessing conformity. This means that the RoHS Directive will, in effect, become a CE marking directive⁹. Currently there is a self-certification process with, in effect, producers declaring that their products comply with the RoHS Directive by simply placing them on the market and there are no requirements for the application of a

⁷ Trace elements of these substances only are permitted.

⁸ Commission Decision 768/2008/EC on a common framework for the marketing of products.

⁹ i.e. a declaration by the manufacturer that the product meets all the appropriate provisions of the relevant legislation implementing certain European Directives.



The ten product categories	WEEE Reuse and recycling targets %	WEEE recovery target %
1. Large household appliances	75	80
2. Small household appliances	50	70
3. IT & telecommunications equipment	65	75
4. Consumer equipment	65	75
5. Lighting equipment	80	N/A
6. Electrical and electronic tools	50	70
7. Toys, leisure and sports equipment	50	70
8. Medical devices	*	*
9. Monitoring and control equipment	50	70
10. Automatic dispensers	75	80

* Target to be set as part of amendments to Directive

specific mark or testing by an independent body. The proposed change will mean there is now a CE label for electrical and electronic products – albeit still a self-certification process – but the assessment process will have to accord with that used for qualitative assessment (conformity and compliance)¹⁰ for other products on the Community market. The specific standards, however, have not yet been produced. Enforcement will then take place under these 'marking' EU directives with the advantage that these require formal liaison between enforcement

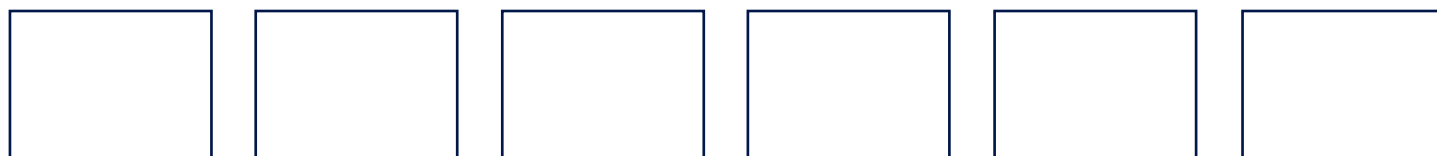
bodies and therefore exchange of information. The hope is that there will be a reduction in the number of non-compliant products on the market.

Proposals to amend the WEEE Directive

The costs and burdens on players in the market of implementing the WEEE Directive has also been a concern. The Commission has therefore also reviewed its provisions to try to simplify and ease some of these burdens. The Commission has

been concerned at the cost of putting the Directive into effect and it has estimated that the proposed revisions to the Directive would lead to around €60 million in savings. The basic principle is, of course, that the polluter pays – i.e. producer responsibility – in the hope that if the producer is responsible for financing the management of the waste from his own products he will be encouraged to design such products in a way that facilitates repair, re-use and recycling.

¹⁰ EC Directive 768/2008/EC and Regulation 765/2008/EC.



(i) Do you need to register in each Member State?

Member States are required to draw up a register of producers and collect information on an annual basis on the quantities and categories of EEE placed on its market and this had led to a requirement on producers to register and report in each Member State where they place products on the market. This has, of course, increased administrative burdens and financial costs. The proposal, therefore, is that such registration and reporting requirements will be inter-operational so producers will only need to register in one Member State for all of their activities in the EU.

(ii) Household/non-household products

Clarification is provided as to the scope of the WEEE Directive. It will cover the same 10 product categories as will be listed in the new annexes to the amended RoHS Directive. Be warned though individual Member States can, in relation to WEEE, still include additional product categories. The proposed amendments also clarify the exclusion of certain appliances, for example, fixed installations, and confirm a number of issues which have been set out in the Commission's FAQ document on WEEE, which is not, of course, a binding document.

A helpful change is the proposal to categorise appliances as either household (B2C – business to consumer) or non-household (B2B – business to business).

