THE REPEAL OF SECTION 51(3) OF THE *COMPETITION AND CONSUMER ACT*: A MISTAKE IN NEED OF CORRECTION

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Section 51(3) of the Competition and Consumer Act 2010 (Cth), which exempted certain conditions in intellectual property licences from some competition law prohibitions, was repealed on 13 September 2019. The repeal goes against recommendations of numerous reform bodies and will expose conditions which are benign or indeed pro-competitive to per se prohibitions (which capture certain forms of conduct whether or not that conduct is likely to have anti-competitive effects). The repeal of section 51(3) is a mistake and is based on a faulty understanding of the recommendations made by the Harper Committee and the Productivity Commission. A new intellectual property exemption should be introduced into the Competition and Consumer Act 2010 (Cth) as a matter of urgency to ensure that competitively benign or pro-competitive conditions in intellectual property rights licences are not exposed to per se competition law liability.

I INTRODUCTION

Section 51(3) of the *Competition and Consumer Act 2010* (Cth) (‘*CCA*’), which exempted certain conditions in intellectual property (‘IP’) licences from some competition law prohibitions, was repealed on 13 September 2019 by the *Treasury Laws Amendment (2018 Measures No 5) Act 2019* (Cth) (‘*Section 51(3) Amending Act*’).[1] For reasons explored in this article, the repeal is a mistake and goes against the recommendations of numerous reform bodies, including those of the Harper Committee and the Productivity Commission, whose reports are both cited in the Explanatory Memorandum in support of the repeal.[2]

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1 The Treasury Laws Amendment (2018 Measures No 5) Bill 2018 (Cth) was passed by the House of Representatives on 17 October 2018 and the Senate (with amendments not relating to section 51(3)) on 14 February 2019. The House of Representatives passed the Bill (as amended by the Senate) on 18 February 2019.

2 Explanatory Memorandum, Treasury Laws Amendment (2018 Measures No 5) Bill 2018 (Cth), 31 [4.3].

This article develops an argument that Australia's competition laws should include an exception that ensures that conditions in one-way IP licences are not subject to inappropriately strict regulation. The article focuses on one-way licences, not arrangements such as patent pools and cross-licences. This is because such arrangements were unlikely to be protected by section 51(3).[3]

Part II of this article explains the scope of protection formerly offered by section 51(3). In Part III, the various reform recommendations made in relation to section 51(3) over the past three decades are considered, with particular focus on the recommendations made by the Harper Committee in its 2015 report ('*Harper Report*')[4] and the Productivity Commission in its 2016 report ('*PC Report*').[5] The discussion reveals a long-held and valid view that there is a need to ensure that conditions in IP licences are not subject to per se treatment. An argument is developed that the ultimate decision to repeal section 51(3) was based on a misunderstanding of recommendations made by the Harper Committee and the Productivity Committee. Part IV explains the key reason why conditions in IP licences need to be shielded from per se treatment, namely that even where the licensor and the licensee are competitors, their relationship often has a vertical dimension to it. Part V begins by considering whether existing mechanisms in the *CCA*, namely anti-overlap provisions, authorisation and class exemptions, provide adequate protection from inappropriate per se treatment. A conclusion is reached that they do not and that it is necessary to introduce an exception that ensures that IP licence conditions are regulated only by competition prohibitions that contain the competition test. Part VI explains why subjecting conditions in IP licences to the competition test strikes an appropriate balance between competition and IP policies. Finally, some concluding remarks are made in Part VII.

II PROTECTION OFFERED BY SECTION 51(3)

The *CCA* has never provided a general exception for dealings in IP rights. The section 51(1) general exception of conduct specified in, and specifically authorised by other legislation (Commonwealth, State and Territory), does not apply to the key IP statutes (patents, trade marks, designs or copyrights). However, in recognition of the need to ensure that incentives to innovate created

3 Section 51(3) may have applied to licence terms in patent pools or cross-licences that include patents which are both/all worked to make the same product 'on the basis that the condition relates to articles made by use of licensed intellectual property': Richard RL Hoad, 'Brave New World or Much Ado About Nothing: Practical Effect of Proposed Changes to Trade Practices Act, s 51(3)' (2007) 18(4) *Australian Intellectual Property Journal* 201, 227. However, this would only be the case if the patents were truly complementary. That said, the exemptions proposed in Part IV should also apply to two-way licence conditions (cross-licences) or multi-party licences (patent pools) which received no protection from section 51(3). Such arrangements should also be also beyond the reach of per se prohibitions.

4 Ian Harper, Peter Anderson, Su McCluskey and Michael O'Bryan, *Competition Policy Review* (Final Report, 6 March 2015) ('*Harper Report*').

5 Productivity Commission, *Inquiry Report: Intellectual Property Arrangements* (Report, 23 September 2016) ('*PC Report*').

by IP laws were not undercut by competition law, and that licensing is often the most effective way of commercialising IP,[6] section 51(3)(a) exempted the imposition of, and giving effect to, conditions in a licence, or attached to an assignment, of a patent, registered design, copyright, or eligible layout right, to the extent that the condition 'relates to' the IP or goods made using the IP. A more limited exception applied when it came to trade marks.[7]

The section 51(3) exception was limited in a number of ways. First, the exception did not apply to all prohibitions in Part IV. Conditions in licences were not exempt from the misuse of market power prohibitions (sections 46 and 46A) nor the resale price maintenance prohibition (section 48). Secondly, not all types of IP rights were covered by the exception. For example, the exception did not apply to unregistered trade marks, confidential information,[8] trade secrets and know-how. Thirdly, the exception only applied to conditions in licences or assignments, not the underlying agreements themselves. So, for example, if an acquisition would cause a substantial lessening of competition, the fact that a condition attached to the acquisition was taken beyond the scope of the *CCA* did not mean that the acquisition itself would not amount to a breach of section 50 of the *CCA*.[9] Fourthly, refusals to license IP rights were granted no exception.[10] Finally, leaving the limited exception provided to trade marks to one side, conditions in licences or assignments were only exempt to the extent to which they 'related to':

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6 In its report, the Intellectual Property and Competition Review Committee ('IPCRC') presented three reasons for this. One, initial owners of IP rights are often not best placed to commercialise their creative efforts. Two, in most instances IP rights do not map simply into products. Cross-licences are often required to ensure that technological inputs owned by multiple right holders can be put to productive use. Three, knowledge is non-rivalrous. Efficient licensing can prevent wasteful 'inventing around' existing knowledge: Intellectual Property and Competition Review Committee, *Review of Intellectual Property Legislation under the Competition Principles Agreement* (Final Report, September 2000) 210–11 <https://www.ipaustralia.gov.au/sites/g/ files/net856/f/ergas_report_september_2000.pdf.> ('*IPCRC Report*'). See also Justice Michael O'Bryan, 'The Repeal of s 51(3) of the Competition and Consumer Act 2010 (Cth)' (Speech, LESANZ Breakfast Meeting, 10 April 2019) 3 [10] <https://www.fedcourt.gov.au/__data/assets/rtf_file/0005/57848/OBryan-J-20190410.rtf>.

7 Section 51(3)(b) exempted provisions in a contract, arrangement or understanding authorising the use of a certification trade mark in accordance with rules applicable under Part XI of the *Trade Marks Act 1955* (Cth) ('*1955 Act*'). It seems that the reference to the *1955 Act* (rather than the current *Trade Marks Act 1995* (Cth)) is an oversight that survived the repeal of the *1955 Act* (see Hoad (n 3) 210). Section 51(3)(c) related to trade marks other than certification trade marks, and exempted provisions in contracts, arrangements or understandings between the registered proprietor of the trade mark and a registered user of the trade mark under Part IX of the *1955 Act* to the extent that the provision relates to the kinds, qualities or standards of goods bearing the mark that may be produced or supplied. Since the *Trade Marks Act 1995* (Cth) does not provide for the recording of registered users, the provision was ineffective well before the repeal of section 51(3).

8 *ASX Operations Pty Ltd v Pont Data Australia Pty Ltd (No 1)* (1990) 27 FCR 460, 471 (The Court).

9 Section 50 prohibits corporations from acquiring assets of a person (which includes natural persons and well as bodies corporate), as well as persons from acquiring assets of a corporation, if the acquisition would have the effect, or be likely to have the effect, of substantially lessening competition in any market.

10 A discussion of when a refusal to license IP should amount to a breach of competition law is beyond the scope of this article, given that section 51(3) provides no exemption to such refusals. Rather, this article focuses on when conditions attached to IP licences or assignments should result in competition law liability.

- the invention to which a patent relates, or articles made by use of that invention;
- goods in respect of which a design is registered and to which the design is applied;
- the work or other subject matter in which copyright subsists; or
- the eligible layout in respect of which eligible layout rights subsist.

The meaning of the words 'relates to' has been described as nebulous, vague and open-ended.[11] In its 1999 report,[12] the National Competition Council ('NCC') identified three potential meanings of the term 'relates to'. On a narrow reading, the condition must relate directly to the goods. On this view territorial restrictions, for example, would not be exempt as they relate to the market for goods, not the goods themselves.[13] On an intermediate reading, a condition relates to IP or the goods produced using the IP right if the condition seeks to 'secure an advantage that is not collateral to the [IP right holder's] exclusive rights'.[14] On this view, a territorial restriction would be protected by the exception as such control is inherent in the IP grant. On a broad reading, a condition relates to IP or the goods produced using the IP right unless 'it seeks to apply to an almost entirely unrelated transaction or arrangement'[15] (for example, it relates to the use of an IP right owned by the licensee).

The High Court has only once considered the meaning of the words 'relates to'. In *Transfield Pty Ltd v Arlo International Ltd* ('*Transfield*')[16] only three of the five judges who decided the case considered the section 51(3) argument and of those judges only one judge, Mason J, provided reasons for his conclusion. By way of obiter comment, Mason J noted:

> [i]n bridging the different policies of the *Patents Act* and the *Trade Practices Act*, s 51(3) recognizes 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. … Section 51(3) determines the scope of restrictions the patentee may properly impose on the use of the patent. *Conditions which seek to gain advantages collateral to the patent are not covered by s 51(3)*.[17]

Thus, Mason J adopted the intermediate view, namely that the 'relates to' requirement limited the exception to conditions that do not seek an advantage collateral to the scope of the grant by the relevant IP statute.

