

**THE SCOPE OF PERMISSIBLE CONTROL  
IN THE INFORMATION AGE**

**THE AUSTRALIAN VISUAL SOFTWARE DISTRIBUTORS  
ASSOCIATION ("AVSDA") SUBMISSION TO THE REVIEW OF THE  
COMPETITION PROVISIONS OF THE TRADE PRACTICES ACT 1974**

## Executive Summary

There has been a discernible trend in recent judicial decisions to find the existence of market power under section 46 of the *Trade Practices Act* in a wider range of circumstances, to the point where there is a danger that normal competitive conduct in a rivalrous market will be impinged by the chilling effect of an over-inclusive interpretation of section 46.

This has the potential, if not corrected, in the case of intellectual property protection, of depriving the community of the benefits over the medium and longer term of an effective intellectual property protection regime which, for fear of a trade practices enforcement action, becomes neutered except in the most narrow of circumstances.

This trend, and investigations by the ACCC, have created uncertainty amongst intellectual property rights holders in Australia as to the circumstances in which the *Trade Practices Act* applies to their commercial activities and exercise of their intellectual property rights. For example, a recent case has found that an intellectual property rights holder may be considered to have a substantial degree of market power on the basis of a "temporary monopoly" over copyright works. This uncertainty detrimentally affects commercial activity by rights holders and, ultimately, the extent to which Australian consumers benefit from the creativity and innovation of rights holders in Australia.

This uncertainty and imbalance between intellectual property rights and the *Trade Practices Act* needs to be addressed by a clarification by way of legislative amendment or administrative guidelines (or both).

It could be addressed by legislation, in particular, by providing an exemption from the application of section 46 to conduct by an intellectual property rights holder in the exercise of intellectual property rights.

At a minimum, the imbalance needs to be addressed by the creation and implementation of long-awaited guidelines which:

- specify when Part IV of the *Trade Practice Act* applies to conduct of intellectual property rights holders,
- in the context of section 46, establish that:
  - a holder of intellectual property rights does not necessarily have a substantial degree of market power by virtue of those rights; and
  - a holder of intellectual property rights does not contravene section 46 of the TPA by

exercising those rights;

- identify conduct which will not be considered under the *Trade Practices Act*; and
- govern the role of the ACCC in investigating conduct to which the *Trade Practices Act* applies, including setting time limits and requiring transparency in the conduct of the investigation and notification to participants of the result of the investigation.

Such guidelines should be developed in conjunction with industry participants. Guidelines which address the intersection of intellectual property law and competition law exist in the US, Canada and the UK. The existence of such guidelines within the regulatory regime of Australia's major trading partners demonstrates the need for such guidelines in Australia. The contents of those guidelines are a good starting point for Australian guidelines.

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## 1. AVSDA

The Australia Visual Software Distributors Association ("AVSDA") was formed in 1983 to represent the interests of owners of copyright in, and distributors of, videos in Australia. Members of AVSDA currently manufacture and distribute copyright videos and DVDs.

Members of AVSDA include the Australian arms of international companies such as Warner, Buena Vista, Twentieth Century Fox, Columbia and Universal, as well as other wholly owned Australian companies, both large and small, such as Roadshow Entertainment, 21st Century Pictures and Rainbow Video. These Australian companies and many small Australian companies which are not members of AVSDA purchase the rights to distribute intellectual property materials within Australia.

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## 2. Terms of reference for current review

This terms of reference for the current review charge the Committee with considering whether Parts IV and VII of the *Trade Practices Act 1974 (Cth)* ("***Trade Practices Act***")

- (a) inappropriately impede the ability of Australian industry to compete locally and internationally;
- (b) promote competitive trading which benefits consumers in terms of service and price;
- (c) provide adequate protection for the commercial affairs and reputation of individuals and corporations;
- (d) allow businesses to readily exercise their rights and obligations under the *Trade Practices Act*, consistent with certainty, transparency and accountability, and use compliance or authorisation processes applicable to their circumstances.

AVSDA considers that these terms of reference directly relate to the manner in which intellectual property rights are affected by competition law for the following reasons:

- (a) the strength of a local intellectual property rights regime affects the extent to which intellectual property is developed in that area, either by local firms or by offshore investment and licensing;

- (b) as recognised by the September 2000 Review of Intellectual Property Legislation under the Competition Principles Agreement Final Report (the "*Ergas Report*") and the US Anti-Trust Guidelines for the Licensing of Intellectual Property (the "*US Anti-Trust Guidelines*"), the licensing of intellectual property is often international.<sup>1</sup> Certainty as to conduct by an intellectual property rights holder which the ACCC and courts considers to contravene the *Trade Practices Act* is vital for such international licensing and investment in creation and innovation in Australia;
- (c) fundamentally, intellectual property rights afford certain legislative protections on the owners of those rights to encourage innovation and, ultimately, consumer benefit. It is essential to ensure that those protections are not eroded by an inappropriate application of Part IV of the *Trade Practices Act* to the exercise of those rights by the intellectual property right holder;
- (d) intellectual property rights holders need to be in a position where:
- (i) the extent of their rights and obligations under the *Trade Practices Act*; and
  - (ii) the manner in which the *Trade Practices Act* will be applied and enforced,

insofar as it relates to the exercise of intellectual property rights is clear and certain.

