DEPARTMENT OF JUSTICE ANTITRUST DIVISION

and FEDERAL TRADE COMMISSION

Hearing on:

COMPETITION AND INTELLECTUAL PROPERTY LAW

AND POLICY IN THE KNOWLEDGE BASED ECONOMY

Session 1: Refusals to License and Compulsory

Licensing in the European Union,

Canada, and Australia

Session 2: Licensing in the European Union:

The Technology Transfer Block Exemption and

Agreements that Fall Outside its Scope

Wednesday, May 22, 2002

Great Hall of the U.S. Department of Justice

333 Pennsylvania Avenue, N.W.

Washington, D.C.

MORNING SESSION PARTICIPATING PANELISTS:

Morning Session: Refusals to License and
Compulsory Licensing

Gwillym Allen, Senior Economist and Strategic Policy Advisor, Competition Policy Branch, Canadian Competition Bureau

Henry Ergas, Managing Director, Network Economics Consulting Group, Australia

Ian Forrester, Executive Partner, White & Case LLP, Brussels

David W. Hull, Partner, Covington & Burling, Brussels

John Temple Lang, Counsel, Cleary, Gottlieb, Steen & Hamilton, Brussels

Patrick Rey, Professor of Economics, University of Toulouse, France, and Research Director, Institut d'Economie Industrielle

James S. Venit, Partner, Skadden, Arps, Slate, Meagher & Flom, Brussels

AFTERNOON SESSION PARTICIPATING PANELISTS:

Afternoon Session: Licensing in the European Union: The Technology Transfer Block Exemption and Agreements that Fall Outside its Scope

Peter Alexiadis, Partner, Squire, Sanders & Dempsey, Brussels

Fiona Carlin, Local Partner, European Law Center, Baker & McKenzie, Brussels

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HEARING MODERATORS:

William J. Kolasky, Deputy Assistant Attorney General, Antitrust Division, Department of Justice

William E. Kovacic, General Counsel, Federal Trade Commission

Mary Critharis, U.S. Patent & Trademark Office

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MORNING SESSION

(9:30 a.m.)

WILLIAM KOLASKY: Good morning, and welcome to everyone. We are delighted that you have joined us for another session of our joint hearings of the Department of Justice and the Federal Trade Commission on competition and IP law and policy in the knowledge based economy.

My name is Bill Kolasky, and I'm one of the Deputy Assistant Attorney Generals. I'm responsible for international and policy matters. I'm most pleased to be joined today by Bill Kovacic, who is the General Counsel of the Federal Trade Commission.

Together we will moderate three comparative law sessions, two here today in the Great Hall, and one tomorrow on Asian licensing issues at the FTC building just one block down Pennsylvania Avenue.

This morning our panelists will be talking about how refusals to license intellectual property and compulsory licensing

are treated in the European Union, Canada, and Australia in comparison to how those issues are approached in the United States, a topic that we examined at some of our earlier sessions.

We will examine the circumstances under which compulsory licensing of intellectual property has been required as a remedy for anticompetitive practices.

One question that arises is how to set prices for such licensing. Whether courts or agencies should be involved in determining a fair royalty rate was a hotly debated topic at our earlier sessions on U.S. law in this area.

In discussing these issues today, we will explore the essential facilities doctrine, which is an important element of recent legal doctrine in Europe and is present in Canadian and Australian law as well.

By contrast those of you familiar with U.S. law know that the essential facilities doctrine is in some disfavor here in the United States.

There seems to be significant agreement in the U.S. that it is difficult to justify mandating access to well defined intellectual property rights as an essential facility.

As part of this discussion we will also explore whether intellectual property is fundamentally different from other types of property and therefore in need of special legal doctrines for resolving antitrust issues.

We may also explore whether there are concerns not present in the United States such as EU integration concerns that affect how intellectual property rights are treated in other jurisdictions.

With this brief introduction let me begin by introducing our panelists. Joining us in representing the agencies at this morning's session is Mary Critharis, an assistant solicitor at the U.S. Patent and Trademark Office.

Time constraints require that our introductions of the members of our distinguished

panel be brief. More complete versions of their biographies are available in the prepared materials.

Gwillym Allen is the senior economist and strategic policy advisor in economic policy and enforcement in the competition policy branch at the Canadian Competition Bureau. He has drafted a number of Competition Bureau guidelines including the intellectual property enforcement guidelines.

Henry Ergas is the managing director of the Network Economics Consulting Group in Australia. He recently chaired the Australian intellectual property and competition review committee set up by the federal government in 1999 to review Australia's intellectual property laws as they relate to competition policy.

Ian Forrester is an executive partner at White & Case LLP in Brussels where he practices European law. He represents the European Commission before the European courts in the well known Magill case about refusal to deal.

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David Hull at the end of the table is a partner in the Brussels office of Covington & Burling. His practice concentrates on EU competition law, representing clients before the European Commission, and advising them on all aspects of competition law.

John Temple Lang is with the Brussels office of Cleary Gottlieb. Prior to that he spent 26 years at the European Commission serving most recently as the director responsible for telecommunications and media in DG Comp.

Dr. Patrick Rey is a Professor of economics at the University of Toulouse as well as research director of the Institut d'Economie Industrielle.

He has researched many aspects of competition policy including the social benefits and private incentives for exclusive dealing, vertical integration, and refusals to deal.

Jim Venit is currently a partner in the Brussels office of Skadden Arps. He concentrates on European competition law

including representing multinational companies before the European Commission and proceedings under the merger regulation and Articles 81 and 82.

We regret that Professor Steve Anderman of Essex University in the U.K. was unable to join us today as planned because of family health problems.

Before we begin we have a few administrative details I've been asked to cover. As you know, we are located in the Great Hall of the main Justice building. And this creates certain security concerns.

If you are not a DOJ employee, you must be escorted around the building. Antitrust Division paralegals who are wearing name tags highlighted in green escorted you into the Great Hall.

They were available at the back of the room to escort you out of the building should you need to leave the session, to the restroom or upstairs to the seventh floor should you need to

make a phone call. Think of them as hall monitors.

Cell phones do not work very well in this part of the building again because of security concerns. Because leaving the building is difficult, refreshments are available in the back of the room.

This morning's session will be a combination of presentations and discussions. Around 11:00 we will take a fifteen-minute break and then come back for another hour, finishing up around 12:30.

The hearings will resume at 2:00 this afternoon for a three-hour discussion focusing on the EU's technology transfer block exemption regulation as well as agreements that fall outside the scope.

As you are undoubtedly aware and have already observed, the acoustics in the Great Hall are less than perfect. For those of you in the audience, if you have trouble hearing you might try moving to a different seat closer to the

podium.

Our audio-visual specialist in the back of the room also has a limited number of amplification devices available. Panelists, I request that you enunciate clearly as I'm trying to do. Speak slowly and talk directly into the microphones. Allow the microphones a second or two to activate before speaking into them.

And finally, please do your best to stick to your presentation times as we have a large number of speakers and we want to hear everyone's views.

During the discussion periods if you would like to raise a comment, make a comment, or ask a question, please turn your name tents up on end like this to signal that you would like to do so.

For those of you in the audience with questions for our panel, please come and talk to either Bill or me during the break. Time permitting we will try to pose your questions to the panelists. Let me now turn the microphone

over to Bill Kovacic who I think has a few remarks to add.

WILLIAM KOVACIC: I simply want to express my appreciation to our colleagues at the Department of Justice and the Patent and Trademark Office for hosting this wonderful event. I think all of us realize that even several decades ago it was incomprehensible that this type of hearing could take place.

And it's been the extraordinary development of competition law globally and the development of a remarkable infrastructure in many countries that permits us to take advantage of a rich collection of international and comparative perspectives.

And I simply want to thank this truly hall of fame panel for committing their time and in the spirit of these hearings bringing a great deal of fresh and imaginative thinking to this set of issues. And again to express my appreciation to Bill and his colleagues for being such wonderful hosts. Thanks, Bill.

WILLIAM KOLASKY: Thank you, Bill. And now let's turn the mike over to Jim Venit who has the initial presentation.

JAMES VENIT: Two things before I begin. I'm going to focus on two cases and kind of run through them very quickly because I think they crystallize what the state of European law is on enforcing licenses and intellectual property rights.

But I think it's very important to realize from the start that these cases both involve copyrights. There is no case that I'm aware of where there's ever been a license that's been required involving patent rights.

And there may be good reasons for that and good reasons why these cases ended up the way they did given the nature of the rights involved. And I think that's an important way to preface the discussion. Nature abhors a vacuum. Antitrust law abhors the monopoly. But there are statutory monopolies that are created.

And the issue of when you interfere

with that obviously becomes a complex one, not just economically but also in terms of overriding legislature. It's easier to do that when you have some doubts about the validity of the property right in question.

The first case I'm talking about is on the screen there. It's Volvo v. Veng. This involved body parts for side panels on automobiles. And subsequently after the European court handed down its judgment, the United Kingdom eliminated the property right.

And basically what the court in Volvo v. Veng said was that there were three situations that it could imagine clearly as illustrative of situations where it might be reasonable to override the existence of the property right.

One of them was the arbitrary refusal to supply spare parts to independent repairers. The second was where excessive prices were charged. And the third was where a decision was made to no longer produce the parts when the vehicles were still running around on the street.

And I think it's interesting just to look at those three things. Refusing to supply and charging an excessive price would arguably be inherent in the monopoly right.

Under patent law the refusal to work the patent or to continue to work the patent might be deemed as an abuse of the patent or might trigger -- if not deemed as an abuse might trigger the granting of a license.

And I think it's always interesting when you look at the European court judgments on these issues to ask yourselves to what extent is the court requiring a license in a situation that would seem to come within the scope of a monopoly and to what extent is it maybe doing something that would happen under the monopoly legislation itself if the right owner did that.

And I think in Volvo v. Veng two of the things clearly come within the scope of the monopoly. The last one might arguably involve a non-exploitation that could trigger a license.

The second case is the famous Magill

case which involved a very valuable listing of television programs. And the plaintiff in that case wanted to put the television listings of three stations together into a weekly listing.

And the television stations that owned

the copyrights refused to grant that right. And a license was required by the Commission. The case was appealed. And the Court of Justice upheld the Commission's decision and set forth four criteria which if they applied the court said could result in the granting of a license.

The big debate about Magill is whether these criteria are cumulative or not. But the four criteria were that the broadcasting companies were the only source of the information, that the refusal to grant a license prevented the appearance of a new product, that there was no justification for the refusal, and that the broadcasting companies were reserving a secondary downstream market for themselves by excluding all competition on the market.

I should point out that there's

been a subsequent judgment of the Court of First Instance which has read these criteria as being non-cumulative and said either the unjustifiable refusal to grant an essential -- to grant access or grant a license to an essential input could be an abuse or the attempt to monopolize the secondary market could be an abuse.

But that's only the Court of First Instance and not the Court of Justice. Again if you look at the Magill case one could rationalize here forgetting the nature of the right and saying, well, this really involved a form of non-exploitation of a property right.

And so one could make an exception in granting the license or requiring the license to be granted there. These are basically the two leading cases.

There's now a third case that the Commission has brought and which is now on appeal where the Commission basically threw out the window the secondary market characteristic and is applying or seeking to apply the Magill reasoning

to a situation where a right holder has refused to grant a right so it can continue to monopolize the same market that the right exists on.

And some of the members of our panel are involved in that case, and I will leave it to them to banter that one around.

I think in summary if one stands back from this there are a couple of things that can be said: One, there haven't been a lot of cases; two, there's never been a case that's involved something other than a copyright; and, three, some of the court's reasoning would clearly seem to be inimical to the notion of the essential right itself.

And some of its reasoning would seem to be consistent perhaps with doctrines of non-exploitation that can come up at least under patent law. I think I'm going to stop at this point so we can allow a lot of time for discussion.

One other thing that I think is worth noting, my personal view when we talk about

essential facilities is that that term is not really useful to this discussion at all. I think it's very useful to focus on the nature of the right and the fact that these rights are statutory monopolies.

Essential facilities doctrine has a very, very rich tradition and its place in analysis, but I think only when there's an essential facility. I think when we're dealing with property rights it's much more useful to focus on statutory monopoly. Thank you.

WILLIAM KOLASKY: Thank you, Jim. Before we turn to other speakers, are there any questions from the other panelists for Jim? I have one if I can start off with that.

In putting up the criteria in the Volvo case, one of the ones you mentioned was that the copyright holder was charging quote, unquote, excessive prices for the spare parts.

I know under Article 82, as written, exploitative pricing would appear itself to be an abuse of dominance. How widely is that actually

enforced in the European Union and its member countries, especially with respect to intellectual property rights?

JAMES VENIT: I think the answer is not at all in my experience. The Commission has recently been complaining about termination charges for roving fees amongst cellular phone operators and has I think initiated a case against the Dutch PTT in that regard.

I was once involved in a case where the Commission was considering the problem of excessive pricing by a pharmaceutical company. We convinced them to abandon that I think wisely on their part. So this is not an area where there's been very much vigorous enforcement at all and I think for obvious reasons.

WILLIAM KOLASKY: And then the other question I had which was obviously provoked by your very opening is whether you have any speculation as to why these cases tended to involve copyrights rather than patents.

JAMES VENIT: Because they came up I

guess. No. There is a case where the Commission rejected a complaint that would involved licensing of patents, the Lederle case.

You know, I think they came up because people wanted to have access to the rights. I think the results came about because we had copyrights and not patents. Beyond that it's hard to speculate as to why.

WILLIAM KOLASKY: Yes, John?

JOHN TEMPLE LANG: Jim, it's perfectly correct to say that there hasn't been a formal decision concerned with patents. But there is a case which is referred to in my paper where the Commission took action and by consent a license of patents was given.

It's the Solara case in which there was a complaint by a small Finnish television set manufacturer. It involved a patent pool of German television transmission and receiving equipment manufacturers.

The Commission took the view that the patent pool had a duty to license the new technology for stereo transmission and reception. And the companies got the message and agreed to grant the license. So there was no formal decision. But there is no doubt there were patents involved.

WILLIAM KOLASKY: Ian?

IAN FORRESTER: I might offer necessarily a partial answer to your question about why the cases have touched copyright. Copyright is particularly unharmonized in the European Union.

And the fifteen member states are obliged by the Berne Convention to extend copyright protection to certain things. Community legislation obliges them to extend copyright protection in the field of databases and software.

But they have the right to extend copyright protection in other directions. And I think that it's no coincidence that the Magill and IMS cases both related to copyright being involved in what would seem a surprising set of circumstances.

WILLIAM KOLASKY: Thank you. Jim?

JAMES VENIT: Just very briefly, on the Solara cases, one of the very, very early cases, I think one has to understand that is a horizontal case where you had a patent pool that essentially created a standard, and then there was a refusal to license a smaller competitor.

To me that's a very set of different facts than unilateral conduct when one owner is acting alone in refusal to license. And I think that's why I didn't focus on that.

There is a case, the Lederle case, where the Commission said, no, we would not force a license in that case for a pharmaceutical patent.

WILLIAM KOLASKY: And that certainly is a distinction under U.S. law as well where the essential facilities doctrine has been used more widely to compel access to bottleneck facilities owned by joint ventures as opposed to individual firms. Mary?

MARY CRITHARIS: Yes. I have a question for any one of the panelists. We're talking about refusal to license. And I wanted to know if there were any cases in Europe where there was a patent involving a patent that has not been worked.

WILLIAM KOLASKY: John?

JOHN TEMPLE LANG: There have been a number of cases that I know of under European Community law. But there were a number of cases under national patent law.

And most, but I think not all, of the national patent legislation provides for compulsory licensing for essentially public health grounds for pharmaceutical products.