The Full Federal Court recently considered section 51(3) in *Australian Competition and Consumer Commission v Pfizer Australia Pty Ltd* ('Pfizer

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11 Ian Eagles and Louise Longdin, 'Competition in Information and Computer Technology Markets: Intellectual Property Licensing and Section 51(3) of the *Trade Practices Act 1974*' (2003) 3(1) *Queensland University of Technology Law and Justice Journal* 31, 31, quoted with approval in *Australian Competition and Consumer Commission v Pfizer Australia Pty Ltd* (2018) 356 ALR 582, 730 [598] (The Court) ('*Pfizer FC*').

12 National Competition Council, *Review of Sections 51(2) and 51(3) of the Trade Practices Act 1974* (Final Report, 5 March 1999) ('*NCC Final Report*'). See below nn 30–2 and accompanying text.

13 Ibid 184.

14 Ibid.

15 Ibid.

16 (1980) 144 CLR 83 ('*Transfield*'). For a more detailed discussion of *Transfield*, see Hoad (n 3) 211–12.

17 Ibid 102–3 (emphasis added).

FC').[18] The Australian Competition and Consumer Commission ('ACCC') alleged that Pfizer Australia Pty Ltd ('Pfizer') had engaged in bundling conduct in connection with the supply of atorvastatin in breach of sections 46 and 47 of the *CCA*. Pfizer raised section 51(3) in defence to the section 47 claim. As was the case in *Transfield*, the court's comments on section 51(3) are obiter, the Court having concluded that the section 47(1) claim failed as the ACCC had failed to prove that the bundling conduct was engaged in for the purpose of substantially lessening competition.[19]

By way of obiter comment, the Full Federal Court stated that section 51(3) did not apply for two reasons. First, the conditions in question were not conditions contained in a licence. Secondly, even if the impugned conditions were conditions contained in a licence, section 51(3) would still not have applied because the conditions did not 'relate to' the invention to which the atorvastatin patent relates, or articles made by the use of that invention. After referring to *Transfield*, the Full Court noted:

> [w]hilst atorvastatin tablets are articles to which the atorvastatin patent relates, the postulated conditions are not confined to the tablets being the *'... articles made by the use of the invention'*. As explained above, the postulated conditions impose restrictions on the ability of community pharmacies to deal with Pfizer's competitors. These are not conditions which deal with the subject matter of the intellectual property right itself, the atorvastatin tablets.[20]

The Full Court also agreed with the trial judge's observation that section 51(3) did not apply as the condition that prevents pharmacies from dealing with Pfizer's competitors seeks an advantage collateral to the IP grant.[21] That is, Pfizer's patent grant did not confer upon Pfizer the legal right to restrict its customers' ability to deal with others.

III THE LONG ROAD TO REPEAL

Whilst section 51(3) received scant judicial attention, it received a lot of attention from review committees.[22] Before considering the findings of these review committees, it is first necessary to understand that there are two types of competition law prohibitions. One, prohibitions that are subject to the competition test. Such prohibitions are only breached where the conduct to which the prohibition applies has the effect or likely effect of substantially lessening competition and/or the purpose of substantially lessening competition.[23] Two,

18 *Pfizer FC* (2018) 356 ALR 582, 730 (The Court).

19 The ACCC did not argue that the conduct had the effect or likely effect of substantially lessening competition.

20 *Pfizer FC* (2018) 356 ALR 582, 732 [606] (The Court) (emphasis in original).

21 Ibid 728 [588], 732 [604]–[606] (The Court).

22 Hoad (n 3) 215–18.

23 The section 45 prohibition against anticompetitive provisions in contracts, arrangements or understandings, the section 46 prohibition against the misuse of market power (which was not subject to the section 51(3) exception), the section 47 prohibition against exclusive dealing and the section 50 prohibition against anticompetitive acquisitions are all subject to the competition test (although section 50 is only breached where the acquisition has or is likely to have an anticompetitive effect).

prohibitions that prohibit conduct on a per se basis (that is, without the need to show that the conduct in question is likely to have anti-competitive effects or was engaged in for the purpose of harming competition).[24]

Those representing rights owners argued strongly in favour of the section 51(3) exception. For example, the Australian Recording Industry Association, in its submission to the recent Harper Review, argued that

> [t]he idea that there is no need for the s 51(3) exemption because IP should be treated like any other form of property is simplistic and misleading. The exemptions under s 51(3) serve partly as a safety net where broadly defined prohibitions under the Competition and Consumer Act would otherwise be too far-reaching. The cartel prohibitions, the prohibition against anticompetitive agreements under s 45 and the prohibition against exclusive dealing under s 47 are all broadly defined and can easily catch conduct that is efficiency enhancing ... The exemptions under s 51(3) are important because they avoid liability where IP licensing conditions are efficiency enhancing.[25]

Such arguments have either been rejected or only partly accepted by numerous review bodies. In 1984, the Industrial Property Advisory Committee ('IPAC') recommended that the section 51(3) exception be repealed, but, as a safeguard, to ensure that conditions in licences or assignments of patents only breach per se prohibitions (with the exception of resale price maintenance, a form of conduct to which the exception did not apply) if such conditions were shown to be likely to have anti-competitive effects or to have been included in the licence or assignment agreement for an anti-competitive purpose.[26] So, for example, if the condition amounted to price fixing, which is ordinarily prohibited per se, the condition would only be caught by the *CCA* if the price-fixing provision had the purpose, effect or likely effect of substantially lessening competition.

The Hilmer Committee conducted a comprehensive review of Australia's competition laws and released its report in 1993. The Committee 'saw force in arguments to reform [section 51(3)], including the possible removal of the current exemption and allowing all such matters to be scrutinised through the authorisation process'.[27] Ultimately, the Committee stated that it was not in a position to make expert recommendations on the matter and recommended instead that section 51(3) be examined by relevant officials, in consultation with interested groups.[28] In 1998, the NCC was commissioned to conduct an inquiry

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24 Cartel provisions (*CCA* ss 45AF, 45AG, 45AJ, 45AK), and resale price maintenance ('RPM') (*CCA* s 48) are prohibited per se. The section 51(3) exception did not apply to the RPM prohibition.

25 *Harper Report* (n 4) 106, quoting Australian Recording Industry Association Ltd, Submission to Competition Policy Review Panel, *Competition Policy Review* (10 June 2014) 4.

26 Industrial Property Advisory Committee, *Patents, Innovation and Competition in Australia* (29 August 1984), 25–6 ('*IPAC Report*'). Although the Committee's terms of reference related only to patents, its report stated that similar arguments may well apply to trade marks, designs and copyright: *IPAC Report* 26.

27 Independent Committee of Inquiry, *National Competition Policy* (Final Report, 25 August 1993) 151 ('*Hilmer Report*'). Re authorisation process, see below nn 78–85 and accompanying text.

28 Ibid.

solely in relation to sections 51(2)[29] and 51(3) as part of the Australian Government's review of legislation that restricts competition.[30] In its draft report, the NCC recommended that section 51(3) be repealed in its entirety. To the extent that dealings in IP rights were pro-competitive, exemption could be provided on a case by case basis under the administrative exemption procedures, authorisation and notification.[31] However, in its Final Report, the NCC made a less extreme proposal, namely, that section 51(3) be retained but amended to remove protection offered to price and quantity restrictions and horizontal agreements.[32] Some such arrangements, for example, price and quantity restrictions in agreements between competitors, are subject to per se treatment. Thus, the NCC's recommendation was to reduce the scope of section 51(3) to a much greater extent than the amendments proposed by the IPAC.

A further review was conducted by the Intellectual Property and Competition Review Committee ('IPCRC') in 2000. Submissions made to the IPCRC were largely opposed to the NCC's recommendations.[33] Concerns were expressed about the potential impact a repeal of section 51(3) (either total or partial, as recommended by the NCC) would have on incentives to innovate.[34] The IPCRC was of the view that the 'adoption of the NCC's proposals would amount to a repeal of the section'.[35] It recommended that section 51(3) be repealed and replaced with an amended version to ensure that a contravention of Part IV of the *CCA*

> 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 the intellectual property statute, so long as those conditions do not result, or are not likely to result in a substantial lessening of competition.[36]

This recommendation is in line with the recommendations of the IPAC in that whilst dealings in IP rights would not be subject to per se treatment, such dealings should not receive complete exemption and should be subject to competition law regulation where they had the purpose, effect or likely effect of substantially lessening competition.

In 2013, the House of Representatives Standing Committee on Infrastructure and Communications,[37] having found evidence of significant global price

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29 Section 51(2) provides for exemptions relating to employment conditions, standards approved by Standards Australia, partnership agreements, sale of business agreements and agreements relating exclusively to exports.

30 This review was undertaken as a result of the Competition Principles Agreement: *NCC Final Report* (n 12) v.

31 National Competition Council, *Review of Sections 51(2) and 51(3) of the Trade Practices Act 1974: Draft Report* (12 November 1998), 94, cited in Hoad (n 3) 215.

32 *NCC Final Report* (n 12) 243.

33 *IPCRC Report* (n 6) 208.

34 Ibid.

35 Ibid 213.

36 Ibid 215. See also Hoad (n 3) 217.

37 House of Representatives Standing Committee on Infrastructure and Communications, Parliament of Australia, *At What Cost: IT Pricing and the Australia Tax* (Report, July 2013), xiii (Recommendation 8) <http://www.aphref.aph.gov.au/house/committee/ic/itpricing/report/fullreport.pdf>.

discrimination against Australian consumers and businesses, recommended the repeal of section 51(3). Also in 2013, the Australian Law Reform Commission's Copyright and Digital Economy Final Report recommended that 'the repeal of s 51(3) should be considered, as an integral aspect of equipping copyright law for the digital economy'.[38]

The section 51(3) exception was recently considered by the Harper Committee,[39] who, like the Hilmer Committee, undertook a root and branch review of Australia's competition laws. In its report, handed down in 2015, the Harper Committee noted that '*as is the case with other vertical supply arrangements*, IP licences should remain exempt from the per se cartel provisions of the *CCA* insofar as they impose restrictions on goods or services produced through the application of the licensed IP'.[40] The Harper Committee recommended the addition of a general exception from the per se cartel provisions for vertical supply/acquisition agreements between competitors ('Vertical Supply/Acquisition Exception').[41] For this reason, the Harper Committee ultimately recommended that section 51(3) should be repealed[42] rather than amended to remove per se treatment of dealings in IP rights. Thus, it is not accurate to say that the repeal of section 51(3) implements the Harper Committee's recommendations. The Harper Committee only recommended that section 51(3) be repealed because the Committee believed that the proposed Vertical Supply/Acquisition Exception offered adequate protection against per se treatment of conditions in IP licences or assignment agreements.

