Trade, Competition and Intellectual Property

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ABSTRACT *TRIPS does not lay down rules on parallel imports. Its provisions, however, do give states the discretion to apply competition rules to the exercise of intellectual property rights. The indeterminacies of competition law and its application mean that intellectual property owners lack objective criteria by which to plan their strategic uses of intellectual property. Competition policy, if not clearly and consistently worked out, may well serve to undermine the incentive effects of intellectual property.*

Keywords: competition policy, intellectual property, licensing, market power, parallel imports, TRIPS.

Introduction

Let us imagine a software publisher in the USA which comes up with a computer game. In the game, the players try to track down a gang of criminals across different countries and continents throughout the world. Apart from anything else, the game (assuming the requirements of originality are satisfied) will attract copyright protection in the USA.

The USA has been a member of the Berne Convention since 1989 and the Universal Copyright Convention for much longer. (Alternatively, the game might have been simultaneously published in a Berne Convention country.) Therefore, copyright protection will also arise in Australia. The US company, for reasons which seem good to it, has appointed an 'agent' with exclusive rights to create and promote a market for the game in Australia. Thus, we have a clear interaction of trade law and intellectual property rights. Once the game has proven a success in Australia, another party approaches the US company seeking rights to import the game into Australia too. The second comer is a notorious discounter. If the US company is minded to honour its arrangements with its agent (who has helped make the product a success here), the US company and the agent arguably find themselves triangulated by intellectual property, trade law and competition policy or antitrust.[1]

In this article, therefore, I propose first to review how the Agreement on Trade-Related Aspects of Intellectual Property (TRIPS) addresses these issues. Then, having found scope for the possibility, I wish to consider some of the complications which arise when we seek to apply competition policy to intellectual property rights.

TRIPS

For common lawyers at least, the intersection of intellectual property law and trade policy has been virtually ever present, even if not always recognised. The most obvious

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examples are amongst the most longstanding of multilateral treaties, the Berne Convention for the protection of literary and artistic works and the Paris Convention for the protection of industrial property. Each of these firmly sets in place the interlinked systems based on national protection so familiar today and were the responses of the age of steamships and the telegraph to problems of international piracy.[2] Simplifying matters drastically, countries were not able to secure protection for their nationals' efforts in other countries without offering corresponding protection in their own territories for the efforts of the other countries' nationals.

Questions of antitrust or, perhaps more appropriately, competition policy have also achieved some degree of direct recognition in this context.[3] There have also been some instances of the intersection of trade policy, intellectual property law and antitrust in the courts.[4]

Nonetheless, with its prospect of potentially substantial sanctions, the starting point for an examination of all three policy frameworks is TRIPS. As a Member of the World Trade Organisation (WTO) through its signature of the Marrakesh Agreement, Australia became obliged to implement TRIPS into its domestic law[5] with effect from 1 January 1996[6] or risk the possibility of censure and trade sanctions under the dispute resolution procedures.[7]

For present purposes, Parts I and II of TRIPS are relevant. Part I is headed 'General Provisions and Basic Principles'; Part II, 'Standards Concerning the Availability, Scope and Use of Intellectual Property Rights'.

TRIPS and Exhaustion

Before turning to those provisions which make express provision for the intersection of trade policy, intellectual property rights and competition policy, it is convenient to mention one issue which is in many respects not addressed. TRIPS does not lay down any specific rules about parallel imports (sometimes called grey goods) provided the basic rules against discrimination are recognised. Article 6 entitled 'Exhaustion' provides:

> For the purposes of dispute settlement under this Agreement, subject to the provisions of Articles 3 and 4 above nothing in this Agreement shall be used to address the issue of the exhaustion of intellectual property rights.[8]

Articles 3 and 4 provide for, respectively, the principles of 'national treatment' and 'most-favoured-nation treatment'. That is, very broadly and at the risk of great simplification, a Member's laws must first treat nationals of other Members no less favourably than the Member's own nationals and, secondly, any advantage, favour, privilege or immunity granted by a Member to nationals of any other country must be immediately and unconditionally accorded to nationals of all other Members.

Subject to these rules against discrimination, therefore, TRIPS does not lay down rules about parallel imports. Each country is largely free to deal with parallel imports as it sees fit. If nothing else, this result indicates that the international community has not reached any consensus about this question and, indeed, there are quite deep divisions.[9]

TRIPS and Competition Policy

The first (and perhaps most basic) provision directly addressing the subject matter of this article is Article 7 entitled 'Objectives':

> The protection and enforcement of intellectual property rights should contribute to the promotion of technological innovation and to the transfer and dissemination of

> technology, to the mutual advantage of producers and users of technological knowledge and in a manner conducive to social and economic welfare, and to a balance of rights and obligations.

In some respects, this is a narrow statement of objectives, possibly constrained by the trade context of its birth.[10] Nonetheless, even without more, its terms suggest considerable scope for the application of competition policy or antitrust to intellectual property rights in a trade context. First and foremost, intellectual property rights *should* promote innovation and the dissemination of technology: goals often claimed to be pursued by competition policy. The protection and enforcement of intellectual property rights apparently should also be undertaken in a manner conducive to both 'social and economic welfare'; enhancement of economic welfare at least being one of the professed objectives (if not *the* objective) of competition policy. Finally, there is a need to *balance* rights and obligations.

For the purposes of this article, further shape is given to those objectives by the principles set out in Article 8. In particular, Article 8.2 of TRIPS in Part I declares:

> Appropriate measures, provided that they are consistent with the provisions of this Agreement, may be needed to prevent the abuse of intellectual property rights by right holders or the resort to practices which unreasonably restrain trade or adversely affect the international transfer of technology.

Through Article 8.2, therefore, TRIPS recognises the *possibility* of arguably three types of situation inconsistent with the objectives sought to be promoted: 'abuse' of intellectual property rights *by* rights holders or the resort to practices which unreasonably restrain trade or adversely affect the international transfer of technology. In such cases, a Member may take 'appropriate measures' (provided of course the measures are not just appropriate but also consistent with TRIPS itself).