WILLIAM KOLASKY: With that, a sort of introduction and overview of the European law with respect to the application of essential facilities to intellectual property, let me turn the mike over to Patrick Rey who has written a very interesting and provocative paper on vertical integration which is in the materials, which frankly I think it would be fair to say challenges the conventional thinking with respect to vertical integration in a way perhaps that it hasn't been challenged for 15 years. Patrick?

PATRICK REY: Thank you, Mr. Chairman. The economics of compensatory licensing correspond to vertical foreclosure concerns which also provided the basis for the so-called essential facility doctrine.

I would therefore like to focus for the most part of this talk on the analysis of vertical foreclosure. And I will at the end if time allows say a few remarks on more specific intersection between IP protection and competition policy.

The general framework where vertical foreclosure can be a concern is one where some upstream good or service, sometimes referred to as a bottleneck of the essential facility, is controlled by a monopolist while the downstream and relative market is potentially more competitive.

There are some variants of this basic scenario. In some cases the bottleneck can be an input, can be a raw material, as in commercial cell phones. In other cases it can be a infrastructure such as a stadium, an airport, a harbor, and so forth.

In other instances other than being an input it can be sold on a stand alone basis. It can be hardware as opposed to software. It can be operating system software as opposed to application software. It can be original equipment as opposed to spare parts and so forth.

Another distinction is whether the upstream monopolist, the bottleneck holder, is itself present or not in the downstream segment, so whether there is vertical integration or not.

The concern in those situations is that the upstream monopolist may prevent or otherwise limit access to its bottleneck in order to prevent or alter, monopolize, or at least arrest the competition in the downstream market.

In the traditional view the way it was

expressed is that for this concern the bottleneck owner may try to seek to leverage its market power in the upstream segment into the downstream market. Depending on the context this monopolization could be achieved through various practices.

When the bottleneck holder is itself present in the downstream market, then it can refuse to deal with other competitors, or it can choose to make its product -- its bottleneck incompatible with the good or service that is being provided by the downstream competitors.

Or it may decide to charge high wholesale prices which being present doesn't -- even if it charged the same price, its purely internal price, that makes a difference.

Or alternatively it can engage in tying and therefore force its customers to buy its own version of the complementary good in order to have access to its bottleneck good.

In the absence of vertical integration the upstream monopolist can alternatively seek

to favor one or a few of downstream competitors either through exclusive dealing or through price discrimination or through other types of discrimination such as not releasing the appropriate information, delaying supply, delaying the delivery of new and important versions of the product and so forth.

This monopoly leverage concern has been criticized by the so-called Chicago school which pointed out that while the bottleneck owner clearly has some market power in the upstream segment and was therefore expected to exploit that market power, it could also act directly in the upstream segment and therefore did not need to distort downstream competition.

And there were two variants of this critique which reflect the two types of models, the input model versus the stand alone model. The bottleneck as an input, used as an input, then the monopolist can simply charge a high price for this input.

And to be sure, the demand for the

final good eventually is a source of profit. But you cannot expect the monopolist to be able to have this profit twice. There is only one profit to be made basically. And charging a high price for the input will suffice.

And therefore if the monopolist chose to not deal with some of the downstream competitors or otherwise affect competition it cannot be because it wants to leverage its upstream market power.

It has to be for alternative and efficiency enhancing reasons: protecting reputation, providing good services, and the like. When the input is sold as a stand alone product, maybe the argument is even clearer.

If the consumer needs the monopolized good or service in order to be used in combination with other goods or services, then the monopolist can simply charge the monopoly price for the good.

And actually if there is more competition in the complementary segment, then

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this increases the value of the monopolized good. And therefore the monopolist should welcome such competition in the complementary segment.

This Chicago view has had the beneficial of effect of forcing industrial economists to reconsider the foreclosure argument and to put it in what I believe is on firmer ground.

In the last ten to fifteen years we indeed have seen developments in the economic culture that account for the Chicago critique and yet provide a rationale for vertical foreclosure concerns. There again one needs to distinguish the input mode and the stand alone mode.

When the bottleneck is used as an input, then the clear idea that was first expressed by Hart & Tirole in a 1990 paper and has been followed by others since then, was that the upstream -- or is that the upstream monopolist in practice will find it difficult to fully exploit its market power without some form of exclusion.

And therefore the concern is not about extending or leveraging the monopoly power from the upstream segment into the downstream segment. The concern is simply that the monopolist will seek to distort or reduce downstream competition in order to better exploit its upstream monopoly power.

I'll come back to this very shortly. If the bottleneck is used and sold directly to consumers on a stand alone basis, then there have been a couple of papers that have also pointed out the possible anticompetitive points.

There is a well known paper by Whinston that shows that committing to tying might be a good way to deter entries or it could be used as an entry deterrence strategy provided that there is not not too much complementarity between one good and the other good.

And more recently there was a paper by Carlton & Waldman that expressed that the upstream -- monopolist in the home market, in order to prevent entry in the home market it

might be a good idea to prevent entry in a related market in some sense.

The entry in the related market, potentially a more competitive segment, may be a first step towards entry into the home market. Actually this is a variant of protecting the monopoly power of the home market but in a dynamic version of the argument.

I will focus on the case where the bottleneck is used as an input which is probably the relevant case when it comes to patents and IP rights. Let me take one example.

Consider an industry where a bottleneck owner supplies an input to downstream competitors and will then transform this input into a final good on a one-on-one basis.

And suppose that the way the industry works is that first each downstream competitor must order a different quantity from the monopolist which determines the level of capacity of the downstream firm in its market.

And then second given those

capacities, given how much they have, the downstream firms compete on price. Now, from an industry perspective it would be a good idea for the monopolist to make sure that overall the capacity remains at the monopoly level and therefore is restricted.

But when its downstream firm negotiates and deals with the monopolist, the downstream firm will have an incentive to order, and the upstream monopolist will have an incentive to indeed supply quantity that is the best reaction to the overall quantity that will be put forward in the market by the others.

In other words, this type of situation

gives rise to a situation that really looks like what we call a Cournot situation, firms attempt to compete in a market.

And we know that this will lead to a more competitive outcome than the monopoly outcome. And if there are more competitors in the downstream market, then the outcome will be even more competitive. And eventually all

profits may be dissipated in this way.

The same problem arises in the context of franchising or licensing agreements. A patent holder, for example, is unlikely to make much money if it cannot commit itself not to flood the market with licenses.

And indeed if everyone holds a license, then downstream competition will dissipate the profits that could have been generated by the patent.

There again the patent holder would like the promise that the number of licenses would be limited or that future licenses will include provisions to limit downstream competition.

However, again there is a commitment problem. Once the patent holder has granted the license, it will naturally be tempted to sell additional licenses. And also in order to increase the value of those additional licenses it will introduce restriction on those future licenses.

Of course anticipating this or a commitment problem which depreciates the value of the first licenses, the first licensees will not be willing to pay as much as they would have for the license.

To solve this commitment problem and better exploit its market power in the battle, the case owner can have one of several approaches. First it can decide to enter itself in the downstream market. And then when dealing with other downstream firms it will no longer incentive to free ride on its own strategy.

It may still choose to deal with other downstream firms, particularly if they have a specific advantage in developing practical applications or in introducing particular customer groups. But it will have a natural incentive to preserve and exploit any overall market power.

Short of entering the market, the upstream bottleneck owner can choose to deal exclusively with some of the downstream firms,

alternately to favor some of the downstream firms over other competitors.

In the context of IP rights this would amount to giving an exclusive right to one particular firm and a refusal to grant any additional licenses.

Let me stress that in this context the outcome and the exclusive dealing arrangements may well be worse than vertical integration and worse I mean both from the point of view of the firm but also from the point of view of social welfare.

If, for example, the upstream monopolist has a specific advantage in developing an improved version of the downstream good as Commissioner Sullivan claimed -- and I'm not saying here that the claim was correct or not. But at least the claim was there.

Then it may indeed be better to have the upstream monopolist producing the downstream good itself rather than leaving the production of the downstream goods to less effective firms.

Note also that there may be a danger in basing the compensatory licensing decision on whether the monopolist, the upstream monopolist is vertically integrated in the upstream market or not.

This might tilt the firm's decision in favor of granting an exclusive license rather than entering the market itself, which again may not be very efficient if the upstream firm has a comparative advantage in the development of new products.

What I'm trying to stress here is that really it is important to keep in mind what would be the relevant counterfactual. Otherwise you might well end up with the result that is the opposite of what you are looking for.

Let me note two remarks on the last two lines on the slide here, the one versus two markets. What matters for the analysis is that the upstream monopolist controls the bottleneck without access to which one cannot compete in the downstream market.

Whether there is actually a market or what someone called a market for this bottleneck is not the issue. And indeed in the case of vertical integration the monopolist may well choose to reserve this bottleneck for its own use so that in that case there may indeed be no market for it.

But it's precisely this type of situation that the foreclosure concern may be relevant.

The second quick point on the new product, what is meant by new product here for the analysis or for competing product is really the fact that it's not you have a competitor that could produce a new version or improved version of the product.

What matters and what is potentially beneficial, what prevents the exploitation of market power is really the fact that there is a competitor.

And if a competitor simply offers the same good or competes with the same good, that's

fine. If in actuality it's competing with an inferior good, it may still exert some competitive pressure on the upstream monopolist and therefore we will have a more competitive outcome.

I have so far focused on identifying and possibly, hopefully clarifying the foreclosure concern. I do not mean of course to give the impression that vertical integration or exclusionary practices are necessarily bad.

And while they may serve anticompetitive purposes, they may also serve legitimate and efficiency enhancing purposes. For the sake of time I will not spend much time on this, and there is a lot of discussion in the written paper that has been submitted.

But let me just mention that in the context of IP rights probably the most relevant line of efficiency defense lies in the need to protect new investments in R & D and innovation. And one may indeed wish to tolerate some foreclosure activity and static inefficiency as a

means to promote dynamic efficiency.

This provides a good reason, for example, for being more tolerant when the bottleneck is the result of innovation as opposed to the result of increasing in terms of scale or as a result of historical accident.

It is first in this context that in

fact we fine tune the amount of tolerance or regulate the rate of return on that bottleneck itself. And we know that such regulation is not an easy task even in industries where regulators have been supervising the bottleneck for years or decades.

So at the very least one should be very cautious when it comes to striking the right balance between static and dynamic considerations.

This brings me to the second topic I would like to briefly touch upon which is about the respective roles that IP rights and competition policy can play in achieving the adequate balance between ex ante incentives to

innovation and ex post competition.

It may actually be useful to recast this in terms of competition in innovation versus competition in the product market itself.

One possibility regarding the division of tasks is that the Patent Office and the competition authority could or should play the roles of advocates for respectively the protection of innovation on the one hand and the promotion of competition, product market competition on the other hand.

As my rephrasing in terms of competition in innovation versus competition in product market suggests, I'm not sure that this approach is a desirable one.

In addition at the moment it's not clear to see who could play the role of the judge in front of those two advocates. Another approach consists of identifying the competitive advantages of patent offices and competition agencies.

For instance, the Patent Office will

be typically in a better position to assess the importance of the investment and also the social value of the innovation, the novelty, for instance, of the innovation.

Still the Patent Office will typically

have to rely on uniform rules that are best designed to fit the average case but may make it difficult to fine tune the level of the rents that an innovator should get.

In practice all sorts of problems call for some case-by-case analysis. For example, lock-in problems may give an excessive reward to the first innovator and prevent the reward of other innovators that later provide alternative ways to service a need.

Competition authorities are typically better suited to operate such a case-by-case analysis. But on the other hand they are often subject to a natural tendency to place a legal weight on ex post product competition.

Even sticking to the design of average standards, patent offices and competition

agencies can play complementary roles. For example, the breadth of the patent affects both the profit of the innovator, of the patent holder, and it also affects this call for imitation.

And therefore in order to both prevent inefficient imitation and at the same time avoiding giving excessive rewards to the innovator, it might be useful to complement the IP protection with antitrust enforcement.

Beyond the potential risk of excessive rent expropriation by competition agencies, striking the appropriate balance between ex ante competition in innovation and ex post competition in the product market is clearly not an easy task.

But I would like to mention that there is a third dimension which concerns the diffusion of innovation. I'm not going to insist on that issue which is more relevant I think for the afternoon panel.

But I would like to stress here that

facilitating the diffusion of innovation is probably a very effective way to enhance both the ex ante incentive to innovate and also the competition for future innovation.

And therefore I think that this is really a key issue on which agencies should put a large emphasis when determining under which conditions technology transfers can be made.

Let me conclude by stressing that from an economic perspective IP rights should be treated according to the same principle as for any other property right. In particular IP and particularly property patents should not be confused with market power.

There was the 1989 OECD report on competition policy and IP rights. There was a survey of licenses that shows that in 27 percent of the cases the patent holder did not -- was not exposed to competition. So there was a real market power there.

But in 29 percent of the cases the patent holder was facing at least ten competitors

or there were ten substitutes in the market in which case even though there was a patent that doesn't mean that there was significant market power.

So that's just a way to emphasize the fact that indeed IP rights are really a form of property rights, but that there is nothing special, nothing magic about it.

That being said, in some cases clearly a patent can be a bottleneck or the essential facility in the sense that without access to this patent you cannot operate in a given market.

But clearly striking the right balance between the ex ante aspect and the ex post product competition is again a very difficult exercise.

And trying to identify what will be the natural duration of effective return on the investment made to achieve this -- to produce this innovation is clearly a bit tricky.

And the idea of giving the -- calling in the courts and asking the courts to determine

the price is an issue that really one should deal with with caution.

Now, that being said I think that on both sides of the Atlantic the institutional development doesn't look for antitrust interpretation when it is clearly wanted.

And on both sides of the Atlantic, competition agencies and court, maybe someone could say that in EU the court may be more than -- the competition agencies have been quite careful in restricting intervention to exceptional circumstances where really such intervention is clearly wanted.

I hope that they will continue to demonstrate the same caution, and I also hope that the economic analysis that I only briefly highlighted here will help competition agencies to determine when and how to intervene. Thank you.

WILLIAM KOLASKY: I think you can see why I described Patrick's paper as provocative and as a challenge to our conventional thinking.

Patrick, let me ask you as a first question and we can try to get some discussion going, on page 5, your statement that an upstream monopolist cannot exercise market power without exclusion, to what extent if at all does that depend on the monopolist being able to price discriminate?

Would that be true if you are in a market in which price discrimination is not possible?

PATRICK REY: We actually make in the paper the funny remark that nondiscrimination laws do facilitate a lot of exercise of market power.

I mean in a good way -- what the monopolist would ideally want is to ensure that prices will remain high, quantity will remain low, and fight requests by individual downstream competitors for more quantity, better conditions, and so forth.

And nondiscrimination laws are a very good and effective way for the monopolist to commit itself not to favor one competitor against the other and resist the temptation or the pressure to provide more output or better access or better conditions.

WILLIAM KOLASKY: But I suppose I'm thinking about situations where due to the characteristics of the market price discrimination is not possible, for example, perhaps because arbitrage is easy. Would the same be true there? Would that have the same effect as having nondiscrimination laws?

PATRICK REY: I will have to double think about this. My gut feeling would be that it's not exactly the same thing. So it may not suffice to evaluate the concern.

WILLIAM KOLASKY: And I think the other question -- and I want to allow time for the other panelists -- is to what extent if at all you try to test these results empirically.

That is, certainly I think many of us think that we have over time observed higher prices in markets where you have monopolists, even though those monopolists have not engaged in exclusion. So the question is: Have you tried to test this proposition empirically?

PATRICK REY: To be sure there are many ways in which this can be done. One way would simply be to develop a reputation not to discriminate and not to give in to terms and so on. So the question is to what extent this commitment problem exists and is severe in practice.

That's a very good question, and I don't think it has been on purpose. That is, looking at this particularly there has been an interesting experience that has been made.

