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ROUNDTABLE ON COMPETITION, PATENTS AND INNOVATION

-- Note by the Delegation of Germany --

This note is submitted by the delegation of Germany to the Competition Committee FOR DISCUSSION at its forthcoming meeting to be held on 9 - 11 June 2009.

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COMPETITION, PATENTS AND INNOVATION

-- Note by Germany --

1. Introduction

1. The development of a dynamic perspective in economic theory has long overcome the traditional focus on static analysis. The significance of competition for dynamic developments, in particular with regard to its effect on innovations, however, has for a long time been discussed intensively and controversially[1].

2. Today it is undisputed that competition incites companies to develop new products and innovative production and business processes. This offers them the possibility to stand out against their competitors.

3. Developing innovations requires investing in research and development (R&D). Companies are only willing to make these investments if there is a prospect that they will pay off. By providing a (temporary) exclusive right, and the competitive advantage this involves, patents guarantee that this is the case.[2]

4. A patent prevents competitors from merely copying an innovation. Instead, they are encouraged to engage in competition from substitutes. Therefore both competition and patents are driving forces behind technological progress and innovation.

2. Patents and competition – area of conflict

5. In spite of the discussions on potential conflict between competition law and patent law, it should not go unnoticed that there is a broad area where competition law and patent law co-exist without conflict. This results not least from the differing foci of patent law and competition law: While patents are granted for individual products or production processes or elements thereof, antitrust enforcement does not focus on individual products but on markets in general.

6. Conflicts between competition law and patent law arise where the market behaviour of a company that has a competitive advantage resulting from a patent raises competition concerns or is considered to be abusive with regard to a relevant market defined under competition law.

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1 Cf. Joseph A. Schumpeter (1908): Das Wesen und der Inhalt der theoretischen Nationalökonomie, p. 176 ff.; only available in German, and Joseph A. Schumpeter (1942): Capitalism, Socialism and Democracy, p. 83; Kenneth J. Arrow (1962): Welfare and the Allocation of Resources for Invention, in: Richard Nelson (ed.): The Rate and Direction of Economic Activities: Economic and Social Factors, p. 609 ff.

2 In order to minimize restraints on competition, close consideration should be paid to the length and scope of the patent.

7. Abuse control under competition law is often criticised for restricting the quasi-property rights of patent holders. This can be countered with the argument that every intervention under competition law to some extent represents an encroachment upon ownership rights or similar rights. The US FTC and the US DoJ, for example, write in their relevant guidelines on the licensing of industrial property rights: "As with other forms of private property, certain types of conduct with respect to intellectual property may have anticompetitive effects against which the antitrust laws can and do protect. Intellectual property is thus neither free from scrutiny under the antitrust laws, nor particularly suspect under them."[3]

8. With the provisions on intellectual property rights the legislator consciously created an area where competition has been "reduced". However, this reduction of competition should not be understood as an elimination of competition per se. In other words: A patent allows its holder the exclusive right to use or license to others his innovation. If the holder abuses his competitive advantage, he leaves the area of protection afforded to him under intellectual property law and enters the area of antitrust enforcement.[4] In this way antitrust law acts as a corrective for any behaviour by which a patent holder might abuse the competition advantage offered by the patent for anticompetitive means.**3.Patents and Abuse Control**

9. It seems that patents are increasingly being used by companies as a strategic instrument. At a meeting of the OECD Competition Committee in October 2008, a representative of the European Patent Office commented on possible anticompetitive practices in the application for and granting of patents[5]

10. In Germany competition law proceedings on the abuse of patents have so far mainly taken the form of civil proceedings. In its expert opinion of March 2007 on the theme "Patent Protection and Innovation" the Academic Advisory Council at the Federal Ministry of Economics and Technology expected the number of competition cases in which intellectual property plays a role to increase.[6]

3.1 Case Examples of Abuse of Dominance

11. Several cases of abuse of a dominant position in the use of intellectual property rights were pending at European[7] and German courts in the past. The essential point was that in using the exclusive rights to his patent, the holder of a patent is bound to the principles of general competition law. The patent holder may not abuse his dominant position either by demanding excessive licence fees or discriminating

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3 See FTC/DoJ (1995): Antitrust Guidelines for the Licensing of Intellectual Property, online: http://www.usdoj.gov/atr/public/guidelines/0558.htm.
A similar framework is set by the Commission Regulation (EC) No 772/2004 of 27 April 2004 on the application of Article 81(3) of the Treaty to categories of technology transfer agreements; online: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2004:123:0011:0017:EN:PDF and the accompanying EC guidelines.

