



Australian  
Competition &  
Consumer  
Commission

# **ACCC submission to the Productivity Commission Inquiry into Intellectual Property Arrangements in Australia**

November 2015

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# 1. Executive Summary

With intellectual property (IP) playing an increasingly critical role in all facets of economic activity, the ACCC welcomes the opportunity to contribute to the Productivity Commission (PC) Inquiry into IP Arrangements in Australia (the inquiry). The ACCC strongly supports the PC's approach, including the overarching framework and principles guiding the inquiry.

The ACCC recognises the market failure that the creation of exclusive IP rights seek to address. IP rights seek to promote innovation and competition between firms by granting the IP rights holder temporary exclusivity over their use. In the vast majority of cases, this is unlikely to raise competition concerns. Indeed, competition and IP laws are for the most part complementary, as both seek to promote innovation and efficiency and ensure markets operate more effectively in the long term interests of consumers.

Innovation and efficiency, however, also arise from the subsequent use of the original IP right, by combining or extending previous creations/innovations. This 'follow-on' innovation can at times be just as powerful, or even more so, than the first. IP rights should therefore be designed to balance incentives to invest in and create the initial intellectual property, with the incentives and ability to make maximum use of it once invented.

The ACCC is concerned that the *extent* of current IP protections may, in some instances, go beyond what is required to provide incentives for the creation of IP. On the *use* of IP, the ACCC is concerned that current arrangements may have the potential to stifle innovation, particularly in the fast evolving digital economy.

The ACCC is of the view that IP should not be treated differently from other property rights under competition law, and reiterates its longstanding view that the exemption of certain IP-related activities under section 51(3) of the *Competition & Consumer Act 2010* (CCA) should be repealed. This would ensure that IP is fully subject to Australia's competition laws, consistent with the approach taken in other major jurisdictions such as the United States, Canada and the European Union.

To better equip the IP system to the opportunities of the modern age, the ACCC supports the introduction of a flexible 'fair use' exception in the *Copyright Act 1968* (Cth) (Copyright Act). This would allow certain forms of use without payment to the copyright owner, providing a desirable degree of flexibility that will enable the law to accommodate and foster technological advances and innovations that might otherwise be curtailed by prescriptive and/or narrow exceptions in the Copyright Act.

The ACCC recommends that the PC review access frameworks for IP with a view to harmonising access arrangements in Australia. The ACCC considers that access frameworks for IP should have a clear focus on promoting competition and economic efficiency. The ACCC recommends that the PC examine whether IP should be outside the scope of the national access regime in Part IIIA of the CCA. The PC may also wish to explore IP access frameworks in other jurisdictions, in particular Canada's Competition Act which provides for 'special remedies' to apply to IP where the court finds that exclusive rights have been used to unduly restrain trade or lessen competition.

The ACCC considers that, in the context of the recently concluded TPP negotiations, it is imperative that Australia retain the flexibility to introduce reforms (such as flexible fair use exceptions) that promote competition, stimulate innovation and, where necessary, limit the ambit of IP protections.

## 2. Introduction

The ACCC welcomes the opportunity to contribute to the PC's inquiry. The ACCC, as noted in its submissions to the Competition Policy Review headed by Professor Ian Harper (Harper Review), is a strong advocate for a review of the IP framework to ensure that the extent of IP protections maintain an appropriate balance between creating and maintaining incentives for the creation of IP, and maintaining incentives for its efficient use.<sup>1</sup>

The views of the ACCC, as set out in this submission, are informed by the ACCC's experience in examining issues regarding IP within the context of its role as the competition regulator. The ACCC considers that it is timely for a broad examination of IP laws in Australia, particularly given the increasing pervasiveness of IP in all markets. The broad remit of the review also makes it a useful context to examine new approaches to meeting the objectives of the IP system as well as raising long standing concerns with the current system.

### 2.1 The ACCC's role in IP

The ACCC administers the CCA. The CCA's object is to enhance the welfare of Australians through the promotion of competition and fair trading, and provision for consumer protection.<sup>2</sup> This reflects the well accepted proposition that, absent market failure, competition is generally the best way to enhance community welfare by promoting economic efficiency.

Intellectual property rights are of particular relevance to the ACCC's functions under Part IV of the CCA, which prohibits anti-competitive agreements, mergers and other practices that substantially lessen, prevent or hinder competition in purpose and/or effect.

Section 51(3) of the CCA exempts certain IP-related activities from the operation of the anti-competitive conduct provisions contained in Part IV of the CCA (other than the prohibitions relating to misuse of market power and resale price maintenance). Consequently, some arrangements between IP rights holders and other entities for the license or sale of copyright material could be exempt from the restrictive trade practices provisions of the CCA, even if they have an anti-competitive purpose or effect or amount to cartel conduct.

Under section 157B of the Copyright Act, the ACCC can join cases brought by businesses before the Copyright Tribunal regarding the price for material licensed by copyright collecting societies. The ACCC has previously been a party to two proceedings before the Copyright Tribunal.

In proceedings concerning voluntary licences and statutory licence schemes, the Copyright Tribunal must, if requested by a party to the proceeding, consider relevant guidelines made by the ACCC.<sup>3</sup>

The ACCC also has the power to intervene as a friend of the Court with respect to IP litigation that it considers has consumer or competition implications. For example, in 2002 the ACCC assisted the Federal Court in the *Stevens v Kabushiki Kaisha Sony Computer Entertainment* matter which concerned the ability of consumers to lawfully import copyright material.<sup>4</sup>

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<sup>1</sup> ACCC, *Submission to the Competition Policy Review*, 25 June 2014, p.65-66.