The Government response to the Harper Committee's recommendations was silent when it came to the recommended Vertical Supply/Acquisition Exception.[43] Despite this, the Vertical Supply/Acquisition Exception was included in the exposure draft of the Bill which would implement the Harper Committee's recommendations (other than those that related to section 46).[44] In response to concerns about the breadth of the exception, it was removed from the Bill that ultimately went before Parliament so that the exception could 'be given further consideration and progressed in a future legislative package'.[45]

In its response to the *Harper Report* recommendation that section 51(3) be repealed, the Government noted the recommendation and stated that it would have regard to the findings of the Productivity Commission's inquiry into

38 Australian Law Reform Commission, *Copyright and the Digital Economy* (ALRC Report 122, 29 November 2013), 74 [3.98].

39 *Harper Report* (n 4) ch 9.

40 Ibid 42 [2.5] (emphasis added).

41 Ibid 59 (Recommendation 27). The need for such an exemption was recognised well before the Harper Committee made its recommendation: see Caron Beaton-Wells and Brent Fisse, *Australian Cartel Regulation: Law, Policy and Practice in an International Context* (Cambridge University Press, 2011), 303–8 [8.6].

42 *Harper Report* (n 4) 42 (Recommendation 7).

43 Australian Government, *Australian Government Response to the Competition Policy Review* (24 November 2015) 23 <https://treasury.gov.au/sites/default/files/2019-03/Govt_response_CPR.pdf> ('*Government Harper Response*').

44 Competition and Consumer Amendment (Competition Policy Review) Bill 2017 (Cth).

45 Explanatory Memorandum, Competition and Consumer Amendment (Competition Policy Review) Bill 2017 (Cth) 139 [15.57].

Australia's IP arrangements.[46] In its 2016 *Inquiry Report: Intellectual Property Arrangements*, the Productivity Commission noted that the 'per se prohibitions have been a brake on the repeal of section 51(3)'.[47] The report also notes that '[r]eforming per se provisions in the *CCA* along the lines suggested by the [*Harper Report*] would address legitimate concerns that socially valuable activities are not impeded'.[48] Ultimately, the Productivity Commission recommended that the Government 'should repeal s 51(3) of the [*CCA*] at the same time as giving effect to recommendations of the (Harper) Competition Policy Review on per se prohibitions'.[49] However, it is not clear that the Productivity Commission appreciated the nature of the Harper Committee's recommendations. In the paragraph immediately preceding the Productivity Commission's recommendation that section 51(3) be repealed, the Commission stated that

> [the Harper Committee] considered each of the per se prohibitions and recommended either a competition test (with respect to price fixing and third line forcing) or repeal (with respect to exclusionary conduct). While not the primary motivation of the [Harper Committee], giving effect to these recommendations would remove the remaining impediment to the repeal of s 51(3).[50]

The Harper Committee did not recommend that the per se cartel prohibitions and offences (such as the prohibition against price fixing) be subject to the competition test. It did recommend the repeal of the per se prohibition against exclusionary provisions but also recommended that the definition of cartel provision in section 45AD be amended to fill the gap in coverage. The only form of conduct that the Harper Committee recommended be subjected to the competition test instead of per se treatment is third-line forcing (a form of exclusive dealing). A generous interpretation of the Productivity Commission's qualified recommendation would be that the Productivity Commission recommended repeal only if the Vertical Supply/Acquisition Exception was added to the *CCA*. The Productivity Commission's report makes no mention of this proposed exception,[51] however, the Harper Committee's recommendations relating to the cartel provisions (including the recommendation that a general exception be introduced) are extracted in the report.

The Explanatory Memorandum that accompanied the Treasury Laws Amendment (2018 Measures No 5) Bill 2018 (Cth) cited the recommendations of both the Harper Committee and the Productivity Commission in support of the repeal of s 51(3).[52] However, it seems that, as Brent Fisse has put it, '[t]he Harper

46 *Government Harper Response* (n 43) 9. The Productivity Commission was tasked, at the recommendation of the Harper Committee, with undertaking an overarching review of intellectual property, focusing on competition policy issues arising from new developments in technology and markets: *Harper Report* (n 4) 41 (Recommendation 6).

47 *PC Report* (n 5) 455.

48 Ibid 443.

49 Ibid 457.

50 Ibid 455.

51 Other than when it reproduces the Harper Committee's recommendation 27 verbatim.

52 Explanatory Memorandum, Treasury Laws Amendment (2018 Measures No 5) Bill 2018 (Cth) 31 [4.3].

Report implementation process has broken down'.[53] The decision to repeal section 51(3) was made on the basis of an inaccurate belief that the Harper Committee made an unqualified recommendation that section 51(3) be repealed when in fact the recommendation was only made because the Harper Committee believed appropriate protection to conditions in IP licences and assignments would be offered by the proposed Vertical Supply/Acquisition Exception. The Government also appears to have overlooked the fact that the Productivity Commission's recommendation was also qualified. Whilst the Productivity Commission's recommendation may be based on a misunderstanding of the recommendations made by the Harper Committee regarding per se prohibitions, the Commission's ultimate recommendation was that the Government should repeal section 51(3) 'at the same time as giving effect to recommendations of the (Harper) Competition Policy Review on the per se prohibitions'.[54] One of the Harper Committee's recommendations was the implementation of the Vertical Supply/Acquisition Exception. Contrary to the outcome intended by the Harper Committee, conditions in IP licences and assignments that were protected by section 51(3) may now be subject to per se treatment even though this could result in legitimate, pro-competitive conditions being inappropriately caught by competition law. That this would be an inappropriate outcome was recognised by the IPAC in 1984 and the IPCRC in 2000, but also by the Harper Committee and the Productivity Commission upon whose recommendations the Government ultimately acted.

IV THE NEED FOR AN EXCEPTION

A Overview

This Part of the article develops an argument that there is a need for some form of exception for dealings in IP rights. First, the potential for dealings in IP rights to be caught by the per se cartel prohibitions is considered. Then, an argument is developed that such treatment is inappropriate given that the relationship between the licensor and licensee typically has both a horizontal and vertical dimension and that the traditional justification for per se prohibitions is thus not met in the case of IP licences.

B Per Se Liability Resulting from the Repeal of Section 51(3)

As foreshadowed in the discussion in Part II, some conditions in agreements that were exempted by section 51(3) are now subject to competition law. This is of particular concern where the licensee and licensor are competitors as certain dealings between competitors are caught by per se civil and criminal cartel

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53 Brent Fisse, 'Harper Report Implementation Breakdown: Repeal of Section 51(3) of *Competition and Consumer Act 2010* (Cth) and Lack of Proposed Supply/Acquisition Agreement Cartel Exception' (2019) 47(1) *Australian Business Law Review* 127, 127.

54 *PC Report* (n 5) 37 (Recommendation 15.1).

prohibitions.[55] A condition in an IP licence that is benign or pro-competitive will be caught if the condition falls within the section 45AD definition of cartel provision and the licensor and licensee are competitors, whatever the effects of that condition on competition.

If the IP owner does not exploit the IP rights to supply goods and/or services, the licensor and licensee are unlikely to be found to be competitors. However, where the licensee is granted a non-exclusive licence and the licensor retains the ability to use the IP in question, the licensor and licensee may be held to be competitors or likely competitors.[56] As Justice Michael O'Bryan has noted:

> [d]ifficult questions will arise where the owner of intellectual property exploits the rights to supply goods or services … but, at the time the licence is entered into, the licensee is not a competitor in respect of the supply of those goods or services and is not likely to be a competitor. It is yet to be determined how the cartel prohibitions apply to licence arrangements between persons who are not competitors at the time the licence is entered into, but have the potential to be competitors by reason of the licence.[57]

The licensor and licensee will be competitors if the licence includes a provision preventing the licensor from competing with the licensee (that is, if the arrangement is that whilst further licences may be granted, the licensor itself will not make use of the IP right).[58] Even if the licensee is granted an exclusive licence, where the licensor produces substitutable goods made without using the IP that has been licensed, the licensor and licensee are actual or likely competitors.

Section 51(3) took conditions that relate to the IP rights, or goods or services made or provided using an IP right, beyond the reach of some competition law prohibitions, even where the conditions are contained in agreements between competitors. Take by way of example an agreement, between a licensor and a licensee who are in competition with each other, as to the price that will be charged for articles made by use of the invention to which a patent relates. If the licensor did not grant a licence, it would be able to control the price at which it supplied the patented goods. Thus, the price condition does not seek to extract a collateral advantage and section 51(3) would apply.[59] The same is true of territorial or quota restrictions that relate solely to such articles.[60]

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55 Division 1 of Part IV of the *CCA* prohibits, by way of criminal offence and civil penalty prohibition, the making of a contract or arrangement, or arriving at an understanding, that contains a cartel provision (s 45AF (criminal), s 45AJ (civil)). Giving effect to a cartel provision contained in a contract, arrangement or understanding is also prohibited (s 45AG (criminal), s 45 AK (civil)). The term 'cartel provision' is defined in section 45AD. The provision must either fix prices (s 45AD(2)), restrict output (s 45AD(3)(a)), allocate markets (s 45AD(3)(b)), or rig bids (s 45AD(3)(c)). Further, two or more parties to the contract, arrangement or understanding containing the cartel provision must compete, in trade or commerce, with respect to the supply or acquisition of the goods or services to which the provision relates (s 45AD(4)).

56 *CCA* s 45AD(4)(a). See O'Bryan (n 6) 4 [13].

57 O'Bryan (n 6) 6 [20].

58 *CCA* s 45AD(4)(b).

59 WMC Gummow, 'Abuse of Monopoly: Industrial Property and Trade Practices Control' (1976) 7(3) *Sydney Law Review* 339, 349.

60 Ibid 358–9. See also *Hilmer Report* (n 27) 150; *NCC Final Report* (n 12) 151, 212; *Harper Report* (n 4) 109.

C Reason for Concern

As section 51(3) has been repealed, the inclusion of price, territorial or quota restrictions in IP licences may now result in the licensor and the licensee facing per se civil or criminal liability for breaching the cartel prohibitions unless the anti-overlap provisions, discussed below, apply.[61] This is true even though such restrictions are often imposed by a licensor without substantial market power, do not involve an attempt to extend the IP grant, and limit intra-brand, not inter-brand competition.[62] The per se nature of the cartel prohibitions makes the factors listed in the previous sentence irrelevant to the question of liability.