Some further elaboration of this basic principle can be found in Part II. Sections 1 to 7 set in place systems of protection for several types of subject matter: copyright, patents, designs, trademarks, geographical indications, layout designs and confidential information. These systems are largely based on existing multilateral regimes of protection and, in very broad terms, provide for right owners to have exclusive rights.

The system of exclusive rights is qualified in a number of respects. First, the Articles defining the subject matter sometimes expressly recognise that the right is merely one to equitable remuneration or the existence of some form of compulsory licence[11] or do so by reference to some other instrument.[12]

Secondly, for a number of subject matters, TRIPS expressly recognises that Members may adopt limitations or exceptions to exclusive rights in (1) special cases which (2) do not conflict with a normal exploitation of the work and (3) do not unreasonably prejudice the legitimate interests of the right holder.[13]

Thirdly, section 8 is headed 'Control of anti-competitive practices in contractual licences'. It consists only of Article 40. Its four paragraphs address three issues.

By article 40.1:

> Members agree that *some* practices or conditions pertaining to intellectual property rights which restrain competition *may* have adverse effects on trade and *may* impede the transfer and dissemination of technology. (my emphasis)

This provision in many respects has the appearance of a recital or acknowledgment of fact and has two elements. There are apparently some, not all, practices or conditions which do restrict competition. The particular practices or conditions which do have this effect are not expressly identified in Article 40.1. In addition, these practices or conditions may, not will, have negative effects on trade and/or the transfer of technology.

The second issue dealt with in Article 40 is one of the consequences arising from that acknowledgment. Article 40.2 provides:

> Nothing in this Agreement shall prevent members from specifying in their national legislation licensing practices or conditions that *may in particular cases* constitute an abuse of intellectual property rights having an adverse effect on competition in the relevant market. As provided above, a member *may* adopt, consistently with the other provisions of this Agreement, appropriate measures to prevent or control such practices, which may include for example exclusive grantback conditions, conditions preventing challenges to validity and coercive package licensing, in the light of the relevant laws and regulations of that Member. (my emphasis)

Article 40.2 at least gives some examples of licensing practices or conditions which might constitute an abuse of intellectual property rights: 'exclusive grantback conditions', presumably the practice whereby licensors require licensees to assign ownership of any improvements to the licensed rights; bans on challenging the validity of intellectual property rights and 'coercive' package licensing, presumably requiring a licensee to accept licences of 'unwanted' rights as a condition of licensing the 'desired' rights. This list, which arguably also applies to Article 40.1, is clearly not exhaustive.[14]

While Article 40.2 endorses the use of laws and regulations to control such practices and conditions, it would appear that the practices and conditions are not necessarily or always an abuse of intellectual property rights or otherwise anti-competitive. These practices or conditions are not proscribed *ipso facto*. The first sentence of Article 40.2 states that they may in *particular cases* constitute an abuse. This quite strongly indicates that Members did not consider these practices or conditions always constituted an abuse having adverse effects in the relevant market. The fact that the article is concerned about adverse effects on competition in 'relevant' markets supports this. Moreover, the second sentence does not make the adoption of measures to prevent or control such practices mandatory as one would expect if there had been agreement that these practices were always evil. Instead, Members 'may' adopt appropriate measures. Further, the measures adopted must be consistent with 'the other provisions of this Agreement'. Presumably, these provisions include the recognition of some rights of remuneration or other compulsory licences and the more general rules that exceptions to infringement be limited to special cases which do not conflict with normal exploitation or otherwise unreasonably prejudice the legitimate interests of rights holders.[15] Moreover, the provision which finally evolved as Article 40.2 initially contemplated permitting parties to specify in their national legislation practices 'deemed to constitute an abuse of intellectual property rights or to have an adverse effect on competition in the relevant market'.[16]

Arguably, Article 40.2 appears to treat the two separate aspects of Article 8—the abuse of intellectual property rights on one hand and, on the other, the resort to practices which unreasonably restrain trade or adversely affect the international transfer of technology—as the same thing, but this is perhaps not so clear.

The third issue addressed by Article 40 is interesting as much for what was not included as for what it embodies. Articles 40.3 and 40.4 provide for consultations where one Member believes its rules implementing Article 40 are being violated by the nationals or domiciles of another Member. Article 40.3 deals with the situation where a Member believes that the nationals or domiciles of another Member are contravening its rules. The Member whose nationals or domiciles are suspect must afford 'full and sympathetic consideration to, and shall afford adequate opportunity for, consultations'.

The Member must also cooperate by supplying information subject to domestic law about confidentiality. Conversely, a Member whose nationals or domiciles 'are subject to proceedings' by another Member has corresponding rights of consultation. Most significantly, however, these rights are 'without prejudice to any action under the law and to the full freedom of an ultimate decision of *either* Member'.

The obligations in Articles 40.3 and 40.4 clearly advance the obligations of a Member to cooperate with another Member which considers its intellectual property laws are being abused to restrain competition and impede trade or the transfer of technology. They must be contrasted, however, with the scope of the obligations originally sought by the so-called Group of 14.[17] The Group of 14 had sought an obligation that:

> ...each Party agrees upon the request of any other Party to consult with respect to any such practices and to co-operate with other parties with a view to ensuring that IPR owners, who are nationals or domiciliaries of its country, comply with the obligations prescribed in this respect by the national legislation of the Party granting them such rights.[18]

If a country's laws on technology transfer prohibited restrictions on the export of goods protected by intellectual property rights, might the proposed obligation to cooperate with a view to ensuring compliance require the mandating of parallel imports?[19] Clearly, the obligations imposed by Article 40.3 do not go so far. In addition, Article 40.4 allows some scope for pressure to be brought in the opposite direction.

Clearly, therefore, TRIPS mandates at least the application of competition policy or antitrust rules to the exercise of intellectual property rights in particular cases. This could arise where the intellectual property right is being in some way 'abused' to affect competition adversely. The scope of Articles 8 and 40 appears broad enough at least to cover both unilateral exercise of power and collusive or bilateral arrangements, the traditional targets of competition policy and antitrust.