<sup>2</sup> See section 2 of the *Competition & Consumer Act 2010* (CCA).

<sup>3</sup> Copyright Act s. 157A.

<sup>4</sup> *Kabushiki Kaisha Sony Computer Entertainment v Stevens* [2002] FCA 906]

The ACCC has a role under the *Trade Marks Act 1995 (Cth)* (Trade Marks Act) to approve the rules governing the use of certification trade marks (CTMs). CTMs are a type of trade mark registered to regulate a scheme which identifies the characteristic of particular goods or services and which is open to other businesses to use if they meet the requirements of the scheme. The ACCC also assesses proposed CTM rules with regard to competition, unconscionable conduct, consumer protection and other factors.

## 2.2 Principles to apply in assessing the IP system

The ACCC notes the PC's objective, in undertaking this review, is to 'maximise the wellbeing of Australians', and has as its overarching goal that the '*...IP system provides appropriate incentives for innovation, investment and the production of creative works while ensuring it does not unreasonably impede further innovation, competition, investment and access to goods and services*'.<sup>5</sup>

The PC's Issues Paper outlines the four principles that it will apply to the IP framework to achieve this goal: effective, efficient, adaptable and accountable.

The ACCC strongly supports the PC's approach, although adds that rather than ensuring that the IP system does not *unreasonably impede further competition* the IP system should actively promote and harness competition to provide *appropriate incentives for innovation, investment and the production of creative works*.

The ACCC considers that competition can play a critical role in promoting the ultimate objective of maximising the wellbeing of Australians. Competition in markets ensures that Australians benefit from continuing innovation and increased choice of products and services, prices reflective of costs and resultant economic growth.

The ACCC submits that the role of competition particularly relates to the principles of ensuring that the IP system is *effective and efficient*. Competition ensures that firms have the incentive to innovate, invest in and produce IP. IP holders as well as users and prospective users of IP in downstream markets will have an interest in ensuring the appropriate dissemination and use of IP to innovate and remain competitive. Competitive forces also apply discipline to market participants to ensure that IP is created and used at the lowest cost and returns are proportional to the risk and value of the IP.

## 3. The economics of IP, and its intersection with competition law

### 3.1 The economics of IP

IP rights are a form of intangible property right for the creation of something new or original. They grant exclusive rights of use to the rights holder which can be exploited. IP includes copyright over literary, musical and artistic works; patents over inventive products and processes; trade-marks; designs; trade secrets and confidential information. Such rights are often of significant value to firms across the economy and their ability to compete effectively can be affected by their holdings or access to particular rights. As observed in the Issues Paper, there are several special characteristics of IP which warrant special treatment under property laws.<sup>6</sup>

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<sup>5</sup> Productivity Commission (PC), *Intellectual Property Arrangements, Productivity Commission Issues Paper*, October 2015 (PC Issues Paper), p. 8.

<sup>6</sup> PC Issues Paper, Box 2.

### **3.1.1. Market failure and ‘free riding’**

IP material has the characteristics of a public good; that is, it is difficult to exclude parties from using it (non-excludable), and/or its use by one party has no effect on the extent to which it is available for others (non-rivalrous).

Creators of IP incur fixed and often high creation costs. Many creators might be unwilling to incur these costs to create knowledge if they are unable to earn a sufficient rate of return on their investment. However, once the IP is created it can be copied and utilised at very low, and often close to zero, marginal cost. Absent IP laws that grant exclusive rights, the price of IP would tend to close to zero which would make no contribution to recovering fixed creation costs. That is, users would be generally unwilling to pay for a good as they could otherwise obtain it for free. As a result, expected returns to the creator would often be insufficient to provide appropriate incentives for efficient investment in IP material to the detriment of welfare.

IP regulation is one way to overcome this ‘free riding’ problem as IP laws grant exclusive statutory property rights to IP rights holders and penalise unauthorised use of IP. By doing so, a positive price of IP is able to be maintained, thus improving the incentives for its creation. However, the resulting ability to exclude may limit access to IP which has implications for its efficient use, including generating further innovation. Thus it is necessary for IP law to provide an appropriate balance between providing incentives for the *creation* of IP material and the efficient *use* of that material.

### **3.1.2. Transaction costs**

The potential for IP rights to address the market failure arising from the potential for ‘free riding’ rests on the assumption that transaction costs are low and the negotiating parties have roughly equal bargaining power. If this is the case, then an efficient outcome will be reached by bargaining between IP owners and potential users of the IP.<sup>7</sup> That is, owners will license as often as they can. Users will find licences or permissions to match their demand.

In reality, however, transaction costs of bargaining over licensing arrangements for IP are often high, and as a consequence, market failure may also arise in relation to licensing of IP. This has the potential to undermine the ability for IP to improve incentives for investment in new IP in those markets.

For IP owners, transaction costs include the costs of negotiating licences, monitoring compliance and taking infringement action if necessary. Transaction costs are likely to be very high for small to medium enterprises (SMEs) seeking to compete by getting their IP rights into the market, whether by themselves or through licensing. SMEs face considerable financial risk in taking Court action to protect their IP rights (and substantial sunk investments). Section 5.4 of this submission proposes some high level reforms to reduce these transaction costs.

Users also incur transaction costs in locating IP owners, negotiating licences and ensuring compliance with IP laws. Licensing will occur if the benefits of entering into a licensing arrangement exceed the costs of the arrangement, including transaction costs. If transaction costs are high, there is likely to be less licensing than is socially desirable.

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<sup>7</sup> This is an application of the so-called Coase theorem. See Coase, RH, (1960), ‘The Problem of Social Cost’ *Journal of Law and Economics*, Vol. 3, October, pp. 1-44.