It is widely accepted that collusion between competitors is, to quote the United States Supreme Court, 'the supreme evil of antitrust'.[63] Why then, is it of concern that price, quota and territorial restrictions in agreements between a licensor and licensee that compete with each other might be caught by competition law on a per se basis? The reason is that unlike a typical cartel, there is a not only a horizontal aspect to the agreement (an agreement between competitors) but also a vertical aspect as well (an agreement between a supplier and acquirer of IP). The licensor is not only a competitor of the licensee, it is also supplying the IP right to the licensee. Given that vertical arrangements carry a significantly lower risk of harming competition, and in fact may promote competition,[64] it is not appropriate to subject dealings that have both a horizontal and vertical aspect to them to per se treatment.[65] The Harper Committee, recognised this and specifically noted that 'as is the case with other vertical supply arrangements, IP licences should remain exempt from the per se cartel provisions'.[66] Even the ACCC, which expressed concerns about IP licence terms in its submission to the Productivity Commission, acknowledged that 'the competitive effects of [price and quota] restrictions depend on the characteristics of the market in which the licensing occurs and/or has an effect'.[67] Although the ACCC is of the opinion that such market characteristics should be taken into account under the authorisation process, it must be noted that such characteristics would be considered by a court when applying the competition test.

Per se treatment is only justified in limited circumstances. In *Leegin Creative Leather Products v PSKS*, Justice Kennedy made the following observation:

> Resort to per se rules is confined to restraints … that would *always or almost always* tend to restrict competition and decrease output … To justify a per se

61 There is also the possibility that such conduct would breach sections 45 and 46 of the *CCA*, however, the cartel prohibitions are of greater concern given they are per se prohibitions. For further examples, see Fisse (n 53) 132–5.

62 See below nn 155–8 and accompanying text.

63 *Verizon Communications v Law Offices of Curtis V Trinko,* 540 US 398, 408 (Scalia J) (2004).

64 See below nn 151–4 and accompanying text.

65 *Harper Report* (n 4) 364.

66 Ibid 42.

67 Australian Competition and Consumer Commission, Submission to Productivity Commission, *Inquiry into Intellectual Property Arrangements in Australia* (November 2015) 9 <https://www.accc.gov.au/system/files/ACCC%20Submission%20-%20PC%20inquiry%20into%20IP%20arrangements%20in%20Australia%20-%2030%20November.pdf>.

> prohibition a restraint must have *manifestly anticompetitive effects* … and *lack any redeeming virtue*.[68]

Whilst in many instances agreements between competitors as to price, territories or production or acquisition will meet this test, there are situations where this is not the case and, therefore, where some form of exception is justified. For example, the *CCA* includes exceptions from the cartel prohibitions for joint ventures[69] and collective acquisitions.[70] As it cannot be said that price, territory or production conditions in IP licences are manifestly anti-competitive, there is a need for an exception to be added to the *CCA* that exempts such conditions from per se treatment.

V CRAFTING AN APPROPRIATE EXCEPTION

A Overview

The risk that conditions in IP licences or assignments might be caught by per se prohibitions, even where they are benign or pro-competitive, suggests that there is a need for some form of exception. This Part starts by considering existing mechanisms that may protect dealings in IP rights from per se treatment, namely the anti-overlap provisions and two administrative exemption processes, authorisation and block exemptions. A conclusion is reached that, despite these mechanisms, there is a need for an exception of some kind to protect dealings in IP rights from per se treatment. This could be provided by introducing an IP-specific exception (different in form to section 51(3)) or a general exception for vertical supply/acquisition agreements between competitors.

B Existing Mechanisms

1 Anti-Overlap Provisions

The need to treat agreements that have both a horizontal and vertical dimension differently from agreements that have only a horizontal dimension is already recognised in the *CCA*. Longstanding provisions in the *CCA* take some dealings that have both a vertical and a horizontal aspect beyond the reach of the cartel provisions. As originally enacted, the *Trade Practices Act 1974* (Cth) (which was renamed the *CCA* on 1 January 2011),[71] included anti-overlap provisions designed to shield vertical conduct from per se treatment.[72] Such provisions are also found in the current *CCA*. If the making or giving effect to a provision in a contract, arrangement or understanding involves exclusive dealing[73] or resale price maintenance[74] then it will be beyond the reach of the cartel prohibitions as a result of the anti-overlap provisions.[75]

68 551 US 877, 886 (2007) (emphasis added).
69 *CCA* s 45AO (criminal cartel offences), s 45AP (civil cartel prohibitions).
70 Ibid s 45AU.
71 *Trade Practices Amendment (Australian Consumer Law) Act 2010 (No 2)* (Cth) sch 5.
72 *Trade Practices Act 1974* (Cth) s 45(5)(a) (as originally enacted).
73 Defined in *CCA* ss 47(2)–(9).

The highly prescriptive way in which 'exclusive dealing' and 'resale price maintenance' are defined means that the anti-overlap provisions do not cover all forms of vertical supply restrictions. The provisions are unlikely to apply to the price, territorial and quota conditions in IP licences. The licensor is supplying the IP but imposing a price, quota or territorial restriction on goods made using that IP. Resale price maintenance involves the specification of a minimum price to be charged for goods or services supplied by the supplier. In the case of a licence to use an IP right, the licensor does not manufacture the IP protected goods and supply them to the licensee subject to a minimum price condition. Thus, price, territorial or quota conditions of the kind under condition are not caught by the definition of resale price maintenance.[76] Similarly, the definition of exclusive dealing only catches conditions that restrict the acquirer's right to acquire goods from, or re-supply the goods of, a competitor of the licensor or to *re-supply* goods or services supplied by the licensor in particular places or to particular customer groups.[77]

2 Authorisation

The main argument that goes against the need to introduce a further exception is that per se liability could be avoided, and market characteristics considered, under administrative regimes which allow the ACCC to exempt conduct on a case-by-case basis. Part VII of the *CCA* establishes two administrative regimes (authorisation and notification) that allow parties to seek exemption.[78]

Under the authorisation regime, upon application by a party or parties,[79] the ACCC can grant exemption from all Part IV prohibitions if satisfied that the conduct would result, or be likely to result, in a benefit to the public that would outweigh the detriment to the public that would result, or be likely to result, from the conduct (the public benefit test).[80] In addition, the ACCC may grant authorisation with respect to liability under a competition-tested prohibition where the conduct would not have the effect, or would not be likely to have the effect, of substantially lessening competition.[81] Conduct that is prohibited on a

74 Defined in ibid s 96(3).

75 Ibid s 45AQ (RPM), s 45AR (exclusive dealing).

76 The specification of a minimum price at which a sub-licence could be granted would be caught by the definition of RPM.

77 *CCA* s 47(2)(f)(ii). See also O'Bryan (n 6) 5 [15].

78 The following discussion focuses on the authorisation regime. The notification regime applies only to exclusive dealing, resale price maintenance and collective bargaining: *CCA* pt VII, div 2. For reasons discussed earlier, the types of conditions in licences under consideration do not amount to exclusive dealing or resale price maintenance (see above nn 76–7 and accompanying text), nor do they involve the licensor and licensee collectively bargaining with a third party.

79 Authorisation cannot be granted retrospectively: *CCA* s 88(6).

80 Ibid s 90(7)(b).

81 Ibid s 90(7)(a). In such circumstances it is more accurate to describe the authorisation as providing comfort to the parties, rather than exempting the conduct, given that breach of a competition tested prohibition will only occur in the uncommon situation where despite a lack of competitive harm, the firm acts for an anticompetitive purpose.

per se basis cannot be authorised on this basis. It can only be authorised where the public benefit test is met.[82]

As discussed earlier, recommendations to repeal section 51(3) have often been justified on the basis that exemption for licensing agreements may be gained via the authorisation.[83] Most recently, the Harper Committee, in support of its recommendation to repeal section 51(3), noted that 'IP licensing or assignment arrangements that are at risk of breaching Part IV of the *CCA* … but which are likely to produce offsetting public benefits, can be granted an exemption from the *CCA* through the notification or authorisation processes'.[84] Further, the Explanatory Memorandum to the *Section 51(3) Amending Act* noted that the delayed commencement of the repeal of section 51(3) 'will give individuals and businesses time to review existing arrangements [and] … [i]f necessary … apply to the Australian Competition and Consumer Commission for authorisation of their existing arrangements'.[85]

Where an authorisation application is made, the competitive effects of the particular licence conditions will be thoroughly examined as is the case under the competition test. Further, the concepts of 'public benefit' and 'public detriment' can accommodate arguments that a condition is unlikely to cause competitive harm (suggesting that public detriment is low) as well as arguments that exempting the condition from competition laws could, in fact, be pro-competitive and/or necessary to preserve incentives to innovate created by IP laws (both of which could be cast as public benefits).

However, there are reasons that authorisation should not be the sole basis on which exemption is provided to IP licences or assignments. There are considerable costs associated with making an authorisation application.[86] Filing fees are significant ($7,500 for a non-merger application)[87] and the cost of preparing applications (which often involves the input of lawyers and economists) can be significantly higher.[88] Further, the ACCC has been criticised for 'lack of transparency and accountability, for uncertainty in the way it applies

82 Ibid s 90(8).

83 As noted earlier, the Hilmer Committee saw force in the argument that section 51(3) should be removed and dealings in IP be scrutinised through the authorisation process: see above n 27 and accompanying text. In its draft report on section 51(3), the NCC recommended that section 51(3) be repealed and that, to the extent to which dealings in IP were pro-competitive, exemption could be provided on a case by case basis under the administrative exemption authorisation and notification procedures: see above n 31 and accompanying text.

84 *Harper Report* (n 4) 42.

85 Explanatory Memorandum, Treasury Laws Amendment (2018 Measures No 5) Bill 2018 (Cth) 32 [4.11].

86 Submissions made to the IPCRC expressed concerns about the cost, delay and difficulties in using the authorisation and notification procedures and the potentially detrimental effect these processes may have on investment and innovation: *IPCRC Report* (n 6) 208.

87 *Competition and Consumer Regulations 2010* (Cth) sch 1B.

88 It is difficult to find information about the costs of making an authorisation application as such costs are borne by private parties and are not typically disclosed. Although dated, the submission made by the Australian Copyright Council ('ACC') to the NCC review provides some guidance. Some 20 years ago, the ACC submitted that the costs of preparing applications often run in the order of $50,000–100,000. This figure excludes the opportunity costs associated with the need for company personnel to be involved in the process: *NCC Final Report* (n 12) 223.

the law, and for a commercially unrealistic application of the law'[89] when determining authorisation applications. The authorisation process can also be inflexible. Exemption is only provided to the precise form of conduct specified in the authorisation application. If the parties replace a condition that has been authorised with a slightly different provision, it will be necessary to apply to vary the authorisation in order for the new condition to be exempt. This is so even where the authorised condition is likely to generate the same level of public benefits and public detriments as the new condition.

