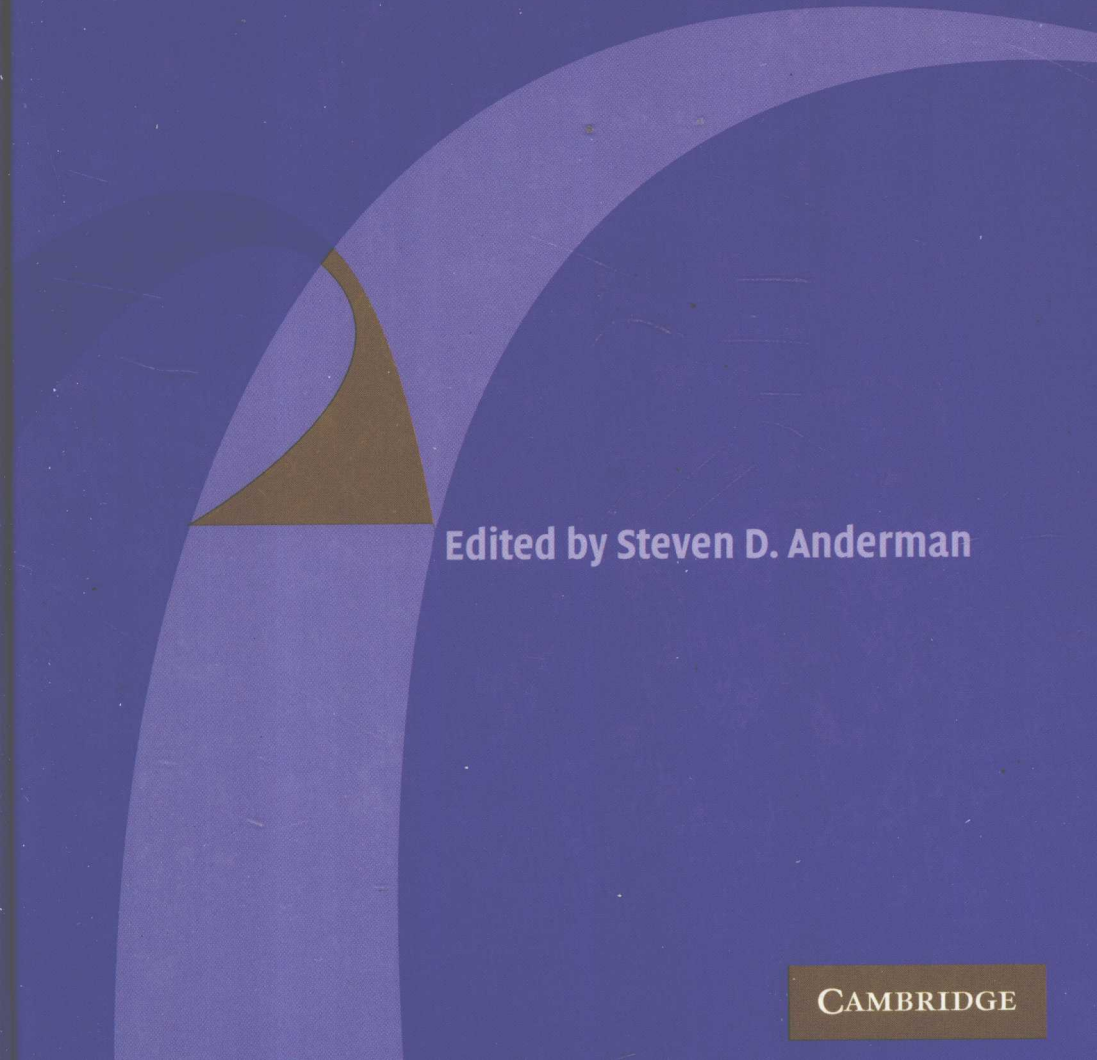
The Interface between

# Intellectual Property Rights *and* Competition Policy



Edited by Steven D. Anderman

CAMBRIDGE

# THE INTERFACE BETWEEN INTELLECTUAL PROPERTY RIGHTS AND COMPETITION POLICY

Edited by

STEVEN D. ANDERMAN

academy SINGAPORE

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# PREFACE

This work owes its origin to the Singapore IP Academy, which was established in January 2003 as a result of a national initiative. Acknowledging the value and importance of intellectual assets and creativity as primary sources of wealth and competitive advantage, the broad objective of IP Academy is to contribute to the building of a thriving culture that encourages the management and harnessing of innovation, and the resultant IP rights for the achievement of success in this global, knowledge-driven economy. Although at present it is largely funded by the Singapore Government, it is an independent body.

Professor Gerald Dworkin and Associate Professor Loy Wee Loon were IP Academy's founding directors from January 2003 to December 2004. They have been succeeded by Professor David Llewelyn as director and Ms. Ng Lyn as deputy director.

One aspect of the IP Academy's work is training. A broad range of courses, of varying lengths, are being provided for all those who can benefit from an understanding of intellectual property. At one extreme are university-based courses. For example, the Graduate Certificate in Intellectual Property provides a foundation course suitable for those seeking to qualify as registered patent agents in Singapore, and the MSc in IP Management is targeted at mid to senior management, executives and professionals with a background in science, technology or engineering who wish to specialize in the management of IP in a technology-related business. At the other extreme are a stream of short courses, for example Negotiating Skills for IP-Related Technology Transactions and Performing Arts Management: Copyright and Performing Rights for Practitioners.

The other major aspect of IP Academy's work is 'Thought Leadership', namely the promotion of research. Its research projects take on a multi-disciplinary focus straddling management, social, economic and legal perspectives. The research faculty supports both local and regional development of best practices in IP policy and endeavours to improve the ability of businesses, professional research institutions and other creators of IP to exploit and commercialise their IP.

Shortly after the IP Academy began its work, the government announced that it was proposing to introduce a framework of competition law for