Transaction costs for IP users can be reduced by laws that authorise uses that appropriately avoid the need for negotiated agreements with IP owners. The three main forms of authorised use are:

- Implied licences (fair use exceptions)
- Compulsory licences (regulated access)
- Collective licensing (rights associations or collecting societies)

Fair use exceptions reduce transaction costs by identifying those classes of uses that need not be treated as infringement of the IP owners' rights. Fair uses are fairly and reasonably limited and in the public interest. Fair use can also address market failure that can be created or exacerbated by the grant of the exclusive IP rights in the first place.

Compulsory licensing more directly addresses market failure where dependent upstream or downstream competitive markets cannot secure negotiated access to IP rights. Compulsory licensing regimes enable a user to obtain a lawful right to use IP in return for a payment that is set by judicial or administrative determination or by arbitration.

Collective licensing provides a particularly efficient way to overcome the high transaction costs of licensing copyright in markets where the value of individual rights may be low relative to transaction costs and it may be difficult or impossible to predict in advance precisely which rights may be required. For example, collecting societies act on behalf of their members who are owners of certain copyrights. The societies grant user licences, collect royalties from those users and then distribute royalty revenues back to members. However, collective licensing can also raise concerns under competition laws as it brings together copyright owners who would otherwise be in competition with one another and may enable the collecting society to exercise market power in the setting of licence fees and/or non-price licensing conditions.

## **3.2 Market power and effects on competition**

### ***3.2.1. IP protections and competition law are mostly complementary***

IP and competition law are for the most part complementary, both being directed towards improving economic welfare (for instance, via encouraging innovation and dynamism in the economy).

Competition law addresses restrictions on the effective functioning of markets to promote efficiency and consumer welfare. Competition drives producers to supply the goods and services that consumers want cost effectively. IP law encourages innovation and creation by recognising and granting exclusive statutory property rights to certain creative and inventive efforts, as outlined above.

IP rights confer on the owners of copyright the exclusive statutory right to exploit their IP and to exclude others from using it. The extent to which this creates market power depends on the availability of substitute products (which may themselves be the subject of IP rights) and other features of the market. The mere granting of an IP right does not conflict with the CCA. Even if granting an IP right confers market power this will not, of itself, conflict with the CCA. Firms are entitled to legitimately acquire or extend their market power by developing a superior product to their rivals. Competition law, like IP laws, encourages innovation.

Similarly, the exercise of various rights conferred by IP laws will not generally conflict with competition and consumer laws. This is because the licensing or assignment of IP is often pro-competitive as it enables IP to be exploited to a greater extent than would occur if the rights were not licensed or assigned at all. In these instances, licensing or assigning

copyright material can increase production, geographic distribution and the rate of introducing new products.

### **3.2.2. Where competition concerns may arise**

Although the mere grant and use of IP seldom conflicts with competition laws, in some circumstances, the *extent* and *use* of those rights may give rise to competition concerns and be detrimental to efficiency and welfare.

Market behaviour that inhibits the dissemination of IP would include both:

- co-ordinated behaviour by two or more firms in restrictive licensing practices; and
- unilateral behaviour by single firms with market power restricting the supply of IP rights.

Accordingly, if IP owners limit competition and extend market power through agreements with rivals, aggregating substitutable rights through acquisitions and/or through practices designed to exclude rivals and/or leverage market power, unrelated to the creation of new products, then efficiency and consumer welfare may be harmed. For example, there may be some circumstances in which a condition of an IP licence or assignment may have a detrimental impact on competition.

Certain licence terms and conditions may have an anti-competitive purpose or effect. For example, collective or cross-licensing arrangements which restrict competition between licence holders may enable the exercise of market power in the setting of licence fees and/or non-price licensing conditions. In addition, IP licences may restrict the extent to which a licensee is able to compete with the owner or rights holder. The form of such restrictions could include price or quota restrictions and non-compete clauses. However, the competitive effects of these restrictions depend on the characteristics of the market in which the licensing occurs and/or has an effect.

In relation to patents, anti-competitive conduct could include licences between competitors which divide markets, fix prices or limit output. Patent pools, which aggregate patent rights held by an individual or organisation for the purpose of licensing patents as a joint package and 'cross-licences' arrangements between rights holders granting rights for use among themselves can have pro-competitive effects as well as anti-competitive effects. The ACCC has noted the potential for price fixing and market sharing from these arrangements particularly where they exclude third party access.<sup>8</sup>

The ACCC notes the OECD's discussion of the ways in which patents can be used for strategic purposes, some of which may be harmful to competition and innovation. For instance, the OECD has found that some of these practices may include:

- *'ambushing' standard setting organisations (SSO's)*, whereby a company that conceals relevant granted or pending patents until a standard has been set and then sues for infringement.
- *patent 'flooding'*, whereby one company files a number of improvement patent applications relating to a technology or an invention developed by some other company, and
- *'Pay-for-Delay' patent settlements* involving pharmaceutical companies, which refer to agreements that 'allow branded manufacturers to share the profits from their

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<sup>8</sup> ACCC, ACCC submission to ALRC review into Competition Law and Intellectual Property, December 2003

branded drugs with potential generic rivals in exchange for delaying the roll out of a lower priced generic, and also prevent other generic manufacturers from entering the market'.<sup>9</sup>

In terms of copyright, increasingly in the digital economy, users may wish to access a copyright work for use as an intermediate product. If the cost of using existing copyright material is raised for such users, incentives to develop new services or markets could be reduced. The licensing or assignment of copyright can be pro-competitive if it enables the licensee to engage in commercial activity that would otherwise be closed to it, or which could only be engaged in by duplicating or 'inventing around' the existing copyright materials.