Further, the availability of authorisation does not automatically justify exposing IP licensing practices to per se liability. Authorisation must not be thought of as a fallback mechanism that protects against overly broad competition law prohibitions.[90] The authorisation regime is intended to address market failure, not overly broad prohibitions, as evidenced by the following statement by the Trade Practices Tribunal in *Re 7-Eleven Stores Pty Ltd*:

> [T]he very existence of authorisation points to the recognition that there may be *exceptional circumstances* in which business conduct *associated with a lessening of competition* may have value to society.[91]

Thus, in the IP context, the type of conduct that the authorisation regime is designed to deal with is conduct that has an anti-competitive effect (public detriment) but is necessary to ensure the incentives to innovate created by the IP regimes, which are designed to overcome market failure caused by the public goods nature of IP, are maintained. For example, where a pharmaceutical company refuses to license a powerful patent to a generic manufacturer, this will arguably lessen competition in that it will preserve the pharmaceutical company's monopoly position in the market. However, such a refusal could be authorised on the basis that despite the anti-competitive effects of the refusal, it is necessary to ensure that incentives to innovate created by IP laws are preserved. The existence of the authorisation regime should not be relied upon to justify imposing per se liability in situations where the law could be crafted so as not to catch conduct unlikely to harm competition.

3 Class Exemptions

On 6 November 2017, implementing a recommendation of the Harper Committee, the ACCC was given the power to issue, by way of legislative instrument, class exemptions for specific types of business conduct.[92] Where a class exemption is issued, this will remove the need for individual businesses to apply for authorisation in order to engage in conduct specified in the class

89 Christine Parker and Vibeke Lehmann Nielsen, 'What Do Australian Businesses Really Think of the ACCC, and Does it Matter?' (2007) 35(2) *Federal Law Review* 187, 217. See also Trade Practices Act Review Committee, *Review of the Competition Provisions on the Trade Practices Act* (Final Report, 16 April 2003) 49.

90 Authorisation does not exist in other competition law regimes. This has resulted in greater care being taken to avoid overreach of competition law prohibitions. See Beaton-Wells and Fisse (n 41) 327–8 [8.13.3].

91 (1994) ATPR ¶41-357, 42677 (emphasis added).

92 *CCA* s 95AA(1).

exemption. As noted in the *Harper Report*, 'the block exemption power … could be used to specify 'safe harbour' licensing restrictions for IP owners'.[93]

Should a class exemption of sufficient breadth and clarity relating to conditions in IP licences be issued by the ACCC, this would overcome concerns about the costliness and timeliness of the authorisation procedure. Further, a class exemption from the per se prohibitions can be issued where the ACCC forms the opinion that conduct would not have the effect, or be likely to have the effect, of substantially lessening competition or where the public benefit test is met.[94] However, before the class exemption regime can be said to overcome the need for some form of exemption in the *CCA* for dealings in IP rights, it is necessary to reflect on two matters. First, is the ACCC likely to use its powers to exempt certain dealings in IP rights? Secondly, if it does, would a conservative approach be adopted?

Dealing with the first matter, the ACCC demonstrated a willingness to use class exemption powers in relation to IP rights in a submission to the Harper Review which stated:

> Should a block exemption provision be introduced, it could be used to clarify the scope of permissible conduct relating to the exercise of intellectual property rights, thereby providing additional certainty for business.[95]

The above statement was made in support of the ACCC's position that section 51(3) should be repealed. However, despite section 51(3)'s repeal, there is nothing to suggest that the ACCC has plans to issue such a class exemption.[96] In an update issued by the ACCC on 9 April 2019 about the repeal of section 51(3), no mention is made of the possible development of class exemptions, the ACCC indicating that its 'immediate focus is on compliance activities to ensure that businesses understand their new obligations under the *CCA*'.[97] On 21 June 2019, the ACCC issued draft guidelines which outline how the ACCC proposes to investigate and enforce Part IV in relation to conduct involving IP rights. The guidelines refer to the class exemption power but give no indication of whether, or how, the ACCC will use such powers to exempt certain dealings in IP, noting

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93 *Harper Report* (n 4) 42.

94 *CCA* s 95AA(1).

95 Australian Competition and Consumer Commission, Draft Submission to Competition Policy Review Panel, Competition Policy Review (26 November 2014) 22 ('ACCC Draft Submission'), quoted in *Harper Report* (n 4) 110. Page 67 of the ACCC Draft Submission, quoted in *Harper Report* (n 4) 404, noted that class exemptions could be used in relation to IP licences.

96 To date, the ACCC has only announced an intention to develop a collective bargaining class exemption. On 23 August 2018 the ACCC released a Discussion Paper seeking feedback on its proposal to introduce a collective bargaining class exemption. On 6 June 2019, the ACCC released a draft collective bargaining exemption notice, a draft guidance note, and a draft legislative instrument. Submissions about the drafts were received in June and July 2019. At the time of writing, the ACCC was yet to make a final decision about the class exemption. See 'Collective Bargaining Class Exemption' *ACCC* (Web Page, 23 August 2018) <https://www.accc.gov.au/public-registers/class-exemptions-register/collective-bargaining-class-exemption>.

97 See Australian Competition and Consumer Commission, 'Removal of the IP Exemption in s 51(3) of the CCA' (Media Release, 9 April 2019) <https://www.accc.gov.au/update/removal-of-the-ip-exemption-in-s513-of-the-cca>.

only that '[t]he ACCC will identify kinds of conduct that may appropriately be the subject of a class exemption'.[98]

It is worth noting that the ACCC's submission to the Harper Committee referred to providing certainty to businesses dealing in IP rights, not exemption. Further, the ACCC has on several occasions made statements that suggest that it is of the view that dealings in IP rights should not receive exemption. For example, in its submission to the IPCRC, the ACCC stated that it 'considered that IP rights should be accorded the same treatment as any other property rights'.[99] A similar sentiment is evident in the ACCC's submission to the Harper Committee in which it stated:

> On the *use* of intellectual property rights, the *CCA* should apply in the ordinary way. The ACCC recommends that section 51(3) of the *CCA* should be repealed and that, in general, there is no reason to treat intellectual property any differently to other services in relation to access.[100]

Even if the ACCC were to issue a class exemption in relation to conditions in IP licences, there is reason to suspect that the ACCC may adopt a conservative approach to the granting of exemption. The statements that suggest that the ACCC may not exercise its class exemption powers in relation to IP licences also suggest that, if it did do so, any exemption is likely to be narrow.

A conservative approach has been adopted in the European Union which it comes to exempting IP licences from competition law. The European Commission has the power to issue block exemptions and has exercised this power to provide technology transfer agreements exemption from the European prohibition against anti-competitive agreements. The current Technology Transfer Block Exemption Regulation ('TTBER') provides a safe harbour to certain IP licensing practices. The TTBER applies only to 'technology rights' such as software copyright, patents and know how; other IP rights are not covered. Further, only transfer agreements between two parties are covered and the agreement must be for the purpose of producing goods or services that exploit the IP right in question. Even if the agreement meets these requirements, the TTBER will only apply to agreements between competitors where the combined market share of those competitors is below 20%.[101] Most relevant for present purposes is that 'hardcore' restrictions will not benefit from the exemption created by the TTBER. In relation to agreements between competitors, hardcore restrictions include price-fixing, output restrictions and territorial restrictions. The European Commission is of the opinion that individual assessment of such conditions is required. Given the ACCC's views that IP rights should be accorded the same treatment as other property rights, it seems likely that should the ACCC choose to grant some form of class

98 Australian Competition and Consumer Commission, *Draft Guidelines on the Repeal of Subsection 51(3) of the Competition and Consumer Act 2010 (Cth)* (Guidelines, 21 June 2019) [6.12].

99 *IPCRC Report* (n 6) 209.

100 Australian Competition and Consumer Commission, Submission to Competition Policy Review Panel, *Competition Policy Review* (25 June 2014) 58, quoted in *Harper Report* (n 4) 105.

101 *Commission Regulation (EU) No 316/2014 of 21 March 2014 on the Application of Article 101(3) of the Treaty on the Functioning of the European Union to Categories of Technology Transfer Agreements* [2014] OJ L 93/17, art 3.1.

exemption, it would also be quite conservative when it comes to granting exemption, especially given that exemption can be granted on a case-by-case basis under the authorisation regime.

C New Exception

A statutory exception is necessary to obviate the need for 'expensive investigations into the acceptability, or not, of particular negotiated positions reflected in licensing agreements'[102] under the authorisation procedure, which was designed to provide exemption in instances of market failure, not to correct over-reaching competition law prohibitions. The inclusion of such an exception in the *CCA* would also overcome the uncertainty as to whether the ACCC will issue a class exemption of sufficient breadth and clarity to resolve concerns of overreach.

1 Key Requirements of the Exception

The exception could take one of two forms, both of which have been foreshadowed by earlier discussion. One would apply specifically to conditions in IP licences, but different in form to section 51(3). The other would provide a general exception from the per se cartel provisions for vertical supply/acquisition agreements between competitors like that proposed by the Harper Committee.[103] Given that the need to exempt conditions in one-way IP licences stems from the fact that such arrangements often have a vertical aspect as well as a horizontal aspect, and from the limited nature of the existing anti-overlap provisions, there is merit to the argument that it would be preferable to exempt conditions in IP licences from per se treatment by introducing a general vertical supply/acquisition exception. However, there are advantages to introducing an IP-specific exception. Such an exception could not only protect conditions in one-way IP licences that do not seek a collateral advantage, which would have been protected by section 51(3) and are thus the focus of this article, from per se treatment but could also offer exemption to conditions in one-way licences that seek a collateral advantage but are not inherently anti-competitive (such as cross-licences, no challenge clauses or grant-back clauses) as well as multi-party agreements (such as patent pools).

Whichever form the exception takes, it should not provide complete exemption. It should, consistent with the recommendations of the IPAC,[104] IPCRC[105] and the Harper Committee[106], ensure that conditions in IP licences contravene the *CCA* only where the condition has the purpose, effect or likely effect of substantially lessening competition. However, it would not be appropriate to require the licensor or licensee to prove that the licence condition

102 *IPCRC Report* (n 6) 208.

103 See *Harper Report* (n 4) 67 (Recommendation 27). See above n 41–2 and accompanying text. For a discussion of the weaknesses of the specific exemption proposed by the Harper Committee, see Fisse (n 53) 128–30.