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### **3. Previous reviews of intersection between intellectual property and competition laws**

#### **3.1 Hilmer Report**

The tension between intellectual property rights and competition law has been the subject of previous reviews dating back to the Hilmer Report<sup>2</sup>, which raised the issue of the intersection of intellectual property rights and competition law in 1993. The Hilmer report appeared to recognise that at that time there was a lack of clarity in the manner in which the *Trade Practices Act* applied to the exercise of intellectual property rights. It recommended that the law be reviewed and assessment made as to whether the current treatment of the intersection of

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<sup>1</sup> US Anti-Trust Guidelines, section 2.1

<sup>2</sup> National Competition Policy Report by the Independent Committee of Enquiry published in Australia 1993

IP and competition rights in the *Trade Practices Act* is appropriate and if so, if it is sufficiently clear and consistent in relation to intellectual property rights it affects or may affect.<sup>3</sup>

### 3.2 National Competition Council

In March 1999 the National Competition Council conducted a review of the *Trade Practices Act*. The National Competition Council recommended that s51(3) be amended to remove protection from price and quantity restrictions and for horizontal agreements. It also recommended that the ACCC formulate guidelines on:

- when intellectual property licensing and assignment conditions might be exempted under from Part IV;
- when intellectual property licences and assignments might breach Part IV of the *Trade Practices Act*; and
- when conduct in relation to intellectual property that does not fall within the exceptions and is likely to breach Part IV of the *Trade Practices Act* might be authorised.

### 3.3 Ergas Report September 2000

The Ergas Report again considered the effect Australia's intellectual property laws have on competition.<sup>4</sup>

The Committee recognised the need for special exemptions from general competition law for intellectual property rights and assets, given the different nature of intellectual property rights and other rights. The Committee formed the view that exceptions currently provided for in the *Trade Practices Act* are flawed and the breadth of exemptions is unclear (and possibly too broad). It considered that the exceptions did not strike the appropriate balance between intellectual property rights and competition law.<sup>5</sup>

The Committee recommended that the *Trade Practices Act* be amended to provide that conditions in a contract, arrangement or understanding related to the subject matter of intellectual property law do not contravene Part IV or section 4D of the *Trade Practices Act* unless the conditions result in a substantial lessening of competition.

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<sup>3</sup> Hilmer Report, pages 151 and 160.

<sup>4</sup> Intellectual property laws considered consisted of: the *Copyright Act* 1968; *Patents Act* 1990; *Trade Marks Act* 1995; *Designs Act* 1906; and *Circuit Layouts Act* 1989.

<sup>5</sup> Ergas Report, page 11.

In particular, it recommended amendments to the Act be to ensure that a contravention of Part IV shall not be taken to have been committed by reason of the imposing of conditions in a licence, or the inclusion of conditions in a contract, arrangement or understanding, that relate to the subject matter of an intellectual property statute so long as those conditions do not result or are not likely to result in a substantial lessening of competition (to be interpreted in a manner consistent with the case law under the *Trade Practices Act* more generally).<sup>6</sup>

It also repeated the National Competition Council's recommendation that the Australian Competition and Consumer Commission issue guidelines that clarify the types of behaviour that are likely to contravene the *Trade Practices Act* and set out how it will implement relevant enforcement activities.<sup>7</sup>

### **3.4 Current issues**

The need for reform of the current intersection of intellectual property law and competition law identified in the Hilmer Report has not yet been satisfactorily addressed and has been brought into sharp focus by recent Federal and High Court decisions in relation to the existence of market power within the meaning of section 46.

There are a number of outstanding issues raised by previous inquiries which have not yet been determined:

- (a) the precise amendments necessary to be made to the provisions of Part IV of the Act to effect the Ergas recommendations; and
- (b) the formulation and issuing of guidelines by the ACCC has not occurred to date.

AVSDA notes that the terms of reference for the current review preclude the Committee from a direct consideration of amendments to section 51(3). However, those outstanding issues clearly fall within the terms of reference for the current review of Part IV in the context of the information economy.

This submission to the Review focuses on these outstanding issues, in the context of recent judicial and administrative applications of the *Trade Practices Act* to conduct of intellectual property rights holders in a manner which is inconsistent with the objects of the intellectual property regime and competition law and considers the consequences of current proposals to amend the *Trade Practices Act*, including section 46.

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<sup>6</sup> Ergas Report, page 215.

<sup>7</sup> Ergas Report, page 19.

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## 4. Intellectual Property Rights and Competition Law

### 4.1 Purpose of intellectual property laws

As acknowledged by the US Anti-Trust Guidelines, intellectual property laws and anti-trust laws:

*"share the common purpose of promoting innovation and enhancing consumer welfare. The intellectual property laws provide incentives for innovation and its dissemination and commercialisation by establishing enforceable property rights for the creators of new and useful products, more efficient processes and original works of expression. In the absence of intellectual property rights, imitators could more rapidly exploit the efforts of innovators and investors without compensation. Rapid imitation would reduce the commercial value of innovation and erode incentives to invest, ultimately to the detriment of consumers. The anti-trust laws promote innovation and consumer welfare by prohibiting certain actions that may harm competition with respect to either existing or new ways of serving consumers".*

Intellectual property rights are awarded to people with creative ideas for reasons including to reward innovation and to encourage further innovation and creative effort. Consumers benefit from intellectual property rights and laws which permit their enforcement in the following ways, by:

- having access to cheaper products;
- being more efficient users of resources and therefore being able to use unspent resources for other purposes;
- having access to new resources; and
- benefiting from higher standards of living.

These benefits are achieved by intellectual property laws through the grant to the owners of intellectual property certain rights to exclude others.<sup>8</sup>

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<sup>8</sup> US Anti-Trust Guidelines, section 2.1

## 4.2 Purpose of competition laws

The purpose of competition law is to promote competition, that is, to protect the competitive process, and not individual competitors. Competition is regarded as desirable because it has advantages including:

- the promotion of economic growth;
- facilitating efficient resource utilisation; and
- the promotion of higher standards of living.

## 4.3 Conflict between intellectual property laws and competition law

There has been considerable material written on both the similarities and differences between intellectual property law and competition law.

The two regimes are complementary in that they both result in benefits to consumers.

However, there are instances in which intellectual property and competition law conflict. It is this point of conflict, and how such conflict is treated in Part IV of the *Trade Practices Act*, that AVSDA contends requires clarification. While the grant of intellectual property rights may result in a restriction in a market, it is well recognised that there must be a balance struck between intellectual property and competition laws such that the universally accepted benefits of intellectual property rights are obtained.

