Chapter I

Intellectual Property Rights and Competition Law: An Overview

“Intellectual Property Rights and Competition Law are both founded with the purpose of achieving economic development, technological advancement and consumer welfare.”

- Jayshree Watal¹

1.0 Introduction

Intellectual property is the creative work of the human intellect. The main purpose of its protection is to promote the progress of science and technology, arts, literature and other creative works and to encourage and reward creativity. The economic and technological development of a nation will come to a halt if no protection is given to intellectual property rights. Therefore, the contribution of intellectual property is sine qua non for the industrial and economic development of a nation.²

The purpose of the Competition law is to avert practices having undesirable effect on competition, to promote and sustain competition in the markets, to protect the interests of the consumers and to ensure freedom of trade carried on by other participants in the markets³. The objective of Competition law is to ensure that the process of competition does not entail

¹ Intellectual Property Rights in WTO and Developing Countries (2nd edn, Oxford University Press 2001) 2
² V.K. Ahuja, Law relating to Intellectual Property Rights (2nd edn, Lexis Nexis 2011) 3
³ T. Ramappa, Competition Law in India (3rd edn, Oxford 2014) 1
stronger enterprises in bringing the market operations for their own advantage and thereby causing disadvantage to the consumers.

Intellectual property rights (IPRs) are intended to reward the author or innovator with the fruits of his or her labour which has been derived from the Locke’s concept of labour. In a sense, the author of intellectual property is given the legal right to exclude others from enjoying the benefits resulting from his work. The justification behind intellectual property rights is that those who invest time and resources for the development of a new technology, system or device should be rewarded with the exclusive right to profit from their investment. Moreover, without the exclusive opportunity to "exploit the invention" through intellectual property rights, there would be no mechanism through which the owner of the intellectual property right could guard against free riders taking advantage of the innovator's research and development.\(^4\)

Moreover, IPR laws also provide that the protection cannot be for an indefinite period, as after sometime it should be made available to the common masses in their general interest. Even within the IPR period, the intellectual asset may be used without restriction for certain purposes, these not being commercial purposes, for example for the purpose of research and training and educational purposes. Further, in some laws, provision exists for compulsory licensing where under the Indian Patents Act, 1970; a compulsory license may be sought after three years of the sealing of the patent on three grounds:

- non-satisfaction of reasonable requirements of the public,

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• non-availability of the patented invention at reasonable price, or
• patented invention not being worked in India.\(^5\)

Tension arises between IPR and competition law because IPR creates market power, even a monopoly, depending upon the extent of availability of substitute products. IPR restricts competition, while competition law engenders it. Hence, competition law takes care of the unreasonable exercise of market power or the abuse of dominant position obtained as a result of the IPR.

The Competition Act, 2002 in India recognizes the importance of IPRs such as patents, copyrights, trademarks, geographical indications, industrial designs and integrated circuit designs. While Section 3 of the Competition Act prohibits anti-competitive agreements, Section 3(5) lays down that this prohibition shall not restrict “the right of any person to restrain any infringement of or to impose reasonable conditions, as may be necessary for protecting any of his rights” enjoyed under the statutes relating to the above mentioned IPRs. This implies that unreasonable conditions imposed by an IPR holder while licensing his IPR would be prohibited under the Competition Act. This provision is not very dissimilar to the laws in other countries. In some jurisdictions, restrictions that have been regarded as unreasonable, and anticompetitive, include - agreements restricting prices or quantities of goods that may be manufactured, or curbing competition between the licensee and the licensor, stipulating payment of royalty after the license period, certain types of exclusivity conditions, patent pooling, tie-in arrangement, so on and so forth.