104 See above n 26 and accompanying text.

105 See above n 33 and accompanying text.

106 See above n 39 and accompanying text.

does not have such a purpose, effect or likely effect in order to invoke the exemption. Rather, as Fisse has argued in relation to the joint venture exemption, the exemption should apply unless 'the dominant purpose of the party relying on the exemption is to lessen competition between any 2 or more parties'.[107] This would mean that those seeking to invoke the exception would not need to prove the scope of the market and the likely effects of the condition in the market. Where the exception applies, the licence conditions would continue to be subject to other prohibitions (in particular sections 45 and 47) that contain the competition test. The party challenging the licence condition (whether that be the ACCC or an affected private party) would then bear the onus of establishing that the licence condition has an anti-competitive purpose or effect.

2 IP Exception

Should an IP specific exemption be reintroduced, it would not be appropriate to simply reinstate section 51(3). Firstly, there is uncertainty as to the meaning of the 'relates to' requirement used to delineate when the exemption applies.[108] Secondly, section 51(3) went further than necessary in that it provided a complete exemption, that is, where it applied it exempted conditions even if they had or were likely to have the effect of substantially lessening competition. It would be sufficient if the effect of an IP exception was to remove per se liability so that conditions would be caught only where they have the purpose, effect or likely effect of substantially lessening competition. To the extent that such liability threatens incentives created by IP regimes designed to correct market failure, exemption could be provided under the authorisation or class exemption processes.

At the very least, the IP exception should be designed to apply where a condition in an IP licence does not attempt to seek an advantage collateral to those conferred by the IP grant. It would be preferable if the scope of such an exception was not determined by asking whether the condition 'relates to' the IP. As the discussion in Part II demonstrates, this is an inherently vague requirement. The 'relates to' requirement could be replaced by a requirement that the condition not seek an advantage 'collateral to' the IP grant (endorsing the approach taken by Mason J in *Transfield*). This would make it clear that the exemption applies to conditions in one-way licences that were likely protected by section 51(3) (such as price, quota or territorial restrictions imposed on a licensee, which have been the focus of this article).

Making the exemption only available where no collateral advantage is sought would mean that two-way licence conditions (such as grant-back restrictions, no-challenge provisions, anti-cloning restrictions and cross-licences) and multi-party licences (such as patent pools) would continue to receive no exemption.[109] A

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107 Brent Fisse, 'Australian Cartel Law Biopsies' (Conference Paper, Competition Law Conference, Sydney, 5 May 2018) 25 <https://www.brentfisse.com/images/Australian_Cartel_Law_ Biopsies_050518_2.pdf>.

108 See above nn 11–21 and accompanying text.

109 Regarding grant-back clauses, see Fisse (n 53) 134–5, Hoad (n 3) 224–5; no challenge clauses see Fisse (n 53) 133–4, Hoad (n 3) 225–6; anti-cloning restrictions see Fisse (n 53) 135; cross-licences and patent pools see Hoad (n 3) 227–8.

detailed discussion of the competition law treatment of such provisions is beyond the scope of this article, which focuses on conditions in one-way licences that were exempt under section 51(3). However, it is submitted that per se treatment of such two-way licence conditions is also inappropriate as such conditions are not inherently anti-competitive. An IP specific exemption could be drafted more broadly so that it also applied to such conditions even though they seek an advantage collateral to the IP grant. After all, cross-licences and patent pools, for example, are often necessary to enable products or services to be brought to market[110] and thus should only be prohibited where they have anti-competitive effects or are motivated by anti-competitive purposes.

The exemption could be given a wider scope if the wording of section 45(1)(a) of the New Zealand *Commerce Act 1986* were to be adopted. Section 45(1)(a) provides that competition law prohibitions (other than those that prohibit misuse of market power and resale price maintenance) do not apply

> to the entering into of a contract or arrangement or arriving at an understanding in so far as it contains a provision authorising any act that would otherwise be prohibited by reason of the existence of a statutory intellectual property right.

Such wording would see the exception apply to cross-licences and patent pools. Grant-back restrictions, no-challenge provisions and anti-cloning restrictions would fall outside of such an exception. In order for such provisions to be covered by the exception, the exception would need to be expressed very broadly so that it applied to all conditions contained in an IP licence. It is submitted that despite its breadth, such an exception is justifiable as such conditions can be pro-competitive and should not be subject to per se treatment.

3 Proposed Vertical Exception

As discussed above, the Harper Committee was of the view that 'a broader exemption should be included in the cartel laws to ensure that vertical supply restrictions are assessed under a substantial lessening of competition test rather than a per se prohibition'.[111]

The Committee recommended that

> [a]n exemption should be included for trading restrictions imposed by one firm on another in connection with the supply or acquisition of goods or services, recognising that such conduct will be prohibited by section 45 of the *CCA* (or section 47 if retained) if it has the purpose, effect or likely effect of substantially lessening competition.[112]

A detailed critique of the precise form of the general exception proposed by the Harper Committee is beyond the scope of this article.[113] All that needs to be noted for present purposes is that the exception would take trading restrictions in agreements between competitors beyond the reach of the cartel prohibitions.

110 See, eg, United States Department of Justice and Federal Trade Commission, *Antitrust Guidelines for the Licensing of Intellectual Property* (12 January 2017), 5, 30–2 ('*US Antitrust IP Guidelines*').

111 *Harper Report* (n 4) 365.

112 Ibid.

113 For such a critique, see Fisse (n 53) 128–30. See also *Commerce Act 1986* (NZ) s 32.

However, such trading restrictions would continue to breach the *CCA* if they have the purpose, effect or likely effect of substantially lessening competition.[114]

4 Resistance to the Exceptions

Any proposed reintroduction of an IP-specific exception is likely to be met with considerable resistance, especially one that applied to a wider range of conditions than section 51(3). Section 51(3) was repealed on the basis of a belief that 'the rationale for the exemption has largely fallen away',[115] rather than on the basis of concerns about the specific form section 51(3) took. The Explanatory Memorandum accompanying the Bill which resulted in the repeal of section 51(3) stated that an IP exception is no longer needed because 'IP rights and competition are no longer thought to be in "fundamental conflict"'.[116] However, the Explanatory Memorandum also stated that 'the immediate costs and benefits of removing the exemption under subsection 51(3) are finely balanced'.[117] The misunderstanding of the recommendation made by the Harper Committee,[118] and Productivity Commission's inaccurate understanding of the extent of per se liability generally,[119] suggests that the 'immediate costs' have been underestimated which could, in turn, lead to a reconsideration of the view that some form of IP exception is no longer needed.

There has also been significant resistance to the introduction of a general Vertical Supply/Acquisition Exception. As noted above, the proposed exception was removed from the Exposure Draft of the Bill designed to implement the Harper Committee's recommendations (other than the amendments to section 46) in response to concerns about the breadth of the proposed general exception and prospects for abuse by firms not genuinely in a vertical relationship.[120] In a submission to Treasury in relation to the Exposure Draft, the ACCC argued that 'the breadth of the proposed provision and the lack of specificity around how such conduct might otherwise be addressed in the *CCA* is of significant concern'[121] and that the exception 'risks inappropriately narrowing the coverage of Australia's cartel prohibitions'.[122] Consideration of the exception has been deferred by the Government and will be 'progressed in a future legislative package together with amendments to section 47'.[123] There are no signs that the introduction of a general vertical exemption is being considered. For example, no

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114 *CCA* ss 45(1)(a)–(b).

115 Explanatory Memorandum, Treasury Laws Amendment (2018 Measures No 5) Bill 2018 (Cth) 31 [4.3].

116 Ibid 31 [4.4].

117 Ibid 31 [4.6].

118 See above n 40–2 and accompanying text.

119 See above nn 46–51 and accompanying text.

120 Explanatory Memorandum, Competition and Consumer Amendment (Competition Policy Review) Bill 2017 (Cth) 139 [15.56].

121 Australian Competition and Consumer Commission, Submission to Exposure Draft Consultation on Competition Law Amendments (5 October 2016) 5 <https://www.accc.gov.au/system/files/ACCC%20Letter%20to%20Treasury%20%20Submission%20on%20Harper%20Exposure%20Draft%20legis....pdf>.

122 Ibid.

123 Explanatory Memorandum, Competition and Consumer Amendment (Competition Policy Review) Bill 2017 (Cth) 140 [15.57].

draft exemption has been published for public consultation by the current government.

VI THE COMPETITION TEST

A Overview

The nature of the exceptions recommended in the previous section of this article would mean that conditions in IP licences would still breach competition law if the condition had the purpose, effect or likely effect of substantially lessening competition. As the discussion in Part III demonstrates, there appears to be wide acceptance of the appropriateness of subjecting such conditions to competition-tested prohibitions.

This part of the article aims to establish that subjecting conditions in one-way IP licences to the competition test will ensure that dealings in IP rights will be appropriately regulated by competition law whilst also ensuring that the incentives created by IP regimes are not undermined. There are several reasons for concluding that this is the case. First, in most instances the IP right holder lacks market power and thus lacks the ability to bring about an anti-competitive effect – where the IP right holder does not have market power, it is highly unlikely that the imposition of a condition in a licence or assignment will breach a prohibition that contains the competition test. Secondly, the courts employ a counterfactual test when determining whether conduct is likely to cause a substantial lessening of competition. Under the counterfactual test, a condition that does not seek to extend the IP grant will not cause a substantial lessening of competition, even when it is imposed by an IP right holder that possesses substantial market power. Finally, the courts appreciate the distinction between intra-brand and inter-brand competition. The imposition of a condition that restricts intra-brand competition will in many instances promote inter-brand competition, even where the condition is imposed by an IP right holder that possesses market power.

B Competition Tested Provisions, Market Definition and Market Power

Unless a firm has market power, it is unlikely that its conduct will have an anti-competitive effect. In most instances, the licensor will lack market power and thus not be in a position to bring about a substantial lessening of competition. Further, it is unlikely that a firm that lacks market power will act for the purpose of substantially lessening competition as doing so would be irrational.