So this remains -- I'm here referring to experimentally other than actual business case studies. This experiment was conducted by Steve Martin and he has published a paper on this which suggests that when you do this experiment that you put players in this type of situation. Then the commitment issue may be a problem.

WILLIAM KOLASKY: And a final

question, not seeing any flags raised, is whether you have thought about or tried to develop what if any legal rules you think should flow from the insights contained in your paper.

PATRICK REY: Well, there were some dividing lines that are suggested. So, for example, one is when you have a bottleneck, one question you may want to start with is what is the origin of the bottleneck.

Is it just there because historically there was a monopoly that was counted without -- and is the conditions of the technology or the market such that it's no longer wanted but you have given -- you have to start from this situation.

Is it because of economies of scale and scope? In those cases intervention may be more warranted than cases where the battle in the case is simply the result of innovation. So these are some ideas like this that are developed.

WILLIAM KOLASKY: Bill?

WILLIAM KOVACIC: As the presentations have mentioned, in using an essential facilities framework there are basically three issues that a court or a tribunal has to address.

It has to define what it means to be essential. It has to identify what justifications for limits or refusing access are acceptable.

And if it decides that access must be provided as Patrick has identified, it has to decide the terms on which access might be provided.

And I was wondering -- if the panelists in looking at their own jurisdictions -- if there is a sense that in setting the last of these conditions, that is the price for access, are tribunals comfortable with undertaking the role of setting the access price.

And are they doing it in a way, as Patrick suggested they might, taking account of incentive consequences of setting a price for access to, say, an intellectual property right?

WILLIAM KOLASKY: Provocative question. And hearing no immediate response -- Jim?

JAMES VENIT: I'm going to duck the question a little bit. But there's been a very interesting Commission decision in granting access to I believe involving Deutsch Post to its delivery system where the Commission used the notion of recoverable costs as one of the benchmarks in formulating the access price, which I think shows a certain amount of greater sophistication in the analysis than one might have been concerned one would get.

But it's obviously a very, very difficult issue. And particularly I think Patrick's distinction between whether you have an historical monopoly as opposed to an earned monopoly I think is very critical in determining that access price because you want to reward the earned monopoly more than you will conceivably the historical monopoly.

WILLIAM KOVACIC: Jim, many of the

formative essential facilities cases come out of an environment that might be called a regulated industries environment.

And perhaps postal services fits into that model. Do you have an intuition about the capacity of a tribunal to account for the element of risk in undertaking the innovation that generates the intellectual property right?

That is, is this a dimension that is captured in the essential facilities jurisprudence, or is this something new that tribunals are going to have to confront in the future if they walk down a path that mandates access to the intellectual property right?

JAMES VENIT: I think it's going to be the latter. They're going to have to confront it again. I mean the Deutsch Post case involved what I would regard as a classic essential facility case. It didn't involve IP.

And so you can deal with cost elements

that were in a sense more knowable. I mean as soon as you get into rewarding the inventor for

his invention, that calculation I think is going to be much more difficult because you want to incentivize the risk involved in going into the invention.

And I think that's why that latter is going to be a much more difficult judgment to make and maybe one that can't be efficiently made.

WILLIAM KOLASKY: Thank you very much, Patrick. As I say, a very provocative paper. It raises a lot of issues that warrant further study and research.

The next presentation will be made by Gwillym Allen who is going to talk about Canadian approaches to compulsory licenses. Gwillym?

GWILLYM ALLEN: I'd like to thank the DOJ and the FTC for inviting the Canadian Competition Bureau to participate here today.

This is a very important and valuable exercise in the knowledge that these and past hearings generate, informing certainly the

Canadian antitrust agencies and other practitioners throughout the world. And the information and knowledge here has always proved and I'm certain will prove to be invaluable.

I have been asked today to talk about and describe the Canadian approach to intellectual property and particularly a refusal to deal. And this is dealt with within our intellectual property guidelines, or as we refer to them in Canada as the IPEGs.

And the IPEGs are available on our website which is at competition.ic.gc.ca. And I'll put that website up at the end. I'll try to keep my comments short, and I won't go through my whole presentation. The presentation is available at the back. And I'm just going to concentrate on a few things.

First of all, the intellectual

property guidelines start out by the usual compulsory requirement that we acknowledge that intellectual property regimes and competition laws are complementary and they share the same

goal and that they are there to promote -- both are there to promote innovation and technological change.

In developing the guidelines, there are two main points that you have to understand in Canada. The development of the guidelines was driven primarily by the structure to the law and to some -- a lesser extent by the jurisprudence.

The point to understand is that the structure of the Canadian law can be thought of as being divided into two general sections. There's what we refer to as the general provisions. The general provisions are divided into civil provisions and criminal provisions.

And as the names apply, we have criminal law and civil law. And they deal with the traditional antitrust offenses or issues of price fixing, price discrimination, exclusive dealing, tied selling, abuse of dominance, and merger review.

But we also have what is referred to as special remedies or section 32. And I will

just jump over.

The only other thing I will say about the general provisions is there is an exception in section 79 which is the abuse of dominance position which basically says that the mere exercise of an intellectual property right cannot be considered an anticompetitive act.

Our abuse sections require that the firm is dominant and that the firm engages in anticompetitive acts. And section 79(5) says that the mere exercise of an intellectual property right is not considered an -- cannot be considered an anticompetitive act.

Section 32 -- and I put the whole section in the outline or in the remarks. And I won't read the whole section.

Basically section 32, the special remedies, provides the Federal Court the power to make remedial orders when it finds that the use of an intellectual property right results in an undue lessening of competition or restraint of trade.

And it has some very broad -- it has broad remedies that it can invoke including declaring any agreement or license relating to the use of the IP void, compulsory licensing, revoking a right, and any other direct action it considers.

Now, with regard to the jurisprudence, Canada has very little jurisprudence with regard to the interface between intellectual property and the Competition Act. However, we have one case which is Tele-Direct and another case in Warner. Warner basically just quoted Tele-Direct.

And basically what the jurisprudence says is what 79(5) says, which is that there has to be something more than the mere exercise of the statute -- of the intellectual property right in order for there to be found a misuse of trademark. This was a trademark case.

And basically what we did in the intellectual property guidelines is we took that concept and applied it to all the general

provisions.

And what that basically meant is that we were in a situation in which we had the general provisions which said that the mere exercise of the intellectual property would not violate or raise an issue under the general provisions of the Competition Act.

But under section 32 it's clear that the mere exercise of the right would raise an issue under the Competition Act which meant that from our perspective we had to define what we meant by the mere exercise of the right.

And in the guidelines we defined the mere exercise of the intellectual property right as the unilateral exclusion from use. And again we were in the situation where the general provisions and the jurisprudence basically told us that the mere exercise of a right is not anticompetitive.

But under section 32 the mere exercise of the right can be anticompetitive which required that we set out in our guidelines the

definition of what we meant by the mere exercise. And the definition is the unilateral refusal and nothing more.

We then defined when the general provisions would apply and when the section 32 would apply. And it allowed us to make what we referred to as the election between the general provisions and section 32.

And basically in the general provisions we took our definition, the unilateral right to refuse and nothing more, and we defined basically when that did not exist.

And that fell into three categories:

joint or coordinated behavior because it is not unilateral, licensing because it is not a refusal, and then situations where you may have a refusal but you have something more.

And with regard to section 32 then section 32 would apply to situations in which there was the competitive harm flowing directly from the exercise of the right.

The only way that you could challenge

or correct the anticompetitive consequence was to challenge or address the exercise of the intellectual property right directly.

So here's my diagram. So basically we had these two situations. There's more than the unilateral exclusion. Then we dealt with it under the general provisions because, as I said before, it will require either joint behavior, licensing, or something more than a simple refusal.

And then under section 32 it's the mere exercise or the unilateral exercise of the

IP right to exclude and nothing more. And that's when section 32 would be applied.

The guidelines outlined when we would and how we would deal with section 32. And we describe a two-step approach. What I should mention is that we have no actual jurisprudence on section 32.

But we were compelled to provide guidance on when section 32 would or would not apply. And this is the adoption of a two-stage

approach to first try to identify when the "unduly" aspect or component of section 32 would apply.

And then we added a second step which we looked at 32 and asked the question that in order to ensure that 32 maintained the integrity of the complementarity between competition law -- the Competition Act and competitive laws in general and the IP laws. We added a second step.

We asked this question: whether or not invoking a remedy, i.e. forcing compulsory licensing would adversely alter incentives to invest in research and development. And the guidelines sort of point out some of the things that we look at in trying to determine each of them.

In the first case with the idea of undueness, two of the factors that we point out that we would look at and deal with would be to try to identify whether the mere exercise of the right indeed resulted in an undue lessening of competition or restraint of trade.

If the holder of the IP is dominant in the market and the IP is an essential input for firms to participate in the market. Here is a diagram I included in the handout which tries to describe the general approach of the IPEGs.

On the left-hand side is the general provisions, what will put you into the general provisions, and what particular sections. And a traditional antitrust type of analysis would apply for each of the three categories in which the harm stems from something more than the unilateral exclusion.

And the right-hand side is our description of how we would apply section 32. And I think my time is up.

But because we have no jurisprudence we did provide in the guidelines a hypothetical case which is example Nine which dealt with a situation which I'm sure the Americans will find very familiar in which we describe how the Bureau would deal with this situation in which we decided that this would be a case in which we

would apply section 32.

There is the website at the bottom, competition.ic.gc.ca where you can access the guidelines. And if you have any questions, I'll be happy to answer them.

WILLIAM KOVACIC: I think all of us who are lawyers realize that one of the great inventions by lawyers in the field of the English language is the use of the word mere. That is, the mere exercise is not unacceptable, but anything -- the interesting question is when do you tread beyond mere exercise.

And I was wondering if I could just pose a couple of quick questions to Gwillym before we go on to Henry's survey of approaches in Australia.

One is, Gwillym, if we think of the problem we were talking about when Jim spoke before about the issue of excessive pricing, would you say that it was contemplated in writing the guidelines that a decision by the holder of an IPR to set a price at any level it wished,

that is, assume a price of infinity, as high as it wanted, was it contemplated that there would be any notion of excessive pricing under the guidelines?

GWILLYM ALLEN: I guess the short answer is no. We thought the majority of the cases that we are going to see are going to fall into general provisions. They are going to be under abuse of dominance.

And we do not have an exploitative or excessive pricing. It has to engage -- the dominant firm has to engage in an anticompetitive act which does not include pricing.

WILLIAM KOVACIC: And maybe just one other quick question. Could you maybe say a bit more about how -- if we go to the special remedy provision in the last box on the diagram you showed toward the end of the presentation, is there a thought about how the tribunal would perform the trade-off between competitive harm and possible harm to innovation incentives?

GWILLYM ALLEN: Well, we gave it a lot

of thought. First of all I should point out that under the special remedies not only is it special in terms of what it says within the law, it's special in how it's treated by the courts.

The civil provisions are referred to the competition tribunal which is a specialized court made up of judges and industry experts.

The criminal provisions, as the name suggests, go to the criminal court. Special remedies goes to the Federal Court.

And the Federal Courts are there to make these -- and judges are there to make that type of trade-off between whether the private interests in the ownership of the intellectual property should be balanced and how it is to balance and should outweigh or not the public interest in free and open competition.

And so the idea here was that it would go to a court where judges traditionally make these types of social/economic trade-offs instead of going to a criminal court for something that's clearly criminal, or the competition tribunal

which makes a decision based on pure economic efficiency grounds.

So that's what we presumed was the legislative intent of why they separated it out and made it so special.

WILLIAM KOLASKY: Thank you very much,

Gwillym. Our next speaker is Henry Ergas, who's going to talk about Australian approaches to compulsory licensing. While they are setting up Henry's slides, Henry will be the last speaker before the break. But we have also allocated twenty minutes after his presentation for discussion.

So I'm going to invite the other panelists to think about questions they may have for each other or comments they may want to make on one another's presentations so we might be able to get a little bit of a free flowing discussion going. Thanks.

HENRY ERGAS: Thank you very much. And thank you for inviting me to participate in these hearings today.

The general issue of whether it's desirable to have some type of obligation to license intellectual property and the economic costs and benefits of any such obligation have been well set out in the written material that's available to you and in the other papers.

And I won't go into them in any detail other than simply to say that there are obviously complex trade-offs involved. The situation in Australia is in some respects complicated but in others perhaps relatively simple.

We have provisions in the main intellectual property statutes that are relevant here. And then there are also provisions in our competition law which is the Trade Practices Act.

And probably the distinction between those is that the provisions in the intellectual property statutes construct obligations to license or define situations in which there is an obligation to license, whereas the provisions in the Trade Practices Act define circumstances in which the refusal to license may be in breach of

the law.

Looking first at the intellectual property statutes which as I said construct some obligations to license, there is a relatively sharp contrast between the Copyright Act and the Patents Act.

Of course consistent with our obligations under TRIPS we do not have any obligations to license in respect of trademarks. So the main obligations to license that are relevant -- there are others in minor IP statutes -- are under the Copyright Act and under the Patents Act.

The difference is that the Copyright Act defines obligations to license in a very wide range of circumstances though those circumstances are then narrowly identified in the statute.

So they are narrowly defined in the statute. And there is a relatively sharp contrast here between the approach to copyright legislation in Australia and that in the United States.

So we have in the Copyright Act these circumstances in which either there are absolute defenses against claims of infringement or obligations to license that are statutorily administered.

In contrast in the Patents Act we don't specify the circumstances in which an obligation to license may arise in any great detail. But we do define a test and then subject individual instances to that case by case test.

It's fair to say -- and I think this comes to a point that was raised earlier in the discussion -- that it is mainly in respect of the copyright legislation that the issue of the extent and implementation of the obligations to license has arisen.

In my view there is a substantial economic or underlying difference between what we attempt to do in the Copyright Act and what we attempt to do in the patents situation, the Patents Act.

In the Copyright Act the main

justification for the fairly extensive provisions that we have that construct an obligation to license lies in the transactions cost difficulties that would be involved in attempting to secure efficient access to copyrighted material.

In other words, the provisions in the Copyright Act broadly deal with situations where the transactions costs involved would be so great in securing negotiation on an efficient basis between the owners of the right and potential users that it is more efficient to in those circumstances convert the property rule into a liability rule and construct a statutory administrator for that liability rule.

In contrast in the Patents Act we're basically dealing with situations which involve market power. And though those two go to transactions costs considerations at a quite fundamental level, they obviously are much more case by case in their nature.

The Patents Act provision dates

back many years though it was reinstated in the

Patents Act of 1990. And it can be broadly seen but not exclusively seen as the ability to secure an order compelling a license in circumstances where a patent is not being worked to the interests of the Australian community.

The provision itself, its precise effect is somewhat unclear as it has not been frequently tested in court.

However, in the proceedings of the committee I chaired for the Commonwealth's government on the act, it was put to us with great strength by particularly the patent attorneys that the provision has a significant impact in their negotiations with rights owners.

The committee recommended changes to the provision. And in particular we recommended that the criterion be changed into a competition test that would be broadly similar to the section 32 provisions that are available in Canada.

The government has recently announced

that it has accepted that recommendation insofar as it will retain the existing test it will add to it a new competition test which is currently being drafted and is expected to be tabled as an exposure draft in the course of the coming months.

Moving from the IP statutes to our competition laws, as I said, the competition laws define circumstances in which a refusal to license may be a breach of the law.

We are first noting at the outset that our Trade Practices Act, our general competition law, differs from that in many countries in having an explicit regime that deals separately with access to essential facilities. And that's part 3(a) of our act.

The act however in the context of part 3(a) constructs the specific exclusion of intellectual property from the scope of the part though it allows applications to be sought for access on those provisions of part 3(a) where the intellectual property is an integral but subsidiary part of a broader service to which application is being sought.

And some use has been made of a similar provision in the telecommunications access regime. And that has actually been implemented. Our committee was asked to review whether the exclusion of intellectual property rights from the general essential facilities regime should continue.