Where IP licensing or assignments are used to restrict or deter competition, for example by collective or cross-licensing, or other practices designed to exclude competition or leverage market power, a conflict may arise with the promotion of competition and efficiency.

As outlined in section 5 below, the ACCC submits that it is important that the rights created through IP laws should be fully subject to competition laws and that section 51(3) of the CCA be repealed. This would better ensure the use of IP rights is pro-competitive rather than anti-competitive in effect or purpose, which would be detrimental to innovation and welfare by undermining the effectiveness and efficiency of the IP system.

## 4. The extent of IP rights

Competitive forces are optimised where the appropriate balance is struck in the IP system between creating and maintaining incentives for the creation of IP, and maintaining incentives for its efficient use.

The ACCC recognises that it is difficult to precisely define this balance, however the guiding principle in assessing the extent of IP protections is that they should not extend beyond the point where the costs of protection start to exceed the benefits. That is, they should be determined within a cost-benefit framework. This aligns with the PC's proposed principles in ensuring that the extent of IP protections is both effective and efficient.

The ACCC notes the Harper Review Panel's observation that 'inappropriately applied intellectual property rights can 'reduce exposure to competition and erect long-lasting barriers to entry that fail to serve Australia's interests over the longer term'.<sup>10</sup>

The ACCC is concerned that, in the granting of IP rights, Australia's current IP system may not be striking the right balance between the extent of property rights and the efficient use of IP. The ACCC is concerned that the extent of current IP protections may, in some instances, go beyond what is needed to resolve the 'free rider' problem and incentivise innovation.

### 4.1 Patents

The ACCC acknowledges that there are often sound economic reasons for the granting of patents and that creation of exclusive rights can provide the incentives to create, and put to use, innovative property. However, the ACCC considers the patent system may not be working as effectively as it should to transmit knowledge and spur further innovation.

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<sup>9</sup> OECD Policy Roundtable, Competition, Patents and Innovation II, 2009, online at: <http://www.oecd.org/daf/competition/45019987.pdf>; See also OECD work on *Competition, Intellectual Property and Standard Setting*, available at <http://www.oecd.org/daf/competition/competition-intellectual-property-standard-setting.htm> and *Generic pharmaceuticals and competition*, available at <http://www.oecd.org/daf/competition/generic-pharmaceuticals-competition.htm>

<sup>10</sup> Competition Policy Review, *Draft Report*, September 2014, p. 30.

As noted in the Issues Paper, there is mixed evidence across different sectors on whether the current patent system is promoting innovation<sup>11</sup>, and may in some instances be having the opposite effect. Patents can be used to impose large costs on businesses that need access to licences or filed defensively to stall or exclude the entry of competitors or products. They can also impose costs on society by providing supernormal returns for patent holders, particularly if they are excessively long in duration.

Many patents are filed and not exploited at all or filed speculatively to extract license fees from firms who subsequently market a similar technology. Where thresholds for filing patents are low, there may be an excess of patents with little prospect of being developed into products that are brought to market, imposing inefficient costs on the administration of the system.

The ACCC notes that the threshold for granting patents and other IP rights was raised in Australia in 2012.<sup>12</sup> Prior to this, thresholds were lower than comparable jurisdictions which may have generated an inefficiently high volume of patents. Evidence is also emerging that Australia's Innovation Patent System (a second-tier patent system with a lower inventive threshold) has not been effective in achieving its objectives of stimulating innovation among small and medium sized enterprises.<sup>13</sup>

The ACCC submits that if patent protections extend too broadly, and if there are inadequate avenues to access patents on reasonable terms and conditions, then this has the potential to seriously undermine sequential innovation and thus reduce dynamic efficiency. The ACCC supports changes to patent protection which facilitate greater sharing of knowledge. This may include more flexible patent rights, incentives to expedite patented technologies to be brought to market and higher thresholds for registering patents.

## 4.2 Copyright

The ACCC is concerned that the extent of current copyright protections may go beyond what is necessary to provide an incentive to create and disseminate original copyright materials, and that they may be providing excessive protections to holders of IP rights.

For example, the extension of copyright protections from 50 to 70 years (following the death of the author or first date of performance/publication) are unlikely to have produced a commensurate incremental value of increased copyright works and may have deterred valuable use of older copyright works. The ACCC recognises that this aspect of the IP system cannot be amended due to international obligations but considers that within these constraints the introduction of a flexible fair use copyright exception can go some way towards rebalancing the system towards greater efficient use of copyright.<sup>14</sup>

The Issues Paper has identified a number of modern pressures facing the IP framework such as the rise of cloud computing, the Internet, digitisation and globalisation.<sup>15</sup> The ACCC has previously described a number of developments impacting consumers, IP holders and creators and those that manufacture and provide devices, platforms and services that form

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<sup>11</sup> PC Issues Paper, p. 17.

<sup>12</sup> Intellectual Property Laws Amendment (Raising the Bar) Act 2012

<sup>13</sup> IP Australia, The economic impact of innovation patents, 25 May 2015 available at <http://www.ipaustralia.gov.au/about-us/what-we-do/reports/The-economic-impact-of-innovation-patents> & response from the Advisory Council on Intellectual Property, Statement by the Advisory Council on Intellectual Property (ACIP) regarding the Innovation Patent System, viewed 2 November 2015 at <http://www.acip.gov.au/>.

<sup>14</sup> Copyright protections were extended pursuant to the 2004 Australia - United States Free Trade Agreement.

