SUBMISSION IN RELATION TO THE ACCC ON THE REMOVAL OF SECTION 51(3) OF THE COMPETITION AND CONSUMER ACT

Thank you for the opportunity to provide comments on the draft Guidelines issued by the Commission regarding the removal of Section 51(3) of the Act. For the record, I am a Consultant to Davies Collison Cave Law and have been involved in intellectual property and competition law matters since 1975.

There are good reasons why dealings in intellectual property rights need to be treated differently. The rationale was well explained in the "Review of Intellectual Property Legislation Under the Competition Principles Agreement", September, 2000 (Ergas) page 210 as follows:

> "As a general matter, the Committee recognises that intellectual property has important features that differentiate it, to a greater or lesser extent, from other property or assets. …
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> Partly reflecting these factors, and of great importance to the issue at hand, contracts and licences and assignments have a pivotal role in securing efficient use of intellectual property. This is for three reasons:
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> 1. The initial owners of IP rights are often not the parties best placed to exploit the output of their creative efforts….
> 2. In many, if not most, areas of technology, rights do not map simply into products. Commercial products often embody technology covered by claims in tens or even hundreds of patents and the interdependence between rights is even greater in the innovation process itself, which frequently involves combining technological inputs owned by multiple rights owners. Complex webs of cross-licences are required if these accumulated technical capabilities are to be put to productive use.
> 3. Even independent of the facts set out above, the costs of impeding efficient licensing of IP can be especially high. As noted above, knowledge is non-rivalrous: increased access to it by one party does not reduce the stock available to others. As a result, when parties are forced to "invest around" existing knowledge, there is a risk that the resources consumed in the process will, in social terms, be largely wasted.
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> All of this means that it is essential that firms have the scope to enter into efficient contracts that involve intellectual property rights, free of onerous and ultimately counter-productive regulatory burdens."

As a result, Ergas recommended that intellectual property transactions not be subject to the per se offences.

This recommendation was reiterated by the Competition Policy Review Panel (Harper) at page 42, where it is stated that:

> "The Panel considers that the IP licensing exception in Section 51(3) of the CCA should be repealed.
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> However, as is the case with other vertical supply arrangements, IP licences should remain exempt from the per se cartel provisions of the CCA in so far as they impose restrictions on goods or services produced through application of the licensed IP."

This treatment reflects the position taken in almost all other developed economies. For instance, in the United States, intellectual property arrangements are evaluated under a rule of reason unless they are naked restrictions on competition. In the European Union, there are a series of detailed block exemptions dealing specifically with intellectual property transactions.

It is therefore concerning that section 51(3) of the Act is to be repealed in circumstances where the Commission believes that territorial restraints and output restrictions will amount to cartel conduct. The result which the expert committees sought to avoid.

However, I would ask the Commission to review its conclusion on at least two bases.

These are that the Commission's analysis of the impact of the Act on dealings with intellectual property rights does not reflect the nature of intellectual property rights and that the determination of who are "competitors" for the purposes of Section 45AD of the Act is more focused than the approach adopted by the Commission.

An intellectual property right is generally exclusionary in nature. It gives a person a statutory right to stop another person engaging in particular conduct. Thus, without permission, that conduct cannot be engaged in by anyone other than the rights owner. When the rights owner grants the licence, the licensee is entitled to engage in that conduct within the scope of the permission given. Even where that permission is limited in some way, there is still the ability of the licensee to engage in activities which it would not otherwise be entitled to do. Therefore, even a limited licence is pro-competitive over no licence at all. This approach reflects reality; it is not an artificial construct.

As the Full Federal Court made clear in the Radio 2UE case (re *Radio 2UE Sydney Pty Ltd v Stereo FM Pty Limited and Another [1983 FCA140]*) it is necessary to analyse what is actually going on in a particular situation rather than taking a shorthand approach of condemning any arrangement, in that case, involving competitors and prices.

This approach is relevant to the interpretation of Section 45AD.

> In the first place, it raises the question as to whether a provision directed to a matter within Sections 45AD(3)(a)(i) – (iv) could ever prevent, restrict or limit those matters when the effect of the grant of the licence is to enable those matters, albeit on a limited basis. If the intellectual property licence by its very nature, cannot prevent, restrict or limit those matters because they could not be achieved without the licence, it would follow that the parties could not have the subjective purpose of achieving those matters unless the licence agreement contained provisions which went beyond the scope of the exclusive rights granted by the intellectual property right. On this approach, the Commission's conclusions in relation to output restrictions would be questionable.