What is Happening Now

At the December 1996 Ministerial Conference, the WTO established a working group:

> ...to study issues raised by Members relating to the interaction between trade and competition policy, including anti-competitive practices, in order to identify any areas that may merit further consideration in the WTO framework.[20]

This is a working group only and the declaration was made 'on the understanding that work undertaken shall not prejudge whether negotiations will be initiated in the future'.[21]

The drivers for this development include the successes in promoting and increasing international trade, the difficulties in enforcing national laws against transnational agents and, eventually, business' increasing need for more uniform and unified enforcement policies. No doubt, there is also an element of 'exporting' or at least legitimating a jurisdiction's own competition policies. Significantly, the USA (which of course has considerable clout in bilateral negotiations) has expressed caution: raising, amongst other things, the difficulty in reaching agreement on 'sound competition rules', the risks of adopting 'lowest common denominator' outcomes, the fact-intensive nature of antitrust inquiries and the consequent surrender of national sovereignty involved.[22]Under the chairmanship of Professor Frederic Jenny from France, the Working Group met three times in 1997 and is scheduled to meet four times in 1998.[23] The work programme has been broken down into four topics:

- relationship between the objectives, principles, concepts, scope and instruments of trade and competition policy;
- stocktake and analysis of existing instruments, standards and activities;
- interaction between trade and competition; and
- identification of any areas that may merit further consideration in the WTO framework.

The meetings in 1998 were scheduled for 11–13 March, 27–28 August, 23–25 September and 17–19 November. It is expected that the relationship between trade-related aspects of intellectual property and competition policy will be considered at the September meeting along with the relationship between investment and competition policy.

Intellectual Property Rights and Antitrust[24]

TRIPS is a clear affirmation that, at least in particular cases, dealings in (or refusals to deal in) intellectual property rights may conflict with competition policy and so may be subjected to 'appropriate measures'. We must exercise a considerable degree of caution, however. There are at least two main reasons why we should not be too ready to impose antitrust sanctions on intellectual property owners. First, in many cases it seems unlikely that owners of intellectual property rights will have the necessary economic power to attract antitrust sanctions. Secondly, competition policy has been largely developed on theories to fit situations quite different and possibly quite inapplicable to issues raised by intellectual property rights. This is not to say that competition policy or antitrust should not apply to intellectual property rights—TRIPS and national legislation such as sections 51(1), 51(3) of the Trade Practices Act 1974 (Cth) (TPA) make it clear that intellectual property rights are subject to competition policy. What I hope to do in the remainder of this article, however, is to examine some of the reasons why we should be cautious in the application of competition policy to intellectual property rights.

The Need for Market Power

The first problem which confronts the frustrated would-be parallel importer identified in the illustration in the Introduction is that ownership of an intellectual property right will generally not give rise to sufficient market power to attract the operation of competition policy.[25] If the owner of the intellectual property right does not have market power, there can be no breach of section 46 of the TPA and it is unlikely that sections 45 or 47 will apply in the absence of horizontal collusion.[26]

Section 46(1) provides:

> A corporation that has a substantial degree of power in a market must not take advantage of that power for the purpose of:
>
> (a) eliminating or substantially damaging a competitor of the corporation or of a body corporate that is related to the corporation in that or any other market;
> (b) preventing the entry of a person into that or any other market; or
> (c) deterring or preventing a person from engaging in competitive conduct in that or any other market.[27]

Since the introduction of sections 4E and 46(3) of the TPA, 'power in a market' clearly requires an assessment of market power in an economic sense.[28] To simplify the inquiry, this process is usually broken down into two stages: definition of the relevant economic market and then an assessment of the defendant's power in that market, although both are part of the same process.[29]

Defining a 'market'. The definition of the relevant market requires an examination of the possibilities of substitution both in terms of what alternative products are available to buyers and what alternative avenues of supply may be available. This basic principle has been elaborated in the Australian context in the *QCMA* case:

> We take the concept of a market to be basically a very simple idea. A market is the area of close competition between firms or, putting it a little differently, the field of rivalry between them. (If there is no close competition there is of course a monopolistic market.) Within the bounds of a market there is substitution—substitution between one product and another, and between one source of supply and another, in response to changing prices. So a market is the field of actual and potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run, if given a sufficient price incentive. Let us suppose that the price of one supplier goes up. Then on the demand side buyers may switch their patronage from this firm's product to another, or from this geographic source of supply to another. As well, on the supply side, sellers can adjust their production plans, substituting one product for another in their output mix, or substituting one geographic source of supply for another. Whether such substitution is feasible or likely depends ultimately on customer attitudes, technology, distance, and cost and price incentives.
>
> It is the possibilities of such substitution which set the limits upon a firm's ability to 'give less and charge more'. Accordingly, in determining the outer boundaries of the market we ask a quite simple but fundamental question: If the firm were to 'give less and charge more' would there be, to put the matter colloquially, much of a reaction? And if so, from whom? In the language of economics the question is this: From which products and which activities could we expect a relatively high demand or supply response to price change, i.e. a relatively high cross-elasticity of demand or cross-elasticity of supply?[30]

Applying this test, the courts have not dismissed outright the possibility that an intellectual property right might constitute an economic market:

> ...there will always be a question of fact whether the relevant market is confined to a single product or brand of products. The test is substitutability. There may be cases where a particular product, or brand of products, is so distinctive that no other product or brand is seen by consumers as a possible substitute. In such a case, the 'market' is constituted by the trade in that product or brand of products. Perhaps more frequently other products or brands present realistic alternatives; in which case they also will be within the relevant market.[31]

Since the clear statutory direction to adopt the economic test, however, the courts in Australia and New Zealand have consistently rejected attempts to define markets in terms of a single trade marked product or copyright work.[32]

Market power. The High Court has defined market power in the following terms:

> Market power can be defined as the ability of a firm to raise prices above the supply cost without rivals taking away customers in due time, supply cost being the minimum cost an efficient firm would incur in producing the product. ...[33]

Further, in forming a view about whether a firm has market power, the High Court has directed primary attention to the potential for competition and the existence of barriers to entry:

> A large market share may well be evidence of market power ... , but the ease with which competitors would be able to enter the market must also be considered. It is only when for some reason it is not rational or possible for new entrants to participate in the market that a firm can have market power. ... There must be barriers to entry.[34]

Mason CJ. and Wilson J. went on to identify a number of factors which *may* be barriers to entry, but Dawson J. noted that what constituted a 'barrier to entry' was a matter of considerable controversy within the economics profession.[35]

Unfortunately, none of these tests are terribly precise. The types of cost and pricing data which might reduce some of the tests to mathematical formulae are not likely to be available. Consequently, the courts have clearly recognised that they are dealing with questions of degree. The process can be very inexact.