<sup>15</sup> PC Issues Paper, p. 12.

part of, or are interdependent with IP and particularly the copyright industries.<sup>16</sup> Broadly these trends include:

- Electronic formats of copyright material, which can be reproduced and distributed at much lower cost, increasingly replacing physical copies.
- Consumer empowerment over consumption, that is, consumers increasingly able to time-shift and format shift content and use third party services to store content remotely.
- The increasing availability of unauthorised copies of copyright over the internet.
- The increased volume of copyright materials such as user-generated 'non-commercial' copyright materials and the ability of consumers to manipulate and combine copyright materials into new materials.
- New services such as cloud computing and other internet services provided by 'internet intermediaries' such as Facebook, Google and YouTube.

The ACCC considers that existing provisions in the Copyright Act may be inhibiting the growth of new services and competition made possible from developments in the digital economy.<sup>17</sup> One reason for this is because digital technologies are largely based on copying, so copyright law applies; however existing laws were not designed for the digital economy and may therefore achieve inefficient outcomes. This view was adopted by the ALRC in its final report.<sup>18</sup>

The ACCC has identified a number of growing uses of copyright that are prohibited by Copyright law that do not necessarily result in the extraction of additional value from the underlying copyright material. These uses include, among others, incidental use by internet intermediaries such as search engines, 'unauthorised' copying, and cloud computing services which permit consumers to time and format shift copyright material. Many of these uses associated with the digital economy sit in a 'grey area' where a conservative and static approach may be to favour rights holders rather than users.

The Optus TV Now matter illustrates how the current copyright framework is ill-equipped to deal with new and emerging services and changing consumer expectations in the digital economy.<sup>19</sup> Optus TV Now was a cloud based service for consumers to record and play copies of free-to-air (FTA) broadcast television programmes. Optus was held to be in breach of copyright, as rather than the consumer making copies for their own private use (consistent with Copyright Act exceptions), the Full Federal Court held that Optus made the copies of the relevant television programmes. As a result of the ruling, Optus ceased offering the service to its customers.

The ACCC submits that in such circumstances, the PC should consider whether the extent of copyright protections and exceptions are having an unintended effect on efficiency in the digital economy. As outlined in its submission to the ALRC's discussion paper, the ACCC broadly supports the introduction of a flexible 'fair use' exception in the Copyright Act as

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<sup>16</sup> ACCC, *ACCC submission to ALRC Copyright and the Digital Economy Issues Paper*, November 2012, p.21-24.

<sup>17</sup> See discussion on third party use of copyright material in ACCC, *Submission to the ALRC Copyright and the Digital Economy Discussion Paper* (31 July 2013) pp.10-12, available at: <http://acc.gov.au/regulated-infrastructure/communications/intellectual-property/alrc-review-of-copyright-the-digital-economy/discussion-paper-submission>.

<sup>18</sup> See in particular ALRC discussion relating to fair use and third parties in the ALRC, *Copyright and the Digital Economy Final Report* (February 2014) available at: <http://www.alrc.gov.au/publications/copyright-report-122>.

<sup>19</sup> *Singtel Optus Pty Ltd v National Rugby League Investments Pty Ltd* [2012] FCA 34

proposed by the ALRC. Such an exception is likely to promote an appropriate balance between socially beneficial incentives to create and incentives to disseminate and use copyright material.

Such an exception would limit the scope of copyright by allowing certain forms of use without payment to the copyright owner. The ACCC considers that such an exception has the ability to provide a desirable degree of flexibility that will enable the law to accommodate and foster technological advances and innovations that might otherwise be curtailed by prescriptive and/or narrow exceptions in the Copyright Act. This view was endorsed by the ALRC who concluded that such a fair use exception finds the right balance between protecting rights holders and promoting efficient use and innovation. The ALRC considers that such a reform would also generate economic advantages, noting that ‘...fair use would make Australia a more attractive market for technology investment and innovation.’<sup>20</sup> Section 5.2 below discusses in further detail how this proposal could be included.

### 4.3 Parallel imports

The ACCC considers that remaining restrictions on parallel imports are not justified by a market failure rationale and should be repealed to promote competition and lower prices for consumers.

Unlike many other IP issues, Australia’s parallel import laws are not governed by international treaty obligations. Restrictions on parallel imports arise out of the Copyright Act and the Trade Marks Act. The Copyright Act has been amended a number of times to remove restrictions on parallel imports on certain categories of copyright material, and a separate regime has been created in relation to books that allows limited parallel importation to address issues of availability.<sup>21</sup> The ACCC welcomes the Government intention to remove remaining parallel import restrictions on books in its response to the Harper Review.<sup>22</sup>

The Trade Marks Act can enable a trade mark owner to prevent prospective importers from importing goods into Australia if the use of trade mark is registered for use in specific territories. Two examples were noted in the ACCC’s submission to the Harper Review where territorial conditions in Trade Mark assignments had been used to prevent products being imported in Australia.<sup>23</sup>

Legislative restrictions on parallel imports are not justified by the traditional ‘free rider’ concerns relating to IP which relate to preventing unauthorised reproduction. Instead, parallel importation restrictions extend IP rights into the process of distribution. They may also lead to inefficient outcomes by providing rewards to creators that are not proportional to the value or risk of their creation and create a public detriment

Parallel import restrictions grant an exclusive right to import to IP owners. By preventing international arbitrage these import monopolies may be used to support international price discrimination by firms with market power. The ACCC considers that restrictions on parallel imports prevent consumers gaining access to an alternative source of goods which can

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<sup>20</sup> ALRC, *Copyright and the Digital Economy*, Final Report, p.23

<sup>21</sup> Under section 37 of the Copyright Act, it is generally an infringement of copyright to import a literary work, among other works, into Australia for commercial purposes without the copyright owner’s consent, where the importer knew, or ought reasonably to have known, that if the literary work had been made by the importer in Australia it would have infringed copyright. Under section 38 of the Copyright Act, it is generally an infringement to sell an imported literary work if the seller knew that if the work had been made in Australia by the importer, it would have infringed copyright. Sections 102 and 103 of the Copyright Act extend importation protection to subject matter other than works. Essentially, in relation to books, these provisions protect the published edition of a book.