And we concluded that there was a case for maintaining the current exclusion essentially for the reason that first the decision of the essential facilities regime was poorly suited to handle intellectual property rights.

Second, we felt that to the extent to which one wanted to construct circumstances in which there were obligations to license, that was more efficiently done in the intellectual property statutes themselves.

And it was in the light of that that we recommended the reform of the Patents Act and also a number of reforms which have since been implemented to the Copyright Act.

And, third, we felt that insofar as refusals are anticompetitive, then the remedies should come in the general provisions of the act rather than in the essential facilities regime.

In terms of those general provisions which broadly define the circumstances in which a refusal to license may be a breach of the laws, the most relevant provision is our section 46 which is loosely equivalent to your monopolization provisions in the United States or to the misuse of power provisions in the EU.

And section 46 defines as a breach circumstances in which a firm that has a substantial degree of power takes advantage of that market power for a set of proscribed purposes which basically go to harming either competitors or the competitive process.

The important words in respect of the section and its interpretation are the words shall not take advantage of that power.

And the key issue that has arisen in

the case law is whether the mere -- and I use that term ill-advisedly I'm sure -- but the mere exercise of an IP right can be a taking advantage of market power given that the firm that lacked that power might still be in a position to exercise that right.

The case law is fairly uneven in this respect. But I think it's fair to say that since the Queensland Wire decision in our High Court it has been clear that -- at least this has been absolutely clear -- that the mere fact that the refusal or the conduct involved intellectual property in no way immunizes that conduct from the reach of the section.

So the mere fact that what is at issue here is intellectual property as against other forms of property is a matter of indifference to the court in determining whether or not a breach of section 46 has arisen.

And that is then apparent if you look at the decisions that are discussed in the paper that I've set out and in particular in a decision that involves the supply by the Australian Stock Exchange of information that it generated where in that decision as in the other relevant decisions the Federal Court both at first instance and on appeal has broadly indicated that there should be no difference between the analysis of the exercise of an intellectual property right relative to the exercise of any other kind of property right in respect of liability under that section.

In conclusion, we have a number of bases in the current Australian legislation that construct situations where either a license is compulsory or where the refusal to supply a license may be in breach of the legislation.

I've discussed the implementation of section 46 of the Trade Practices Act. It's worth saying that the government has just announced a review of that provision, and the issue of exactly when a breach arises will be one of the subjects of that review.

Also very important at least in

Australia are the provisions that are made under our intellectual property statutes themselves. And here we are seeing very significant reform both in the Copyright Act and in the Patents Act.

And if I may just say one word in conclusion, it seems to me that part of the impetus for reform of the provision in the Patents Act is that the change in the nature of patentable subject matter and of patented subject matter and in particular the growth of patenting related to software and to business methods has created at least in Australia concern that the types of provisions that we had in the Copyright Act may be rendered ineffective to the extent to which they are not paralleled by similar provisions in our patent legislation. Thank you very much, Mr. Chairman.

WILLIAM KOLASKY: Thank you, Henry. Because we're running a little bit late, I'm not going to direct any questions to Henry specifically. I would like to have a little bit of a discussion by the panel of the general

issues that have been raised.

And I would throw out three suggestions for things we might focus on. The first is that a number of speakers in describing the approach in their jurisdiction talked about the need to balance the adverse effect on competition of a refusal to license against the potential adverse impact on incentives to invest and innovate if compulsory licensing were to be required.

And I think that that invites consideration of what the best approach is given the institutional limitations of competition agencies and courts. That is, should that balancing be done on a case-by-case basis?

Should we have strong presumptions in place going in one direction or the other? Or should we have more akin to flat per se rules that unless a very clear set of criteria are met we will not require compulsory licensing of intellectual property rights?

A second sort of broad theme that came

through is that in all of the jurisdictions one of the factors considered is whether there is a quote, unquote, legitimate business justification for the refusal to license.

And again I think that invites an inquiry as to whether that is something that should be reviewed on a case-by-case basis, or whether we can deal with that through presumptions and general rules.

I think in the United States decisions such as Data General it's been suggested that a refusal to license, that is a desire to keep one's own property to one's own use and not share it with rivals, is a presumptively legitimate business justification because it promotes the policy of rewarding the inventor for their efforts to innovate and invest.

Is that the case in the other jurisdictions? To what extent have the courts and agencies actually engaged in a case-by-case review of the business reasons for the refusal to license? And then the third question really for

the entire panel is the one that I asked Patrick.

And that is given his challenge to us, if you will, to the conventional wisdom with respect to vertical integration, does that argue in favor of broader competition rules in terms of granting access to bottleneck facilities including intellectual property? And if so, what should those rules be? Comments? Questions? Henry?

HENRY ERGAS: I have a question with respect to per se rules versus case-by-case treatment.

It's worth noting that at least in Australia we do have particularly in respect to copyright a broad number of situations in which there is a per se obligation to make third-party access available and absolute defenses against infringement.

And the one that I think is most interesting that's recently enacted are the provisions that go to issues of computer or software interoperability where we have

provisions now in the copyright act that make it an absolute defense against infringement if the infringement or what would otherwise be infringement occurs only to the extent necessary to ensure that one can design programs that are interoperable.

And the question that was grappled with there -- and my committee recommended in favor of this provision -- was whether you should subject interoperability issues to a case-by-case treatment where you would say in this specific case is competition materially promoted or retarded by an obligation to make access available, or whether the uncertainty, complexity, and risk, and more generally the transactions costs for those users and owners of such a case-by-case approach would be so great that it would be preferable to go with some per se type of rule.

And we came to the view that an important factor making for per se requirement was first the simplicity of specifying the

circumstances in that case. I don't believe that that's always true.

And secondly if you had a case-by-case treatment and you had some type of process whereby an individual had to seek access, there would be an externality that would arise whereby one party would bear the costs of seeking that access.

But the benefits of that access would flow very widely. And so because of that we went for a per se approach which is now in the copyright act. Thank you.

WILLIAM KOLASKY: Thank you. That's very interesting to hear how that was dealt with in Australia. Ian?

IAN FORRESTER: I could mention that

the approach followed in Australia with respect to computer programs I think followed the European example where Article 6 I think it is of the software directive creates a legislative obligation to tolerate technical infringements of the copyright in order to pursue

interoperability.

And in European legislation on other fields database protection, the patenting of biotechnological inventions, other areas, the black letter law obliging the member states to implement national legislation executing the instructions conveyed by the directive also obliges them to insert provisions guaranteeing or confirming that the rights are always exercised subject to the competition rules.

So I think it may be that in Europe we see more in the form of legislative guidance lacking the richness of American jurisprudence in the form of many, many decided cases.

WILLIAM KOLASKY: Thank you. Jim?

JAMES VENIT: The courts have been involved in the European Union. The rule that's enunciated in Magill is that there's a presumption against the need to license. And the exception to that is exceptional circumstances which were -- you know, the Magill court attempted to define that.

And then that's like a word mere; what is an exceptional circumstance. But that I think is the basic approach, is a presumption against and then exceptional circumstances may override that presumption.

WILLIAM KOLASKY: And I suppose on the exceptional circumstances point in the United States the leading article on the essential facilities doctrine was Phil Areeda's 1990 article entitled "An Epithet in Need of Limiting Principles" which frankly came close to putting a spike through the heart of the doctrine at least insofar as it was being applied outside of the area of regulated utilities.

If you look at our case law over the last seven years, you will not find a single case in which the court imposed a duty of access that did not involve either a regulated utility or a joint venture.

And that I think leads to the question of whether there is support at least on this panel and if so what you think the likelihood

is that the courts and commissions in your jurisdictions would likewise move in this direction to limit the application of the essential facilities doctrine as someone suggested to situations where the bottleneck is the result of in effect a natural monopoly, that is substantially economies of scale and scope, as opposed to the result of invention and innovation.

And I would add in circumstances where the industry is regulated so that there is an expert agency that can regulate the terms of access rather than having the competition, authorities have to undertake that task.

GWILLYM ALLEN: I'm sorry. I'm not sure. I wasn't about to answer that question, but I was going to just return to your idea about the presumption and the balance between the adverse effect on competition versus the adverse effect on innovation.

And certainly we gave that a lot of thought with regard to section 32. And I guess

if you look at the way that we've approached it, it is that -- I guess our presumption is that we would find it very rare that we would use 32.

And basically what we did was we said that we would only apply 32 in situations where it was very clear to us that the effect on innovation or the effect of issuing a remedy or issuing an order would unlikely have any real adverse effect on innovation.

Now, how do you deal with that? What we did is we said we would only do this in those very rare situations where it is very clear that there was virtually very little time, effort, or resources devoted toward something that resulted in intellectual property protection.

And therefore if you took that protection away, would that adversely effect the incentives to have put time, effort, and resources?

And the answer was clearly no, because although they knew when they did that that they could have gotten protection in the future or

that protection was a possibility, they didn't bother putting anything in there.

So taking away the protection should indicate that there is not going to be a real adverse effect. But how often those situations arise is probably very, very seldom.

Therefore, there is this presumption that you would always -- if you were going to err, you were going to err on the side of allowing protection to stimulate innovation as opposed to on the other side.

WILLIAM KOLASKY: John?

JOHN TEMPLE LANG: Two comments. First it seems to me that there is an extremely strong argument against a case-by-case approach which is it just takes too long. And if you're trying to encourage innovation, the last thing you want is litigation between two interested parties lasting for several years.

Therefore you should try as far as you can to have general rules or at least presumptions which will deal with whatever issues

you can foresee in advance and give a resolution, good or bad, within a reasonably short time. That's my first point. Second point is an entirely different one.

It seems to me that in fact in most countries competition authorities, properly so-called competition authorities acting on the basis of pure competition law without regulatory powers are really not well placed to fix the terms, in particular the terms with regard to price of a compulsory license.

They may be able to do it easily by saying it has to be done on a non-discriminatory basis. But that will only deal with the simplest cases.

And I suspect that a competition authority that is serious about imposing compulsory license -- compulsory access obligations whether or not it concerns intellectual property will find itself trying to do the job of a regulator whether it particularly wishes to do so or not and whether it has the

power to do so or not.

WILLIAM KOLASKY: I think we're almost out of time. So let me just let David Hull who hasn't spoken yet have the final word, and then we'll resume after the break.

DAVID HULL: I just wanted to say that I agree very much with what John said, that there is a need for general principles. I think in the EU there is a presumption against licensing. And then that has been limited by various exceptional circumstances and developed on a case-by-case basis.

And the problem with that is that that list seems to keep getting longer, and it's difficult to predict what will be next. So it would be useful to have some principles of more general application.

WILLIAM KOVACIC: If I could just leave one thought with our panelists perhaps for the rest of the discussion this morning and going into the afternoon.

I was wondering if you detect any

degree to which competition authorities implicitly or explicitly make judgments about the appropriate breadth of the intellectual property right as granted or as defined in deciding whether there has been an abuse of that right, or in deciding what kind of remedy should be provided for access.

That is, do you see in any instance

the tribunals in effect second-guessing statutory definitions of rights, not directly challenging them, but silently in effect saying "I think that's a terribly broad right and I know how to fix it; I'll define abuse broadly, or I'll mandate access widely?"

Do you see that phenomenon at all work in the way in which tribunals are addressing cases? Just a thought for the future discussion.

WILLIAM KOLASKY: And with that provocative question we're going to take a short fifteen-minute break. We will resume between 11:25 and 11:30.

And after the break we're going to

hear a discussion of the IMS case in order to see how these principles are applied in the context of a particular case. We're not going to relitigate the IMS case, but rather talk about the issues in the case and their broader implications. Thanks.

(Recess.)

WILLIAM KOVACIC: We're going to resume with a segment featuring three presentations that will focus to a large extent on the IMS Health case in the European Union. And to start us off will be John Temple Lang. John?

JOHN TEMPLE LANG: I have been asked to comment on the issues raised by the IMS case and to make as clear as I can which of these issues, however it may be resolved, will give rise to a principle limiting the power of the Commission to order compulsory licensing.

Two introductory points: First, I have a fairly strong impression that the Commission has not really got a policy on

compulsory licensing of intellectual property rights. It has reacted opportunistically to the Magill case and the IMS Health case.

Secondly, the main fundamental limiting principle is of course the principle stated very clearly by the Court of Justice in the Veng, Volvo, and Renault cases that in general even a dominant company has no duty to license intellectual property rights unless there is something extra, something additional to the mere refusal to license.

And the question of course is what kind of additional behavior or additional effects of the behavior will qualify for compulsory licensing.

The first set of issues -- I'm going to distinguish between the issues that had arisen before the IMS case and haven't been completely resolved and those which are raised for the first time by IMS.

The first couple of issues concern the downstream market. Does the company which is

dominant in the upstream market also have to be dominant in the downstream market? Or does some lesser degree of lack of competition suffice for compulsory licensing, at least for compulsory access to an essential facility?

My view is that the company must be dominant in both markets. But the point hasn't been settled. Secondly, it seems to me that there is an issue again giving rise I believe to a limiting principle.

There must in my view be scope for added value competition in the downstream market. Otherwise the transaction costs of imposing a compulsory license are not justified.

This sounds unfamiliar, but everybody in Europe accepts without thinking about it very much that you can't have an essential facility situation in a downstream market which is merely retailing or reselling a product.

The explanation for that is in the absence of a possibility of providing added value. Then there is the question what is meant

by what was said by the Court of Justice in the Magill case about a new product.

Must the competitor which is seeking the license be offering a new kind of product which is not offered in the market and for which there is an unsatisfied demand? Or is it enough to be merely one more competitor providing one more example of more or less the same kind of product that is already available?

Once again the issue hasn't been resolved. The Magill case concerned clearly a new kind of product, a comprehensive television program magazine, for which there was a clearly unsatisfied demand.

Then there is an issue mentioned by Jim Venit this morning: Are the Magill requirements monopolizing a second market and depriving consumers of a new kind of product in some sense or another? Are these separate alternative requirements or are they cumulative?

I've given some reasons in my paper to suggest that they are in fact cumulative

requirements. But clearly the question has not yet been answered and may have to be answered or may be answered by the Community Courts in the

IMS case.

I think there are very important issues not yet faced and certainly not yet resolved about pricing of intellectual property licenses.

I think that competition authorities in Europe at least underestimate the difficulties of determining the right level of remuneration on competition law grounds if you haven't got a basis for comparison in the particular case.

In other words, if you can't simply say you gave a license already to those people; you must give another license to this plaintiff on substantially the same terms.

There are very considerable difficulties about risk. In doing this the Commission has frankly not faced these issues. It hasn't faced them -- it didn't face them in the Magill case, and it hasn't yet had to face

them in the IMS case.

And I repeat what I said a moment ago

before the coffee break. I think that we will find that a lot of these pricing issues are only dealt with satisfactorily if they can be dealt with satisfactorily at all by an authority with regulatory powers and not one acting only on the basis of pure competition law.

Another issue which hasn't been resolved is the question already mentioned several times this morning and raised by Bill Kolasky: How much difference does it make in fact if the competition authority or the court believe that the copyright, because it's copyright we're talking about -- really hasn't got a very strong justification.

This is often offered as a possible explanation for the Magill case. It has been mentioned by commentators as a possible explanation of the IMS case.

The fact is that the Commission and the companies that are in the case which agree

with the Commission haven't made this argument at any stage.

So in my view it is not a particularly important argument unless somebody is better at doing long distance psychoanalysis of the judges and the Commission than I am. But there may be an element of it there.

Well, I said that I would point to several of the issues that have been raised for the first time in the IMS case. I think there are basically three.

The first one is can a facility become essential not because the competitors are unable to produce a rival facility of their own, but because the customers prefer the dominant company's facility and are not interested in alternatives.