## 4.4 Example of conflict - section 46

AVSDA is particularly concerned about the ramifications of the current interpretation and enforcement of section 46 of the *Trade Practices Act* for copyright owners in particular and intellectual property rights holders generally, and its impact on innovations and investment both by offshore rights holders in Australia and by Australian innovators seeking to enforce protection of their innovations. As a result of recent Federal Court decisions and investigations by the ACCC, copyright holders are uncertain about the extent to which section 46 applies to the enforcement of their rights and their commercial activities generally, including negotiations with retailers and action against pirates and parallel importers, where such action is permitted under the *Copyright Act*. This uncertainty affects competitive trading by rights holders which, ultimately, detrimentally affects consumers.

AVSDA understands the objectives of section 46 of the *Trade Practices Act* and is supportive of misuses of market power being prohibited by the *Trade Practices Act*. However, AVSDA

considers that an inappropriate balance has been struck in the current application of the section by the Australian Competition and Consumer Commission or by courts in recent matters such as *Australian Competition and Consumer Commission v Universal Music Australia Pty Limited* [2001] FCA 1800. AVSDA also considers that it is imperative that there be greater certainty as to the circumstances in which section 46 will apply to copyright holders, to enable copyright holders to engage in legitimate commercial activities without the risk of investigation or enforcement action. AVSDA considers this imbalance must be addressed to ensure that Australian consumers continue to benefit from the creativity and innovation by rights holders in Australia.

#### **4.5 Section 51(3)**

It was acknowledged by the Ergas Committee that:

*"In 1974 when, the Trade Practices Act was amended, intellectual property laws were widely believed to confer on the owners of intellectual property a limited economic monopoly. This led to a concern that the unrestrained application of competition law to intellectual property could undermine intellectual property rights."<sup>9</sup>*

Section 51(3) is intended to address this intersection of intellectual property rights and competition law. However, the extent to which conduct is exempt from the application of Part IV of the *Trade Practices Act* under section 51(3) in its current form is not clear. There is an absence of any guidance from the Courts as to how this section is intended to operate. For example, in *Transfield Pty Ltd v Arlo International Limited* (1980) 144 CLR 83, Mason J stated:

*"In bridging the different policies of the Patents Act and the Trade Practices Act, s. 51(3) recognises that a patentee is justly entitled to impose conditions on the granting of a licence or assignment of a patent in order to protect the patentee's legal monopoly. Even under American anti-trust law, where there is no equivalent exception to s. 51(3), the patentee is entitled to exercise some measure of control over the licensee consistent with the scope of the patent monopoly, though there has been some controversy as to the scope of permissible control."<sup>10</sup>*

AVSDA considers that an exemption for intellectual property rights holders insofar as they engage in conduct which is permitted under an intellectual property statute is crucial. That

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<sup>9</sup> Ergas Report, p.206.

<sup>10</sup> Page 12.

exemption could operate in the manner of s51(3). Alternatively, specific exemptions could be made for each section of Part IV which potentially conflicts with an exercise of statutory intellectual property rights by the rights holder.

AVSDA considers that a general exemption mechanism is preferable to specific amendments to each provision of Part IV. However, if the Review contemplates specific exemptions to the application of Part IV for the exercise of intellectual property rights from contravention of those provisions, AVSDA contends that exemptions should be implemented from the application of Part IV, including the per se contraventions and section 46.

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## **5. Enforcement of copyright v breach of *the Trade Practices Act*?**

The Hilmer Report noted that it had received few concrete examples illustrating the need for different treatment under the *Trade Practices Act* for the holders of intellectual property rights. AVSDA below sets out two recent examples which demonstrate the unsatisfactory approach taken by the ACCC and the Courts to the application of the *Trade Practices Act* to the exercise of intellectual property rights, in both cases, the exercise of rights under the *Copyright Act* because of the lack of specific guidance from Parliament in the *Trade Practices Act* as to how the intersection of the intellectual property laws and the *Trade Practices Act* is to be treated.

AVSDA is also concerned about the uncertainty created by informal investigations by the ACCC in relation to conduct by copyright holders in Australia. AVSDA notes that the ACCC has, in conjunction with regulatory authorities overseas, undertaken informal investigations of conduct by copyright holders in Australia, requesting rights holders to provide information in a very short time frame and without notifying those investigated of the outcome of the investigation. Such conduct results in uncertainty by the rights holders as to the extent to which they can engage in legitimate commercial activity without risk of investigation or action by the ACCC, hence stifling such activity.

This uncertainty would be avoided by legislative guidance, or at minimum, administrative guidelines as to:

- how the *Trade Practices Act* applies to commercial activities of rights holders and the exercise of intellectual property rights; and
- the manner in which the ACCC investigates such activities, in particular, the timeliness of such investigations and notification to participants of the outcome.

## 5.1 Preventing piracy using technological protection devices

The following statements demonstrate the different and conflicting consequences of the Copyright Act and the ACCC's approach to the enforcement of the *Trade Practices Act* in relation to the exercise of copyright by owners.

The Report of the House of Representatives Standing Committee on Legal and Constitutional Affairs "*Cracking Down on Copycats: enforcement of Copyright in Australia*" November 2000 ("**Piracy Report**") stated:

*"Copyright infringement is a real problem affecting Australia's economy<sup>11</sup>... The Committee recommends that the industry be encouraged to develop technological protection devices that are used to protect copyright material<sup>12</sup>"*

The ACCC has stated:

*"The ACCC is currently investigating whether Australian consumers are paying higher prices for DVDs because of the ability of copyright owners, such as film companies, to prevent competition by restricting imports from countries where the same (authorised) video titles are sold more cheaply".<sup>13</sup>*

The ACCC approach does not take into account the need and the right for copyright holders to protect the works in which they hold copyright.