<sup>22</sup> Australian Government, *Australian Government Response to the Competition Policy Review*, p.13

<sup>23</sup> ACCC, *ACCC submission to the Competition Policy Review*, 25 June 2014, pp. 60-61.

promote competition and potentially provide consumers with lower cost products and improve the international competitiveness of user industries.

The ACCC has consistently held the view that parallel importation restrictions extend rights to IP owners beyond what is necessary to address the 'free rider' problem. The ACCC submits there is no further economic reason to justify remaining restrictions on parallel imports.

## 5. Efficient use of, and access to, IP

On the use of IP, the ACCC considers that IP rights should be treated no differently from other property rights in terms of the application of competition law and the right to access.

### 5.1 Section 51(3) of the CCA

Where there are significant competition concerns it is imperative that the use of IP rights is subject to the CCA in the same way as any other property. In particular, the ACCC has a longstanding view that the IP-related 'exception' in section 51(3) of the CCA should be repealed.

The ACCC's view is based on three key reasons:

1. Although the vast majority of arrangements where IP rights are licensed or assigned to other entities are likely to be pro-competitive there is still a significant risk that some licensing arrangements can unduly damage efficiency and welfare. Where these arrangements are exempt because of the operation of section 51(3) this conduct cannot be addressed.
2. Most IP licensing arrangements do not require the benefit of the exemption as the vast majority do not damage competition.
3. Although the exemption is crafted with a view to narrowing its application there remains considerable uncertainty about its application in certain circumstances. The uncertainty about the scope of section 51(3), arises chiefly in relation to the interpretation of the term 'to the extent that the condition *relates to*' which is contained in section 51(3)(a).<sup>24</sup> This creates costs for firms unsure whether they can challenge licensing conditions whilst not providing material benefits to firms who are doing the right thing.

In light of the above factors, the ACCC submits that the removal of the exemption together with availability of the normal authorisation process for IP arrangements would provide the appropriate certainty and flexibility.<sup>25</sup>

The Harper Review Panel (Panel) also proposed the repeal of section 51(3) in its 2015 final report, recommending that the assignment and licensing of IP rights be subject to the CCA in the same manner as transactions involving other property and assets.<sup>26</sup> The Panel recommended that the repeal occur immediately, irrespective of the overarching review of IP

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<sup>24</sup> See ACCC, *ACCC submission to the ALRC Copyright and the Digital Economy Issues Paper*, November 2012, pp.31-33.

<sup>25</sup> ACCC, *ACCC submission to the ALRC Copyright and the Digital Economy Issues Paper*, November 2012 & ACCC *submission to the ALRC Copyright and the Digital Economy Discussion Paper*, 31 July 2013.

<sup>26</sup> Competition Policy Review, Final Report, p. 108 & ACCC, *ACCC Submission to the Competition Policy Review*, 25 June 2014 & ACCC, *ACCC Submission to the Competition Policy Review – Response to the Draft Report*, 26 November 2014, p. 21.

it recommended be conducted by the PC.<sup>27</sup> The Panel also noted that the block exemption power that it recommended could be used to specify 'safe harbour' licensing restrictions for IP owners, as suggested by the ACCC.<sup>28</sup> The ACCC supports such a power.

Other advisory panels to recommend its repeal include the Australian Law Reform Committee (ALRC) (in their review into Copyright and the Digital Economy), who in November 2013, noted that the repeal of section 51(3) is *an integral aspect of equipping copyright law for the digital economy*.<sup>29</sup> In addition, in July 2013, the House of Representatives Standing Committee on Infrastructure and Communications recommended the repeal of section 51(3) on the basis that it constrains the ACCC unjustifiably from investigating restrictive trade practices in relation to IP rights.<sup>30</sup>

The ACCC emphasises that key jurisdictions, including the US, the European Union and Canada, do not exempt IP from competition laws. The ACCC notes that Canada's competition regulator has issued guidelines describing 'safe harbours' for IP conduct to assist industry licensing practices. There is little evidence that efficiency enhancing and pro-competitive IP licensing is harmed in those jurisdictions. Repealing s 51(3) would therefore bring Australia more in line with international practice.

## 5.2 Flexible fair use exceptions and implied licensing for copyright

Broadly, the ACCC considers that there are certain uses of copyright that are prohibited by IP law that do not necessarily result in the extraction of additional value from the underlying IP. These uses are largely associated with the trends of economic activity and consumption that have emerged in the digital economy, outlined in section 4.2 above. In addition, such uses may also fail to recognise the benefits that may be flowing to the copyright owner. In certain circumstances, these uses may even present opportunities for exploiting further value in the copyright and provide some additional value to the underlying owner of the copyright.

Where the current legislation does not contemplate the emergence of these services, incentives for the market to innovate with new technologies and services to meet consumer expectations may be diminished with detrimental long term effects on efficiency. To ensure the system's adaptability, the ACCC submits that an explicitly technology neutral flexible fair use exception implemented through principles or standards-based legislation has the ability to provide a balance of flexibility and certainty for industry participants to accommodate and foster innovations that may be hindered by narrow or prescriptive exceptions.

The ACCC recognises that rights holders may fear that an expansion of fair use exceptions may affect their inherent rights to exploit their IP and deny them potential revenues or undermine existing business models. The ACCC accepts that the scope of fair use exceptions should consider the effect of the use upon the potential market for, or the value of, the copyright material and incentives to create copyright material.