On this basis, the *Broderbund* decision has been attacked on at least two grounds: first, setting the threshold for market power too high and, secondly, for not taking into account barriers to entry.[36]

The basis for the complaint that the threshold for market power was set too high appears to be Beaumont J.'s reference to remarks by Dawson J. in *Queensland Wire* that market power 'is thus the advantage which flows from monopoly or near monopoly.[37] There can be no doubt that the current wording of section 46(1) was introduced to extend the reach of the prohibition.[38] Beaumont J., however, found that Broderbund's market share in the two relevant markets was in the range of 10–17% in a context where his Honour accepted evidence that there were 'many' alternative games.[39] Therefore, in context, a ruling that Broderbund did in fact have a substantial degree of market power would seem very controversial; certainly its market share was considerably lower than that found in *Bursill* when Wilcox J. did find a substantial degree of power in a market.[40]

The criticism of *Broderbund* on barriers to entry was summarised thus:

> ...the exclusive distributorship between Broderbund Software Inc. and Dataflow creates an artificial barrier to entry. Other distributors who may have been prepared to supply the product at a lower price than Dataflow were restricted from entering the market. Similarly, the importation provisions were not discussed as a form of legal barrier to entry.

With respect, this is to confuse the product with the market. It makes the very mistake committed in the *Ira Berk* case and which section 4E of the TPA was introduced to preclude. In the original analysis from which the PSA drew its analysis, Dr Corones also raised the possibility that the importation provisions might have been used by a barricaded oligopoly to entrench market discipline or otherwise foreclose competition. This is a possible problem, but not one which arose on the reported evidence.

The other suggested barrier to entry was the role of product differentiation as there was a claim that 'Carmen SanDiego' was superior in quality. Even more than in the case of the barricaded oligopoly argument, one must be very slow to rely on product differentiation as a barrier to entry. In principle, one might think it a very strange outcome for a law designed to promote consumer welfare such as competition policy to impose disincentives to improve quality. One might have thought that giving better value for money was to be encouraged. Moreover, the existence of variety and choice is generally desirable. Not everyone can afford a Rolls Royce or Lamborghini, nor should people be forced to pay for four-wheel drives when all they need are city runabouts.

Thus, the economic evidence is far from condemnatory except perhaps in very severe cases.[41]

The Paradox of IP

As already noted, it is clear that competition policy is intended to apply to owners of intellectual property rights. What is (much) less clear is how competition policy should be applied to intellectual property rights. As discussed in the above section, the problem should not arise in many cases because the intellectual property owner will be unlikely to have market power in a properly defined, economic market. What do we do, however, when the owner does have market power? I shall try to explore this problem from two different directions: cases of refusal to deal and cases of charging 'unreasonably' high prices.

The *Magill* case in the European Union concerned what in many respects could be considered a fairly bizarre situation.[42] The various television networks provided their scheduling information—programme listings—to their respective subsidiaries which each published their own 'entertainment' magazines containing weekly listings. As in Australia, the daily listings for all networks were published in the daily papers. However, in the UK and Eire, it was not possible to buy a comprehensive weekly listing in advance. It was necessary to buy each of the network's own magazines. The networks refused to license the listings for a comprehensive publication, allowing only publication of highlights and licences to foreign language publishers on the continent where broadcaster reception was possible.

On a complaint by Magill which had been denied a licence to publish a comprehensive weekly listing, the European Commission, the Court of First Instance and, in a ruling with apparent similarities to *Queensland Wire*, the European Court of Justice (ECJ) condemned the practice.

The ECJ affirmed that a refusal to license an intellectual property right could not of itself amount to an abuse but, where the right owner was dominant, could do so in 'exceptional circumstances'.[43] As already discussed, there is nothing new in the ECJ's view that the holder of an intellectual property right is subject to the competition rules. The ECJ found the copyright owners had abused their market power because:

- there was no actual or potential substitute for a weekly television guide, a product for which there was a specific, constant and regular potential demand;
- there was no justification for refusing to license the material; and
- the copyright owners (broadcasters) were attempting to reserve to themselves a secondary market (weekly guides) by excluding all competition from that market.[44]

Having found abusive conduct, therefore, the ECJ upheld the Commission's order that the copyright owners must license the protected material at 'reasonable' rates.[45]

It has been suggested that the ruling was really an application of the traditional principal that a monopolist in one market cannot extend that monopoly into a secondary (or downstream) market.[46] At least in the case of a copyright owner, that type of theory could be quite dangerous. Every novelist (or short-story writer) who refuses to grant film or television rights (or purports to do so on an exclusive basis) seeks to reserve to him or herself a secondary market. Arguably, the novelist might make out a case that the economies of film production make exclusivity justifiable. But that is an uncertain sea to set sail on; worse, what would be the justification of the copyright owner who refused to license at all?[47]

These risks may highlight the significance of the ECJ's conclusion that there were no actual or potential substitutes. As I have argued above, a novelist (or short-story writer) is very unlikely to have market power in the relevant sense. If there were market power, however, perhaps the ECJ meant that liability arose not just because the copyright owners had market power. It was a special kind, possibly akin to a situation where there was a true single-product market.

In *Queensland Wire*, the High Court also appears to have condemned BHP for the absence of justification. Each of the judgments relied on the fact that Y-bar was the only product which BHP did not sell into the wholesale market and that it could do this only because it faced no competition.[48] That is, it would seem that the defendant would escape liability if it would not have acted differently in a competitive market.