Singapore. Because of the close relationship between competition and intellectual property law, this development provided an excellent opportunity for the IP Academy to promote its research programme and to assist those responsible for determining the nature of such legislation.

The IP Academy was fortunate in enlisting Professor Steve Anderman to lead an internationally based team to provide an examination of this interface between competition and intellectual property rights in different legal systems. It was hoped that the outcome of the study would produce findings and set out policy options of relevance to those responsible for the drafting and implementation of competition legislation in Singapore; an opportunity to provide customised national legislation in its broader international context.

As the policy formulation and draft legislation proceeded, some of the research work and the experts involved fed in their own contributions, at the very least to better inform and assist the decision makers. Thus, in the early stages, there was an expert Roundtable meeting: 'Issues at the Interface between Intellectual Property and Competition Law: Dealing with the Residual Conflicts'. This was followed by a conference for the Singapore legal profession and others: 'The New Competition Bill and its Implications for Intellectual Property Rights'.

The Singapore Competition Act is now in place. It is hoped that the IP Academy played a useful role in assisting the way in which the legislation was framed. The IP Academy is most grateful to Steve Anderman and to all his colleagues who embarked upon the project with such enthusiasm. It is to be hoped that the work which they have done will be of interest and of value to a wider international audience.

# CONTENTS

*Notes on contributors* *page* vii
*Preface* xi

1 The competition law/IP 'interface': an introductory note 1
STEVEN D. ANDERMAN

**PART I Intellectual property rights and competition law in the major trading blocks** 35

2 EC competition policy and IPRs 37
STEVEN D. ANDERMAN AND HEDVIG SCHMIDT

3 Competition policy and its implications for intellectual property rights in the United States 125
RUDOLPH J. R. PERITZ

4 The interface between competition law and intellectual property in Japan 250
CHRISTOPHER HEATH

**PART II Intellectual property rights and competition law in smaller and medium sized open economies** 313

5 Intellectual property rights and competition in Australia 315
FRANCES HANKS

6 Irish competition law and IP rights 348
IMELDA MAHER

7 The interface between intellectual property law and competition law in Singapore 375
BURTON ONG

PART III **Issues related to the interface between intellectual property rights and competition law** 427