The ACCC considers, however, that the IP framework should implicitly recognise that changing technology and consumer expectations can erode and disrupt existing business models. Third parties and consumers should not be precluded from incidentally using or transforming copyright material (or manipulating that material for which they have paid)

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<sup>27</sup> Competition Policy Review, Final Report, p. 110.

<sup>28</sup> Competition Policy Review, Final Report, p. 110 & Recommendation 39 – Block exemption power, p. 406

<sup>29</sup> ALRC, *Copyright and the Digital Economy*, Final Report p.74

<sup>30</sup> House of Representatives Standing Committee on Infrastructure and Communications, *At What Cost? IT Pricing and the Australia Tax* (2013) Recommendation 8.

where the rights holder has had a reasonable opportunity to exploit those rights and the value of those rights or incentives to create copyright are not diminished. Indeed, rights holders may be required to adapt to these changes in technology and consumer behaviour and not leverage or extend their rights to inhibit these developments or monopolise emerging and ancillary markets to the primary copyright. For example, with the development of new format and time shifting technologies, consumers who have already purchased copyright material should not have to seek the permission of the rights holder in order to take advantage of new services developed by third parties which provide new ways of consuming that copyright (or be tied to the services provided by that copyright owner). As rights holders bring future rights to market, those licensing arrangements and business models will be informed by the potential for copyright to be used in a growing number of ways.

As recommended by the ALRC, the ACCC notes that a non-exhaustive list of 'fairness factors' could be incorporated into the legislation to assess fair use. These fairness factors involve assessing the purpose and character of the use and the effect of the use on the value of the copyright material (and incentives to create copyright material) and are framed in a manner to ensure their adaptability to technological change. The ALRC also supported the ACCC's proposal for a non-exhaustive list of illustrative purposes or examples to be included in any reformed legislation to further mitigate concerns over uncertainty.<sup>31</sup> The illustrative purposes would assist courts in determining whether a copyright holder was seeking to define the markets for their copyright material in ways that would enable foreclosure of markets ancillary to the core purpose and nature of those rights.<sup>32</sup>

### 5.3 Access regimes and compulsory licensing

The ACCC recommends that the PC review access frameworks for IP with a view to harmonising access arrangements in Australia. In this regard, the ACCC considers that access frameworks for IP should have a clear focus on promoting competition and economic efficiency in the event access to IP is mandated.

The ACCC notes that while it is important that IP rights be subject to the CCA in the same way as other property rights through the repeal of section 51(3) it is important to recognise the limitations of competition law in relation to certain types of anti-competitive conduct. For example, there is no general competition remedy for conduct that simply reflects an exercise of unilateral market power such as monopoly pricing or refusal to licence, that does not either involve an anti-competitive agreement or unilateral conduct that is exclusionary under section 46 or substantially lessens competition under section 47 of the CCA.

In this respect, if access to particular IP becomes more restricted in the future due to the pace of technological advancement, there may be a need to consider the effectiveness of existing access mechanisms.

Currently, access regimes for certain types of IP (e.g. the compulsory licensing regime for patents and the power of the Copyright Tribunal to determine charges and conditions for use of copyright materials in statutory and voluntary licensing arrangements) exist to provide an avenue for access to IP as well as a deterrent for unreasonable refusal to licence. Such provisions exist in recognition of the potential for excessive harm to competition from the withholding of supply by a rights holder. In practice, however the compulsory licensing scheme for patents is utilised relatively infrequently.

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<sup>31</sup> ALRC, *Copyright and the Digital Economy*, Final Report, Chapters 4 & 5.

<sup>32</sup> The application of proposed 'fairness factors' and illustrative purposes was discussed in more detail in the ACCC submission to the ALRC Copyright and the Digital Economy Discussion Paper, 31 July 2013, Chapters 4 & 5.

The ACCC notes that in March 2013 the PC released its report on its inquiry into the Compulsory Licensing of Patents.<sup>33</sup> The PC made a number of recommendations to increase the efficient operation of the scheme, including to confine compulsory licensing orders on anti-competitive conduct grounds to CCA remedies rather than the *Patents Act 1990* provisions. No changes have yet been made to the scheme in response to the PC's recommendations.

In the event that existing frameworks prove not to be effective in ensuring efficient access in the future, some legislative change to access regimes may require further consideration. In its submission to the *Intellectual Property and Competition Review Committee* in 1999, the ACCC noted that there is no reason to treat IP any differently to other services in relation to access.<sup>34</sup> The ACCC reiterated this view in its submissions to the Harper Review, noting that one way of achieving this might be to remove the IP exclusion from the national access regime in Part IIIA of the CCA.<sup>35</sup>

The ACCC notes that provisions promoting efficient access to intellectual property exist in other jurisdictions; for example, section 32 of Canada's Competition Act provides for 'special remedies' to apply to intellectual property where the court finds that the exclusive rights have been used to unduly restrain trade or lessen competition. The Canadian Competition Bureau has indicated the strict criteria it will apply before requesting a special remedy, including that the intellectual property holder is dominant, the intellectual property is essential for competition in a second market, and the special remedy would not adversely affect incentives for research and development investment in the economy.<sup>36</sup> These criteria are similar to the criteria that must be satisfied in Part IIIA of the CCA.

#### **5.4 Other methods to address transaction costs**

The ACCC supports the PC in exploring how transactions costs can be reduced both by utilising technology and by other legislative reforms.