This is useful as different financial and organisational obligations fall on producers depending on whether the appliance is provided to a consumer or not. In relation to B2C, Member States are required to set up a collection system where private householders or distributors can deliver the WEEE free of charge.

(iii) Will producers be required to fund additional take back schemes?

The basic premise for B2B products is that the producer is responsible for providing arrangements for financing the cost of collection and recycling or agreeing appropriate contractual arrangement with its customers in this respect. So it is fairly open ended. However, you then need to look at when the EEE was placed on the market. If it was after 13 August 2005 then the producer is responsible for providing arrangements for financing the costs of collection and recycling of that WEEE. For historic WEEE, i.e. placed on the market before 13 August 2005, the person responsible for that financing will be the producer who is selling a product to replace the waste equipment. But this was then complicated by the fact that the Member States could, as an alternative, make the last user of the equipment partly or fully responsible for financing these costs. Where the historic waste is not being replaced then the last user is responsible for financing the collection and recycling. Certain Member States, e.g. Germany, France, Belgium, Poland and The

Netherlands, have chosen to make the last user responsible for all historic waste, regardless of whether a replacement is purchased or not.

The amendments aim to encourage Member States to harmonise producer financing across the EU.

(iv) Higher but more flexible collection rates and targets

The proposed amendments also make changes to the collection rate of waste electrical and electronic equipment. The Commission notes that, at the current collection and recycling target rates (a minimum target of 4kg per inhabitant per year for private households), the expectations of the WEEE Directive to reduce the amount going to landfill will not be reached as the target is not ambitious enough.

So the proposal is that there will be a variable collection target to take into account the differences in the consumption levels of individual Member States. As a result the proposal is for a collection target equal to 65% of the average weight of EEE placed on the market in the two preceding years in each Member State. This will become a binding target in 2016 to give individual Member States time to adjust. This rate will apply both to household and non-household waste electrical and electronic equipment.

Producers will be responsible for achieving this target and so as a producer you need to make sure you have in place proper



systems for recording EEE sold and its ultimate collection on disposal.

The amendments also propose an increase of 5% in the combined recycling and re-use targets, but a producer can now include the re-use of **whole** appliances, which was previously not counted in this way, so as to make re-use an attractive option.

Targets for medical devices are proposed to be set at the level of the targets for monitoring and control instruments.

(v) Enforcement

The revisions propose the setting of minimum inspection requirements for Member States and also minimum mandatory requirements for WEEE that is shipped. The reason for this is that experience points to a significant amount of illegal shipments of WEEE to developing countries.

What next?

The Commission, having published its proposals at the end of December 2008, is now in the consultation phase. It is likely the various amendments will need to be complied with by 2014 so producers need to start adapting now and keep an eye on developments. In particular, the standards for the CE labelling requirements and the Candidate List for REACH need to be monitored to see what other substances may, in due course, be banned from use in electrical and electronic equipment.

Linda Fletcher, London

Interception of internet telephony calls in the European Union

Eurojust (the EU's judicial co-operation unit) is investigating the possibility of intercepting internet telephony calls in order to help fight organised crime. Internet telephony services are more difficult to intercept than conventional landline and mobile services, and are therefore attractive to criminals and other groups. Non-technical issues that need to be addressed include data protection rules and civil rights.

Peter Ward, London

European Council reaches political agreement on EU communications regulatory framework

The European Council has reached political agreement on proposals to reform the EU regulatory framework for electronic communications networks and services. The Council has approved consolidated versions of the amended Framework Directive (2002/21/EC), Authorisation Directive (2002/20/EC), Access Directive (2002/19/EC), and Universal Services Directive (15758/08/EC, 15702/08/EC,

15695/08/EC and 15896/08/EC). The Council's press release highlighted a number of points. In the Framework Directive, the focus is on national regulatory authorities, consolidating the internal market, and the management of radio frequencies. The Authorisation Directive concentrates on the granting of individual rights to the use of radio frequencies and harmonising radio spectrum. The Access Directive allows functional separation of services and the Universal Services Directive focuses on the provisions concerning the definition of publicly available telephone service.