This confronts us with the immediate difficulty that in a competitive market an intellectual property owner may well refuse to license the right, or may choose to license only one person or even several people but in different territories or fields of use.[49] Broadly speaking, an intellectual property right confers on the owner power to decide whether or not to put the product or process protected by the intellectual property right on the market and, if the owner does decide to do so, when the product is released, where the product is released and how (i.e. in what form and quality).[50] The basic premise of intellectual property rights is that the owner is in the best position to assess the best way to exploit the right and, if he or she gets it wrong, that is his or her bad luck.

The High Court's apparent adoption of a requirement of justification, therefore, might force us to reconsider the outcome in the *Bursill* case. There, the defendant Bursill was found to have taken advantage of the market power conferred by the Salomon brand because it refused sales of the current range to a discounter. On the evidence, Wilcox J. concluded it was clear one of the reasons for the refusal to supply the discounter was the desire to protect established retailers from the discounter's competition and, consequently, a breach of section 46(1)(c) of the TPA was made out.[51]

What is surprising about this result is the suggestion in the report that Bursill was condemned for engaging in exactly the same conduct which had enabled it to take the Salomon brand from an 'also ran' to the market leader, in the process drastically reducing the dominance of the previous market leader.[52] As Dr Corones has noted in his comment on the *Broderbund* case, at least some economists would consider Bursill's continued use of this strategy dangerous and deserving of sanction; but economists have not reached any consensus on this issue. It seems very hard to condemn someone for continuing his or her successful competitive strategy. Moreover, how will Bursill ever know when it has crossed the line?

The allegation that the owner of the intellectual property right is seeking to charge 'unreasonable' prices highlights the problem from a different perspective.

In *Magill*, the ECJ upheld the Commission's order that the copyright material be licensed at no more than 'reasonable rates'. This raises the question of how to determine what is reasonable. That, in turn, raises the question of adopting a standard to determine what is reasonable. The ECJ and the Commission were spared these difficulties in *Magill* as the UK Parliament had intervened and stipulated a compulsory licence of programming information, conferring jurisdiction on the Copyright Tribunal to arbitrate disputes.[53]

In a number of cases, this may not really cause a problem as the monopolist has helpfully licensed the subject matter (or sold the product) to someone else and a benchmark can be calculated.[54] (Even this may not be a solution, however, if contrary to my view the novelist is a monopolist: how many novels will support two films by competing movie houses?)

This approach at least has the appearance of ostensible fairness. It may not provide a perfect solution if the monopolist has been misusing market power against all customers. It clearly cannot work, however, where the right owner has not previously licensed the intellectual property. Even if the incumbent monopolist concedes it has a duty to supply (license), the issue is only postponed. It could set the price so high that for all practical purposes it has refused to deal or will still secure monopoly rents. Thus, the sanction of antitrust lurks.

The problem is compounded by the nature of intellectual property rights. The very purpose of the right is to enable the right owner to raise the price of products above marginal cost as the bulk of the investment lies in the research and development stage with the marginal costs of production being relatively small in comparison.[55] Computer programs provide a striking demonstration of the problem. In its *Final Report on Computer Software*, for example, the PSA reported that the investment in developing a sophisticated wordprocessing program could involve 137 employee years. Once made, however, it could be copied for the cost of some disks and the electricity consumed in the short minutes of the copying process; even more cheaply where the program is stored 'on-line'. In a perfectly competitive market in the absence of intellectual property rights, the price of the product would be reduced to those costs of copying plus some small (usually described as 'reasonable') allowance for the cost of funds utilised. Accordingly, intellectual property laws such as copyright aim to confer on the copyright owner the power to raise unit price above marginal cost to provide an incentive to make the risky upfront research and development investments.

The lack of certainty and absence of any objective criteria by which to judge (or advise) the intellectual property owner which has achieved a sufficient degree of market power is dramatically illustrated in the Federal Court litigation over the supply of stock exchange information. After several years of supplying information, the stock exchange's marketing vehicle sought to raise the price substantially to a competing wholesaler. The marketing vehicle was found to have breached section 46 of the TPA. At first instance, the trial judge imposed a licence fee for data transmitted electronically from the stock exchange at $100 per annum—the marginal cost of supply plus a 'reasonable profit'. On appeal, the fee was upgraded to $1.45 million per annum.[56]

In arriving at an annual licence fee of $100, the trial judge in *Pont Data* had concluded:

> Once it is accepted that ASXO is not entitled to misuse its monopoly position, it ought not to be regarded as unfair to compel ASXO to supply signal C *at a price which reflects the cost of supplying that signal together with a margin of profit similar to that charged by competitive suppliers in the data industry*. I accept that such a price is likely to be low, compared with the fees charged in the subject contracts. But that is because the cost of supply is low. In a competitive situation that low cost would be reflected in a low price.[57]

The Full Court described this as 'a drastic interference'. It considered his Honour's reasoning to be in error because the requirement of a price 'which reflected the cost together with a low margin of profit' (i.e. the equilibrium price in a perfectly competitive market) was not dictated by the finding of anti-competitive market power.[58] The Full Court then substituted its own formulation of 'terms designed to attain broad and substantial justice between the parties'. Closer examination of the issue was avoided by reinstating the prices which had applied before the stock exchange sought to raise the price to a level which Pont Data objected to. This latter finding unfortunately does not advance matters much. If Pont Data had objected when the price was originally 'imposed' rather than when ASXO sought to revise the arrangements, what standard would have been applied?

Does it Matter?

It might be argued that these concerns are not really of great significance. The problems (if problems they be) arise only in very special situations like *Magill* where it is 'obvious' to 'everyone' what should happen. I suggest that this is to dismiss the dangers too readily.

First, indeterminacy can have devastating consequences at the practical level. The monopolist may never know in advance whether its demands are reasonable or will expose it to condemnation. The legal costs, let alone the potential damages, for getting it wrong could well be prohibitive. In addition, as illustrated by the *Pont Data* case, the price payable (licence fee) will vary widely.

Secondly, there is no 'bright line' between the 'special' cases and the 'others'. Opinions will invariably differ about what are the 'special' cases. Moreover, rules which might seem justifiable when applied to very special cases can be extended quite easily. As already noted, there is much scope for interpretation and matters of degree in applying section 46 of the TPA. The Prices Surveillance Authority has lent its considerable institutional authority to the view that copyright creates what appears to be a remarkable number of 'single product markets'.

