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Intellectual Property Arrangements Inquiry
Productivity Commission
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Your Ref
Our Ref MDL ZM
File No. 010444444

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Dear Sir / Madam

Submission in response to the Productivity Commission's Issues Paper, *Intellectual Property Arrangements* (October 2015)

1 We refer to the Productivity Commission's Issues Paper, *Intellectual Property Arrangements* dated October 2015 (**Issues Paper**).

2 We welcome the opportunity to make this submission in response to the Issues Paper, as part of the Productivity Commission's Inquiry into Australia's Intellectual Property Arrangements (**Inquiry**).

3 The Inquiry's Terms of Reference are extremely broad. In this submission, we focus on a number of specific issues that, in our submission, should be considered by the Productivity Commission in the Inquiry. Those issues are:

(a) the relationship between intellectual property and competition law;

(b) the exception for intellectual property licensing in s 51(3) of the *Competition and Consumer Act 2010* (Cth) (**CCA**);

(c) legal costs orders in minor intellectual property disputes; and

(d) the introduction of a "patent box" regime.

The relationship between intellectual property and competition law

4 The Inquiry's Terms of Reference specifically direct the Productivity Commission to have regard to the findings and recommendations of the Commonwealth government's recent Competition Policy Review, chaired by Professor Ian Harper. We were extensively involved in the Competition Policy Review, and made submissions at each stage of the consultation process.

5 The relationship between intellectual property and competition law has grown in importance in recent times, and this is set to continue, in line

with the rise of the knowledge economy.[1] The issue may be illustrated by the ACCC's recent litigation in relation to an alleged misuse of market power based on a pharmaceutical patent: *ACCC v Pfizer Australia Pty Ltd* [2015] FCA 113.

6 It is sometimes asserted that intellectual property and competition law are inherently at odds. This is because the owner of intellectual property is granted exclusive rights or a "monopoly" to exploit that intellectual property, whereas competition law aims to prevent or restrain monopolies and facilitate close competition between different businesses. However, that view is too simplistic.

7 Claims of intellectual property infringement may, in some cases, be used improperly in an attempt to stifle or eliminate legitimate competition. However, the intellectual property regime plays a crucial role in well-functioning markets by providing incentives for businesses to compete by innovating to create new and desirable goods and services. It does so by:

(a) protecting a firm's costs and investment in research, development and innovation; and

(b) prohibiting competitors from taking advantage of (or "free-riding" on) the innovation or reputation of another business.

The exception in *Competition and Consumer Act 2010* (Cth) s 51(3)

8 Section 51(3) of the CCA provides a limited exception to the restrictive trade practices provisions of the CCA (other than in respect of misuse of market power and resale price maintenance). The exception applies to conditions in intellectual property licensing and assignment arrangements.

9 The Competition Policy Review recommended that this exception be repealed. Previous government reviews have also considered whether the exception should be repealed or amended: the Hilmer Review in 1993, the National Competition Council's review in 1999 and the Intellectual Property and Competition Review Committee's (the "Ergas Committee") review in 2000.

10 In its recent response to the Competition Policy Review, the government noted the recommendation of the Competition Policy Review and stated that it would have regard to the Productivity Commission's findings on this issue.

11 The Competition Policy Review was concerned about the exception in s 51(3) applying to restrictions that might substantially lessen competition in cross-licensing arrangements that are entered into to resolve an intellectual property dispute.[2] However, the Competition

[1] Joaquin Almunia, "Intellectual Property and Competition Policy", European Commission, Speech to the IP Summit 2013, Paris, http://europa.eu/rapid/press-release_SPEECH-13-1042_en.htm.
[2] Commonwealth of Australia, *Competition Policy Review: Final Report* (March 2015) 109.

Policy Review considered that, as with other "vertical" supply arrangements, intellectual property licences should be exempt from the *per se* cartel provisions of the CCA and should only be prohibited if they have the purpose, effect or likely effect of substantially lessening competition.[3]

12 The Competition Policy Review's recommendation to repeal s 51(3) must therefore be seen in the context of its view that the CCA should not generally interfere in "vertical" supply arrangements.[4] To that end, the Competition Policy Review recommended that:

(a) third-line forcing only be prohibited where it has the purpose, effect or likely effect of substantially lessening competition (Recommendation 32); and

(b) the prohibition on exclusive dealing in s 47 of the CCA be repealed (Recommendation 33).

13 The Competition Policy Review argued that intellectual property licensing or assignment arrangements that might breach the CCA could be protected by ACCC authorisation or notification, or potentially a "block exemption" (under a new power recommended by the Panel).[5] The Competition Policy Review dismissed concerns that this would entail increased compliance costs.

14 In our submission, there is a place for an appropriately-drafted exception to the competition laws for intellectual property. Intellectual property disputes commonly arise between competitors. In those situations, the law should encourage parties to settle their differences commercially, without the public and private costs of litigation. Such settlement agreements therefore involve a legitimate reason for an agreement between competitors and, in our view, it is not appropriate to apply *per se* prohibitions such as the cartel laws. This is shown by the following hypothetical example.

15 **HYPOTHETICAL EXAMPLE**

Company A claims that its registered patent is infringed by its competitor company B importing and selling a similar product in Australia. Company B then seeks to dispute the validity of company A's patent for lack of an inventive step, and denies that its products infringe company A's patent (even if it is valid). Company A maintains that its patent is valid and seeks damages for infringement.