Where conduct is only prohibited where it has the purpose, effect or likely effect of substantially lessening competition, the first step is to define the market(s) affected by the conduct in question. The market is an analytical tool used to identify any constraints faced by the firm whose conduct is under challenge and in turn determine the likelihood that the conduct will have anti-competitive effects.[124]

Typically, an analysis of the competitive effects of licensing can be addressed by analysing the market in which goods or services made or provided using the IP are sold (the end market).[125] This approach has been adopted by Australian Courts in cases such as *Broderbund Software Inc v Computermate Products (Aust) Pty Ltd*[126] ('*Broderbund*'), *Universal Music Australia Pty Ltd v Australian Competition and Consumer Commission*[127] ('*Universal Music*') and *Pfizer FC*[128] (all of which are considered below). In some cases, it may be necessary to consider the effect of the restraint in a second market, namely a 'technology market'. This may be appropriate where, for example, IP is marketed as a property asset separately from any goods.[129] Finally, licensing restrictions could be analysed in an 'innovation market' where the conditions relate to goods or services that do not yet exist, or the arrangement affects the future development of new or improved goods.[130]

All substitutable goods or services should be included in the market.[131] In a seminal decision, *Re Queensland Co-operative Milling Association*,[132] the Trade Practices Tribunal (since renamed the Australian Competition Tribunal) provided the following explanation as to the role played by substitution when determining the outer boundaries of the 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

124 Maureen Brunt, *Economic Essays on Australian and New Zealand Competition Law* (Kluwer Law International, 2003) 203.

125 *US Antitrust IP Guidelines* (n 110) 8–9.

126 (1991) 22 IPR 215 ('*Broderbund*').

127 (2003) 131 FCR 529 ('*Universal Music*').

128 (2018) 356 ALR 582.

129 *US Antitrust IP Guidelines* (n 110) 8–10.

130 Ibid 11–12. See also Marcus Glader, *Innovation Markets and Competition Analysis: EU Competition Law and US Antitrust Law* (Edward Elgar Publishing, 2006); Giovanni Battista Ramello, 'Intellectual Property and the Markets for Ideas' (2005) 4(2) *Review of Network Economics* 68; Richard J Gilbert and Steven C Sunshine, 'Incorporating Dynamic Efficiency Concerns in Merger Analysis: The Use of Innovation Markets' (1995) 63(2) *Antitrust Law Journal* 569.

131 Section 4E of the CCA provides that:

> For the purposes of this Act, unless the contrary intention appears, ***market*** means a market in Australia and, when used in relation to any goods or services, includes a market for those goods or services and other goods or services that are substitutable for, or otherwise competitive with, the first-mentioned goods or services.

132 (1976) 8 ALR 481.

likely depends ultimately on customer attitudes, technology, distance, and cost and price incentives.[133]

The Australian High Court has stated that 'intellectual property rights are often a very clear source of market power'.[134] With respect, this seems to overstate the likelihood that IP rights confer market power. In most instances, there will be a range of substitutes available for products made using the IP rights in question. Or, there will be substitutable forms of IP that can be used to achieve the same or a similar outcome.[135] This will lead to a broader market definition (one that extends beyond the particular IP right or product). In such a market, the IP right owner is constrained and is unlikely to possess significant market power. In *Broderbund*, Beaumont J had to determine the legality of an exclusivity provision in a copyright licence in relation to a particular piece of educational software, 'Where in the World Is Carmen Sandiego?'. Broderbund Software Inc ('Broderbund') appointed Dataflow Computer Services Pty Ltd ('Dataflow') as its exclusive distributor for a territory that included Australia. Dataflow was also granted an exclusive licence in the territory to use Broderbund's copyright. Computermate Products (Aust) Pty Ltd ('Computermate') sold parallel imported versions[136] of the game in Australia. Broderbund, relying on its exclusive copyright licence, sued Computermate for copyright infringement. By way of a cross-claim, Computermate alleged, inter alia, that the exclusive copyright licence and exclusive distribution agreement between Broderbund and Dataflow involved exclusive dealing[137] which had the purpose, effect or likely effect of substantially lessening competition in breach of competition law. Two potential markets were identified – the national market for educational computer games and the national market for computer games that had an entertainment character.[138] In either of these markets, the Carmen Sandiego game had between 10 and 17% market share[139] – that is, there were ample choices available to potential customers of such games. This led the court to conclude that Broderbund did not possess significant market power[140] and, in turn, that the

133 Ibid 513 (Woodward J, Member Shipton and Member Brunt).

134 *NT Power Generation Pty Ltd v Power and Water Authority* (2004) 219 CLR 90, 136 [125] (McHugh ACJ, Gummow, Callinnan and Heydon JJ).

135 *IPAC Report* (n 26) 24; *NCC Final Report* (n 12) 157–8; *IPCRC Report* (n 6) 138.

136 A parallel import is a non-counterfeit product imported from another country. Such products are typically sold outside of the formal manufacturer distribution channels.

137 Computermate argued that Dataflow had acquired the program on the condition that Broderbund agreed not to supply the program the program within Australia to anyone other than Dataflow and that this fell within the definition of exclusive dealing contained in section 47(4) of the *CCA*. Broderbund was said to have been involved in Dataflow's breach. Little attention was devoted to determining whether Dataflow's acquisition was subject to such a condition because, even if it was, there would have been no contravention of section 47. This is because of the finding that the conduct had neither the purpose, nor effect, of substantially lessening competition. If the conduct had such a purpose or effect, it would not have mattered whether the conduct amounted to exclusive dealing because if it did not, it could have been challenged under section 45, which prohibits provisions in contracts, arrangements or understandings that have the purpose or effect of substantially lessening competition.

138 *Broderbund* (1991) 22 IPR 215, 238 (Beaumont J).

139 Ibid 241.

140 Ibid.

exclusivity arrangements did not have the effect of substantially lessened competition.[141]

It should be noted that a firm without substantial market power can be caught by section 45 or section 47 if it acts for the purpose of substantially lessening competition even though its conduct is unlikely to have anti-competitive effects. The *Universal Music* case provides a useful example. Universal Music (and other record companies)[142] threatened to refuse (and on a few occasions actually refused) to supply their products (CDs) and support services (such as the right to return unsold stock and marketing support) to retailers who dealt with parallel importers. The Full Court held that there had been no breach of section 46 of the *CCA* as Universal did not possess substantial market power.[143] It also held that the conduct amounted to exclusive dealing but that, consistently with the finding that Universal Music lacked market power, the exclusive dealing conduct did not have the effect or likely effect of substantially lessening competition.[144] However, Universal Music was held to have breached the exclusive dealing prohibition on the basis that it acted with the purpose of substantially lessening competition. Universal Music believed (albeit incorrectly) that retailers would desire timely and frequent delivery of CDs and access to support services and back catalogues and that by threatening to withhold supply of such services and access it would be possible to deter retailers from dealing with parallel importers not only in the short term but also over the longer term.[145]

Universal Music is the only case in which liability has been imposed on a firm held not to possess market power and whose conduct was held not to have anti-competitive effects. Universal Music was facing a competitive threat (parallel imports) for the first time. This helps explain why it may have overestimated its power in the market and acted for the purpose of substantially lessening competition even though, with the benefit of hindsight, the strategy it employed was unlikely to achieve such an effect. In cases involving IP licensing, the IP right owner is far more likely to be aware of its position in the market, the constraints it faces and of its ability to bring about an anti-competitive outcome. For example, in *Pfizer FC* (discussed in more detail below), the court rejected an argument that Pfizer's terms of trade were underpinned by an anti-competitive purpose. Pfizer was very familiar with strategies engaged in by generic manufacturers and appreciated that it was not possible to thwart generic competition in the long-term. This led the Full Court of the Federal Court to reject the ACCC's argument that Pfizer acted for an anti-competitive purpose. In support of the purpose finding, the Full Court noted that it was 'clear to Pfizer that, no matter what it did and no matter what strategy it adopted … it was going to face intense competition … from the major generics manufacturers and their

141 Ibid 244 (Beaumont J). The court also found that Broderbund and Dataflow did not have the purpose of substantially lessening competition.

142 It was not established that the record companies had colluded. Rather, the case proceeded on the basis that each company adopted its refusal policy as a unilateral act.

143 *Universal Music* (2003) 131 FCR 529, 569 [164] (The Court).

144 Ibid 584–7 [239]–[248] (The Court).

145 Ibid 587–92 [249]–[274] (The Court).

aligned wholesalers'.[146] To put it simply, Pfizer could not logically have believed it was able to hamper competition in the market meaning that it was not possible to ascribe an anti-competitive purpose to the conduct engaged in.

C Competition Tested Provisions and the Correct Counterfactual

There will be situations in which an IP right confers market power. For example, it may not be possible to supply a substitutable product without infringing a patent, as was held to be the case by both the primary judge and the Court of Appeal in the *Pfizer* litigation.[147] Pfizer Australia Pty Ltd ('Pfizer') manufactured Lipitor (atorvastatin), a drug which made a very significant contribution to Pfizer's earnings. With the impending expiry of the patent, Pfizer developed strategies designed to discourage customers from switching to generic products. The ACCC argued that these strategies involved prohibited exclusive dealing, in breach of section 47 of the *CCA*, as well as a misuse of market power in breach of section 46. To determine both claims, it was necessary to define the market. The ACCC argued that the relevant market was an Australian-wide market for the supply of atorvastatin to, and the acquisition of atorvastatin by, community pharmacies.[148] The court accepted the ACCC's argument.[149] There were no demand-side substitutes for atorvastatin (as the primary judge noted, a pharmacist presented with a prescription for atorvastatin was required to fill the script by supplying atorvastatin).[150] Further, the patent prevented supply-side substitution by generics until the expiry of the patent. In the narrowly defined market identified by the court, Pfizer, as the sole supplier, possessed substantial market power at the time that it engaged in the impugned conduct.

However, even if a firm has substantial market power, not all licence restrictions imposed by the firm will have the effect or likely effect, or be held to have been extracted for the purpose, of substantially lessening competition.[151] In determining whether or not a licence condition harms competition, a counterfactual approach is adopted. Two future market states are identified – the likely state of the market in the 'future with' the conduct and the likely state of the market in the 'future without' the conduct under examination. Identifying any differences between the 'future with' and 'future without' identifies the likely effect of the conduct.

When it comes to IP licences that include a restrictive condition, the relevant 'future with' is clear. In this market state, the licence is issued subject to the condition under consideration. However, it is less clear how to define the 'future without'. In the 'future without', is a licence issued without the condition in question? Or, is no licence issued at all? Imagine that a patent holder currently manufactures and distributes a patented good in Victoria and New South Wales.

146 *Pfizer FC* (2018) 356 ALR 582, 724 [560] (The Court).
147 *Australian Competition and Consumer Commission v Pfizer Australia Pty Ltd* (2015) 323 ALR 428 ('*Pfizer Trial*'); *Pfizer FC* (2018) 356 ALR 582.
148 *Pfizer Trial* (2015) 323 ALR 428, 432 [10] (Flick J).
149 Ibid 507 [278] (Flick J), affd *Pfizer FC* (2018) 356 ALR 582, 662 [307]–[309] (The Court).
150 *Pfizer Trial* (2015) 323 ALR 428, 504 [270] (Flick J).
151 *NCC Final Report* (n 12) 221–2.