Thirdly, there is the potential impact of uncertainty and interference on incentives. When considering the price of access to 'essential facilities', the Hilmer Inquiry expressly recognised the lack of any objective criteria and the consequent uncertainty and unpredictability:

> Neither the application of economic theory or general options of fairness provide a clear answer as to the appropriate access fee in all circumstances. Policy judgments are involved as to where to strike the balance between the owner's interest in receiving a high price, including monopoly rents that might otherwise be obtainable, and the user's interest in paying a low price, perhaps limited to the marginal costs associated with providing access. Appropriate access prices may depend on factors such as the extent the facility's existing capacity is being used, firmly planned future utilisation and the extent to which the capital costs of producing the facility have already been recovered. Decisions in these areas also need to take account of the impact of prices on the incentives to produce and maintain facilities and the important signalling effect of higher returns in encouraging technical innovation. For example, relatively low access prices might contribute to an efficient allocation of resources in the short term, but in the longer term the reduced profit incentives might prevent technical innovation.[59]

Those observations are equally applicable in the context of intellectual property; the warnings about the impact on incentives particularly so given the rationale for intellectual property regimes.

The Hilmer Inquiry's reference to incentives is important for another reason. Surprisingly, regulators and to some extent the courts when determining prices in these situations have usually opted for a concept of 'fairness'.[60] This suggests that, of the economic justifications for intellectual property systems, the decision makers are opting for the 'reward' theory instead of the 'incentive' theory generally supported by economists.[61] Such an approach could well reduce the incentives which intellectual property seeks to create. It also seems at odds with the High Court's emphasis on competition policy as concerned with the competitive process, not protection of competitors.[62]

Notes and References

1. Obviously, the situation is taken from *Broderbund Software Inc. v. Computermate Products (Australia) Pty Ltd* (1991) 22 IPR 215.
2. See e.g. S. Ricketson, *The Berne Convention for the Protection of Literary and Artistic Works: 1886–1986*, Queen Mary College/Kluwer, London, 1987, pp. 17–21.
3. The most obvious examples are the recognition of rights limited to equitable remuneration and the concern to ensure that the introduction of new rights like the right of public performance and broadcast did not disrupt national licensing systems. It is perhaps not often recalled that section 6 of the Statute of Monopolies 1623 (Eng 21 Jac I c3) stipulated the following express limitation on patents for inventions: 'so as also they be not contrary to the Law, nor mischievous to the State, by raising Prices of Commodities at home or Hurt of Trade, or generally inconvenient ...'.
4. See e.g. the UK Court of Appeal's defence of an exclusive licence of a patent in the face of a US court's antitrust decree: *US v. Imperial Chemical Industries Ltd* 100 F Supp 504 (SDNY 1951), *British Nylon Spinners Ltd v. Imperial Chemical Industries Ltd* [1953] 1 Ch 19 (CA) and the US sequel at 105 F Supp 215 (SDNY 1952).
5. World Trade Organisation Agreement, Article II.2.
6. TRIPS Article 65.1.
7. TRIPS Article 64.
8. Note also footnote 13 to Article 51.
9. The lack of consensus and the depth of division has recently been confirmed in the negotiations for the adoption of the WIPO Copyright Treaty and the WIPO Performers and Phonograms Treaty which, after strong debate, once again did not address the issue.
10. Note the express exclusion of the protection of moral rights from the obligation to comply with the Berne Convention imposed by Article 9 of TRIPS.
11. For example, TRIPS Article 14.4 allowing the continuation of a system of equitable remuneration for the rental of phonograms in some situations; TRIPS Article 31 recognising government and other third-party use of patents without authorisation.
12. For example, TRIPS Article 9.1 requires Members to comply with Articles 1–21 of the Berne Convention (apart from Article 6*bis*) some of which articles allow for rights of remuneration or other unauthorised use: e.g. Berne Convention Article 11*bis*(2), 13(1).
13. For example, see TRIPS Article 13 (copyright), 26 (industrial designs) and 30 (patents) where a fourth element is added: the need to take into account the legitimate interests of third parties and a similar formulation in 17 (trademarks).
14. Contrast the list of 14 practices which could be deemed to be abusive or anti-competitive contained in an earlier draft: see article 42.2 of the Chairman's draft attached to the text of the document 'Status of work in the Negotiating Group', 25 October 1990. The list was (i) grant-back provisions; (ii) challenges to validity; (iii) exclusive dealing; (iv) restrictions on research; (v) restrictions on use of personnel; (vi) price fixing; (vii) restrictions on adaptations; (viii) exclusive sales or representation agreements; (ix) tying arrangements; (x) export restrictions; (xi) patent pooling or cross-licensing agreements and other arrangements; (xii) restrictions on publicity; (xiii) payments and other obligations after expiration of industrial property rights; (xiv) restrictions after expiration of arrangement.
15. Arguably, these provisions include Part III relating to enforcement which sets out a range of requirements largely designed to ensure that fair and equitable decisions on the merits are the means for resolving disputes about infringements of intellectual property rights.
16. See Article 42.2 of the Chairman's draft attached to the text of the document 'Status of work in the Negotiating Group', 25 October 1990.
17. Argentina, Brazil, Chile, China, Colombia, Cuba, Egypt, India, Nigeria, Pakistan, Peru, Tanzania, Uruguay and Zimbabwe.
18. Document MTN.GNG/NG11/w/71, 14 May 1990.