The Piracy Report considered the extent to which pirate products (infringing copies of copyright material made in commercial infringement operations) occurs in Australia. The Committee found that copyright infringement in Australia is a real problem affecting Australia's economy,<sup>14</sup> noting that the extent of pirated products in Australia as follows:

- (a) piracy in the Australian sound recording industry is around 7%<sup>15</sup>;
- (b) 33% of all software programs used in Australia were illegal copies<sup>16</sup>; and
- (c) piracy of films is around 4%<sup>17</sup>.

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<sup>11</sup> Piracy Report, 2.45

<sup>12</sup> Piracy Report, 3.49

<sup>13</sup> ACCC media release, 21 December 2000

<sup>14</sup> Piracy Report at 2.45

<sup>15</sup> Piracy Report at 2.11

<sup>16</sup> Piracy Report at 2.12

The Piracy Report noted the direct and indirect costs of infringement to copyright owners in terms of loss of income to the copyright holder, with the flow-on effect of contraction in the industry, as creators are unable to sustain themselves from their incomes, in turn depriving the industries of creativity and innovation, especially that contributed by the small-medium business sector<sup>18</sup>. It also involves losses in the distribution process, to retailers and the wider community<sup>19</sup>.

The Committee then considered mechanisms available to copyright owners to protect their rights from such infringement. Those mechanisms included the use of a technological protection device, which operates "by either aiding the identification of copyright material or by restricting access to, or the use of copyright material".<sup>20</sup> The Committee recommended that the industry be encouraged to develop technological protection devices that are used to protect copyright material.<sup>21</sup>

By contrast, the ACCC media release referred to above indicates that the implementation of such devices, which was a technique suggested by the Committee should be adopted to restrict access or the use of copyright material, is said to raise concerns under Part IV of the Trade Practices Act.

This is a clear example of where legitimate activity which is permitted under copyright legislation and supported by the Committee and which is intended to prevent the damage to the industry caused by piracy identified by the Committee, may be investigated and the subject of enforcement action by the ACCC for breach the *Trade Practices Act*.

## **5.2 Warner/Universal - substantial market power?**

By way of further illustration, the problems faced by an intellectual property rights holder under the current form of section 46 as interpreted by the ACCC and the courts were clearly demonstrated in the recent Federal Court decision in *Australian Competition and Consumer Commission v Universal Music Australia Pty Limited* (2002) ATPR 41-855.

In its current form, section 46 prohibits a corporation which has a substantial degree of power in a market from taking advantage of that power for a proscribed purpose. This section only applies if the relevant corporation has a substantial degree of power in a market, that is, is able

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<sup>17</sup> Piracy Report at 2.13

<sup>18</sup> Piracy Report at 2.23

<sup>19</sup> Piracy Report at 2.24

<sup>20</sup> Piracy Report at 3.43

<sup>21</sup> Piracy Report at 3.49

to act in a manner in which it could not act, if faced with competition.<sup>22</sup> Once a corporation is found to have such a degree of market power, it is viewed through a "special lens"<sup>23</sup>.

The question of whether the owner of copyright in a particular works or portfolio of works was an issue which the Court was required to determine in this case. The Australian Competition and Consumer Commission succeeded in arguing that Universal Music and Warner Music breached sections 46 and 47 of the *Trade Practices Act* and substantial penalties were imposed. The decision is under appeal.

The parties agreed that the relevant markets were for the wholesale and retail of recorded music and that CDs formed the majority of this market. Hill J concluded that the defendants did possess market power and furthermore had misused their market power within the meaning of section 46 of the *Trade Practices Act*.

A central dispute in this case was whether each of Universal Music and Warner Music possessed a substantial degree of market power. The views of two economists were advanced in the *Universal Music* case: Professor Hausman, on behalf of the record companies, and Mr Henry Ergas, on behalf of the Commission. These experts favoured different views as to how the existence of market power should be determined. Essential to Hausman's view was that market power could only be found to exist where a corporation is able to increase prices. Hausman used the term "market power" to mean "*the ability of a firm to charge a price significantly above the competitive level for a non-transitory period of time*"<sup>24</sup>. That is, Hausman considered whether firms could give less and charge more as being essential. Ergas considered that the threat of refusal to supply so as to impose a unilateral vertical restriction having an anti-competitive effect as being the relevant question. Ergas referred to market power as meaning "the ability of a firm to act persistently in a manner unconstrained by competition"<sup>25</sup>. He considered that the ability of a firm to raise prices was not necessarily relevant. Ergas considered that the record companies had a substantial degree of market power by reason of the temporary monopoly they enjoyed over particular titles.

AVSDA is concerned with the finding in the *Universal Music/Warner* case in two respects:

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<sup>22</sup> Goldberg J in *ACCC v Australian Safeway Stores & ors* [2001] FCA 21 December 2001 paragraph 1023.

<sup>23</sup> *Melway Publishing Pty Ltd v Robert Hicks Pty Ltd t/as Auto Fashions Australia* (2001) 178 ALR 253 at para 29

<sup>24</sup> (2002) ATPR 41-855 at para 532

<sup>25</sup> (2002) ATPR 41-855 at para 353.

- (a) it appears that possessing copyright in a popular title is equated with possessing a temporary monopoly which in turn is found to constitute substantial market power, in circumstances where:
- they each possessed less than a 30% market share;
  - products are differentiated such that a small change in consumer demand will affect price; and
  - there was strong countervailing power.
- (b) that a portfolio of exclusive intellectual property rights gives rise to market power in itself.

This approach to determining whether a copyright holder has substantial market power is inconsistent with the approach taken in other jurisdictions. For example, the US Department of Justice and Federal Trade Commission expressly acknowledge that they *"will not presume that a patent, copyright, or trade secret necessarily confers market power upon its owner. Although the intellectual property right confers the power to exclude with respect to the specific product, process, or work in question, there will often be sufficient actual or potential close substitutes for such product, process, or work to prevent the exercise of market power"*<sup>26</sup>.