This is the first time as far as I am aware that it has been suggested that consumer preferences can make an essential facility when competitors can produce alternatives.

And I don't think it matters for

this purpose what the customers' reasons are for preferring the existing dominant company's facility. They may have good reasons. They may have bad reasons. They may have costs or convenience of changing their software to adopt to another facility.

But this is I think the first time that it has been suggested that consumer preferences can make something essential that isn't otherwise essential.

The second issue raised by the IMS case is I think the most fundamental one. Can there be a violation of Article 82 if the only action of the dominant company has been the refusal to license?

In other words, if there is no additional conduct, no additional element over and above the bare refusal to license, it seems to me that if the IMS decision is ultimately upheld then there has been a very big change in the basic principle mentioned at the beginning which seems to be the law more or less in Canada and Australia and in other countries that the mere refusal -- I don't think I can avoid using the word -- the refusal to license by itself cannot be an abuse.

There must be something else that makes the situation special and particularly bad in some way.

If the IMS decision is right, then it seems to me that what it implies is that in some circumstances which I'll try to define in a moment a dominant company must always license if the refusal to license would lead to a monopoly.

That's substantially what the Commission said in the decision. It seems to be the gist of what the Commission is saying in its pleadings before the court. And that is a fundamental change which would be made if the decision is ultimately upheld.

The last question raised by the IMS Health is the question whether you need to -- I'm going the use the phrase, two markets. And I think one has to be clear about this, as clear as we can be.

First of all, we are not talking about defining markets. We are not talking about market definition for the purposes of assessing market power.

We're talking only about the question whether the intellectual property right can be used for two different purposes and whether you could have a license for one of those purposes which left untouched the value of the intellectual property right for the other purpose.

I think we're obliged in Europe to accept that the Court of Justice thinks that you have to have two markets. In most at least of these cases the court has often referred to the use of market power in one market to limit competition in another market.

However, I think it's important to make a couple of other points. First, I don't think it's important whether this particular dominant company has ever granted a license of the IP right or not.

The question whether there are two separate uses for the intellectual property right is an objective one and one that doesn't depend on what the dominant company has actually done.

It would be relevant however if no company in a similar position had ever granted a license and if there were good reasons for not doing so because in particular if there's only one market it normally doesn't make sense for you to grant a license of your principal competitive advantage to a competitor or a potential competitor if you're planning to stay in the market.

So there are good reasons why licenses are not granted. I think you can answer the question do you need two markets if you ask the question the other way around.

Suppose you didn't need two markets. Suppose it was quite clear that in the case of a process patent which could be used only for producing one particular product you could have an obligation to license.

Suppose that the process is cheaper, produces a purer product and does so more quickly and more efficiently.

If you say that only one market is necessary and you can have a compulsory license in these circumstances, it seems to me that you are saying that a dominant company if the competitive advantage is great enough to give rise in due course to a monopoly -- that's what the Commission says -- a competitive advantage which is valuable must be shared.

And that is once again an extremely surprising proposition and one with enormous implications if the decision is ultimately upheld in this particular respect.

I don't know whether the courts are going to uphold the IMS decision. But if they do, it seems to me they can strike it down on one or more of these grounds and we won't know the answers to the other questions.

However, it seems to me that the

courts will probably have to face all of these issues and answer them appropriately if they are going to uphold the decision in due course.

WILLIAM KOVACIC: Thank you, John. What we thought we would do because each of our three presentations in many ways are closely related here would be to hear from all of our panelists for this segment first and then go to the discussion. So if we could, please turn to Ian's talk now.

IAN FORRESTER: About twelve, thirteen years ago I was given the delicious task of representing the Commission before the European Court in the Magill case.

And even though the fees paid by the public authority are less generous than those of the private sector, I was nonetheless very pleased to have the case.

And just after that I met an eminent retired member of the legal service who had always taken an interest in my career and had been terribly kind and encouraging.

And I said, well, very nice. I've got a case for the Commission before the court. He said, really, well, very good; what's the case? And I said Magill. And his face changed utterly and he said that's a disgrace; I'm shocked; I very much hope you lose.

And such passion is characteristic of the field of IP rights, especially when they come in contact with competition law. The episode illustrates also that Magill at the time was regarded by many as an extremely bad and even reckless case.

And now I think it is regarded perhaps as an interesting one, but not a terribly surprising one in the light of hindsight. The next thing I'd like to say is that there have been enormous encroachments on the rights of IP holders due to the application of community law, enormous encroachments.

But those encroachments have been far

more significant by the application of the rules of free movement than the very small number of

decisions on compulsory licensing.

And indeed the vocabulary that's used to discuss the free movement cases has almost tainted and distorted analysis in the case of competition matters.

Now, the early cases related to the use of IP rights to hinder cross border trade. Classically the patentee or the trademark holder in The Netherlands could prevent the unwelcome importation of genuine goods which its affiliate had put on the market in, let's say, Germany.

It could prevent their importation and sale in The Netherlands. Now, it was clear to the European Court for whom market integration was a kind of civil religion that the use of national IP rights to prevent such importations had to be blocked. It wasn't acceptable.

The court created a theory distinguishing between certain kinds of rights, core rights and less core rights, existence and exercise. And it said that you would retain always the core ones, but you could lose the

non-core ones.

Now, that vocabulary was the technique used by the court to reach an acceptable result in the free movement of goods cases. It has been argued and is still argued that the existence/exercise doctrine is relevant also for competition cases.

I've never really believed that that was correct. But there is still debate. But in my view we're probably moving now to a situation where existence and exercise as a way of deciding whether or not an IP right can be removed, that that -- the use of that vocabulary is rather passing.

Now, there are many cases, at least there seem to be 50 on the subject of trademarks and copyrights and patents in the context of free movement.

However, in the field of compulsory licensing it is a very, very small basis. There is Volvo v. Veng. There is Ladbroke and Bronner which have to do with refusals to deal.

There is Magill of course. And now there's IMS. So I think that that is too small, too fragile, too narrow a basis of authority to make confident predictions for the future.

Putting it differently, you can find better guidance about the constraints placed by community competition principles in community legislation. And then you can glean guidance from Magill and IMS.

So there have been two big cases which have aroused immense attention. And before I say anything about them procedurally I state my thesis which is that both cases are to be understood more easily as reactions by competition enforcers to the non-harmonized state of EC copyright law.

And I believe that if we were talking

about mainstream, orthodox, common, whatever word you like, IP rights, it is unimaginable that the decisions taken in Magill and IMS would have been taken.

Now, each of the Magill and the IMS

cases involved serious arguments as to -- and ongoing arguments as to whether the national IP rights did indeed exist.

The Commission acted before there had been a final decision on the merits before the national court. That was the case in Magill and also in IMS.

In Magill the Irish High Court gave its judgment only long after the Commission decision. And in the IMS case the Commission decision was taken in the summer of last year, and the German courts -- there have been many, many decisions, but there is no final decision on the merits.

So the Commission says we are acting in order to keep the complainant alive pending --

during the progress of the national litigation.

Now, another procedural interesting phenomenon is in both cases the European court suspended the Commission decision as having been too bold.

So we have in both cases

Europe-specific procedural context with a strange, I assert, national IP right being invoked successfully by the dominant enterprise in the national courts driving the complainant out of business or preventing him entering the business, and the Commission intervening to try to keep things alive while matters get sorted out.

And in each case the European court has overruled the Commission's procedural intervention.

Now, that seems to me intriguing and also relevant for the future because it would suggest that intrameasures cases involving licensing will be extremely difficult, conceivably impossible to reconcile with the judgments -- the orders of the precedence in the IMS and Magill cases.

Now, both cases involved the Commission going absolutely to the limit of its internal consensus procedures in order to take the decision. The Commission had to screw up its

courage and I think that it's best seen as the remedying by the application of Article 82 of a bizarre national copyright right.

In Magill it seems strange that the data "Dallas 8:00, sport 9:30, news 9:00" would be regarded as a copyright or that that would be sacred.

In the case of IMS it seems to me surprising, interesting, that while clearly a map of post codes for a country can be copyrighted, and although many of the post codes are just single post codes -- a number of them are joined together -- conceivably that map could and should be copyrighted.

But what is more surprising is the proposition that the presentation of information, commercial information about what's going on in each of these regions on that map should also be copyrighted.

That seems a surprising and bold assertion. German courts have said it right. They said it is correct. The battle goes on in

Germany.

So I think that in each case we can see a cluster of unusual circumstances which together justify the use of Article 82. Article 82 applies to dominant enterprises the higher burdens that are required, especially high burdens imposed by the Treaty.

However, we may also note that by far the great majority of cases where dominant enterprises are the subject of a complaint where the complainant requests that they be ordered to deal, by far the great majority of those complaints are rejected and deserve to be rejected.

I note that a recent OFT report says answering the questions from our chairman or some of the questions from our chairman -- I found this interesting this morning. I heard it by phone -- that an authority confronted with the request to order trading, and notably in the context of licensing, should ask itself a number of questions:

What was the investment made by the dominant company? Is the work of trivial intrinsic value or significant? That does seem to be a relevant consideration. It was mentioned as relevant by the Commission in the Magill case.

Is the marketplace dynamic? Will remedies naturally emerge if we do nothing to sort out whatever problems arise? In the IMS case I think the answer to that question would be no.

What will be the impact on future innovation, future R & D if we challenge the right in this case? Again I think that properly viewed both the IMS and the Magill cases can be regarded as specific reactions to very, very particular problems arising under national law.

I think that if we're looking for mainstream criteria about the application of competition principles constraining the use of IP rights it's better to look at community legislation rather than to draw conclusions from Magill and IMS.

In the very rare cases where the Commission does consider that Article 82 justifies its intervention, I think that it is almost unimaginable that a bare, mere refusal to license an important IP right of true valuable economic significance, it's unimaginable to me that the Commission would ever invoke Article 82 against the refusal to license such a right.

In the IMS case the Commission relied on a three-step approach. It said Magill talks about exceptional circumstances.

And then it looked at two refusal to deal cases in each of which the complainant had been unsuccessful but where the Court of Justice gave some guidance as to what the principles -- what relevant principles would apply.

Those are described in my paper. That's Ladbroke where a bettor shop wanted to show horse race pictures. The European Court said, well, you don't really need horse race pictures to run the facility of a betting shop.

And finally Oscar Bronner where a

free rider wanted to get benefit from a larger enterprise to describe his newspapers. And there the advocate general and the court in Brunner both indicated very, very cautious reasons -- cautious reflections which an administrative agency should go through before ordering a duty to deal.

And the Commission in IMS looked at those three cases and decided that there was enough merit to justify them going ahead in the particular circumstances of the IMS case.

Now, conclusions to be drawn from all this: I believe that in the mainstream European companies and American companies and competition law enforcers are really very little different in their interest in respect for R & D and the exploitation of technological innovation.

Europeans expect patent and copyright protection to be given and to be enforced. The great majority I repeat of requests for compulsory licenses have been unsuccessful and deservedly so.

Next conclusion, the vocabulary of the European Court in analyzing competition law problems involving IP rights have been distorted by older judgments of the European Court concerning free movement of goods. I think that that distortion is gradually being corrected.

Next, there have been only two cases in which a compulsory license has been granted for a genuine -- for a refusal to license a copyright right upheld genuinely provisionally by a national court. That's to say Magill and IMS.

In neither case was the finding of an abuse based merely on refusal. In both cases there were extra additional elements. And I think it's very, very important that both cases involved curious, aberrant as I have called them national IP rights.

Now, predictions of the end of alarm for holders for high technology companies due to the Magill and IMS cases, there were immense discussions at the time of Magill about the long-term implications. It did not materialize.

There have been grave murmurings about the implications of IMS judgment. I submit that those grave tidings may also not emerge. The substantial result I think with the current situation is not alarming.

So other than those two exceptional cases which I've mentioned, I think that the European law is not disturbing, shouldn't be disturbing even in the Great Hall of the Department of Justice.

And I offer the observation that if Louisiana, my favorite American state, were to adopt a law whereby TV listings were eligible for copyright protection or to adopt a law whereby the post codes of the state would be eligible for copyright protection, and moreover that marketing information reflecting commercial activity in those post codes was also copyright, then I'm sure there would be screams either to the courts and we would have a solution as in the case of Festo or to the antitrust authorities.

And I would have thought that the

antitrust authorities would also have been perhaps tempted to intervene if the IP right was as bizarre as I have asserted it was. Thank you.

WILLIAM KOVACIC: Thank you, Ian. And if I could ask David to close out this trilogy of presentations on the EU jurisprudence on compulsory licensing, we can then go to a general discussion. David?

DAVID HULL: I want to just briefly look at the IMS case from a comparative perspective. I should start with a caveat that despite what you might infer from my southern drawl I'm an EU competition lawyer, not an American antitrust lawyer.

And I don't profess to have any expertise in American antitrust. So most of you know the American cases much better than I, and I apologize for any misstatements I may make.

Just a general comment on looking at what's going on on the two sides of the Atlantic, it's interesting over here the debate on compulsory licensing in the IP field in the wake

of the Federal Circuit's decision in Xerox seems to be -- the debate seems to be have we gone too far in protecting IP rights in this context.

Whereas in Europe in the wake of the IMS case the debate seems to be have we not gone far enough.

In the wake of IMS there was concern I think that in the general context of this discussion going on in the wake of GE/Honeywell of the need for greater convergence among antitrust jurisdictions on how they treat various competition law problems.

I think in putting the IMS case in that context there was a concern that IMS represents greater divergence, a move away from the approach to this issue in the U.S.

I think that's certainly true if you look at the theory that the Commission used. I think that it would be -- as Bill said, it would be very rare in the U.S. to use an essential facilities doctrine in this context.

So in that sense IMS -- the approach

used by the Commission in IMS is much different from the approach in the U.S. What I'd like to do briefly is look and see how the U.S. courts might come out on IMS to see if in fact the gap is as wide as it appears to be at first blush.

There are three U.S. cases I'll discuss very briefly. First there is a split in the U.S. it appears on how you deal with this issue.

The Federal Circuit in the Xerox case adopted a very strict test of saying that the refusal to license would not be a violation of the antitrust rules except there were certain exceptional circumstances: sham litigation, illegal tying, or fraud on the Patent Office, all three of which would be very difficult to show.

So essentially the Federal Circuit set a very high bar to compulsory licensing. I think if the Federal Circuit were presented with IMS, it's very likely it would not compel IMS to license its IP rights.

The Ninth Circuit in the Kodak case

took a different view. The Ninth Circuit essentially said that there's a presumption that it's okay not to license your IP rights, but it's a rebuttable presumption, and it can be rebutted by showing that the refusal to license is but a pretext for anticompetitive conduct.

In that case Kodak refused to supply spare parts to independent service organizations. And the court suggested that in fact that refusal was not legitimate -- out of a legitimate concern to protect the IP rights, but was rather to exclude competition in an anticompetitive way.

And it pointed out that the Kodak parts manager testified that the last thing on his mind was protecting Kodak's intellectual property right when he refused to supply the parts.

I guess that means that we -- I guess in the wake of that decision there was a lot of briefing of managers about what they should say when they refused to supply parts in order to protect their markets.

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How would the Ninth Circuit come out with the IMS case? It seems to me that it's conceivable that if the Ninth Circuit looked at the facts of IMS it could find that IMS's refusal to license was a pretext.

Reading between the lines when you read the Commission's decision, there seems to be a notion that IMS asserted its rights late in the game for the sole purpose of excluding a new entrant to the market.

And in those circumstances I'd wonder whether the Ninth Circuit might find that that was simply a pretext for anticompetitive conduct.

Finally I would mention the Dell Computer case decided by the FTC. In that case in the context of standard setting Maurits Dolmans will talk more about this this afternoon. So I won't really go into it.

But I'll simply say in this case the idea is that in the standard setting process if one of the participants doesn't disclose it has IP rights and then comes along very late in the

game and asserts its IP rights, that is considered to be anticompetitive.