19. See e.g. Brazilian law 5772, Article 90 at issue in *Colgate-Palmolive Limited v. Markwell Finance Limited* [1989] RPC 497 (UK CA).
20. WTO, Singapore Ministerial declaration, para. 20, WT MIN(96)/DEC/W, 13 December 1996 reproduced at <http://www.wto.org/govt/mindec.htm> . I am grateful to Alana Harris, an articled clerk at Mallesons Stephen Jaques, for collating research materials on this section.
21. *Ibid.*
22. Joel I. Klein, 'A note of caution with respect to a WTO agenda on competition policy,' 18 November 1996 reproduced at <http://www.usdoj.gov/atr/speeches/jikspch.htm>
23. These comments draw on Working Group on the Interaction between Trade and Competition Policy, Report (1997) to the General Council, WT/WGTCP/1, 97-5284, 28 November 1997 <http://www.wto.org/ddf/cgi-bin/dispdoc.pl?url=/ddf/cgi-bin vdkw_cgi@8001/xac/91cad-340/Search/5370802/12117>; WTO, Programme at Meetings in 1998, <http://www.wto.org/about/yearmt.htm>. Apparently, vol. I of the WTO's Third Annual Report contains a review of policy issues: 'WTO Secretariat Releases 1997 Annual Report', Press/85, 8 December 1997 <http://www.wto.org/wto/new/press85.htm>
24. A more detailed discussion of aspects of this section is Warwick A. Rothnie, 'Computer software and parallel imports', in Alexiadis (ed.), Sweet & Maxwell, London, forthcoming.
25. A point acknowledged in the then Trade Practices Commission's own background paper, *Application of the Trade Practices Act to Intellectual Property*, July 1991, para. 4.7 ('*Background Paper*').
26. See e.g. *Outboard Marine Australia Pty Ltd v. Hecar Investments No. 6 Pty Ltd* (1982) 66 FLR 120; 44 ALR 667 at 66 FLR 143 per Fitzgerald J. and the *Broderbund* case 22 IPR 215, 244.
27. Corresponding, albeit differently worded provisions, can be found overseas: see e.g. Article 86 of the EEC Treaty and section 2 of the Sherman Act (USA).
28. *Queensland Wire Industries Pty Ltd v. Broken Hill Proprietary Co Ltd* (1989) 167 CLR 177 ('*Queensland Wire*'). See generally, Maureen Brunt, 'Market Definition' issues in Australian and New Zealand Trade Practices Litigation', (1990) 18 ABLRev 86.
29. *Queensland Wire* 167 CLR at 187 per Mason CJ. and Wilson J.
30. *Re Queensland Co-operative Milling Association Ltd* (1976) 25 FLR 169, 190 endorsed by the High Court in *Queensland Wire Industries Pty Ltd v. BHP* (1988) 167 CLR 177. See generally, F. M. Scherer & D. Ross, *Industrial Market Structure and Economic Performance*, 3rd edn, Houghton Mifflin, Boston, 1990, pp. 74–76, 454–458.
31. *Mark Lyons Pty Ltd v. Bursill Sportsgear Pty Ltd* (1987) 75 ALR 581, 589–590; See also *Tru Tone Ltd v. Festival Records Retail marketing Ltd [1988] 2 NZLR 352, 361 (NZ CA).*
32. *Ah Toy Pty Ltd v. Thiess Toyota Pty Ltd* (1980) 30 ALR 271 rejecting the 'market' for Toyota brand vehicles in favour of the motor vehicle market in the Northern Territory; *Carson Machinery Nominees Pty Ltd v. Chamberlain John Deere Pty Ltd* (1989) ATPR 40-934; *Mark Lyons Pty Ltd v. Bursill Sportsgear Pty Ltd* (1987) 75 ALR 581 rejecting an alleged market for Salomon brand ski boots in favour of the Australian ski boot market; *Broderbund* 22 IPR 215 rejecting the alleged market for a particular computer game or range of games in favour of national markets for computer software having, respectively, an educational character or an entertainment character; *Tru Tone Ltd v. Festival Records Retail Marketing Ltd* [1988] 2 NZLR 352 rejecting an alleged market for single albums as ignoring commercial realities (see also Brunt, 18 ABLRev at 97–98).
33. *Queensland Wire* 167 CLR at 188 per Mason CJ. and Wilson J. and to similar effect at 200–201 per Dawson J.
34. *Idem.* at 189 per Mason CJ. and Wilson J., see also 201 per Dawson J. (citations omitted).
35. *Idem.* 190 per Mason CJ. and Wilson J. identifying as potential barriers: legal barriers such as patent rights and exclusive government licences and tariffs; economies of scale where the minimum efficient size for a firm is large in relation to the size of the market; and vertical integration and 201–202 per Dawson J. The reference to patents is at odds with the more modern recognition that single brand or product markets are unlikely. The then TPC's background paper recognised that matters were not nearly so cut and dried: *Background Paper*, para. 4.11. The more modern approach would seem to gain some support from the rather patchy economic evidence about the effects of the patent system: see W. A. Rothnie, *Parallel Imports* (Sweet & Maxwell, London, 1993), pp. 109–112. On barriers to entry generally, see Valentine Korah, *EC Competition Law and Practice.* 5th edn, Sweet &

Maxwell, London, 1994, pp. 10–12; V. Korah & W. A. Rothnie, *Exclusive Distribution and the EEC Competition Rules*, 2nd edn, Sweet & Maxwell, London, 1992, pp. 8–15.