The patent holder is approached by a Queensland distributor who wants to manufacture and distribute the patented good in question. Keen to protect its sales in Victoria and New South Wales, the patent holder offers to issue a licence that contains a condition that prevents the licensor from selling goods made using the patent in places other than Queensland. In the 'future with' the conduct, the Queensland distributor is prevented from selling the patented goods other than in Queensland. But what is the relevant 'future without'? If it is taken to be a situation in which the licence is granted without the restriction (that is, the licensor is free to compete in New South Wales and Victoria), then it is possible that the condition would be held to lessen competition (although this will only be the case where the patented product faces limited competition from other products or, to put it another way, the patented product is sold in a narrowly defined market). However, if the 'future without' is that no licence is issued then the imposition of the condition may, in fact, be seen to be pro-competitive, even if the licensor possesses market power. In this 'future without' the condition, there would be nobody selling the patented good in question in Queensland and the licensor would not be competing with the licensee in Victoria or New South Wales.

The second scenario (ie, a market in which no licence is issued) properly defines the relevant 'future without'. IP right holders do not have a general duty to issue a licence. There is support for such an approach in the now dated Trade Practices Commission's Background Paper *Application of the Trade Practices Act to Intellectual Property*[152] and the limited academic literature.[153] Further, comments in the *Harper Report* suggest that its drafters were of the view that the second scenario accurately describes the relevant 'future without' and explain why in most instances the imposition of a condition is unlikely to fail the competition test. The report notes:

> [section 51(3)] applies where an owner of an IP right licences another person to commercialise that right, but imposes restrictions on the manner in which the commercialisation occurs; for example, quality specifications, quantity restrictions or territorial restrictions. If the IP owner were to commercialise the right, the owner would itself make decisions about quality, quantity and selling territory. The rationale for subsection 51(3) is that the grant of a licence to another person, subject to conditions or restrictions that the owner could have imposed upon itself, should not be regarded as anti-competitive and should be exempted from the competition law.
>
> However, the Panel considers that the rationale for subsection 51(3) is flawed. In the relatively benign example given, the conditional licence would not substantially lessen competition and would not contravene the *CCA*. Without the licence, the licensee would have been unable to commercialise the IP right; therefore, a conditional licence does not restrict the level of competition that would have existed but for the licence. Accordingly, on the benign example, the exemption is not required.[154]

152 Trade Practices Commission, *Application of the Trade Practices Act to Intellectual Property* (Background Paper, July 1991) [2.21].

153 See, eg, Hoad (n 3) 221.

154 *Harper Report* (n 4) 109 (emphasis added).

The Harper Committee's views as to the operation of the counterfactual test are convincing. However, the suggestion that this demonstrates that an IP exception is not needed overlooks the fact that the counterfactual test is not applied to determine per se liability.

D Intra-Brand Restrictions v Inter-Brand Restrictions

Even if the relevant 'future without' is taken to be a situation in which the licence is granted without the restriction, the mere imposition of a condition on a licensee in the 'future with' does not establish a substantial lessening of competition. There are two different 'types' of competition that are relevant when assessing the effect of conduct on a 'with' and 'without' basis: competition between suppliers of different brands of the same or similar products (that is, inter-brand competition), and competition between distributors of the same brand (intra-brand competition). A restriction on intra-brand competition (to return to the example above, the condition that prevents the licensee from selling goods made using the patent in places other than Queensland) will not necessarily result in harm to inter-brand competition. Conferring exclusivity on a licensee will mean that others are unable to compete with the licensee with respect to goods or services produced by use of the IP right which is the subject of the licence – that is, intra-brand competition has been completely restricted. However, it may be necessary to confer exclusivity on the licensee to overcome the 'free-rider' effect whereby one licensee enjoys the benefit of another licensee's investment in the IP. By ensuring that the chosen licensee is appropriately committed to, and invested in, the goods or services produced by use of the IP, the intra-brand restriction may see products made using the IP better promoted by the licensee and, in turn, promote inter-brand competition.[155]

The *Broderbund* case, considered above,[156] provides an example of intra-brand restrictions being held to be pro-competitive. The appointment of Dataflow as the exclusive Australian distributor restricted intra-brand competition (competition between potential sellers of the Carmen Sandiego game). However, such protection from intra-brand competition did not result in competitive harm in the market. The intra-brand restrictions ensured that Dataflow had the incentive to invest in promoting the software by overcoming concerns that other distributors would free-ride on such investments. These investments led to more effective inter-brand competition, which was strong as there were numerous substitutable pieces of software available to consumers.

The legitimacy of intra-brand restrictions and the capacity for such restrictions to promote effective inter-brand competition was recognised by the High Court in *Melway Publishing Pty Ltd v Robert Hicks Pty Ltd* ('*Melway*').[157] The *Melway* case is of particular interest because Melway Publishing Pty Ltd ('Melway') was found to possess substantial market power yet its use of intra-

155 Ibid 364.

156 See above nn 138–41 and accompanying text.

157 (2001) 205 CLR 1.

brand restrictions was nevertheless viewed as efficient and pro-competitive. Gleeson CJ, Gummow, Hayne and Callinan JJ noted:

> The distinction between interbrand and intrabrand competition has been examined by the United States courts in considering the application of that country's antitrust legislation to vertical restraints imposed by manufacturers on distributors. Such restraints typically include limiting, geographically or otherwise, the customers to whom a particular distributor may sell. The overall effect on competition of such restraints is not necessarily negative; it may be positive.[158]

Melway, the producer of the popular 'Melway' street directory, had substantial market power in the Melbourne street directory market owing to its large market share, its copyright-protected maps and strong trade mark. It adopted a segmented distribution system. Each distributor was allocated a segment of the market and prevented from selling the Melway street directory in other market segments. A majority of the High Court accepted that although Melway had imposed intra-brand restrictions on its distributors, these were not anti-competitive. By protecting each distributor from the threat of free-riding, Melway had created incentives for each distributor to invest in maximising sales in its allocated territory.

E What Conditions Might Fail the Competition Test?

Conditions in one-way licences may be caught by competition law prohibitions that contain the competition test where the licensor seeks to obtain a collateral advantage. Such potential liability was not identified as a basis of concern by review bodies as the repeal of section 51(3) changes nothing – conditions that seek a collateral advantage were not exempted by section 51(3).[159]

Where the licensor seeks an advantage collateral to the IP grant by, for example, tying the supply of the IP right to other goods, such conduct may involve a lessening of competition and thus breach competition laws. Imagine that there are no substitutes for the licensor's patent and that the owner of the patent licenses the patent on the condition that the licensee agrees to purchase other goods (for example, raw materials used to produce the patented product) from the patent holder. If the tying condition makes the supply of the IP licence conditional on the licensee acquiring a specific quantity of the tied goods, but there is no restriction on the licensee acquiring goods from other sources, then sections 45 and 46 regulate the conduct.[160] If the licensor makes the supply of the IP licence subject to a condition that prevents, restricts or limits the licensee from acquiring goods from other sources, sections 46 and 47 regulate the conduct. Either way, the conduct will only breach competition law if it has the purpose, effect or likely effect of substantially lessening competition. If the tying condition results in a significant portion of sales in the raw materials market

158 Ibid 14 [20].

159 For example, the tying conditions discussed in the following paragraph do not 'relate to' the invention to which the patent relates, or articles made by the use of that invention, but rather to the tied goods (the raw materials).

160 Section 47 does not apply because of the lack of a condition restricting acquisition from other sources: *Monroe Topple & Associates v Institute of Chartered Accountants* (2002) 122 FCR 110, 139 (Heerey J).

accruing to the patent owner, this foreclosure effect may cause a substantial lessening of competition in the raw materials market, exposing the patent owner to competition law liability.[161]

VII CONCLUSION

Whilst the policy objectives originally behind section 51(3) are unclear,[162] it seems that a key reason the exception was enacted was to prevent a perceived clash between the interests of IP right holders and competition law[163] at a time when the power conferred by IP rights, and in turn the likelihood that dealings in IP rights would fall foul of competition law, was overstated. Section 51(3) was repealed in the belief that 'the rationale for exemption has largely fallen away'[164] given that 'IP rights and competition are no longer thought to be in "fundamental conflict"'.[165] However, the growing understanding that there is no 'fundamental conflict' does not mean that there is no need for the *CCA* to contain an IP exception. Conduct can be caught by per se competition law prohibitions even if it does not harm competition. With one exception,[166] all review bodies that have seriously considered section 51(3) have concluded that it should not be repealed but instead amended so that that conditions in one-way licences that do not seek an advantage collateral to the IP grant are not subject to per se treatment. This includes the Harper Committee and the Productivity Commission, whose reports were cited as supporting the repeal of section 51(3). The decision to repeal section 51(3) is a mistake and based on a faulty understanding of the recommendations made by the Harper Committee and the Productivity Commission. A new IP exception should be introduced into the *CCA* as a matter of urgency to ensure that competitively benign or pro-competitive conditions in IP licences are not exposed to per se competition law liability.

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161 It should be noted that tying conduct can be pro-competitive. For example, it may allow for metering. Imagine a business has just designed a commercial photocopier that uses approximately one tenth of the ink used by most modern machines. Whilst anybody that needs to use a photocopier would prefer a machine that uses less ink, most are unable to afford the new machine as it is very expensive to produce. Tying can overcome this problem by making the machine available at a cheaper price on the condition that the customer also commits to purchasing a second product (the tied product – here, for example, paper). Customers may not mind paying more for the tied product, or accepting a tied product that is not as good as other available alternatives, because they have access to the tying product (the copier) at the cheaper price. Metering not only more effectively markets the machine, it also further disseminates the innovation, a key policy goal of intellectual property regimes. If a metering condition lessens competition in the product in which the tied product is sold it will breach the law and an IP right holder would need to seek authorisation before imposing such a tie.

162 The Explanatory Memorandum to the *Trade Practices Act 1974* referred generally to section 51. It noted that section 51 covers 'a number of specific instances of conduct to which special considerations apply' but did not specify the 'special considerations': See Explanatory Memorandum, Trade Practices Bill 1974 (Cth) 13. The Second Reading Speech is silent as to the objectives of section 51.

163 *NCC Final Report* (n 12) 166.

164 Explanatory Memorandum, Treasury Laws Amendment (2018 Measures No 5) Bill 2018 (Cth) 31 [4.3].

165 Ibid 31 [4.4].

166 The review undertaken by the National Competition Council: see *NCC Final Report* (n 12).