Whilst the validity of company A's patent, and whether there has been any infringement, remain unclear, the parties wish to resolve their dispute commercially on the basis that company B agrees to cease importing and selling the allegedly-infringing product. However, as the parties are competitors, such an agreement might arguably be a form of

[3] Ibid 110.
[4] Ibid 63.
[5] Ibid 110.

cartel conduct (an output restriction under s 44ZZRD(3)(a)(iii) of the CCA).

In our view, that type of agreement should only be prohibited under competition law if it has the purpose, effect or likely effect of substantially lessening competition.

16 Similarly, in our view, agreements between competitors (or parties who are "likely" to be in competition with each other) to assign or license intellectual property should only be prohibited under competition law if they have the purpose, effect or likely effect of substantially lessening competition. Again, we do not consider it appropriate to apply the *per se* cartel rules in this situation. Such rules decrease the value of intellectual property rights, and may prevent those rights from being exploited as effectively or efficiently during the period of intellectual property protection.

17 We strongly disagree with the Competition Policy Review's reliance on ACCC authorisation or notification or any "block exemption" process. In our view, that would impose an unjustifiable regulatory burden on business. Further, even if this "block exemption" process becomes available, we consider the exemption should be written into the legislation rather than based on a decision by the ACCC that is subject to a change in the ACCC's views.

18 We also see no reason why the exception should not apply to plant breeders' rights, which are not currently covered by s 51(3).

Legal costs in minor intellectual property disputes

19 In some intellectual property disputes, one party may lack the financial resources to defend a claim of intellectual property infringement that is made against it by a larger, well-resourced intellectual property owner. This creates an incentive for the intellectual property owner to make dubious claims of infringement, to pursue trivial claims vigorously or to make excessive demands.

20 This situation may arise where the weaker party is a consumer or a smaller competitor of the intellectual property owner (such as a licensed distributor of the allegedly infringing product). In the latter case, it may suit the intellectual property owner to drag out the dispute so that the smaller competitor is substantially damaged by the cost and time (of both its own management and its lawyers) required to defend the claim.

21 These concerns are heightened in the digital age, where it is practically very easy to infringe intellectual property. All that may be required is a few mouse clicks or key strokes. A consumer or unsophisticated small business may not appreciate that they are infringing intellectual property.

22 However, we are also mindful of the importance of protecting valuable commercial intellectual property from abuse and appropriation, particularly by competitors. Where the intellectual property owner has

suffered real loss or damage, they should not be denied appropriate compensation.

23 In our submission, the Productivity Commission should consider introducing new measures to deal with the issue of legal costs in what might be considered relatively minor breaches of intellectual property — in particular, breaches that do not result in any (or any substantial) loss or damage being suffered by the intellectual property owner. In that situation, the law should encourage the parties to act reasonably to resolve the matter without recourse to litigation.

24 To that end, we propose that the Productivity Commission consider the introduction of a new costs rule in relatively minor intellectual property disputes. The rule would be presumptive, in that the Court could always decide (in its discretion) to order costs otherwise. However, the rule could make clear that the Court will not award substantial legal costs in favour of an intellectual property owner who has not suffered any significant loss or damage but pursues a claim for intellectual property infringement to eliminate smaller competitors from the market.

25 In our submission, the new rule should provide that where:

(a) a person is proven to have infringed the intellectual property rights of another;

(b) the infringement was not flagrant; and

(c) the person promptly took all reasonable steps to cease the infringing conduct once the person received notice of a claim in relation to the infringement,

then, unless the Court otherwise orders, the person will not be ordered to pay the other person's costs in an amount that exceeds the amount of damages (compensatory or punitive) awarded to that other person.

Patent box regime

26 The Australian Government has recently highlighted the importance of innovation to the performance of the Australian economy.[6] One way of encouraging innovation and its commercialisation is through "patent box" regimes. Such regimes provide a tax benefit for income relating to intellectual property rights.

27 In a recent report, the Australian Government's Office of the Chief Economist considered that the implementation of a patent box regime would likely lead to a net negative return in tax revenues.[7] The Report also suggested that the value of additional patent applications was likely to be low. However, as the report acknowledges, patent box regimes have been introduced by a number of jurisdictions — including

[6] See, eg, the Hon Christopher Pyne MP, Minister for Industry, Innovation and Science, *Innovation policy linked to a nation's performance*, Media release dated 27 November 2015.
[7] Office of the Chief Economist, *Patent Box Policies* (November 2015).

jurisdictions with higher spending on direct research and development funding for business. In fact, in that regard, Australia ranks a disappointing 34th out of 36 OECD and BRICS nations.

28 Based on our discussions with clients involved in research and development, a patent box regime in Australia could have a significant impact on the commercialisation of research. Anecdotally, Australia has very good research capability, but would benefit from an increased focus on commercialising that research.

29 In our view, this issue is worthy of further consideration as part of the Productivity Commission's Inquiry — particularly given the renewed importance of innovation to the Australian economy.

30 Please do not hesitate to contact us if you have any queries. We look forward to receiving the Productivity Commission's draft report.

Yours sincerely

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