It's relevant to the IMS case because there is a lot -- in the Commission's decision and in the commentary on the case there's a notion that the brick structure involved in IMS is at least akin to a standard -- some sort of open standard.

And IMS should be perhaps estopped from asserting its rights so late in the game. It comes along after this structure has been widely used in the industry, has been developed with the participation of customers.

And it comes along and asserts its rights at the last minute. I think the difficulty with applying this notion of estoppel in IMS in the standard setting process is IMS didn't set the standards with competitors. It set it with its customers.

So it's really different from I think a normal standards process. But still there's this notion that perhaps this estoppel argument

would be an interesting one.

My conclusions are first that I wonder if the gap between the U.S. and the EU is as great as it might appear at first blush. I think the U.S. courts -- I don't know if they would reach the same result in IMS, but they might reach a similar result if presented with the IMS facts.

I also think when I read the IMS case I come away with the impression that this is not simply -- although the theory used by the Commission makes it appear that this is simply a bare refusal to license case, it seems that the Commission is troubled by other things in this case.

First of all it's troubled by the fact that perhaps the IP right is weak as Ian has suggested. But it also seemed troubled by the fact that this is a standard that was developed in cooperation with the entire industry and was used by the entire industry until very late in the day IMS asserted its rights.

That seemed to be troubling for the Commission, but it had a hard time articulating that when it used the essential facilities doctrine.

So perhaps some of the reasoning in the U.S. cases if the Commission had taken maybe the estoppel approach or some of the other the reasoning you find in the U.S. cases, it might have done a better job articulating what was truly -- what's considered to be truly the problem in this case.

I'll stop there.

WILLIAM KOVACIC: Thank you, David. We have just about fifteen minutes before we break for lunch for discussion among our panelists.

And we certainly have a considerable collection of topics that we could address, both the panelists' views about the underlying rationale for the IMS decision, its consistency with other national approaches for evaluating demands for access and for evaluating refusals to deal.

So again I'd simply like to invite our panelists to respond to what they have heard and perhaps for our speakers in this segment to respond to the interpretations they have heard from their colleagues. Henry?

HENRY ERGAS: Thank you very much. I wanted to comment really on two points. The first relates to John Temple Lang's presentation, the second in respect of a number of issues that were raised by Ian Forrester.

With respect to Dr. Lang's presentation, Dr. Lang emphasized the difficulties he saw arising involved in determining appropriate prices for access to intellectual property when that access had been mandated.

And I of course agree with him that the difficulties are substantial. What I would say though is this, that we have had in Australia as in many other countries schemes or statutory licenses in respect of copyright for many years now.

And within those schemes and as part of the implementation and administration of those schemes the bodies administering them have had to determine appropriate remuneration.

And indeed we now have -- for example, in respect to the copyright tribunal in Australia, we have a relatively well established way of approaching the issues involved in determining reasonable remuneration for compulsory licenses in respect of copyright.

And we are extending that now to those, for example, multimedia publications or works that fall within the scope of the compulsory or statutory licensing arrangements.

So while it is indeed difficult, it is not exceptional and is a problem with which our tribunals and our courts have grappled with for many years and have made I think some quite sensible decisions in seeking to address them.

My second and perhaps more important point goes to the issues that were raised by Ian

Forrester in his very comprehensive discussion of the background to IMS.

And Ian emphasized his view that in understanding the decisions at issue, and in particular Magill and IMS, it was important that the IP rights involved were in some respect he claimed aberrant.

And it seems to me though that the reality that we face is that those rights which he believes are aberrant are by no means aberrant, and that the situation that we're dealing with is one where the scope of IP rights around the scope of subject matter that is covered by IP rights has become ever greater, particularly in the last decade.

And to evidence that I would merely point to two things: First, the reform of copyright so as to extend copyright protection both to works in digital form and perhaps even more importantly and controversially to access to works in digital form as occurs for instance in the U.S., DMCA, the Digital Millenium Copyright

Act, and as is being reflected in copyright legislation virtually throughout the world.

The second trend I would point to in that respect is the de facto extension of the patent right to areas where either it previously did not exist or if it did exist it existed in very minor form.

And this is especially the case with respect to material that is in digital form, most notably in respect of the business process or business method patent.

This is something that really began in the United States and is now apparent if you look, for example, at the patenting statistics in Australia, New Zealand, or the EU.

It has grown spectacularly since from a virtually trivial category in our patenting statistics to now one of the larger single categories of patenting in Australia. That has really happened over a period of a very small number of years.

And so what does that mean for

competition authorities? Well, what it means is that the type of dilemma that Ian viewed as aberrant far from being aberrant is occurring across an extremely wide range of cases, in a growing range of cases.

And so we face the difficult tensions as we try to adjust to the changing nature of technology and to the results of creative output which is a tension between the desire on the one hand to provide fair, effective, and enforceable intellectual property rights in respect of the output, and the reality that in so doing we both create significant new problems because of the complementary nature of much of the intellectual property at issue, the network nature of the material that it covers, and creating new scope for market power to both arise and be exercised.

WILLIAM KOLASKY: If I may, I'd like to follow up on Henry's comments by noting that I thought this is exactly the point that Henry was going to. And that is that one of the most important things in this area as in any area is

the need to develop limiting principles.

And I thought that Ian's talk and David's talk were very useful in terms of suggesting a possible limiting principle in the IMS case, namely the notion that the brick structure had become an industry standard and that there may have been some reliance on the part of customers to the notion that it might be treated as though, if you will, open source and that therefore there might be an estoppel element.

It seems to me that -- I don't know whether factually that is the case in IMS. But that certainly would seem to be a useful limiting principle. I'm more troubled by the limiting principle suggested in the Magill case, namely that it was a new product for which there was a customer demand.

And I'd like to try to put to the speakers a hypothetical. As you know, here in the United States, and I think this was common throughout the world, we had something called

Napster where teenagers were able to listen to recorded music off of all labels for free.

In the wake of Napster's demise there are proposed joint ventures among the various record label companies to aggregate their libraries in order to be able to provide a Napster like service for a monthly subscription fee.

And their sense is that consumers, teenagers won't subscribe just to the music of a single label, that you really need to aggregate it.

And so the question is applying the Magill principle could I go out and say I want to create a Napster clone aggregating the music of all labels. It's a new product because nobody else has offered it or is able to offer it, and therefore I'm entitled to a compulsory license to Warner's and EMI's entire library of music.

IAN FORRESTER: I can offer an answer on the last one. I think again one has to look at Magill, all the circumstances which were

present.

The material in question was indeed copyrighted, but it was promotional material that was given by the broadcasting companies to hundreds, indeed thousands of periodicals which were encouraged to reproduce it on a daily basis.

And the controversy related to whether it could be reproduced by Magill on a weekly basis in competition with the weekly magazines of the broadcast companies.

I think that just that set of circumstances, those elements, would justify the confident rejection by the European record industry to Mr. Napster Europe who wanted to have a compulsory license with respect to information.

Yes, there would indeed be a new product being offered. But I don't think the circumstances would be exceptional enough to come within the Magill principle.

WILLIAM KOVACIC: Jim?

JAMES VENIT: The easy way out of Magill is that it's the record companies

themselves who are going to pool to be able to offer the product, and they wouldn't run into the horn of dilemma that there couldn't be the new product because the owners hadn't put it out and they were preventing someone else from doing it, which is a facile answer to the question, but I think it's relevant.

The issue on the standard to me is a very different thing if one develops something that is accepted by customers as a standard as opposed to coordinating with other rivals to develop a standard which then becomes industry standard and shutting people out.

One could make the argument that the IMS thing is even more disturbing because you are punishing them because they were successful.

WILLIAM KOVACIC: Patrick?

PATRICK REY: I have remarks on this and on the questions you raised before. As you can infer from my presentation and the paper, I believe that it's fair to say that there can exist particular circumstances where vertical

foreclosure can raise legitimate antitrust concerns.

And I think that this should be recognized particularly in the U.S. where the vertical foreclosure is essentially perceived as a non-issue.

That being said, I'm not sure that IP rights would be the first rights, the first property rights that a competition authority should try to focus on.

And indeed when the bottleneck results from innovation, then I would tend to agree with the suggestion that there should be a presumption in favor of the right holder.

And clearly the dilemmas that John Temple Lang has mentioned regarding the difficulty to regulate access particularly for competition authorities and for courts -- of course the courts will have to be involved at some point. And as the time arises the issues that are considered we do advocate for being very cautious.

I'd like to react first to the interpretation of the Magill and IMS case. I think it is quite a realistic interpretation.

But I really found it quite dangerous to try to second guess national Patent Offices and to use competition policy cases which establish generally applicable standards in order to resolve without being able to say so explicitly to try to resolve possible errors in national IP statutes.

I'm not sure that this line of reasoning provides a very good approach to possible limitations or limiting principle.

WILLIAM KOVACIC: And John?

JOHN TEMPLE LANG: I just want to

repeat the fact that all this theory about rights does not appear anywhere in anything that the Commission has written about the IMS case. It's not part of the Commission's case. Maybe they might have made it into their case, but they didn't do so.

They argued the case very clearly on

the basis that an IP right may not give rise to a monopoly and that if it does give rise to a monopoly even if the monopoly is due to customer preferences and not the inability to have competitors to produce an alternative facility, then it must be licensed.

That is the Commission's proposition, whether you like it or not or whether you think that another proposition might have been made. That's what the Commission is saying very clearly to the court.

WILLIAM KOVACIC: Ian, did you have a response to Patrick's comment?

IAN FORRESTER: A brief one. I think

that we should distinguish between patents and copyright rights. In the case of patents, patents are the subject of examination and there is a very careful consideration of the merits, the technical merits of the claim and it is granted for a limited period of time.

I think the situation of copyright in the unusual circumstances of these two cases can

be rather different, although I fully recognize that copyright may be absolutely crucial, absolutely vital for the protection of the heavy investment in important industries. But that's just one small correction to Patrick.

WILLIAM KOVACIC: Gwillym?

GWILLYM ALLEN: I have two comments. One involves the breadth issue. And indeed we had many debates about this. And I'm just wondering is this the same issue?

I mean we called it fine tuning and whether you should use antitrust enforcement to step in and try to fine tune -- use it as a fine tuning so that when you think that the breadth of an intellectual property right was too wide you have very vigorous antitrust enforcement, and when you think it's too narrow then you change your antitrust approach to the particular intellectual property law.

We had long debates about this, and we decided that it was inappropriate to use enforcement mechanisms to try to fine tune the

existing intellectual property law. We put in a section in our guidelines saying that that would not deter us from engaging in advocacy, and encourage either legislative change or when the IP laws were being reviewed to use our advocacy role to step in to provide our opinion on the appropriateness of the breadth and scope of the intellectual property law or where appropriate at least bring to the table the competitive implications of the existing law.

The second comment was this idea about the de facto standard and the comments of Henry about how the sort of natural development of reality has changed the appropriateness of intellectual property and maybe it has extended it to some degree.

And indeed that was the idea that we had in our application of section 32, to try to deal with that particular problem, that the situation -- and these were based on some ideas that we basically stole or borrowed from a number of academics on the idea that the architecture of

the law can change such that the objectives in the intellectual property are actually being undermined by their very use.

And as a marker that that may be happening would be the effects on competition. And that may be that competition law or authority should step in and try to readjust the balance or at least put it before a court -- and in our case it's the Federal Court -- to consider the readjustment of that balance.

WILLIAM KOLASKY: Thank you very much,

Gwillym. I think that will have to be the last remark. This is obviously a fascinating subject and we could stay here all day debating it. But we have another session this afternoon.

I want to on behalf of the Justice Department -- and I'm sure Bill would echo this on behalf of the FTC -- thank all of our speakers enormously for coming here. They all obviously came from other countries, other continents. I think Henry gets the prize for coming the longest distance.

But we do very much appreciate your sharing with us your perspectives on how your jurisdictions are dealing with these very difficult issues and it will very much help to inform our consideration of the issues here in the United States. So thank you.

(Applause.)

WILLIAM KOLASKY: We will resume at 2:00, and as I mentioned before, I gather you need to be escorted out of the building and then find your way back here. Thank you.

(Lunch recess.)

AFTERNOON SESSION

(2:00 p.m.)

WILLIAM KOLASKY: Good afternoon. I want to welcome everyone back as we continue our discussion of international comparative issues in this next session of our joint hearings on competition and intellectual property law and policy.

My name is Bill Kolasky. I'm the

International Deputy Assistant Attorney General for antitrust. I'm happy to have with me as my co-moderator Bill Kovacic, General Counsel of the FTC, who served also as co-moderator this morning.

This morning we heard from a distinguished panel about refusals to license intellectual property and compulsory licensing in the EU, Canada, and Australia. This afternoon we will focus on the European Union's technology transfer block exemption regulation, referred to as the TTBE, as well as agreements that fall outside of its scope.

In the European Union, bilateral licensing of some types of intellectual property is covered by the technology block exemption which was adopted in 1996 and will expire in 2006.

Last year responding to criticism that the block exemption was both overly formalistic and complex and too narrow in scope, and noting that there was a need to harmonize treatment of intellectual property with other recently re-enacted regulations on vertical agreements, R & D agreements, and the like, the European Commission commenced a mid-term review of the TTBE.

We're most fortunate to have with us today Dr. Kirti Mehta, a director in DG Comp, who will discuss that review process. As part of that process, the EU solicited public comments about its proposed changes, some of which will be discussed by the panel today.

We will then expand the discussion of licensing practices to address licensing

agreements that do not currently fall within the block exemption.

Such agreements include multiparty licenses of intellectual property such as patent pools and cross-licenses, some of which are affected by the activities of non-governmental standard setting organizations. With that introduction let me move on and introduce our panelists. But before I do, Bill, do you want to add anything?

WILLIAM KOVACIC: No, Bill.

WILLIAM KOLASKY: Bill and I will be representing the Justice Department and the FTC this afternoon. We have with us Mary Critharis, an assistant solicitor at the U.S. Patent and Trademark Office.

Unfortunately I do not have time for lengthy introductions of our panelists, but more complete versions of their biographies appear in the prepared materials.

As I mentioned, Dr. Mehta is a Director in DG Comp. He is responsible for

competition policy, coordination, international affairs, and relations with other institutions. His main areas of responsibility are policy and legislative initiatives, trade and competition, and international cooperation.

Fiona Carlin, to Dr. Mehta's left,

is a partner with Baker & McKenzie at their European law center in Brussels where she specializes in antitrust and trade practices, EU law, and privacy. Ms. Carlin was the rapporteur for the comments prepared by the American Chamber of Commerce on the block exemption review.

Yee Wah Chin, who is at the far left and one in, is senior counsel in the Washington, D.C. office of Mintz Levin. She was on the American Bar Association committee that commented on the block exemption review.

James Leavy, next to her at the far end, practices intellectual property law as a partner at Serra, Leavy, & Cazals in Paris, France. He has held various positions in the

Licensing Executives Society and acted as the rapporteur for its comments on the block exemption review.

Peter Alexiadis is a partner in the Brussels office of Squire, Sanders & Dempsey.

His practice includes advising clients on competition and regulatory law issues including IP.

Next to him is Will Tom, a partner at Morgan, Lewis & Bockius here in Washington. In the 1990s Will served as deputy director at the Bureau of Competition at the FTC.

Prior to joining the FTC he worked here in this building as a counselor to the Assistant Attorney General in the Antitrust Division, and was a member of our intellectual property task force which drafted the joint DOJ/FTC IP guidelines.

Next to him on the far right is Maurits Dolmans, a partner at Cleary Gottlieb in Brussels. Mr. Dolmans' practice focuses on competition law as well as EC regulatory,

intellectual property, and court law in The Netherlands and the European Union.