Similarly to how the digital economy is facilitating new models of commerce and reducing transaction costs by connecting buyers and sellers, there is scope for these trends to lower barriers in IP trade. The ACCC supports market based mechanisms where possible to reduce transaction costs in searching for and licensing IP rights. The ACCC notes that digital technologies can be used to administer rights in a manner that can promote more direct licensing and potentially reduce the role of collecting societies. This can overcome some of the market power and above-efficient pricing practices associated with collective licensing, and promote efficiency benefits and improve the overall effectiveness of the regime.

The ACCC therefore supports the PC in exploring how new approaches, such as the UK's Copyright Hub, may operate in the Australian context.

As noted in section 3.1.2, the ACCC considers that it is important to recognise the high transaction costs faced by SMEs in protecting their IP rights, which for many is a substantial sunk investment that will be irrecoverable if legal enforcement mechanisms are not commercially realistic.

The ACCC suggests that reforms could also be made to improve access to enforcement remedies for SMEs. For example, this could include the establishment of a specialist

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<sup>33</sup> Productivity Commission Inquiry Report, *Compulsory Licensing of Patents*, 28 March 2013.

<sup>34</sup> ACCC, *Submission to the Intellectual Property and Competition Review Committee* (1999).

<sup>35</sup> Section 44B(E).

<sup>36</sup> Competition Bureau Canada, 2014, *Enforcement Guidelines: Intellectual Property*, pp12-13.

Tribunal to administer alternative administrative enforcement options at a lower cost. Reforms that enable more cost effective protection of IP rights are likely to enhance the competitive position of SMEs in relevant markets and thereby promote greater competitive activity in those markets.

## 6. Trade Agreements

The ACCC agrees with the recent Harper Review Panel recommendation that international trade negotiations should be informed by an independent and transparent analysis of the costs and benefits to Australia of any proposed IP provisions. The ACCC notes that the PC conducted an assessment of the IP provisions of the Australia – US Free Trade Agreement in 2004 and found that Australia would lose more than it gained from the strengthening of IP rights.<sup>37</sup>

The ACCC reiterates its views expressed to the Harper Review Panel that caution should be exercised when entering international treaties or agreements that may have the effect of significantly limiting the ability of the Australian Government to make substantial and effective reforms to IP regulation.

Pursuant to the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), to which Australia is a signatory, efforts have been made in recent years to further harmonise patent and other IP regulations. While there may be benefits to harmonisation, the appropriate balance between the extent of IP protections and access will differ internationally, and therefore, Australia should be highly mindful of the impacts on competition and the Australian economy in approaching future negotiations.

The ACCC notes that Australia has recently signed up to the Trans-Pacific Partnership (TPP), a trade agreement among 12 countries. The TPP contains a range of IP-related obligations that may have significant consequences for the granting and use of IP (and consequently for competition) over decades.

The ACCC recommends that, while the agreement has already been signed, prior to enacting the agreement, it is critical that there be a comprehensive and robust analysis of the actual impacts of the IP provisions in the TPP on competition and consumers. Further, the IP provisions should be examined using the PC's guiding principles outlined in its issues paper—that is, are the IP provisions in the TPP effective, efficient, adaptable and accountable, and do they promote the overarching objective and goals for the IP system in the PC's issues paper?

In the ACCC's view, the IP chapter of the TPP is complex and a number of questions remain as to its impact on Australia's current and future IP settings. The ACCC is concerned that the agreement appears to impose IP restrictions beyond existing international treaties, and this may tilt the balance in favour of IP rights holders to the detriment of competition and consumers. The ACCC is of the view that any evaluation of the IP provisions in the TPP should consider, among other things, whether these provisions:

- facilitate competitive IP markets
- have the effect of extending patent protections and/or expand what can be patented
- promote the further emergence of disruptive technologies and dynamic innovation.

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<sup>37</sup> Intellectual property rights and the Australia- US Free Trade Agreement, Research Paper No. 14 2003-04, retrieved 26 November 2015 at [http://www.aph.gov.au/About\\_Parliament/Parliamentary\\_Departments/Parliamentary\\_Library/pubs/rp/rp0304/04rp14](http://www.aph.gov.au/About_Parliament/Parliamentary_Departments/Parliamentary_Library/pubs/rp/rp0304/04rp14).

The ACCC also has concerns about the impact of the TPP's investor-state dispute settlement provisions. The ACCC agrees with the PC's view expressed in its 2013-14 Trade and Assistance Review<sup>38</sup> that such provisions risk impeding domestic reforms in the public interest. The ACCC supports an evaluation of the extent to which these provisions are consistent with ensuring Australia has sufficient scope to introduce IP law reforms that meet the evolving needs of consumers and the encouragement of disruptive, innovative technologies.

The ACCC notes the PC's observation that 'the Australian Government (2015) has stated that the TPP will not require any changes to Australia's patent system or copyright regime'.<sup>39</sup> In the ACCC's view, an equally, and perhaps more important consideration, is to what extent the TPP might impede Australia from making changes to IP settings in the future, particularly as a key aim of the review is to ensure that Australia can identify and make improvements to the IP system in light of ongoing economic and technological changes.

In light of the recently concluded TPP negotiations, the ACCC is of the view that it is imperative that Australia introduce reforms that promote competition and stimulate innovation and, where necessary, limit the ambit of IP protections. Specifically, the ACCC recommends the introduction of a flexible fair use exception, and is of the view that legislative change should be considered to ensure that the National Access Regime under Part IIIA of the CCA applies to IP.

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<sup>38</sup> Productivity Commission, *2013-14 Trade and Assistance Review* <http://www.pc.gov.au/research/ongoing/trade-assistance/2013-14/trade-assistance-review-2013-14.pdf>

<sup>39</sup> PC Issues Paper, p. 29.