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Gowers Review of Intellectual Property  
Room 4/E1  
HM Treasury  
1 Horse Guards Road  
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Date 13 June 2006

Dear Mr Gowers

Thank you for your Call for Evidence to inform the Gowers Review of Intellectual Property. The OFT welcomes the opportunity to provide its comments to the review and looks forward to continuing its participation in the Cross Whitehall stakeholder meetings.

The Call for Evidence document raises a number of wide-ranging, fundamental questions about the most effective means of encouraging innovation in different markets and about the appropriate boundaries between competition and IP policy. While in some respects these broad questions mark a departure from the traditional role of the OFT in relation to IP - that of investigating potentially anticompetitive behaviour in the use of IPRs - the OFT would like to signal its keen interest in engaging with them. Indeed, I and several colleagues met members of the Gowers review team in January to discuss our interest in broad terms.

Our thoughts on many of these policy questions are at a relatively early stage. Therefore, rather than committing preliminary views to paper, we consider that the best way to proceed at this point is through continued constructive engagement with the Cross Whitehall Stakeholder Group and further bilateral meetings with the review team. We intend during this period to develop our views on how the OFT should take forward its interest in IP policy.

In the rest of this response, we set out in broad terms some of the key principles applying to the use of IPRs under EU and UK competition law. We hope this will provide a useful factual grounding for taking forward the discussion over the months ahead.

#### Treatment of IPRs under EU and UK Competition Law

As a starting point, it is generally understood that the mere fact that intellectual property laws grant exclusive rights of exploitation does not imply that intellectual property rights are immune from the application of competition law. Articles 81 and 82 of the EC Treaty and the Chapter I and Chapter II prohibitions of the UK Competition Act 1998 are in particular applicable to agreements whereby the holder licenses another undertaking to exploit his or her intellectual property rights.



At the same time, there is no inherent conflict between intellectual property rights and the competition rules. Indeed, both bodies of law share the same basic objective of promoting consumer welfare and an efficient allocation of resources. Innovation constitutes an essential and dynamic component of an open and competitive market economy. Intellectual property rights can promote dynamic competition by encouraging undertakings to invest in developing new or improved products and processes. At the same time, effective competition can put pressure on undertakings to innovate. Therefore, both intellectual property rights and competition can promote innovation, although their effectiveness in doing so may vary between different types of market.

EC and UK competition law draws a distinction between the mere existence of intellectual property rights and the exercise of those rights. The former is not subject to competition law, whereas the latter might, in some cases, infringe Article 81 or Article 82 of the EC Treaty or Chapter I or Chapter II of the Competition Act 1998. Part of the reason for developing this distinction was to ensure that competition law does not prejudice the private property system which is essential in a free market economy.

Activities such as licensing of intellectual property rights would fall into the category of “exercise” and, it is generally agreed, can be subject to competition law scrutiny, as discussed below. In contrast, questions about what subject matter ought to be protected by intellectual property rights fall into the category of “existence”, and would not be subject to scrutiny under competition law. If competition law were to attempt to regulate or limit the grant or the scope of intellectual property rights on an ad hoc, ex post basis, there is risk that this would lead to considerable uncertainty for firms, undermining incentives to innovate.<sup>1</sup>

#### Technology licensing

Technology licensing (which includes patent and know-how licensing) is addressed in the European Commission’s Technology Transfer Block Exemption Regulation<sup>2</sup> and *Guidelines on the Application of Article 81 of the EC Treaty to Technology Transfer Agreements*.<sup>3</sup> These guidelines make it clear that there is no presumption that intellectual property rights and licence agreements as such give rise to competition concerns. They state that most licence agreements, for example, do not restrict competition and instead create pro-competitive efficiencies. Indeed, the guidelines state that licensing as such is pro-competitive as it leads to dissemination of technology and promotes innovation. In addition, even licence agreements that do restrict competition may often give rise to pro-competitive efficiencies, which must be considered and balanced against the negative effects on competition. The great majority of licence agreements are therefore compatible with EC and UK competition law.

The technology transfer guidelines also recognise that the creation of intellectual property rights often entails substantial investment and that it is often a risky endeavour. In order not to reduce dynamic competition and to maintain the incentive to innovate, they acknowledge that the innovator must not be unduly restricted in the exploitation of intellectual property rights that turn out to be valuable. For these reasons, the guidelines state that the innovator should normally be free to seek compensation for successful projects that is sufficient to

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<sup>1</sup> We should reiterate that this does not preclude OFT from engaging in the debate about questions of existence through its “competition advocacy” role of advising Government on the impact of policies and regulations on competition.