And last but not least, Mark Janis who is a professor of law at the University of Iowa

College of Law in Iowa City. He teaches and writes in the fields of intellectual property and antitrust.

Professor Janis is coauthor of a two-volume treatise, IP and Antitrust, with Professors Herbert Hovenkamp and Mark Lemley.

Before we turn to the substance of this afternoon's session, I need to go over a few administrative details, many of which are probably familiar to you. Because we are in the Great Hall of the main Justice Department building, we are required to observe certain security procedures.

If you are not a DOJ employee, you must be escorted around the building. Antitrust paralegals who are wearing name tags highlighted in green escorted you into the Great Hall.

They are available at the back of the

room to escort you out should you need to leave the session or to take you to the restroom or upstairs to the seventh floor should you need to make a phone call. Cell phones do not work well here in the Great Hall.

Because leaving the building is difficult, we have refreshments at the back of the room. Hopefully the coffee will hold out. But if not, you might want to get up and get some now. Like this morning's session, this afternoon's session will be a combination of presentations and discussion.

Around 3:20 we will take a fifteen-minute break and then come back for another hour and a half, finishing this session around 5:00 p.m. These hearings will resume tomorrow morning at 9:30 at the FTC, just one block down Pennsylvania Avenue with a discussion of many of these same issues from an Asian perspective.

As you are no doubt already aware from this morning's session, the acoustics here in the

Great Hall are less than perfect. Those of you in the audience, if you have trouble hearing you may want to move to a different seat. Our audio-visual specialist in the back of the room has a limited number of amplification devices available if you would like to try one.

Panelists, I would ask that you speak directly into the microphones and try to enunciate even more clearly than I'm sure you always do. And speak perhaps a little more slowly. Also for some reason the microphones take a second or two to activate.

So after you first start it may be a second before people can hear you. I'm going to ask the speakers to stick as closely to their presentation time as possible so that everyone has a fair opportunity to present their views and so that we have time for discussion.

If there are people in the audience who have questions that you would like us to put to the panelists, please come up at the end of the session or during the break and we'd be happy

to put those questions.

For the speakers if you want to offer an intervention, please raise your flag OECD-style and I will call on you. With that introduction, let me now turn to our first presentation by Dr. Mehta from the European Commission.

KIRTIKUMAR MEHTA: Good afternoon, ladies and gentlemen. And my special thanks to Bill Kolasky and Bill Kovacic first for the invitation to come and also the opportunity to present to you our current legislation and how we see it being reviewed.

Let me first start with what the block exemption -- what it means in our situation. As most of you are aware, Article 81(1) of the EC treaty prohibits agreements that prevent, restrict, or distort competition, and 81(3) allows for exemption for those agreements which confer sufficient benefit to outweigh the anticompetitive effects.

And the Commission currently has

the exclusive power to write those exemptions and also it can provide those exemptions for categories of agreements. And in fact the block exemption is the regulatory way we do that. If you look at the block exemption regulation today, a number of restrictions are permitted both on licensor and on licensee.

Many of these are indeed often the common situation when the licensor wants to territorially assign the license, and quite often will also have some other restrictions that are enumerated in the block exemption. The block exemption has the advantage that it provides legal security.

It means that in national courts our national competition authorities will not challenge agreements that are in line with the block exemption. And in a way we have a situation where much of the litigations that result from those are agreements that fall outside of this block exemption.

The current block exemption as was

pointed out came into force in '96. And midway through we had put in the regulation that there would be a review. This review has been preceded by a fact finding.

And in the report on the block exemption you see that a lot of detail is given on how the block exemptions worked because we addressed this question as to people who we are told are using the block exemptions or those in the licensing field to find out whether they do use them.

As you see from the report, the number of the agreements that are notified to us are actually not so many. So the bulk of it either falls under the block exemption or the bulk of it is simply not notified to anybody.

So I think that is an experience we also have, and we have looked. In the process of our reform of Regulation 17 something like 80 percent of agreements are simply not notified either to Commission or to any other competition authority.

The review process that we have started we hope will lead towards the end of this year to a draft proposal for certain modifications based on the consultation we've had up to now. And we hope that we will continue to get detailed comments from those who are familiar with the block exemption. And that will help us draft these suggestions.

Let me say I think the report is quite frank on what we found in this fact finding. And many of the comments were largely that the block exemption as it stands today is rather proscriptive. It forces agreements into certain rather narrow straitjackets.

Secondly, the scope is limited to bilateral licensing agreements and doesn't cover those between several parties. Presumably people can do a sequence of bilateral agreements, but this is from a transaction cost point of view quite expensive and may not lead to the same results.

Thirdly I think many people have

found that there is no distinction in the block exemption between licensing between competitors and licensing between non-competitors. This is a notion which is not very well developed in the block exemption.

You have certain situations where licensing between what is often competitors may be block exempted, and there is no market power threshold there at all. The only major concern of the block exemption is precisely these territorial restrictions. So long as they are not territorial restrictions, much is allowed.

A further point that comes out is that often the block exemption is not so clear as to how the territorial restrictions, customer allocation restrictions, the field of use, side license, et cetera, are going to be treated in the block exemption. And there is a need to make this more clear.

So I think that gives you a brief overview of the main points that come out of the fact finding and which are then detailed in the report which also gives an economic assessment of how the different articles of that -- of the block exemption are supposed to work in practice.

I think that if you were to look at -- and this audience perhaps is probably most interested in looking at where are the major differences in policy. And I think in the little paper I presented you see already that I have highlighted some of these aspects.

Firstly, as I say, these territorial restrictions, because these are taken in Europe -- you must remember Europe is a community that is a single market which has evolved over time. It has been from national economies that were separated perhaps by important barriers.

And hence one of the most important roles for competition policy has been to ensure that those barriers which are removed by our single market program are not re-established by agreements or anticompetitive agreements which lead to segmentation of the market.

And that is something that is the

reason why we have duration limits on territorial exclusivity and the focus that is there on active and passive sales. I think that is perhaps something which is very important.

And you find it in several other areas of our competition policy. A similar issue which is not impeding parallel trade, this is an important aspect.

Secondly, we up to now have not made a distinction between horizontal licensing agreements and vertical licensing agreements. And so the distinction between licenses to competitors and non-competitors is not there.

And this is something that we are certainly looking at to see whether or not that could be useful to bring it to the future block exemption. In the report now it also mentions several issues for discussion, and perhaps I would leave you with some of these elements for reflection and comment.

First is the question whether the

block exemption currently covers patents, pure

patents, or know-how and only covers trademarks and other rights if they are ancillary to the main transaction. Should we broaden this scope?

I think the issue here is that if we wanted to do that we would have to change the Council Regulation which is the one we call a negative regulation.

Our legislative architecture is that the Council Regulation indicates the areas in which the Commission may make a block exemption.

And the existing Council Regulation limits it to essentially patents and to the know-how. And if you were to change that, that would take a period of two to three years before we could do that.

It may well be that in our proposal for Regulation 17 which currently is being discussed by Council we have put rather a broad article which says that the Commission would have the power to bring in block exemptions where they felt that they were needed.

But this article is currently -- delayed in Council and it's not clear that the Council will accept that article and give this power to the Commission.

Secondly, an issue that we have is that of multiple -- licensing agreements between multiple parties. This in the current one is limited. And even if you take the possibilities that are every joint venture, there again it's limited by a market threshold.

And it is one of the questions that today we are considering, whether or not we should also allow multiple parties in license agreements. The issue here is rather that such agreements have become quite important. And today we have a number of them notified to us because they don't fall in the block exemption.

In the future, under the reform of Regulation 17, the new procedural regulation does not foresee any notification. It will also not foresee therefore a non-opposition procedure.

So in what we would like to call the

modernized world, we shall have -- the natural question people raise is what will happen if this block exemption doesn't cover the agreements between multiple licensors or licensees.

It may well be that we cover it in the block exemption. But currently our reflections are not complete on that subject. There is of course the alternative that in the future we would do like it is done in the U.S., a business review letter in relation to such type of agreements.

They cannot be notified, but of course we could make business review letters. In fact in the last year we have made already -- I'll give an example of a business review letter by producing one on on-site licenses which was an issue that was very controversial some ten years ago.

Thirdly, the question of license agreement between non-competitors, and here without excluding other options the report proposes a framework where you will see that we

are thinking of making this distinction and to have a much more lenient regime with a shorter list of hard core articles or restrictions as regards licensing between non-competitors and a longer list of hard core and the market share threshold for licensing between competitors.

This is an idea that of course has interested several people who have commented on our report. Of course people are not happy with having a market share threshold. And, secondly, people are not very happy with whatever definition we may come up with for competitor and hence non-competitor.

Already if you look at our vertical restraints block exemption and the horizontal restraints block exemption, we have defined there what we understand to be competitor, and more important potential competitor.

But this is not an area where you can say very clearly in black and white what are the situations in an exhaustive way that you are thinking of. And quite clearly this option will

have support depending upon how we resolve these two issues. These are I would say the most important issues.

The other one which is to see how the other property rights would be dealt with. Clearly there we are currently having the review of these direct European patents. And what the directive will have as regards certain rules on licensing will be an important element.

A second point is that we are also discussing protecting software. There once again we are not at this stage quite clear what will be the final compromise on those directives. So that will depend on developments in those areas before we have a clear idea.

I can say that up to now the

consultations with our Member States have more or less shown that the enthusiasm for extending the scope to software, to other IP rights is not I would say so important.

I think that too many complications come with that vis-a-vis the national laws in

those areas. And so it's not something that we would be able to undertake in this exercise.

I think I wanted to basically stop there because I think these are the main elements. You can read the report and also the written submission of comments that I have made which goes into a bit more detail on the issues that I touched upon. Thank you very much.

WILLIAM KOLASKY: Thank you, Kirti. Because most of the other speakers will be commenting on the block exemption report, I'm not going to ask them at this point to comment on Kirti's presentation.

But if any of you have any clarifying questions that you would like to ask Kirti, we have time for you to do that before we move on to the next speaker. In that case let's move on to Fiona Carlin who is going to give us her comments on the block exemption report.

FIONA CARLIN: Good afternoon. I'd like to start by thanking our hosts for inviting me to speak this afternoon. It is my pleasure to

be here. And I'm going to probably repeat to some extent some of the points that have already been expressed by Dr. Mehta. And I apologize for doing that from the outset.

But what I thought I would do is focus primarily on how industry sees the current rules and how difficult they are to apply in practice and then give you some reaction from an industry and private practitioner side on the Commission's proposals to change.

It's already been mentioned that the current block exemption entered into force on the 1st of April, 1996. That happened one year after the U.S. licensing guidelines were published.

And yet there is very little policy from the U.S. guidelines that finds its way into the block exemption regulations.

And if you compare the new proposals for a revised technology transfer block exemption with the American guidelines, you see how far the EU/U.S. dialogue has advanced. And I think that's generally welcomed in Europe.

The word straitjacket has often been applied to the existing block exemption regulation. And I will go a little bit further than that because I believe that the current rules are a minefield of quirky drafting and pitfalls for the uninitiated.

So I think all in all the Commission's evaluation reports and the proposals to change the current rules have been very widely welcomed by industry and private practitioners in Europe. I'd like to say a few words about why the date 2004 is important. Two things will happen in 2004, one of which Dr. Mehta has already referred to.

First and foremost the EU is likely to enlarge from an existing 15 member countries to up to potentially 25 member countries, and some of those nations will join the EU it is expected in 2004.

And as part of that development, the European Commission has launched this modernization debate of the competition rules

and Article 81 in particular. It's proposing to abolish the individual exemption procedure.

Dr. Mehta has already mentioned that a lot of license agreements don't fall within the safe harbor of the existing block exemption regulation because it's so narrowly drafted. And yet they haven't been notified to the European Commission for exemption.

But I think it's important to bear in mind that maybe one of the reasons why those agreements haven't been notified is that the parties know that there is the possibility that if their license agreement is challenged they can go to the Commission and seek an individual exemption which offers them some degree of protection.

Currently an individual exemption would not apply retroactively, but it would be certainly influential in a court's discussion as to the acceptability or not of particular restraints.

What's being proposed is that

individual exemption procedure will be abolished and that national courts and national competition authorities will be able for the first time to apply Article 81 in its entirety. So the current monopoly that the Commission has in granting exemption will be abolished which will mean much more enforcement I think at the national level.

So coupled with the fact that we're going to have a lot more enforcement at the national level and a lot of new authorities enforcing the new regime, industry is very concerned that any revised block exemption regulation be as clear and consistent as possible so that the enforcement environment is predictable.

Whereas the current block exemption, in the Commission's own words, is so proscriptive that it tends to discourage efficient transactions and hamper the dissemination of new technologies. The drawbacks of the current regulation are many.

First of all, it applies only to

patent licenses, know-how licenses, or mixed patent and know-how licenses. It's already been said that it only applies to bilateral agreements. It does contain rather old rules limiting the duration of any territorial exclusivity that is conferred on licensees.

And just a few words on that. Under the current system in a pure patent license territorial exclusivity is accepted for as long as there are parallel patents in force in the territory of the licensor and the territory of the licensee.

For pure know-how licenses territorial exclusivity is accepted for a period of ten years starting on the date on which the products are first put on the market anywhere in the European Union.

And with regard to mixed patent and know-how licenses, territorial exclusivity is accepted for as long as there are necessary patents in force in the territories concerned or for the period of ten years or whichever of

those periods is the longest. So that's already a complicated system to apply.

One of the major drawbacks of the regulation as well is that it expressly prohibits any extension of the duration of the territorial restraints by the inclusion of any improvements. And that's a serious drawback, a disincentive to license if you like.

Dr. Mehta has already outlined the

main issues that the Commission is proposing to change. And very briefly, a new block exemption will be available up to dominant thresholds for agreements between non-competitors.

Agreements between competitors will be subject to a 25 percent market share threshold with quite an extensive blacklist of prohibited restraints including not only price fixing but output restraints, territorial and customer restraints.

And he has mentioned the narrow definition of competitors which would exclude from the notion of competitors the situation

where one company's innovation constitutes a sweeping breakthrough so that its competitors would require access to that breakthrough to remain competitive.

And it would also exclude from the notion of competitors the situation where two companies are in a blocking position. And I think that's to be welcomed. Industry reaction generally to the new proposals has been broadly in favor of a more liberal system that's on the table.

The Commission, we're glad to see, is proposing to abandon this arbitrary ten-year duration limit on territorial restraints in know-how licenses. We're opposed to the per se exclusion of licenses involving dominant firms. And we welcome the proposal to extend the block exemption regulation to cover a wider range of intellectual property rights.

In particular at least the American Chamber of Commerce welcomes the notion of expanding the block exemption to cover software

copyright and design rights, although we don't particularly see any need to have a regulation covering pure trademark licenses or copyright contents licenses.

I've mentioned that industry is broadly positive to the suggestions to narrow the definition of competitors which means that a greater range of agreements will fall within the more generous system envisaged for agreements between non-competitors.

We urge a more nuanced approach to the blacklist of prohibited restraints that the Commission is proposing to insert in relation to agreements between competitors. The Commission is proposing to prohibit as such all territorial and output restraints.

And we would argue that where the licensor is below a 25 percent market share threshold and for as long as an agreement is non-reciprocal and for as long as a licensee is not restricted in the use of its own technology, perhaps in those situations the Commission could

be a little more generous or a little less suspicious of agreements between competitors.

I suppose the main concern that industry has is the proliferation of market share thresholds that are being proposed. These are the thresholds that parties will have to look at when in the future they try to determine whether or not they fall within the new block exemption safe harbor.

I think industry has been very vociferous in the past in opposing the introduction of market share thresholds in licensing block exemptions. I think this time around there's resignation to the fact that we're going to have to live with market share thresholds.