Peter Ward, London

Commission publishes guidance paper on applying Article 82 EC to abusive exclusionary conduct by dominant undertakings

On 3 December 2008, the European Commission published guidance on enforcement priorities in applying Article 82 to abusive exclusionary conduct by dominant undertakings. This guidance continues the more economics-based approach to the enforcement of EC competition law. The Commission's economics-based approach in the guidance has already been used in recent



Article 82 cases, including *Wanadoo*, *Microsoft* and *Téléfonica*. Cases now under consideration are the alleged anti-competitive actions by IBM in breach of Article 82, in tying the sale of its operating system to its mainframe hardware, and withholding patent licences and certain intellectual property to the detriment of mainframe customers, and the current investigation into Microsoft in relation to alleged illegal tying of various software products (in particular, Microsoft's Internet Explorer) with its dominant Windows operating system.

The guidance will be used by the Commission in current and future abuse of single dominance cases, and brings the Commission's Article 82 policy in line with Article 81 and merger cases in using an economics-based approach.

The finalised guidance paper is considerably streamlined and shortened as compared with the original discussion paper issued by the Commission in December 2005. The guidance sets out the Commission's intended enforcement principles in relation to identifying market power, anti-competitive foreclosure and price-based exclusionary conduct, before analysing specific forms of abuse, namely exclusive dealing, tying and bundling, predation and refusal to supply (including margin squeeze). This article summarises the main principles set out in the guidance in these areas.

The Commission states that it will normally intervene under Article 82 where, on the

basis of cogent and convincing evidence, the allegedly abusive conduct is likely to lead to anti-competitive foreclosure i.e. where competitors are excluded from the market. The Commission also states as a general policy in relation to price-based exclusionary conduct, the principle derived so far from its margin squeeze decisions, that it will normally intervene only where the allegedly abusive conduct has already been or is capable of hampering competition from competitors which are as *efficient* as the dominant undertaking. In certain areas, in particular predation and refusal to supply, the principles set out in the guidance go beyond the position established in the existing case law.

Dominance

In determining dominance, the Commission will follow the position established in case law particularly *United Brands*, that dominance is a position of economic strength which enables an undertaking to prevent effective competition being maintained on a relevant market, by affording it the power to behave independently of its competitors, customers and ultimately consumers. Competitive constraints are not effective and the firm enjoys substantial power over a period of time, even if some actual or potential competition remains. Therefore, a dominant position is derived from a combination of factors, and although market shares are a useful first indication, they have to be interpreted in the light of

relevant market conditions. Although experience has shown that dominance is not likely at a market share under 40% in the relevant market, there may be exceptions where dominance is found below this threshold. Both the size of market share and the period of time that the share is held are important preliminary indicators of dominance.

Generally, the ownership of an Intellectual Property Right (IPR) will not in itself place the owner in a dominant position. It may, however, be an important factor in determining whether the owner can impede effective competition, and in certain circumstances the IPRs concerned may be of such importance for competition on the market that their possession alone comes close to conferring dominance.

A dominant company can have advantages such as economies of scale and scope which are barriers to expansion or entry in a market, and may create barriers to entry, by making significant investment, which new entrants or competitors would have to match, or where it has concluded long-term agreements with customers which have appreciable foreclosing effects. If behaviour appears only to raise obstacles to competition, and not create efficiencies, anti-competitive effect may be inferred.

Price-based exclusionary conduct

The Commission will intervene in price-based exclusionary conduct where



behaviour is, or is capable of, hampering competition from competitors which are considered to be as efficient as the dominant undertaking. The cost benchmarks the Commission is likely to use are the average avoidable cost (AAC) and the long-run average incremental cost (LRAIC). The AAC includes fixed costs incurred during the period under examination. The LRAIC is the average of all variable and fixed costs to produce a particular product, and includes product-specific fixed costs made before the period in question; therefore the LRAIC is usually above the AAC. Failure to recover LRAIC indicates that the dominant firm is not recovering all the attributable fixed costs of producing the goods or services and that an efficient competitor could be foreclosed from the market.