This is also the position taken by the New Zealand High Court, which held that even in the case of an outstandingly popular album, *"charting records are too short-lived to qualify as any form of dominance"* for the reason that there are clearly substitutes.

*"At any one time when an album is enjoying popularity, promotion of another is gathering momentum. In our view, the places at the top of the charts are a constant battleground in which rivalrous conduct abounds...In reality no distributor or retailer could run a business on the basis of a market confined to one unique album...one of the most unique features of the market is that there is no consistency about the product that wins a share in it. Competition revolves primarily around finding and promoting those albums which will appeal to the majority of charting album purchases for a period of sufficient duration to meet the heavy costs of promotion and production and still leave some profit"*<sup>27</sup>.

The New Zealand Court of Appeal (per Richardson J) affirmed this approach, criticising a single album definition of market as:

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<sup>26</sup> US Anti-Trust Guidelines, section 2.2

- ignoring commercial reality both in terms of product and time;
- incorrectly focussing on short run phenomena, "*a snap shot rather than a moving picture of continuing commercial activity*".

The approach taken by Justice Hill ignored the commercial reality of the arrangements between manufacturers, distributors and retailers of works such as recorded music. As pointed out by Justice Richardson:

*"Supply to distributors is not acquired on an album-by-album basis, but by licenses giving rights to any album produced by the artist or label. In arranging supply the distributor achieves economies of scope in what is a continuing activity. And retailers and consumers along with distributors are dependent on a flow of new albums to join and, in part, to displace existing albums - a process recognised and encouraged in the promotional and pricing arrangements. Promotion is undertaken in accordance with normal competitive practice for the purpose of differentiating one album from a whole range of possible substitutes and the evidence of promotion of particular albums by retailers emphasising price concessions belies the argument that purchasers of albums are not price sensitive. The emphasis on product differentiation arises precisely because there is a range of products competing for the consumers attention. And the movement of albums in and out of the charts and their constantly shifting positions are clear evidence of the manner in which, and the extent to which substitution takes place".*

Finding that a copyright holder has substantial market power on the basis of a temporary monopoly is also inconsistent with the approach generally taken by Australian Courts to assessing whether a corporation has substantial market power for the purposes of section 46. Since the judgment of the High Court in *Queensland Wire*, it has been accepted that it is necessary to take a long run dynamic view of competition as a process.<sup>28</sup> Any analysis of the extent of a copyright holders power in any market requires an analysis of competition over time, including potential competition.

The ACCC and the Court clearly currently consider that at least in some circumstances, a copyright holder has substantial market power by virtue of its copyright in a particular work or portfolio of works at a particular point in time.

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<sup>27</sup> (1988) 2NZ BLC 99-113 at 103, 089-090

<sup>28</sup> (1989) ATPR 40-925 at 50, 010 (per Mason CJ and Wilson J)

This approach has adverse consequences for the system of intellectual property protection and should be prevented, either by amendment to section 46 or, at a minimum, by the formulation and implementation of guidelines which limit the circumstances in which the ACCC may take action against copyright holders in circumstances where the exertion of their intellectual property rights falls within the protection which is fundamental to the achievement of the objectives of intellectual property protection.

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## **6. A Comparison of Misuse of Market Power and Intellectual property rights in Australia and other jurisdictions**

### **6.1 Current Australian approach to market power and intellectual property rights**

There has been a discernible trend in recent judicial decisions (*Melway*, *Boral*<sup>29</sup>, *Safeway*, and particularly the findings in the *Universal* case) to find the existence of market power under section 46 of the *Trade Practices Act* in a wider range of circumstances, to the point where there is a danger that normal competitive conduct in a rivalrous market will be impinged by the chilling effect of an over-inclusive interpretation of section 46.

This has the potential, if not corrected, in the case of intellectual property protection, of depriving the community of the benefits over the medium and longer term of an effective intellectual property protection regime which, for fear of a trade practices enforcement action, becomes neutered except in the most narrow of circumstances.

### **6.2 United States Anti-Trust Law Approach to Market Power and intellectual property**

The policy settings which have given rise to the point of intersection of intellectual property and competition laws in the United States and Canada as compared to Australia have resulted in a considerable difference between the thresholds applied to determine whether market power is possessed by a firm, and, if so, when that power is exercised, it will be considered actionably anticompetitive.

Both of these Australian trading partners include sections similar to s. 46 of the *Trade Practices Act* in their anti-trust legislation. In the United States, s. 2 of the *Sherman Act* provides:

*Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or*

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<sup>29</sup> *Australian Competition and Consumer Commission v Boral Ltd* (2001) 106 FCR 328

*commerce among the several States, or with foreign nationals, shall be deemed guilty of a felony...*

In the United States the view is held that in order for a firm to be guilty of illegal monopolization it must be the dominant player in the market, or must act in concert with others to monopolize. There, courts have held that:

- a market share of less than 50% is insufficient to establish the existence of power<sup>30</sup>.
- "Substantial market power can only exist where there are significant and continuing barriers to expansion and entry"<sup>31</sup>.

In Canada the relevant sections are ss. 78 and 79 of the *Competition Act*. Section 79(1) of the *Competition Act* provides:

*Where, on application by the Commissioner, the Tribunal finds that*

*a. one or more persons substantially or completely control, throughout Canada or any area thereof, a class or species of business,*

*b. that person or those persons have engaged in or are engaging in a practice of anti-competitive acts, and*

*c. the practice has had, is having or is likely to have the effect of preventing or lessening competition substantially in a market, the Tribunal may make an order prohibiting all or any of those persons from engaging in that practice.*

Section 78 of the *Competition Act* lists conduct that will be regarded as anti-competitive.

Because the threshold for a market power finding is less inclusive in the US and Canada, the risk that an intellectual property rights holder will be found to have the requisite degree of market power for those provisions to potentially apply is lower than in Australia.