Therefore, in the case of unreasonable restrictive practices by the IPR holder, relief is available to the affected parties under the Competition Act. The Commission can pass a variety of orders including: penalty up to ten percent of the turnover, cease and desist order, direct modification of the (license) agreement, and any other order or direction that it may deem fit.\(^6\)

1.1 Nature of Intellectual Property Rights

(i) Intangible Rights over Tangible Property

The major feature that distinguishes IP from other forms of property is its intangibility. As per Lionel Bently and Brad Sherman, while there are a number of important differences between the various forms of IP, one factor that they share in common is that they establish property protection over intangible things such as ideas invention, signs and information while there is a close relationship between intangible property and the tangible object in which they are embodied\(^7\)

(ii) The role of intellectual property rights in encouraging innovation

Intellectual property rights (IPRs), granted by patents, copyrights, trademarks, etc., play an important role in fostering innovation and supporting economic growth. These rights allow their holders to exclude, for a limited duration, other parties from the benefits arising from new knowledge and, more specifically, from the commercial use of innovative products and processes based on that new knowledge. The ability to temporarily exclude others from the enjoyment of the potential benefits

\(^6\) Supra note 4

deriving from innovation contributes to provide the incentive for individuals and enterprises to allocate financial and human resources in research and development (R & D) and other costly activities to build new discoveries, innovative products and production processes.\(^8\)

In the nonexistence of the legal protection granted by IPRs, rival firms and companies would be entitled to free-ride on the successful results of R & D investments, imitating and thereby exploiting commercially new inventions. IPRs also contribute to promoting the dissemination and commercial application of intellectual property. Firms, in fact, can be expected to be more leaning to transfer new technologies and inventions when a adequate degree of legal certainty regarding the returns from sharing precious innovative ideas is guaranteed. However, even in the absence of IPRs, firms may still be able to exclude competing firms from having access to their innovations. In these cases, IPRs would not be necessary to recover the investments incurred.

However, excluding other firms from sharing know-how is not always possible. Also, a sizeable waste of resources can result from the efforts aimed at maintaining secrecy. In the absence of strong IPRs, an inefficient tendency to allocate resources particularly to those innovative activities which can be more easily kept secret can be expected.\(^9\)

(iii) Incentive to invent

The granting of intellectual property right is a mode of providing incentive to the inventor for his invention. The inventor will not be able to


\(^9\) Ibid
appropriate the full value of his invention because of certain persons who may be enjoying the benefit of the commodity without paying anything for it.

(iv) To encourage disclosure

Incentive encourages the inventor to disclose his invention to the public. In India, patent is granted to the inventor only when he gives the complete details of his invention. This has various advantages, first of all, the information about the intellectual property is useful in the ulterior development of other assets, disclosure increases the economic development of a country and finally the patent office publishes the specification which can be used by others for research and development.

(v) Exhaustion of Rights

Intellectual property rights are generally subject to the principle of exhaustion. Exhaustion basically means that after the first sale by the right holder or by his exhaustion authorization, his right comes to an end and he is not entitled to stop further movement of goods. Thus, once an IP right holder has sold a physical product to which its IPRs are attached, he cannot prohibit the subsequent resale of that product. The right is exhausted by the first consensual marketing. A third party may, after legitimately purchasing these goods, sell them in any of the country-markets. The owner or any one deriving title from him cannot prevent sale of such goods, as the exclusive right to sell goods is ‘exhausted’ by the first sale. Thus he loses all his control over the goods on his first sale and the rights therein are not infringed by further circulation of the product. The principle permits the goods to move through the stream of commerce unhindered by multiple claims to IPRs.
This doctrine is based on the concept of free movement of goods put into circulation by the consent or authority of right holder. The exclusive right to sell goods cannot be exercised twice in respect of the same goods. The right of restricting further movements is exhausted because the right holder has already earned his part, by the act of putting the goods for first sale in the market.

Exhaustion may be either domestic exhaustion or international exhaustion. Under domestic exhaustion, once the goods have been put on the domestic market by the right holder or by third party with his consent, his right is exhausted in the domestic territory. Domestic exhaustion is generally provided for in almost all countries. In international exhaustion when the goods are put into the market, by the right holders or with his consent in any country, the rights are exhausted for other national jurisdictions as well. As per the doctrine, the owner of an IPR who consents to the marketing of his products in one member state cannot use that right to prevent the importation of the products into another member state\(^\text{10}\). The characteristic of non-exhaustion by consumption is an important feature of intellectual property.