8 Parallel imports 429
MIRANDA FORSYTH AND WARWICK A. ROTHNIE

9 Technology transfer 466
ROHAN KARIYAWASAM

10 The relationship between intellectual property law and competition law: an economic approach 505
PIERRE RÉGIBEAU AND KATHARINE ROCKETT

*Index* 553

# 1

# The competition law/IP 'interface': an introductory note

STEVEN D. ANDERMAN

## I. Introduction

Competition policy and intellectual property rights (IPRs) have evolved historically as two separate systems of law. Each has its own legislative goals and each its own methods of achieving those goals. There is a considerable overlap in the goals of the two systems of law because both are aimed at promoting innovation and economic growth.[1] Yet there are also potential conflicts owing to the means used by each system to promote those goals. IP laws generally offer a right of exclusive use and exploitation to provide a reward to the innovator, to provide an incentive to other innovators and to bring into the public domain innovative information that might otherwise remain trade secrets. Competition authorities regulate near monopolies, mergers and commercial agreements with the aim of maintaining effective competition in markets. This regulation occasionally results in limits being placed on the free exercise of the exclusive rights granted by IP laws.

In recent decades, competition authorities and courts have prohibited conduct by intellectual property owners which was otherwise lawful under intellectual property rights legislation, because it contravened the rules of competition law. This has occurred in four main spheres of activity of IP owners. First, cases have been brought by the competition authorities in the USA, the EU and Japan to place limits on the anticompetitive commercial conduct of individual owners of IPRs where they protect a market standard or de facto monopoly.[2] The competition issue presented in these cases has generally been the IP owner's exclusionary conduct towards innovators and potential competitors on markets which are secondary to and dependent upon an IPR protected industrial standard or de facto monopoly. The anti-competitive conduct has tended to take the form of a 'refusal to deal', 'refusal to license', 'refusal to provide proprietorial software interface codes', or a 'tie-in' or illegal 'bundling', but the act is prohibited because it is viewed as an attempt to 'lever' the IP reinforced market power in the 'primary' market into exclusionary conduct in the secondary market.[3] Secondly, the competition

authorities in the USA, the EU and Japan have created a detailed framework of regulation for certain terms of bilateral IPR licensing agreements, whether by means of official guidelines or legislation. Thirdly, the practices of collecting societies, R&D agreements and patent and technology pools have raised the issue of the appropriate treatment of cooperation between competitors in IP related fields under the competition rules. Finally, in the field of mergers and acquisitions, the owners of intellectual property rights have found that competition authorities have intervened on occasion to limit IPR owners from acquiring competing technologies[4] as well as to require compulsory licences of IPRs to third parties as a condition of merger approval.

As modern commercial practices involving the use of intellectual property rights have encountered these forms of 'second tier' regulation by competition authorities, concerns have been raised about the nature of the accommodation between the two systems of law.[5] First, to what extent and on what basis do the competition authorities and the courts have authority to limit the exercise of intellectual property rights in these ways? If IPRs are granted by laws which have their own elaborate system of checks and balances, why is it necessary for competition law to add a second layer of legal regulation to the exercise of IPRs? It appears as if the competition authorities in a number of jurisdictions take the view that their role is a form of public law regulation while the exercise of an IPR is essentially the exercise of a private property right. Certainly, in the USA and the EU, the competition authorities have at times described IPRs as 'essentially comparable' to any other form of private property for the purposes of the competition rules.[6] To what extent do legislation and judicial decisions support the competition authorities in that view?

Secondly, despite the use of this description, when competition law is actually applied to the exercise of IPRs, in these same jurisdictions, concessions are often consciously made *within the competition rules* to the unique nature of intellectual property rights: to their legislative and, in the USA, their constitutional basis as well as to their contributory role in the process of innovation. Indeed, the compatibility between the aims of the two systems tends to ensure that the normal exercise of the prerogatives of intellectual property rights is consistent with the competition rules. The competition rules applied to IPRs, either explicitly or implicitly, almost inevitably acknowledge a form of 'comity' between the two systems of law. Yet, the forms of comity developed within the competition rules in different legal system have tended to differ from system to system.