### **6.3 Europe**

The European regime contains various block exemptions for defined categories of agreements on the basis of public interest. These include Commission Regulation (EC) No 240/96 on the application of Article 85(3) of the Treaty to certain categories of technology transfer

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<sup>30</sup> *Valley Liquors v. Renfield Importers*, 822 F.2d 656 (7th Cir.), cert. denied, 484 U.S.977, 108 C.Ct. 488 (1987); H. Hovenkamp, *Federal Antitrust Policy: The Law of Competition and Its Practice*, 2nd edition, p. 270.

<sup>31</sup> <http://www.aspenpubs.com> at paragraph 506.

agreements and Commission Regulation (EC) No 2659/2000 on the application of Article 81(3) of the Treaty to categories of research and development agreements<sup>32</sup>.

AVSDA does not consider that such an approach would adequately deal with the problems identified in this paper with s. 46 of the TPA for the reason that those problems arise from the very fact of ownership and enforcement of intellectual property rights. AVSDA considers that the other approaches to dealing with the problems concerning the application of s. 46 of the *Trade Practices Act* suggested in this submission are preferable.

## 6.4 UK

The *Competition Act* 1998 prohibits conduct by undertakings which amounts to an abuse of a dominant position in a market and which may affect trade within the United Kingdom (the Chapter II prohibition). There is no power to grant exemptions from this prohibition, although some agreements which are exempted by way of individual exemption from Chapter I (which prohibits agreements which distort competition) cannot be looked at under Chapter II<sup>33</sup>.

Unlike the current "purpose" test of section 46 of the *Trade Practices Act*, the UK prohibits conduct which constitutes an abuse of a dominant position, with no separate "purpose" element.

The Office of Fair Trading has issued guidelines to the Chapter II prohibition which give examples of conduct which is most likely to constitute an abuse of market position. Those Guidelines recognise the role of intellectual property rights in encouraging creative and innovative activity and expressly acknowledge that the exclusive rights provided by an intellectual property right do not necessarily give rise to a dominant position, and that even where an undertaking is dominant, the legitimate exercise of an intellectual property right is not an abuse<sup>34</sup>. These guidelines are in addition to specific guidelines addressing the application of the UK *Competition Act* to intellectual property rights which are discussed below.

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## 7. Guidelines

Importantly for the practicable guidance of intellectual property rights holders, in the US and Canada, the relevant competition law enforcement agencies have published guidelines which assist rights holders in determining when their activities permitted by intellectual property legislation may raise concerns under antitrust legislation.

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<sup>32</sup> European Commission, <http://europa.eu.int/comm/competition/antitrust/legislation/>.

<sup>33</sup> "The *Competition Act* 1998 - The Chapter II Prohibition" para 2.7

<sup>34</sup> "The *Competition Act* 1998 - The Chapter II Prohibition" para 4.4

## 7.1 United States Approach

In 1995 the US Department of Justice and the Federal Trade Commission issued Anti-Trust Guidelines which make the approach to determining market power in the context of intellectual property rights holders clear as follows:

- Importantly, the United States guidelines make it clear that market power is to be analysed over "A significant period of time". This is the opposite to the approach of the Federal Court in the Universal Music case, in which the Court adopted the approach that the possession of a temporary monopoly in a portfolio of copyright work could in itself denote possession of market power by the relevant firm. AVSDA considers that the US approach is the correct approach to the analysis of market power.
- The Agencies will not presume that a patent, copyright, or trade secret necessarily confers market power upon its owner."<sup>35</sup>
- The Agencies do not presume that intellectual property creates market power in the anti-trust context."<sup>36</sup>
- The Agencies recognise an antitrust "safety zone". The rationale for the existence of the safety zone is that it will facilitate certainty and encourage licensing arrangements, which commonly "promote innovation and enhance competition"<sup>37</sup>.

The US Anti-Trust Guidelines provide that<sup>38</sup>:

*Absent extraordinary circumstances, the Agencies will not challenge a restraint in an intellectual property licensing arrangement if (1) the restraint is not facially anticompetitive<sup>39</sup> and (2) the licensor and its licensees collectively account for no more than twenty percent of each relevant market significantly affected by the restraint. This "safety zone" does not apply to those transfers of intellectual property rights to which a merger analysis is applied...*

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<sup>35</sup> Us Anti-Trust Guidelines page 4.

<sup>36</sup> US Anti-Trust Guidelines Page 3.

<sup>37</sup>[5] <http://www.usdoj.gov/atr/public/guidelines/ipguide.htm>, p. 18.

<sup>38</sup> <http://www.usdoj.gov/atr/public/guidelines/ipguide.htm>, pp. 18-19

<sup>39</sup> A facially anticompetitive restraint is one that is regarded as generally being deemed to be per se illegal or that would always or almost always tend to reduce output or increase prices: <http://www.usdoj.gov/atr/public/guidelines/ipguide.htm>, p. 18.

Slightly different criteria are applied to considerations of restraints in intellectual property licensing arrangements where:

- (a) there is a lack of reliable or representative market share data; and
- (b) the affect on competition in an innovation is at issue<sup>40</sup>.

AVSDA contends that the existence of the antitrust safety zone both evidences that firms in the United States will be less scrutinised than Australian firms to determine whether they have engaged in anti-competitive conduct and furthermore, assists in clarifying the meaning of the competition law in the United States and its affect on intellectual property rights and rights owners.

The current Australian approach results in a disadvantage to the global competitiveness of local firms and is detrimental to the activity for Australian innovators to compete internationally.

## 7.2 Canadian approach

Canada has also implemented guidelines which make the intersection between intellectual property law and anti-trust law clear.