4 Cf. Busche, Jan: Kartellrechtliche Zwangslizenzen – Schranken für gewerbliche Schutzrechte?, online unter: http://www.uni-muenster.de/Jura.iwr/Pohlmann/forumk_berichte/f3b_1.htm; available only in German

5 OECD Competition Committee (2008): Dialogue with European Patent Office, Issue Paper "Patenting and Competition".

6 Cf. Academic Advisory Council (2007): Patentschutz und Innovation, Expert Opinion 1/2007, p. 20; online at: http://www.bmwi.de/BMWi/Redaktion/PDF/Gesetz/entwurf-eines-dreizehnten-gesetzes-zur-aenderung-aussenwirtschaft,property=pdf,bereich=bmwi,sprache=de,rwb=true.pdf. only available in German.

7 Cf for example European Court of Justice: ITT Promedia NV ./. Commission (Slg. 1998 II, 2941, 2987), AB Volvo ./. Erik Veng (UK) Ltd (Slg. 1988, 6232, 6235), Radio Telefis Eireann (RTE) ./. Magill TV Guide Ltd (Slg. 1995 I, 808, 823).

against companies without objective justification. Rather, in using his patent rights he has to abide by the FRAND principles, i.e. "fair, reasonable and non-discriminatory".

12. In one case the German courts had to deal with a case of refusal by a patent holder to grant a non-discriminatory licence for a certain type of industrial drum, the so-called standard tight-head drum.[8]

13. In early 1990 some major German chemical industry companies, members of the German Chemical Industry Association VCI (*Verband der Chemischen Industrie e.V.*, *VCI*) stated their need for a new type of plastic drum that could be more easily drained of liquid residue. Four German drum manufacturers submitted different proposals. One patented proposal was agreed upon and incorporated into the "VCI framework conditions for the new L-Ring Drum – as of 31.7.90" ("*VCI Rahmenbedingungen für das neue L-Ring-Fass – Stand 31.7.90*"). These framework conditions were signed by the major German chemicals manufacturers [9] so that the patented standard tight-head drum thus more or less became the industrial standard. Drums deviating from this standard had only little sales prospects.[10]

14. The patent holder granted the three other drum manufacturers which had also submitted proposals to the VCI free licences, other manufacturers were granted licences against payment of royalties. One competitor, however, was denied a licence. This competitor went on to manufacture the drums in question without a licence.[11] The company's nullity action before the Federal Patent Court, which was aimed at revoking the patent, was not successful. An appeal against this decision was dismissed by the Federal Court of Justice.[12]

15. After the patent holder had sued for damages, the Federal Court of Justice ruled that this case was a possible violation of the ban on discrimination, i.e. if the patent holder had refused to grant a licence which it had granted to other domestic and foreign drum manufacturers (either with or without the payment of royalties). Similar companies would thus have been treated differently without any objective justification.[13]

16. In May 2009 the Federal Court of Justice decided on a case in the IT sector in which also the amount of the licence fees was subject to dispute.[14] The company Koninklijke Philips Electronics N.V.

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8 Cf. Federal Court of Justice (BGH), decision of 13.07.2004, KZR 40/02 – Standard-Spundfaß, online at: http://juris.bundesgerichtshof.de/cgi-bin/rechtsprechung/document.py?Gericht=bgh&Art=en&sid=afd17569ae503cb56f3e1ee98d7e8745&client=12&nr=47897&linked=pm&Blank=1; only available in German.

9 Cf. BGH, Judgement of 13.7.2004, KZR 40/02, loc. cit., p. 4.

10 Cf. BGH, Judgement of 13.7.2004, KZR 40/02, loc. cit., p. 8.

11 Cf. compulsory licence of a patent that has become an industrial standard, in: WuW of 10.11.2004, issue no. 11, p. 1159-1165.

12 Cf. Federal Court of Justice (BGH), decision of 9.5.2000, X ZR 45/98, online at: http://juris.bundesgerichtshof.de/cgi-bin/rechtsprechung/document.py?Gericht=bgh&Art=en&sid=7aacd183a773de293b2ba2910eb8354e&client=12&nr=22802&pos=0&anz=1; only available in German.

13 Cf. Federal Court of Justice (BGH), decision of 13.7.2004, KZR 40/02, loc. cit., p. 12.

14 Cf. Federal Court of Justice (BGH), decision of 6 May 2009, KZR 39/06, online at: http://juris.bundesgerichtshof.de/cgi-bin/rechtsprechung/document.py?Gericht=bgh&Art=en&sid=b5343b8e4b42c68ccd0ee220ba41f048&client=12&nr=48134&pos=0&anz=1; only available in German; press release online at: http://juris.bundesgerichtshof.de/cgi-

(Philips) is the owner of a patent that is essential for the production of recordable and rewriteable optical data carriers (CDR and CDRW). This is a basic patent which every manufacturer of standard CDRs or CDRWs must have and which therefore gives Philips a dominant position. Philips has granted many companies a licence to the patent on the basis of a standard licence agreement. One company manufactured and marketed CDRs and CDRWs without such a licence. The company argued that the licence fees were excessive and also discriminatory because other companies had been granted more favourable conditions. According to the company, Philips had abused its dominant position.