<sup>2</sup> Regulation 772/2004, OJ 2004 L123/11.

<sup>3</sup> OJ 2004 C101/2.

maintain investment incentives, taking failed projects into account. Technology licensing may also require the licensee to make significant sunk investments in the licensed technology and the assets necessary to exploit it. According to the guidelines, Article 81 is not therefore to be applied without considering such *ex ante* investments made by the parties and the risks relating thereto. The risk facing the parties and the sunk investments that must be committed may thus lead to the agreement falling outside Article 81 entirely or fulfilling the conditions for exemption.

Under the technology transfer guidelines, the assessment of whether a technology licence agreement restricts competition must be made within the context in which competition would occur in the absence of the agreement with its alleged restrictions. For example, it is necessary to take account of the likely impact of the agreement on inter-technology competition (i.e. competition between undertakings using competing technologies) and on intra-technology competition (i.e. competition between undertakings using the same technology). Article 81 prohibits restrictions of both inter-technology competition and intra-technology competition. It is therefore necessary to assess to what extent the agreement affects or is likely to affect these two aspects of competition on the market.

It is generally understood that licence agreements that could infringe EC and UK competition law would include those containing provisions in licences between competitors restricting the licensee's ability to determine its sale prices, stipulations that share markets or customers as well as restrictions on the licensor's ability to exploit its own technology or to carry out research and development. Where the licence is between non-competitors, licence agreements that restrict the licensee's sale prices or (depending upon the circumstances) that restrict the territory into which or the customers to whom the licensee may passively sell goods or services produced with the licensed technology may infringe the competition rules.

Specific provisions in a technology licence may infringe the competition rules, irrespective of whether they are made between competitors or non-competitors. These could include any direct or indirect obligation on the licensee to assign or grant an exclusive licence to the licensor (or a third party designated by the licensor) for the intellectual property rights in its own severable improvements to the licensed technology or to its own new applications of the licensed technology.

## Relevant Cases

The key cases at an EU level that have dealt with the alleged anti-competitive exercise of intellectual property rights include *Volvo v Veng*<sup>4</sup>, *Magill*<sup>5</sup>, *IMS*<sup>6</sup> and most recently, *Microsoft*<sup>7</sup>. Some commentators have suggested that EC competition law has on occasion intervened to correct anti-competitive effects of intellectual property rights that ought not to have been

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<sup>4</sup> Case 238/84 [1988] ECR 6211.

<sup>5</sup> Commission Decision (89/205) OJ 1989 L78/43, upheld on appeal by the CFI in Cases T-69/89 etc. [1991] ECR II-485 and by the ECJ in Cases C-241/91P etc. [1995] ECR I-743.

<sup>6</sup> (Interim Measures) OJ 2002 L59/18. Interim measures were suspended by the CFI and ECJ (see, e.g. Case C-481/01P (R) [2002] ECR I-3401.

<sup>7</sup> (Case COMP/C-3/37.792 Microsoft).

granted in the first place, but the general view is that EC competition law does not intervene in this fashion.<sup>8</sup>

It may well be the case, however, that competition law can have a place in dealing with some situations in which intellectual property rights have been obtained or extended by fraudulent means, at least where the IPR-proprietor is a dominant company.<sup>9</sup>

The OFT has from time to time been asked to consider complaints under the Competition Act 1998 concerning the exercise of intellectual property rights. To date, the OFT has not however adopted any infringement decisions involving the anti-competitive exercise of intellectual property rights. It is nevertheless the view of the Office that competition law can be deployed effectively in order to deal with the possible anti-competitive exercise of intellectual property rights.

Yours sincerely,

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<sup>8</sup> These views were expressed by some commentators following the European Commission decisions in Magill and IMS in which copyright holders in a dominant position were required to license their intellectual property rights.

<sup>9</sup> See, e.g. Astra AB, Commission decision of 15.6.2005 (IP/05/737 of 5 June 2005) where one of the abuses relates to applications for supplementary protection certificates in several Member States. However, this decision has not been published yet and is under appeal to the Court of First Instance in Case T-321/05 [2005] OJ C271/24.