A third issue raised by the emergence of an extra layer of regulation of IPRs by the competition authorities is to what extent could and should the various IPR laws themselves, the patent, copyright, and design rights laws be reformed in order to reduce the extent of the 'external' regulatory role now played by competition law. To what extent does the experience of interface

cases suggest that the IP laws can enhance the nature and degree of comity by embarking upon a process of 'internal' reform? Some issues of reform that have been considered are: (i) the optimum width and duration of patent and copyright protection; (ii) the issue whether industrial copyright laws should provide for compulsory licensing where innovation is improperly obstructed by IP owners along lines similar to patents; (iii) the extent to which industrial copyright such as software programs and databases should be subject to interoperability obligations under IP law; and (iv) the extent to which IP laws can and should acknowledge when the IPR itself creates a monopoly and place limits on the scope of the IP protection. Underlying these enquiries is perhaps the largest policy issue of all: what is the most appropriate relationship between competition policy and IPRs in a growing industrial economy?

If we look at the major legal systems with extensive experience of the coexistence of the two fields of law, the EU, the USA and Japan, we can see considerable variation in their chosen forms of accommodation. The major legal systems have generally accepted that there are cases where the market maintenance concerns of competition law can prevail over the exercise of IPRs associated with substantial market power. However, the nature of this accommodation varies considerably with each system; both in terms of method and where the line is drawn. Moreover, the experience of these countries makes it plain that the true extent of variation cannot be appreciated by a cursory examination. To see it clearly and accurately requires a look in some depth. For example, in Japan, at first sight its competition law gives an extensive legislative immunity to intellectual property rights; the Japanese Antimonopoly Act exempts intellectual property rights from the scope of its application. Yet, on closer examination, the provision has not been interpreted as an overall exemption to all exercises of intellectual property rights but can be limited in cases of private monopolisation or undue restraint of trade (See Chapter 4). In the EU and US, in contrast, there are no explicit legislative immunities in the competition rules of Articles 81 and 82 of the European Treaty or Sections 1 and 2 of the Sherman Act. Instead, the general competition rules in both legal systems have been given judicial and administrative interpretations that result in their application to the exercise of IPRs in extreme cases. Both systems have created wide general norms of competition law which if not modified can apply to limit the exercise of IPRs. Yet, on closer examination, the application of the general competition rules in the US and the EU has resulted in the evolution of judicial and administrative doctrines which apply special rules and even self-denying ordinances acknowledging to a considerable extent the sui generis nature of IPRs, their constitutional foundations in the USA and their legislative foundations in the EU. Sometimes these forms of comity are given expression in special rules explicitly designated for IPRs. One example is offered by the 'exceptional circumstances' test devised by the European Court of Justice when applying Article 82 to an issue of abusive refusal to licence by an IP

owner. More often, there are powerful partial immunities or safe havens built into the logic of the general competition rules when they are applied to the acts of the conduct of the IP owner. Often this is the logical outcome of the two systems of law pursuing similar aims. For example, both US and EU competition law make it clear that if a company grows by internal investment in R&D and IPRs to a position of significant market power that is perfectly lawful under the competition rules. Moreover, if the owners of IPRs wish to charge high prices for their successful products protected by IPRs, the risks of investment ex ante will be respected by the competition rules in each legal system albeit in different ways. The normal exercise of IPRs is by judicial doctrine viewed as lawful under the competition rules but each system has its own line where the exercise of an intellectual property right is not viewed as normal under the competition rules.

The purpose of this book is to examine the experience of a number of countries in grappling with the problems of reconciling the two systems and dealing with interface issues. The book is divided into three parts. The first two parts of the book indicate the variation in legislative models as well as the wide variety of judicial and administrative doctrines that have been used to attempt to deal with problems raised at the interface between intellectual property rights and competition law. The jurisdictions selected for study are the three major trading blocks with the longest experience of case law: the EU (Chapter 2), the USA (Chapter 3) and Japan (Chapter 4) and three less populous countries with open economies, Australia (Chapter 5), Ireland (Chapter 6) and Singapore (Chapter 7).