Exclusive dealing

A dominant company may try to foreclose competitors by use of exclusive purchase obligations or rebates which in the guidance are together termed "exclusive dealing". The foreclosure effect will be greater the longer the duration of the obligation. However, if the dominant firm is an unavoidable trading partner for all or most customers, an exclusive purchasing obligation of short duration can lead to anti-competitive foreclosure.

Rebates are not usually capable of foreclosing in an anti-competitive way as long as the effective price remains consistently above the LRAIC of the dominant firm, as usually this would allow

an equally efficient competitor to compete profitably. As a general rule when the effective price is below the AAC, the rebate scheme is capable of foreclosing even "as efficient" competitors. When the effective price lies between the LRAIC and the AAC, the Commission will investigate what other factors are likely to affect the entry or expansion by an equally efficient competitor.

Tying and bundling

Tying and bundling may be used by a dominant firm to foreclose the market. Tying occurs where customers purchasing one product, the tying product, are also required to purchase another product, the tied product, from the same firm. Bundling usually refers to how products are offered or priced. Pure bundling is where the products are only sold jointly in fixed proportions; mixed bundling is where products are available individually, but cost less when sold together (this is also called a multi-product rebate). While recognising that tying and bundling are marketing practices to offer products in a cost-effective way, a dominant firm can use this strategy to foreclose the market. As an example, *Microsoft* was found to have breached Article 82 by making the Windows client personal operating system conditional on the acquisition of Microsoft's Window Media Player software, (bundling) which foreclosed the market for media player software. The risk of anti-competitive foreclosure is expected to be greater where the tying or bundling

strategy is long-lasting, for example through technical (as opposed to contractual) tying, which can only be reversed at a high cost.

In the case of multi-product rebates, assessing incremental revenue is complex; it is not easy to see whether the incremental revenue covers the incremental costs for each product in the dominant undertaking's bundle. The Commission states that in practice the incremental price will therefore be taken as a good proxy. If the incremental price that customers pay for each of the products in the bundle remains above the LRAIC (of including the product in the bundle), intervention by the Commission is unlikely since an equally efficient competitor with only one product should in principle be able to compete profitably against the bundle. However if the incremental price is below the LRAIC, enforcement action may be warranted, as an equally efficient competitor may be prevented from expanding or entering the market. By contrast, where rivals also sell in similar bundles, the Commission will consider the relevant question to be one of predation rather than bundling.

Predation

The Commission will generally intervene when there is evidence that a dominant firm engages in predatory conduct by deliberately incurring losses or foregoing profits, termed a "sacrifice", with a view to strengthening or maintaining market power, and by doing so, cause consumer



harm. Pricing below AAC will in most cases clearly indicate sacrifice. In addition, the Commission may also investigate whether the net revenues were lower than could have been expected from reasonable alternative conduct.

The Commission states that normally only pricing below LRAIC is capable of foreclosing as *efficient* competitors from the market. However the Commission does not consider it necessary to show that competitors have actually left the market in order to show that there has been anti-competitive foreclosure. This is because the dominant undertaking may prefer to prevent the competitor from competing vigorously and have it follow the dominant firm's pricing, rather than eliminate it from the market altogether. Generally, consumers will be harmed if the dominant undertaking can reasonably expect its market power after the predatory conduct ends, to be greater than it would otherwise have been. However, it is not necessary to show that the dominant firm will be able to increase its prices above the pre-predation level, it may be sufficient that the conduct would stop or delay a fall in prices that would have otherwise occurred.

It may be easier to predate if specific customers are selectively targeted with low prices, as this will limit losses. In relation to the effects of predation on competitors, the Commission is broadening the grounds on which it may intervene and is in effect proposing a broader definition of predation as an abuse of dominant position, compared with the existing case law.