On 21 September 2000 the Canadian Competition Bureau released its Intellectual Property Enforcement Guidelines ("**Canadian Guidelines**"). The Canadian Competition Bureau adopts a different approach to assessing of market power and unilateral anticompetitive conduct to the current Australian approach as follows:

- (a) "The Bureau does not consider an owner of IP to have contravened the *Competition Act* if it attained market power solely by possessing a superior quality product or process, introducing an innovative business practice or other reasons for exceptional performance."<sup>41</sup>
- (b) "(i)n assessing whether a particular licensing arrangement raises a competition issue, the Bureau examines whether the terms of the licence serve to create, enhance or maintain the market power of either the licensor or the licensee. The Bureau will not consider licensing agreements involving IP to be anti-competitive unless they

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<sup>40</sup> <http://www.usdoj.gov/atr/public/guidelines/ipguide.htm>, p. 18.

<sup>41</sup> Page 6 of Enforcement Guidelines.

reduce competition substantially or unduly relative to that which would have likely existed in the absence of the licence."<sup>42</sup>

(c) the Bureau considers efficiency is at the principal stage of analysis.

The Canadian Competition Bureau adopts a five stage analysis in the Canadian Guidelines.

That process is as follows:

- identifying the transaction or conduct;
- defining the relevant *market(s)*;
- determining if the firm(s) under scrutiny possess *market power* by examining the level of concentration and entry conditions in the relevant *market(s)*, as well as other factors;
- determining if the transaction or conduct would unduly or substantially lessen or prevent competition in the relevant *market(s)*; and,
- considering, when appropriate, any relevant efficiency rationales.

In explaining its consideration of efficiency principles criterion, the Canadian Guidelines state:

*In assessing whether conduct involving IP substantially lessens or prevents competition under the abuse-of-dominant-position or exclusive dealing, tied selling and market restriction provisions, the Bureau considers any pro-competitive effects (efficiencies or business justification) generated by or associated with the conduct. For example, a licensing arrangement between an IP owner and a distributor may restrict intra-brand competition, but at the same time further inter-brand competition. A licensing arrangement between two potential competitors may result in a new product being developed that would not otherwise have been developed. In each case, the level of competition in the market would be enhanced.*

*The Bureau also considers whether the firms could have used commercially reasonable means to achieve efficiencies that are or were less harmful to competition. If such alternatives exist, the Bureau would compare the anti-competitive effect of the transaction or conduct to such alternatives. In making this comparison, the Bureau does not attempt to uncover all of the theoretically possible alternatives for achieving the efficiencies. It considers only those means that are*

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<sup>42</sup> Page 6 of Enforcement Guidelines.

*commercially reasonable and consistent with the firm's IP rights. The Bureau also considers the impact that using an alternative would have on the firm's ability to exercise its IP rights*<sup>43</sup>.

The Canadian Competition Tribunal has explained its role in considering efficiencies as follows<sup>44</sup>:

*What the Tribunal must decide is whether, once all relevant factors have been taken into account and weighed, the act in question is, on balance, "exclusionary, predatory or disciplinary". Relevant factors include evidence of the effects of the act, of any business justification and of subjective intent which, while not necessary, may be informative in assessing the totality of the evidence. A "business justification" must be a "credible efficiency or pro-competitive" business justification for the act in issue. Further, the business justification must be weighed "in light of any anti-competitive effects to establish the overriding purpose.*

Like the US Agencies, the Canadian Competition Bureau has indicated its view that a firm cannot be held to possess market power if its power is merely transitory. It considers that in order for a firm to be found to possess market power, it must be able to maintain prices above competitive levels or restrict non-price aspects of competition for "a significant period of time"<sup>45</sup>.

### **7.3 UK Approach**

Chapter II of the *Competition Act 1998* prohibits conduct by undertakings (which includes natural or legal persons) that amounts to an abuse of dominant position in a market and which may affect trade in the United Kingdom<sup>46</sup>.

The Office of Fair Trading has published various guidelines that assist in clarifying the interpretation and application of competition legislation in that jurisdiction. They include a general guideline, *The Major Provisions*, which relates to the operation of certain sections such as *Assessment of Market Power*, as well as specific guidelines that relate to particular industries, such as *Intellectual Property Rights: A Draft Competition Act 1998 Guideline*.

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<sup>43</sup> Canadian Competition Bureau, Enforcement Guidelines on the Abuse of Dominant Provisions, at <http://strategis.ic.gc.ca/SSG/1/ct02214e.html>, p. 11

<sup>44</sup> *Director of Investigation and Research v. Tele-Direct Inc.* CT-9403\_14, at <http://www.canlii.org/ca/cas/cact/1997/1997cact6.html>.

<sup>45</sup> Canadian Competition Bureau, Enforcement Guidelines on the Abuse of Dominant Provisions, at <http://strategis.ic.gc.ca/SSG/1/ct02214e.html>, p. 1.

<sup>46</sup> Office of Fair Trading, *The Major Provisions: The Competition Act 1998*.

The *Intellectual Property Rights: A Draft Competition Act 1998 Guideline* outlines how the Director General considers that the Competition Act will operate in relation to intellectual property rights. It explains in detail how they also discuss issues of significance for the intellectual property community. The guidelines provide a degree of certainty as to the extent to which intellectual property rights will create a "dominant position" and examples of conduct that is considered to be an abuse of dominant position. Specifically, the guidelines state:

- "ownership of an IPR<sup>47</sup> will not necessarily create a dominant position"<sup>48</sup>;
- "Although the existence of an IPR may impede entry into a market in the short term, any other undertaking may in the long term be able to enter the market with its own innovation. In markets where undertakings regularly improve the quality of their products, a persistently high market share may indicate no more than persistently successful innovation"<sup>49</sup>;
- "a refusal by a dominant holder of IPR to licence its IPR is not in itself an abuse"<sup>50</sup>;
- the grant of an IPR licence by a dominant IPR proprietor on the condition that the licensee also agrees to buy another product or service would be unlikely to infringe the Chapter II prohibition if such provisions "are necessary for a satisfactory exploitation of the licensed IPR, or for ensuring that the licensee conforms to quality standards"<sup>51</sup>; and
- "there will not necessarily be an infringement of the Chapter II prohibition where a proprietor of IPR holds a dominant position and it charges a higher selling price or royalty rate for a product, process or work protected by its IPR as compared with a product, process or work not protected by an IPR"<sup>52</sup>.