36. Prices Surveillance Authority, *Inquiry into Prices of Computer Software: Final Report*, PSA, December 1992, Report No. 46 at 36 and 71 citing Stephen Corones, 'Parallel importing computer software: consumer welfare considerations', (1992) 3 AIPJ 188, 192–193.
37. 22 IPR at 240 per Beaumont J. citing Dawson J. at 167 CLR 200.
38. Prior to 1 June 1986, section 46 applied to corporations in a position 'substantially to control a market...' Note that the explanatory memorandum for the Trade Practices Revision Bill 1986 referred to the meaning of 'substantial' in the context of section 46 as being 'intended to signify "large or weighty" or "considerable, solid or big" ': *Dowling v. Dalgety Australia Ltd* (1992) 34 FCR 109.
39. 22 IPR at 241 for market share and 238, 240–241 for the number of products competing in the market with at least one of the witnesses accepted by his Honour claiming there were 100 software programs available in Australia which were educational games, at least 35 of which were used to develop some of the skills claimed for 'Carmen SanDiego' and at least a dozen directed to geographical knowledge.
40. Wilcox J. found that the Salomon brand had at least one-third of the relevant market, was the market leader and at least 90% of retailers found it necessary to stock the brand: *Mark Lyons Pty Ltd v. Bursill Sportsgear Pty Ltd* (1987) 75 ALR 581, 592. Note also the European Commission's tentative proposal that market shares under 20% should not give rise to competition concerns except in exceptional cases: European Commission, *Green Paper on Vertical Restraints in EC Competition Policy*, COM (96) 721, (Brussels, 1996); xiii; <http://europa.eu.int en/comm/dg04/entente/en 96721en.htm>
41. F. M. Scherer & D. Ross, *Industrial Market Structure and Economic Performance*, 3rd edn, Houghton Mifflin, Boston, 1990, esp. Ch. 16. *Bursill* illustrates the weakness of this kind of 'market power': in less than 5 years the Salomon brand had overtaken the clear market leader, Nordican; see text at Note 52 below.
42. Cases C-241/91 and C-242/91 *Radio Telefis Eireann and Independent Television Publications Limited v Commission* [1995] FSR 530.
43. [1995] FSR 530 at paras 49–50.
44. *Idem.*, paras 52–54. Although the terminology is not identical, each of those factors contributed to condemnation in the *Queensland Wire case.* See also *Pont Data Australia Pty Ltd v. AXS Operations Pty Ltd* (1990) 27 FCR 460; 97 ALR 513; 19 IPR 323 and (No. 2) at (1991) 27 FCR 492; 100 ALR 125; ACCC Media Release 'Telephone directory data now available to all', 19 February 1997; ACCC Media Release 'Weather court case settled', 22 May 1997.
45. *Magill* [1995] FSR 530 at para. 12.
46. Rhodri Thompson, 'Magill' [1996] Ent LR 143 at 145. For the criticism of the leveraging theory the traditional analysis is based on see e.g. Richard A Posner, *Antitrust Law: An Economic Perspective*, University of Chicago Press, Chicago, IL, 1975, pp. 196–207, 171–184.
47. The Australian Competition and Consumer Commission, seemingly without any reference to market power, has recently asserted that a producer of video games restricted competition 'in the downstream markets' by refusing to license them 'on reasonable terms': Australian Submission No. 1 to OECD Competition Law and Policy Committee Round Table on Intellectual Property Rights, 7.
48. *Queensland Wire* 167 CLR at 192–193 per Mason CJ. and Wilson J., 195 per Deane J., 202 per Dawson J., 216 per Toohey J. See also Sandra J. Welsman, 'In Queensland Wire, the High Court has provided an elegant backstop to 'use' of market power' (1995) 2 *Competition and Consumer Law Journal* 280, 284, 290–291 and 305. Noticeably, however, the High Court did not treat Y-bar as a 'single product market'.
49. Although not expressed in this way, this consideration seems to underlie the general exoneration of these types of practices in the TPC's *Background Paper*, Ch. 5.
50. A trademark owner who does not use the trademark, however, runs the risk that the registration will be removed for non-use or that the reputation it signifies will dissipate.
51. 75 ALR 581, 595. Contrast the opposite result in *Monsanto Co v. Spray-Rite Service Corp.* (1984) 465 US 752.

52. *Idem.*, 582–583 and at 594–595 attributing the success of the Salomon brand partly to Bursill's aggressive marketing and partly to product innovation.
53. *Broadcasting Act* 1990, schedule 17. For the determination of fees, see *News Group Newspapers Ltd v. Independent Television Publications Limited* [1993] RPC 173. For a limited form of legislative intervention in the context of telephone directories, see *Telecommunications Act* 1997 (Cth), Section 472 and Telstra's licence conditions.
54. For example, in the context of copyright, see *Feist* 737 F Supp at 624.
55. For this reason, intellectual property rights have attracted the strictures of some economists. For an eloquent exposition which indirectly provided the source of the PSA's inspiration, see Arnold Plant, 'Economic aspects of copyright in books' (1934) 1 *Economica* 167 and 'Economic theory concerning patents for inventions' (1934) 1 *Economica* both reprinted in Arnold Plant, *Selected Essays and Addresses*, Routledge & Kegan Paul, London, 1974.
56. *Pont Data v. ASX Operations Pty Ltd* (1990) ATPR 41-007 and 41-038 (trial) and (1991) 19 IPR 323, 97 ALR 513 and 100 ALR 125, ATPR 41-069 and 41-109 (Full Court) cited in Warren Penguilley, 'The Privy Council speaks on essential facilities in New Zealand' (1995) 3 *Competition and Consumer Law Journal* 27, pp. 48–49.
57. 21 FCR 385 at 427–428; 93 ALR 523 at 564 cited by the Full Court in 19 IPR 323 at 347 and 100 ALR 125 at 133 (my emphasis).
58. 100 ALR 125 at 135. This approach would appear to be consistent with that taken by the Privy Council in *Telecom Corporation of New Zealand v. Clear Communications Ltd* (1996) 33 IPR 573 at 596.
59. Report by the Independent Committee of Inquiry, *National Competition Policy*, AGPS, Canberra, 1993, p. 253. Machlup put it pithily in the context of patents: 'it is difficult to conceive of economic criteria by which one could judge whether output is less than "reasonably practicable" and price is "unreasonably high"!' *An Economic Review of the Patent System*, Study No. 15 of the US Senate Judiciary Committee, Sub-committee on Patents, Copyrights and Trademarks, US Government Printing Office, Washington, 1958, p. 12.
60. See e.g. ACCC Media Release, *op. cit.*, Ref. 44; *Pont Data* at notes 57–58, above. On the theory that the patent system, however, provides a much needed spur for technological investment, see *US v. Studiengesellschaft Kohle mbh* 670 F 2nd 1122 (DC Cir 1981).
61. See F. Machlup, above at Note 59, pp. 25-43; W. M. Landes & R. A. Posner, 'An economic analysis of copyright law' (1989) 18 JLS 325. The importance of incentives are captured most graphically by the proponents of the 'casino of technology': W. Brian Arthur, 'Increasing returns and the new world of business', *Harvard Business Review*, July–August 1996, 101 at 105.
62. See the discussion of *Queensland Wire* in Welsman, above at Note 48, pp. 293–294.