Refusal to supply and margin squeeze

The concept of refusal to supply includes a refusal to supply new or existing customers, refusal to license intellectual property rights, including supply of the necessary interface information, or refusal to grant access to an essential facility or a network. It also includes constructive refusal, which could be unduly delaying or downgrading the supply or imposing unreasonable conditions.

Further, instead of refusing to supply, a dominant company may charge a price for the product on the upstream market which compared to the price it charges in the downstream market, does not allow even as an *efficient* competitor to trade profitably. This is a so-called "margin-squeeze". The Commission will largely rely on LRAIC of the downstream division of the integrated dominant firm as a benchmark, or a non-integrated competitor when it is not possible to allocate the dominant firm's costs between downstream and upstream operations.

These will be an enforcement priority if the refusal (i) relates to a product or service that is objectively necessary to be able to compete effectively on a downstream market and (ii) the refusal is likely to lead to the elimination of effective competition on the downstream market and (iii) the refusal is likely to lead to consumer harm.

However, the Commission states that in the case of obligations to supply in regulated

markets, where it is clear from the considerations underlying such regulation, that the necessary balancing of incentives has already been made by the public authority when imposing such an obligation to supply, it is likely to make a finding of anti-competitive foreclosure without considering whether the above three cumulative circumstances are present. This may also be the case where the upstream market position of the dominant undertaking has been developed under special or exclusive rights granted by the state or financed by state resources. In this respect, the Commission restates a principle which was set out in its margin squeeze concerning *Téléfonica* regarding a margin squeeze in relation to the grant of upstream access to broadband facilities. The Commission here appears to be generalising a stricter policy in relation to questions of refusal or constructive refusal to grant access to infrastructure derived for example, from the operations of a former statutory monopoly, than are applied in relation to questions of supply of access to infrastructure created through private sector investments. However these cases raise complex issues of law, economics and policy. There is insufficient case law at this stage to regard this Commission policy as equivalent to a general rule that would necessarily be applied in all cases.

A priority for the Commission will be the investigation of refusal to supply where the competitor has no actual or potential substitute in the downstream market. The



Commission is placing the onus on the dominant company to demonstrate why circumstances have changed to require it to change existing supply arrangements. Importantly, the Commission states that its general criteria on refusal to supply will be applied both to cases of disruption of previous supply (as per the existing case law) and to refusals to supply goods or services which the dominant company has not previously supplied (*de novo* refusals to supply). The Commission states that it is more likely to find the termination of an existing supply arrangement to be abusive than a *de novo* refusal to supply. However under the case law to date, *de novo* refusals to supply have generally only been regarded as abusive in cases involving essential facilities. Therefore the Commission appears to be seeking potentially to broaden the scope of application of Article 82.

In examining the likely impact of a refusal to supply, the Commission will assess whether the likely negative consequences for consumers will outweigh the negative consequences of imposing an obligation to supply, over time. Consumer harm will arise where, as a result of being excluded from the market, competitors are prevented from introducing innovative goods or services and/or where follow-on innovation is likely to be stifled. In particular, where competitors intend to produce new or improved goods or services (and not simply to duplicate those of the dominant undertaking) for which

there is potential consumer demand, or are likely to contribute to technical development. In this respect, the Commission's guidance directly reflects the case law as extended in its *Microsoft* decision of 2004 on refusal to supply interoperability data, thus preventing competitors from using this information to develop innovative competing products, therefore foreclosing the market. That decision was upheld by the European Court of First Instance in September 2007.

Impact of the guidance

The guidance contains some departures from case law. Whilst the guidance sets out the Commission's enforcement policy, the European Courts can ordinarily be expected to follow the case law. The national courts will also follow the current case law, at least until the Commission has adopted formal decisions to apply the principles set out in the guidance. National competition authorities such as the OFT are likely to examine abuse of dominance cases in line with the Commission guideline.

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