AVSDA considers that these approaches should be considered in the context of Part IV of the *Trade Practices Act*, or at least in the preparation of guidelines to give certainty to intellectual

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<sup>47</sup> IPR means intellectual property rights.

<sup>48</sup> *Intellectual Property Rights: A Draft Competition Act 1998 Guideline*, p. 13.

<sup>49</sup> *Intellectual Property Rights: A Draft Competition Act 1998 Guideline*, p. 13.

<sup>50</sup> *Intellectual Property Rights: A Draft Competition Act 1998 Guideline*, p. 14.

<sup>51</sup> *Intellectual Property Rights: A Draft Competition Act 1998 Guideline*, p. 15.

<sup>52</sup> *Intellectual Property Rights: A Draft Competition Act 1998 Guideline*, p. 16.

property rights holders in Australia and to promote the benefits of the Australian intellectual property regime.

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## **8. Regulatory reform**

### **8.1 Need for clarification**

The examples set out above concerning technological protection devices and the *Universal* case illustrate the need for regulatory reform to ensure that the provisions of Part IV of the *Trade Practices Act* are clear and precise to enable members of the intellectual property community to be clear about the extent of permissible control over proprietary works and the circumstances in which competition policy will override IP rights.

AVSDA considers that such a clarification has been warranted for some time and points to calls from their Hilmer Report<sup>53</sup>, the National Competition Council Review of section 51(2) and section 51(3) of the *Trade Practices Act* and the Ergas Report<sup>54</sup>, which have each called for review and consideration of the area of overlap of intellectual property and competition laws.

### **8.2 Section 46 - effects test and intellectual property rights?**

This need for reform is particularly important if section 46 is amended in accordance with the submission by the ACCC, that is, to prohibit a corporation with a substantial degree of market power from taking advantage of that market power with the effect of:

- (d) eliminating or substantially damaging a competitor of the corporation in that or any other market;
- (e) preventing the entry of a person into that or any other market; or
- (f) deterring or preventing a person from engaging in competitive conduct in that or any other market.

Such an effects test is inconsistent with the policy of the *Trade Practices Act*, which is to protect the competitive processes rather than to protect individual competitors. The courts have consistently acknowledged that the process of competition can be ruthless and can damage individual competitors.<sup>55</sup> Indeed, if the process of competition is to achieve benefits to

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<sup>53</sup> Pages 151 and 160.

<sup>54</sup> Page 9.

<sup>55</sup> *Queensland Wire Industries Pty Limited v The Broken Hill Proprietary Pty Limited & Anor* (1989) 167 CLR 177 per Mason CJ and Wilson J.

the community it must drive down prices to cost and drive down costs to an efficient level. Less efficient competitors will not survive in a competition market. Conduct by an intellectual property rights holder to protect those rights in accordance with intellectual property legislation, for example, taking action to prevent the importation and retail sale of pirate copies of works in which the corporation is the copyright holder, could have the effect of damaging an importer who specialises in importation and distribution of pirated works. If an effects test is introduced to section 46, there is an even stronger argument to amend section 46, insofar as it applies to an intellectual property rights holder who has a substantial degree of market power, applying the proper analysis set out above, so that conduct by that rights holder to enforce those rights does not constitute a contravention of section 46 of the *Trade Practices Act*.

### **8.3 Form of reform**

AVSDA submits that such reform could take any of the following forms:

- amending section 51(3) of the *Trade Practices Act* so that it does not exclude section 46 conduct from its ambit; or
- amending section 46 of the *Trade Practices Act*, including consideration of whether Australia and in particular, intellectual property rights holders in Australia, would benefit from the import of efficiency considerations into s. 46 of the *Trade Practices Act*, particularly if the relevant test in s. 46 of the *Trade Practices Act* be changed to an "effects test"; and
- at minimum, preparing, with industry consultation, guidelines to be followed by the ACCC to give rights holders certainty in the extent to which the ACCC will challenge the exercise of intellectual property rights as a breach of Part IV of the *Trade Practices Act*.

### **8.4 Guidelines**

AVSDA also submits that guidelines need to be produced to clarify how conflicts between intellectual property laws and competition law will be treated by the Australian Competition and Consumer Commission and courts.

As set out above, enforcement guidelines exist in both Canada and the United States. Although none exist in Australia, various committees have recommended that they be

developed in Australia.

AVSDA considers the guidelines published by the United States Department of Justice and the Federal Trade Commission and the Canadian Competition Bureau to be extremely useful in assisting to clarify the relevant law which they discuss and supports the production and implementation of similar Guidelines in Australia, to be created in consultation with relevant industry participants.

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## **9. Conclusion**

AVSDA acknowledges the benefits that both competition and intellectual property law and policy make to consumer and community welfare as a whole. It also recognises that whilst the two systems are ultimately aimed at enhancing consumer welfare, the two regimes sometimes conflict. AVSDA considers that in matters involving a conflict between intellectual property law and competition law, particularly where the existence of market power is at issue, the balance has tipped too heavily in favour of competition law in recent cases and ACCC enforcement action, such that Part IV (and section 46 in particular) has become over-inclusive of legitimate conduct which has as its objective the protection by rights holders of their rights. AVSDA considers that this has resulted and will result in detrimental effects for the intellectual property community in Australia.

This imbalance and the uncertainty surrounding the interplay of competition and intellectual property laws should be rectified by legislative amendment and the implementation of effective guidelines to provide the intellectual property community with certainty as to the application of the law and its effects to the benefit of international licensing and investment in creation and innovation in Australia and to achieve the primary goals of intellectual property law - to reward and encourage innovation and creative effort and ultimately to benefit consumers.

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