In these parts, the intent is not to attempt to arrive at a definitive model of reconciliation between the systems of legal regulation or even a recommended 'best practice'. The examination in depth of the different jurisdictions makes it plain that each system must determine its own appropriate accommodation. It is true that recently, efforts have intensified in different jurisdictions to find the most appropriate basis upon which to combine the two policies into a coherent whole for the purposes of innovation policy. In the USA the Antitrust Division of the Department of Justice and the Federal Trade Commission have held extensive hearings on the interface issue.[7] In the EU the Technology Transfer Block Exemption Regulation has recently been significantly reshaped and a series of conferences have been held with the aim of obtaining a clearer idea of the best way to apply competition law to the commercial exercise of intellectual property rights.[8] In Australia the Intellectual Property Review Committee was established both to review IP laws from the standpoint of competition and to recommend a reform of the width of the exemption the Trade Practices Act gave to the exercise of intellectual property rights. In many countries with new competition laws which have already enacted IP legislation, such as India, China, Singapore and Hong Kong, there is a need to shape the overall system to deal with the

inevitable conflicts that can arise when the exercise of IPRs runs into the buffers of the competition rules. Finally, in the USA, EU and Japan, the interest in the interface has been whetted by the growth of digital multi-media technology and the potential legal roadblocks in the new technological environment. Nevertheless, it seems almost inevitable that the optimum method of reconciliation will differ for each national system depending upon its legal culture and its state of economic development.

Hence the overall aim of this book is the more modest one of setting out the array of options on offer, the legislative and judicial and administrative alternatives available in those constituencies with some experience of dealing with the interface. The intention is to produce research findings in sufficient depth so that the experience of the selected legal systems can be understood and used as points of reference by competition authorities and the parties involved in interface disputes. This is a research study that should be viewed as a reference work and a resource to be adapted to the particular circumstances of any one legal system.

In the third part of the book we look at a number of issues closely related to the interface between competition law and intellectual property rights. Chapter 8 analyses the issue of parallel trading and exhaustion of IPRs, a system of legal rules that creates its own interface with the exercise of IPRs alongside the competition rules. Chapter 9 discusses the issue of technology transfer showing the important differences between international IP licensing and foreign direct investment as well as highlighting how limits on technology spillover are set in bilateral investment treaties. Finally, Chapter 10 examines the economics of the interface to suggest how economic thinking may find a way of interacting with legal argument in this field.

## II. A note on the compatibilities between the two systems of legal regulation

Even without a legislative immunity for IPRs, the case law interpreting the competition legislation in the countries studied demonstrates that the competition rules create certain self-denying ordinances to ensure that there is an extensive reconciliation between the two systems of legal regulation. This is entirely to be expected since, within each legal system, the different means used by intellectual property rights legislation and competition law operate in many ways in conjunction rather than in conflict with each other. IP laws, such as patent and copyright laws, confer an exclusive right to exploit an invention or creation commercially for a limited period as an incentive to creation and innovation. These rights are essentially 'negative' rights; they prevent copying of the protected innovations. They do not ensure profitability but if the IPR is combined with a successful product, the legal exclusivity provides a stimulus to innovation by acting both as a reward to the

inventor/creator and as an incentive to innovation more generally. In the case of patents, without the protection of exclusivity, firms may choose to keep their innovative ideas secret as opposed to disclosing them in their patent claims. This stimulus to the spread of information is also a stimulus to innovation resulting in new products and processes entering existing markets and creating new markets. In these ways, intellectual property rights can actually enhance the forces of competition.