> Secondly, where an intellectual property right exists and a licence is granted which is limited by geography or customer, there is not an "allocation" for the purposes of Section 45AD(b). It is not a situation where two or more parties are each lawfully able to deal with whole of an available market and are agreeing to divide the market up between them. It is a situation where the licensor is permitting one or more licensees (who may be competitors) to engage in an activity which is limited in scope. The alternative is that the licensee or licensees would not be entitled to engage in the activity at all. This suggests that the Commission's conclusions in relation to geographic restrictions is also questionable.

The second issue is the basis on which parties should be regarded as competitors for the purposes of Section 45AD.

Section 45AD(4) makes it clear that the relevant nexus is in respect of the goods or services to which the relevant provision under scrutiny relates. In other words, "those goods or services" in respect of which price is fixed, controlled or maintained or production, capacity, supply or acquisition is prevented, restricted or limited, or persons or geographical areas are allocated. In the context of an intellectual property licence, these will be the licensed goods or services. The issue then is whether clause 45AD(4) requires the parties to be in competition with each other solely with respect to the licensed goods or services disregarding any substitutable products or services, or whether all that is required is that the parties are in competition with each other in the market in which the licensed goods or services compete. The language of Section 45AD(4) lends itself to the first construction.

If that is correct and the competition nexus is required to be solely in respect of the licensed goods or services disregarding substitutable goods, then, in any intellectual property transaction, the licensor and the licensee are unlikely to be in competition with each other and, but for the arrangement, would not be.

An associated issue is whether the "giving effect to" prohibition requires a fresh determination to be made of whether or not a cartel provision exists or the existence of the cartel provision is only assessed at the time the arrangement embodying it is made. This has obvious implications for intellectual property licensing where prior to the grant of a licence, the parties might not be in competition with each other on any assessment of that requirement but that, after the grant of the licence, they are in competition with each other in relation to the licensed goods or services. This is an issue which will be of critical importance to licensors and licensees and it would be useful if the Commission took a view on this matter.

My submission is that the determination is made when the arrangement is entered into because Section 45AG(4) would otherwise be redundant. Furthermore, this construction sits more comfortably with Section 45AG, particularly when one considers that it is the subjective purpose of the parties in including the provision which is critical to the question of whether or not a cartel provision exists.

I also suggest that the Commission ought factor in the capacity of intellectual property rights to confer market power on a rights owner in the draft Guidelines and particularly be conscious of these when preparing the examples.

For instance, a trade mark is merely a sign applied to a good or service. It does not affect in any way the ability of other to compete with the trade marked goods or services other than by using that or a confusingly similar name on those goods. Even the most valuable trade marks dot insulate the products they are applied to from competition, e.g., IBM, Google, Apple. Trade marks are valuable for their reputational value, not any exclusionary reason. A patent is the most potent of the intellectual property rights and gives exclusive rights over an invention. However, that rarely, if ever, translates into a single product market as is evident from the comments from Ergas set out above. This reality needs to be built into the various examples set out in the draft Guidelines.

If the Commission's conclusions on the application of the Act to intellectual property arrangements are correct, the removal of Section 51(3) will have a profound effect on what would otherwise be regarded as normal pro-competitive provisions in intellectual property arrangements by resulting in them being treated as cartel provisions. This will have an immediate effect on the franchising industry where geographic restrictions and franchisor owned outlets, in particular, are common. Overall, the uncertainty created by the removal of Section 51(3) in light of the conclusions reached by the Commission is likely to have a chilling effect on the licensing of intellectual property rights, increase transaction costs and increase the amount of "red tape" faced by business in respect of innocuous transactions from a competition point of view.

In order to remove this uncertainty, the Commission would ideally implement a class exemption in respect of intellectual property transactions to achieve the result recommended by Ergas and Harper or implement a class exemption in terms of the vertical restraints exception as recommended by Harper. Obviously, any such implementation action would lead to a complete rewrite of the Guidelines. A less desirable but valuable and necessary response would be for the Commission to amend the draft Guidelines adopting the views set out in this submission.

Should the Commission wish to discuss any of these issues, I would be pleased to do so.

RODNEY DE BOOS

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