17. In its decision the Federal Court of Justice stated that the patent holder may not discriminate against a company wishing to conclude a licence agreement by charging this company higher licence fees than others would have to pay without any objective justification. Patent holders who violate this ban on discrimination thus cannot enforce a claim for injunction under patent law. Just as the patent holder's refusal to conclude a licence agreement with the company seeking to obtain a licence, a claim based on the patent would constitute an abuse of his dominant position.

18. The Federal Court of Justice also held that a company which manufactures products under a patented industrial standard without a licence could use the "competition law defence" against the holder of the patent. This means that the user of the patent can claim that the patent holder is abusing his dominant position by depriving him of the use of the patent. According to the court the user would have to prove that he tried unsuccessfully to obtain a licence under adequate terms and conditions, and that by refusing to grant the licence the holder of the patent was violating the prohibition under competition law of hindering other companies or treating them differently from similar companies without any objective justification. However, the user may only use the patent in anticipation of the licence agreement unlawfully denied, if he fulfils the obligations arising from the licence agreement he seeks to obtain; in particular if he pays the patent holder an appropriate licence fee or at least guarantees this payment.

19. The Federal Court of Justice also referred to the particularly difficult clarification of the maximum amount of a licence fee that would (still) be admissible under competition law. As the company requiring a licence is not aware of the appropriate amount of a licence fee, the Federal Court of Justice held that it would be admissible to offer the holder of the patent an unspecified fee to be determined by the patent holder at his reasonable discretion, and to deposit an amount which at least corresponds to the objectively appropriate amount of the licence fee or possibly exceeds this level. The Federal Court of Justice held that, if necessary, the licensee could clarify in later proceedings whether the licence fee imposed was within the limits set by competition law.

4. Patents and Merger Control

20. Patents also play an important role in merger control. This applies above all to the technology markets in which innovation competition is particularly important.

21. The Academic Advisory Council noted some developments which could be of relevance for the competition authorities, inter alia in the area of merger control. In its opinion the Academic Advisory Council stated that in many sectors a number of patents are used in a product or manufacturing process. This can lead to a “patent maze” in which it is often unclear whether or not patent rights have been violated.[15] In the semiconductor industry, for example, imminent conflicts are eased by a cross-licensing

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bin/rechtsprechung/document.py?Gericht=bgh&Art=en&sid=afd17569ae503cb56f3e1ee98d7e8745&client=12&nr=47897&linked=pm&Blank=1; only available in German.

15 Cf. Academic Advisory Council, loc. cit., p. 13.

system under which the major patent holders grant each other rights of use.[16] However, patent pools or entire cross-licensing networks can have a dampening effect on competition in a market.

4.1 Case Example of Merger Control

22. In 2007 the Bundeskartellamt had to examine the acquisition of the hearing aid business of GN Store Nord A/S, Denmark, by Phonak Holding AG, Switzerland. The companies to be acquired are known in the market concerned under the name GN ReSound. Phonak is one of the world's leading producers of hearing aids. The other two main producers are Siemens and the Danish company William Demant/Oticon.

23. During the last few years a transfer from analogue to digital technology took place in the hearing aid market and digital technology has since been continuously refined. This technological change could have raised expectations of a good environment for competition with profound innovations and market share gains and losses among innovative competitors. However, the examination of the planned merger revealed a largely uncompetitive structure, at least within the group of the three leading suppliers. A comprehensive market information system, patent pools and cross-licensing agreements, which secured free access to the patent portfolio of the other two companies, largely eliminated innovation competition within the leading group. If one of the companies achieved an important innovation, the other two parties had access to this via the cross-licensing system and could use the new development as well. Not the existence of patents proved to be problematic from a competition point of view, but the strategic use of the patent system to create collusion. By allowing each other access to their innovations free of charge, the leading companies signalled to each other that they did not intend to make innovative progress a competition parameter.[17]

24. In its decision of 26 November 2008 the Düsseldorf Higher Regional Court supported the opinion that the anti-competitive effects of the system of patent pools and cross-licensing were such that effective innovation competition could not be assumed to exist.[18]

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16 Cf. Academic Advisory Council, loc. cit., p. 13.

17 Cf. Prohibition decision of the Bundeskartellamt in the B3-578/06 case, "Phonak/GN ReSound" of 11 April 2007, online at: http://www.bundeskartellamt.de/wEnglisch/download/pdf/entscheidungen/07_Phonak_e.pdf; Press release: http://www.bundeskartellamt.de/wEnglisch/News/Archiv/ArchivNews2007/2007_04_12.php

18 Cf. Düsseldorf Higher Regional Court, decision of 26 November 2008, VI-Kart 8/07, online at: http://www.justiz.nrw.de/RB/nrwe2/index.php , File VI-Kart 8/07 (V); only available in German.