Moreover, each IP law, as well as competition policy, strikes its own balance between protecting early innovators and protecting the claims of 'follow on' innovators. IP laws, such as patent and copyright laws, strike an 'internal balance' between the rewards for 'the improvements on earlier invention by later innovators', and the rewards to 'early innovators . . . for the technological foundation they provide to later innovators'.[9] As Merges and Nelson have pointed out: 'Ultimately it is important to bear in mind that every potential inventor is also a potential infringer. Thus a strengthening of property rights will not always increase incentives to invent; it may do so for some pioneers, but it will also greatly increase an improver's chances of becoming enmeshed in litigation.'[10] In copyright, the idea/expression dichotomy operates to ensure that copyright contributes to common knowledge while protecting the originator or creator from copying the expression of his or her work. In other words, IP laws usually attempt to strike a balance between providing sufficient incentives to innovation by the creator/inventor and avoiding the protection of any single innovation operating as a disincentive to cumulative 'follow on' innovation.

At the same time, the basic doctrines of modern competition law work in conjunction with IP laws by acknowledging their positive role in the process of innovation in at least five major respects. First and foremost, both the US and the EU competition laws accept that the achievement of an economic monopoly by means of investment R&D and intellectual property rights is a legitimate course of conduct for a firm, a form of 'competition on the merits'. Secondly, and relatedly, both EU competition law and US antitrust law acknowledge that the pricing of IPRs, even by dominant firms, must include a return which *adequately* reflects the reward/incentive function of IPRs as well as the ex ante investment risks of their owners. Thirdly, the competition laws in both systems *in most cases* give recognition to the right of IPR owners to prevent copying even if the exercise of this right denies access to markets to competitors. Fourthly, the competition laws in both systems no longer automatically assume that the legal monopoly conferred by IP laws, such as patent and copyright legislation, automatically amounts to an economic monopoly or even confers market power. That issue is left to be established empirically. Finally, in their analysis of IP licensing agreements both systems of competition policy work with the presumption that the licensing of IPRs is in general pro-competitive in its effects.

Nevertheless, as we have seen, modern competition policy, does act in reserve to prevent the excesses of private property owners in order to maintain effective competition on, and access to, markets,[11] operating as a 'second tier' of regulation of intellectual property rights.

It is also worth noting that the Agreement on Trade Related Intellectual Property Rights (TRIPS) spells out at various points that there is a role for competition policy to supplement the intellectual property rights policy of the Treaty. In formal terms, it does not require such laws. It permits them. For example, Article 8 (2) TRIPS states that 'Appropriate measures, provided they are consistent with the provisions of this Agreement, may be needed to prevent the abuse of intellectual property rights by right holders . . .' Article 8 also makes it clear that in principle Member States may enact legislation to prevent practices by the right holder that adversely affect the international transfer of technology. Moreover, in Article 40, the TRIPS agreement specifies the types of licensing practices or conditions relating to intellectual property rights which restrain competition and impede the transfer and dissemination of technology including exclusive grant-back conditions, coercive package licensing and clauses preventing challenges to the validity of the IPR. Nevertheless, as this note and the following studies will show, it is wise not to have a system of IPR legislation which is unaccompanied by a system of competition law.

## III. The changing nature of the interface between the exercise of IPRs and competition policy in the major competition law systems

From the early years of the twentieth century, the conflict between the exercise of IPRs and competition policy tended to be exaggerated by judicial and administrative doctrines initially in the USA and later in the EU. During these and later decades, patents were equated with monopolies[12] and patent licensing was subject to tight restrictions by competition law, initially following a doctrine of patent misuse,[13] and latterly by the regime of the 'Nine No-Nos' in the USA and its counterpart in the EU.[14] Since the 1970s, a new antitrust legal framework has emerged in both trading blocks with a greater appreciation of the economic benefits of IPRs and a move away from any automatic association of real market power with exclusive IP rights.[15] This change was prompted in part by judicial and administrative acceptance of the law and economics analysis of the 'Chicago School',[16] initially in the USA and later in the EU. Yet the Chicago School's initial success in restoring greater economic realism has been followed by a 'post-Chicago School' view emerging both in the USA[17] and in the EU[18] that acknowledges that not all IPRs are monopolies but recognises that some can be. There are cases where IP owned assets make a right holder dominant in a product market in established