(vi) Statutory requirement

IPRs are statutory rights governed in accordance with the provisions of corresponding legislations. To put it differently, intellectual properties are creations of statutes. The protection to the right holder is given to ideas, technical solutions or other information that have been expressed in a legally admissible form and that are, in some cases, subject to registration procedures. Further, subject to the relevant statutory provisions, registration of the work is mandatory in relation to some kinds of IPR as in the case of patents and industrial designs while in relation to some other kinds of IPR,

\(^{10}\) J.K. Das, Intellectual Property Rights (1\(^{st}\) edn, Kamala Law House, Kolkata 2008) 11
registration is optional as in the case of trademarks, copyrights and geographical indications. In respect of certain IPRs, the moment the work is completed; protection automatically springs into, as in the case of copyrights. By continuous use also, IPR can be claimed as in the case of trademarks.

Granting of IPR is strictly subject to all statutory conditions and pre-requisites. As the IPR is conferred by the state, it can be revoked by the state under very special circumstances even if it has been sold or licensed or marketed in the meantime. In this sense, there is no guarantee for an IPR once it is granted; it can be challenged or revoked at any time on several grounds including national security or under the provisions of relevant statutory laws of the land.

(vii) Intellectual property rights and the tradeoff between allocative and dynamic efficiency

IPRs, by granting legal exclusivity, may also grant their holders the ability to exercise market power\(^{11}\), when similar technologies and products representing practicable constraints are not present. Such exercise of market power can result in allocative inefficiencies where owners of exclusive rights will likely restrict output levels compared to more competitive situations, in the markets for the goods and services incorporating those rights. They will do so in order to maximize their profits. However, it has been observed that IPRs, while ensuring the exclusion of rival firms from the exploitation of patented technologies and derived products and processes, do not necessarily confer market power to their holders. In fact, technologies which can be considered, at least to a sufficient degree, potential substitutes do represent

\(^{11}\text{Market power can be defined as the ability to maintain prices above competitive levels for a significant amount of time and profit from such rise in prices.}\)
effective constraints to the ability of IPRs holders to raise the price of their products above competitive levels. Only when alternative technologies are not available, it can be said that IPRs grant their holders monopolistic positions in relevant markets.\textsuperscript{12}

The exercise of exclusive IPRs which lead to a monopolistic behaviour resulting in allocative inefficiencies, in the absence of competing technologies and products, may appear contrary to what is generally perceived in most jurisdictions as the main objective of competition policy that is, the protection of the competitive process to ensure an efficient allocation of resources, lower prices and better consumer preference.

Competition policy, however, recognizes that in some situations, society would be benefitted by allowing for limited market restrictions, monopolistic profits and short-term allocative inefficiencies, when these can be proven to promote dynamic efficiency and long-term economic growth\textsuperscript{13}. This trade off which has to be looked into by the competition policy makers is clearly a central issue in the interface between competition policy and intellectual property protection where short-term inefficiencies are expected to be the price that society needs to pay in order to receive the reward of long-term economic growth.

However, competition policy certainly plays an important role in limiting the exercise of market power associated with the IPRs, ensuring in particular that such power is not excessively used as leverage. Thus, competition policy has a role in limiting monopolistic abuses related to the exercise of IPRs. It exercises this role by preventing firms holding competing intellectual property rights from engaging in anticompetitive practices.

\textsuperscript{12} Supra note 7
\textsuperscript{13} Ibid
1.2 Nature of Competition Policy

The term competition law refers to legislation, judicial decisions, and regulations specifically designed avoiding the concentration and abuse of market power. Competition policy is a broad term, covering all aspects of government actions that affect the conditions under which firms or the companies compete in a particular market. Competition law has emerged as an issue largely because exporting firms in the high-income developed economies argue that anticompetitive practices of competitors in foreign markets hinder their ability to penetrate those markets. Such practices may be largely private in nature and could be facilitated by the absence or weak enforcement of local competition laws.14

(i) Role of competition law in effective functioning of markets

The aim of competition law is primarily to protect the processes essential for efficient and effective functioning of markets. Markets are essentially dynamic in nature and experience the birth of new firms and products, the death of inefficient firms and outdated products, and the natural expansion, contraction, and reorganization of firms. Competition law further recognizes that firms compete in both static and dynamic terms, requiring that some balance must be struck between ensuring competitive access and encouraging innovation.15

(ii) Preventing Anti-competitive practices

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15Ibid
The fundamental purpose of competition law is to ensure that markets are effectively contestable, meaning thereby that incumbent firms are not able to sustain anticompetitive practices for extended periods of time. Such practices include merging with competitors to attain monopoly, refusing to supply goods or to license technologies on market terms in order to prevent competition, and agreeing with other firms to establish collusive restraints on trade.

(iii) Preventing abuses

Competition law aims at preventing such abuses by establishing conditions or guidelines under which they would be examined for legality which is difficult in reality. For example, published guidelines differ considerably across the United States and the European Union in which practices are viewed as potentially anticompetitive, which practices should be banned outright, and what circumstances should be investigated by authorities for anticompetitive effects.

(iv) Process of rivalry

Competition may be read as the process of rivalry. This is the meaning normally attributed to the word because rivalry is the means by which a competitively structured industry creates and confers benefits and because the event that triggers off the applications of the law is often the elimination of rivalry by merger or cartel agreement. This loosely added word rivalry defeats the very nature of competition. In the US this was realized by the Chicago School and through its writings it destroyed the erstwhile myth of the pre-1980s US antitrust era that concentration is always bad.
State of economic freedom and dispersal of private economic power\textsuperscript{16}

In the first half of the last century, the German Freiburg School of ordo liberalism had developed a theory that competition is a process whereby market players participate in the economy without constraints from accumulated private or public power. The goal of competition policy is seen as the protection of the individual economic freedom as an end in itself so that distributive concerns lead this school to use competition law to protect competitors and small and medium sized enterprises.\textsuperscript{17}

State of perfect competition

GJ Stigler\textsuperscript{18} says that ‘individual buyer or seller does not influence the price by his purchases or sales’. Perfect knowledge, large numbers, product homogeneity and divisibility of output are the ingredients for a competitive market. But Borke clarifies this and says that economic model of perfect competition can never serve as a policy prescription and it is also wrong to assume that markets do not work efficiently if they depart from this model.

Maximizing consumer welfare

The best definition provided by Chicago school, namely that ‘competition’ may be read as designating a state of affairs in which consumer welfare cannot be increased by moving to an alternative state of affairs through the intervention of antitrust law and that, conversely, monopoly designates a situation in which consumer welfare could be so improved so

\textsuperscript{16} Eugene Buttigieg, \textit{Competition Law: Safeguarding the consumer interest} (2\textsuperscript{nd} edn, Wolters Kluwer 2009) 5
\textsuperscript{17} Richard Whish, \textit{Competition Law} (2\textsuperscript{nd} edn, Butterworths 2003) 19-20
\textsuperscript{18} GJ Stigler, \textit{The Theory of Price} (1\textsuperscript{st} edn, Macmillan New York 1966) 87-88
that to ‘monopolize’ would be to use practices inimical to consumer welfare. Borke claims that this interpretation of ‘competition’ coincides with everyday parlance as competition for the man in the street implies low prices, innovation and choice among differing products. Competition thus equates with consumer welfare.

1.3 Concluding remark

Intellectual property Law and Competition Law are the two major areas of law governing the market and promoting economic efficiency, consumer welfare, competition, innovation and technology transfer. Intellectual property rights are vital in our society today. Their existence stimulates both investments and development of new ideas, which in turn promotes economic growth. By providing a number of protective forms for various industrial property rights the incentive to invest in research and development naturally will increase, as these investments become more secure and the right owner will reap the rewards for his creative effort and innovation. Intellectual property rights, by their very nature, give a monopolistic status to the holder of the right, and so put some short-term restraints on competition in the market. However, in the long run they promote increased competition since a good deal of innovation on the part of competitors is promoted, which will lead to new, competing and substitutable products on the market. 19 On the other hand the objective of Competition Law is increased efficiency in the market and consumer welfare.