However, we are asking the Commission to produce guidelines which will make our life as easy as possible in trying to apply some of these thresholds, particularly, when you are talking about tension in multiple markets, not only the product market, but the technology market

concerned as well as innovation markets in some cases.

When you think about the modernization proposals and the fact that in a couple of years' time we're going to have 25 national authorities and national courts applying these rules, I think the need for clarity on market definition issues and market threshold issues becomes really paramount.

I'd like to turn briefly and consider a couple of particular restrictions and look at how the current rules deal with those restrictions and what the Commission is proposing in terms of their treatment in the future.

First of all, non-compete clauses, the current regulation prohibits non-compete clauses all together. However, it does say that if the licensee chooses to compete with the licensor's technology the licensor can terminate any territorial exclusivity conferred and may stop licensing future improvements to the technology.

The new rules would appear to be

much more rational in that they would permit non-compete clauses in agreements between non-competitors but continue to prohibit non-compete clauses where a license is entered into between competitors. And we would welcome this more liberal approach.

The provisions currently dealing with assignment and grantbacks of improvements are complicated to say the least. The current regulation prohibits any obligation on the licensee to sign its improvements back to the licensor.

And it does permit reciprocal license back obligations provided that such obligations are non-exclusive for as long as the improvements are not severable.

And that means that if a licensee comes up with an improvement which can be exploited independently of the licensed technology, it must be free to exploit that improvement independently.

And therefore it may grant the

licensor a non-exclusive license to use those improvements, but it must remain free to exploit the improvement on the market itself.

This is a complicated regime. The new rules we're told will be more generous in terms of grant back clauses. But we're not very clear on just how generous they will be.

But I will say since we have the benefit of Dr. Mehta's presence here today that when you consider in particular a licensor that has technology that maybe he licenses out to multiple licensees in different fields of use, these grant back provisions and the prohibition of assignment makes his life very difficult in terms of managing the relations with multiple licensees and making sure that the technology is exploited to its maximum.

So I think there is certainly room for a more generous approach to assignment and grant back clauses. The block exemption regulation today contains some very odd drafting on no challenge clauses. Basically the licensor may

not prohibit the licensee from challenging the validity of the patents or know-how it has licensed.

However, the licensor may terminate an agreement if the licensee disputes the validity of the underlying know-how or patents or may terminate the license of a patent if the licensee challenges that such a patent is not a necessary patent. I'm not going to go into this in more detail.

But just even comparing those two indents, the difference in language, it is not clear why in one case you can terminate the agreement and in another case you can terminate the patent license. Drafting problems I think prevail throughout the current block exemption regulation.

The Commission in its evaluation report says in any future regime they may take a slightly less restrictive approach to no challenge clauses.

And they are aware of the fact that if

the licensor is a weaker party perhaps in that kind of situation a no challenge clause would be acceptable in order for the licensor to ensure that the licensee is not going to run away with its confidential know-how. I think that's also very welcome.

I think I'll just say a few words in conclusion. Given the complexity and the narrow scope of the current regulation, industry is very generally positive towards the Commission's proposals to change.

There are nonetheless pitfalls that we would urge the Commission to consider very carefully, some of the main ones being: a very strict approach that they seem to be taking towards license agreements involving dominant companies;

A very strict approach they want to take concerning all agreements between competitors; the dangers inherent in multiple market share thresholds in a decentralized enforcement system.

And therefore we would urge the Commission when it produces its draft block exemption regulation for consultation later this year to present at the same time draft guidelines which as much as possible clarify some of these issues so that we get a whole package to comment on in the hope that the new system moving forward will be more coherent and more generous to technology transfer. Thank you very much.

WILLIAM KOLASKY: Thank you very much, Fiona. Kirti, is there any part of Fiona's comments that you would like to respond to or any questions you may have for her?

KIRTIKUMAR MEHTA: No. I think overall the comments are very useful. And I think as regards the conclusions I would agree that what we are foreseeing is generally regarded as in the right direction. This is the comments that we have had. We realize the issue with both is defining potential competitors.

Secondly, because after all you know, technology, almost everybody in that field or related fields you could say can be on that very similar technology trajectory. So how do you define who is the potential competitor?

I think the case of very drastic innovation is a very distinct case and people can recognize that very easily. But that is not a very common situation. The common situations we are talking about are really incremental improvements in technology. And hence that is an issue that we are looking at.

Market definition, certainly I agree. And I think if we look at our guidelines and horizontals and R & D you see we have the market for the product. Then there is a technology. Then there's what you might call the R & D or innovation market. And the innovation market I must say is rather difficult to define.

And very often you end up by saying, well, if there are three or four pools, well, then we will take this into account. But why four? Why not two? Why not five? I mean it is absolutely arbitrary how you go about doing it.

Nevertheless we have certainly followed this line for the R & D pools.

But that is an issue that we are looking at very much. And certainly we take to heart the comments that people have made. I also think Fiona's comments bring out many of the elements that are already there.

For example, the reason why people don't notify is because there is this possibility retroactively to come to the Commission, the possibility that of course in the future we will not have the notification system, but for the technical license we have had it right from the start for a long time.

One last point which is on modernization and enlargement, I think perhaps one should not too much exaggerate that there will be many players in the enforcement. It's true. But the Commission still remains there at the center and will be developing policy. Block exemption is certainly an important instrument which we will do.

In the modernization, the draft regulation, you also talked about business review letter which is an instrument we have not had up to now. So you should look in the perspective that you have block exemption, certainly also guidelines. We are thinking here too to develop guidelines. What happens when the block exemption safe harbor doesn't cover you?

And these business review letters I personally see as a way of dynamically keeping the guidelines up-to-date because issues in which we will do the business review type of thing are those which are not covered in block exemption, which are not covered in guidelines, and there is a specific issue that comes up for which we will make a response rather than -- a response because we think it's not covered at that point.

And so I think in that respect there will be uniform application of the EU rules which of course will be another major advantage of the modernization, that you have a common set of substantive rules being applied. And we would like to also let our guidelines be applied also by the national authorities and by the courts.

WILLIAM KOLASKY: Thank you very much. You anticipated my next question which was going to be whether you were thinking about guidelines, and I'm pleased to hear that you are. Yee Wah Chin is now going to offer a summary of the ABA's comments and views on the technology block exemption report.

YEE WAH CHIN: Good afternoon. Thank you to the Antitrust Division and the Commission for inviting me to participate in these hearings. My assignment, as Bill said, is to discuss the ABA comments on the EC evaluation report on the technology transfer block exemption.

I'm speaking only as a member of the working group that drafted the comments, not on behalf of the ABA or any of its sections. These comments on the TTBE report were issued jointly by the ABA sections of antitrust law, international law and practice, and the intellectual property law section.

The comments compared the EU and U.S. approaches in the IP area. We endorse the basic thrust of the TTBE report. And we certainly urge the Commission to apply additional flexibility and incorporate a broader scope in any future block exemptions in the IP area.

Since the focus of these two days of the hearings is an international comparative law perspective, I'm going to focus on those parts of the ABA comments that are comparing the EU and the U.S.

My PowerPoint actually covers all the comments, and I understand that the PowerPoint will be posted on the FTC website so that if anyone is interested they can see all of my PowerPoints which I don't expect to go through today.

And in any event, the ABA comments themselves are posted on the ABA website on both the web pages of the antitrust law section and the international law section. And I believe they will also be posted on the FTC website. So

you can't miss them if you went looking for them.

The joint comments are comments of the three ABA sections only. They are not ABA policy, and they are not approved by the house of delegates or the board of governors of the ABA. I think I now have gotten all the categories covered.

In comparing the EU and the U.S. we had six areas that particularly struck us where our differences in approach can lead to significantly different results. First and most fundamentally is the view of the role of competition law with respect to intellectual property rights.

Second is the view of market power that's in intellectual property, approaches to dominant positions and to monopolization, our characterizations of licenses, our view of vertical restraints, and certainly our very different procedural contexts that we act in.

The role of competition law in the IP area, the EC report discusses the potential role

of competition law in intervening and trying to improve the balance that's provided by IPR law, the balance that is provided in the IPR law for incentives to innovate and not to overprotect or underprotect the innovator's work.

As a result of this sort of urge to intervene in this way, an IPR holder might not be able to obtain maximum royalties in the EU without offending the competition law. There is this concept there of excessive prices. And it might be more likely that a dominant IPR holder might be subject to compulsory licenses.

In comparison in the U.S. the balance of incentives to innovate is determined by Congress in the patent laws. We don't see the antitrust law as seeking to improve in particular cases the balance that was reached by Congress in the patent law. The IPR holder is entitled to get what royalties the market will bear.

And it is very rare that we might find that somebody has an essential facility that may require compulsory licensing. I mean it's not

that it hasn't happened, but it is certainly a rare beast. On the other hand of course if patent rights are used as a sword instead of a shield it might violate the antitrust laws in the U.S.

The EU seems to have developed a distinction for the role of competition law in the IP area by distinguishing between the granting and existence of IP rights which are granted of course by member states and still not centralized in any way.

And in that area they have concluded that it is not affected by competition law, whereas the exercise of IP rights is subject to competition law. In contrast I believe in the U.S. with Walker Process we do have the concept that if you had obtained a patent fraudulently that may be an antitrust violation. So I think there is some difference there.

In terms of the market power of intellectual property rights, there's still some indication that in the EU there is an inference

that there is a legal monopoly from IPR. And that term is used several times in the TTBE report so that there is sort of a presumption that you have a substantial market power that can exist simply by holding some intellectual property rights.

In the U.S. we now have a feeling that IPR is really just another property right. And it is a property right -- of an exclusive right over certain technology. So we apply the same general antitrust principles to IPR as to any other property right. So therefore there is really no presumption of market power from merely holding certain IPR.

For example, take paper clips which now are quite mundane. There have been many patents issued over the years on paper clip designs. And maybe the first patent on paper clips which embodied the concept of trying to clip together items with a twisted wire has a certain amount of market power.

But I tend to think that the

one hundredth patent on paper clip design doesn't give you much except exclusive rights over the particular way you're twisting your wire to make that paper clip. So you can also analogize it to having ownership of a factory.

The market power that you have from ownership of a factory really turns on how many other factories are nearby that produce a similar product. You may not have any market power at all, or you may have a lot if you are the only one in town with that factory. Our view towards monopoly or dominant position is also very different.

Article 82 prohibits the exploitation of market power by a dominant firm. And again you have this concept of excessive pricing, so therefore monopoly pricing may generally be frowned upon. Whereas in the U.S. we prohibit monopoly only if it is obtained or maintained by improper means.

So therefore simply having high prices generally is not enough if you were to get those

high prices as a result of a monopoly that was gained by having a superior product on the marketplace.

The combination of these differences in terms of the inferences that we draw from the mere holding of intellectual property rights and the differences in how we treat the holding of market power leads to significant differences in the treatment of IP licenses.

In the EU therefore you might find more frequently that IP licenses are unacceptable for competition law reasons than in the U.S. The characterizations of licenses is a major area that we thought was a difference. In the EU you focus on the competitive relationship of the parties to the license.

So depending on whether you are characterized as competitors or non-competitors different rules apply to you in terms of the IP license types and terms that you enter into. As we see it under the existing TTBE, you're a competitor if you manufacture competing products

or you are competing manufacturers.

The proposal in the TTBE report proposes to limit the definition of competitor so that you would be a non-competitor even if you produce competing products if, one, the license involves a sweeping breakthrough so that no longer would you be competing unless you both have that breakthrough or if the licensor or licensee are in a blocking position with respect to the licensed IPR.

But the focus is still primarily in terms of the characterization of the parties to the license. The focus in the U.S. is much less on the competitive relationship of the parties, although that is not to say that if Coca-Cola and Pepsi were to enter into a license between the two of them for some IP that our agencies would not start scrutinizing it very closely indeed.

But the rules that would be applied to that license would not be dictated by that competitive relationship between Coke and Pepsi per se. I think we consider much more the nature

of the competition absent the license. We consider the relationship of the parties relative to the subject matter of the license. So suppose again you take paper clips.

If one of the paper clip manufacturers developed some new machine to make paper clips that really does a great job whatever design paper clip you've got, and a competing manufacturer of paper clips has basically been just buying paper clip making machines from other folks to make the design that they've got, suppose the two enter into a license where one of them gets the license to use that new machine.

Well, under the EU concept if I understand correctly those two would be competitors and therefore the license would be subject to tougher rules than between non-competitors. Whereas in the U.S. they would be considered as having a vertical license and would be subject to the more rule of reason general approach of vertical restraints analysis.

Or suppose you have both paper clip

makers developing new machines on their own. Unfortunately neither of them can use their own machine without infringing on the patents of the other.

In that case under the proposals in the TTBE report these two entities would not be considered competitors. But in the U.S. a cross-license between those two in order to clear their blocking positions might be considered more of a horizontal relationship. And it might be viewed a little more skeptically.

Or suppose that you've got one paper

clip maker that has found a new way to make paper clip wire very efficiently and another paper clip maker has found a new way of twisting the wire in any way you would like. And it's best of course if you have those two in a combination and they could really make super paper clips.

Well, in that case it does seem that under both EU and the U.S. approaches, under EU they would be considered non-competitors and in the U.S. it would be considered more of a

vertical license. So therefore they would be both looked at less stringently.

But the key is that in the U.S. we seem to focus much more on the vertical or the horizontal nature of the license and not on the parties. The vertical restraints, we have differences there. And the EU seems to apply their vertical restraints analysis to where the IP license is as between non-competitors.

And the U.S. of course we apply to vertical licenses. And the restraints that we cover are things like exclusivity, field of use, customer groups, and territories. The EU has much more concern on intrabrand competition. They are concerned about the possibility of coordination among licensees to a licensor.

And they have special concerns about territorial restrictions perhaps in light of its market integration objective. I guess you could characterize the EU approach perhaps more like what we had in Schwinn bicycles plus the market integration imperative. Whereas in the U.S. we

may have an approach that's guided very much by GTE/Sylvania.

We focus much more on interbrand competition. And in the vertical context we do have concerns about foreclosure of access to input, the possibility of raising rivals' costs, and certainly of course the possibility of coordination among competitors, especially if you have a network of vertical arrangements.

The procedural context in which IP

licenses are considered are very different between the two jurisdictions. For IP licenses in the EU you have to analyze first how you categorize that license. And then within the license each restriction has to fit within the exemption.

And under the block exemption the restrictions are mostly questionable unless they are specifically exempted or fall into one of the categories in some way, you know, how they are treated: if it's white listed, if it's black listed, or under gray clauses.

And then again there might be exclusions from any of the above depending on again the situation. The block exemption covers only patents and patents with know-how licenses. And so you don't have any guidance at all really for, say, a copyright license or a peer know-how license.

There is also some concern about consistency across exemptions as the TTBE report points out. There are areas where the various exemptions that are out there now may not be fully consistent so that it might be a challenge to see where a particular arrangement actually fits within which exemption.

And with modernization indeed there is a prospect of review by various member states. And in each case you've got the deal right now with the whole process of possibly individual notification and opposition possibility and possibility of withdrawal of exemption.

In the U.S. our general concept is that everything is permitted unless it is

specifically prohibited. And the IP guidelines provide safety zones outside of which rule of reason applies. And the guidelines do provide a strong road map as to the approach that the agencies will take where there are scenarios that fall outside the safety zone.

And the guidelines cover patents, copyright, and know-how. But basically again we focus on a functional analysis and not so much of categorization of the licenses as such. So this is a quick tour over the comparisons between the EU and the U.S. that we discuss in the ABA comments on the TTBE report. Thank you very much.

WILLIAM KOLASKY: I don't want to get us too far behind schedule. I do have one question for Kirti though. I thought that one of the most provocative comments of Yee Wah was the suggestion that the EU presumes market power from the existence of IP rights, whereas in the United States we do not.

And, Kirti, I wonder if you could

respond to that. Is that true? And if not, maybe you can give us some reassurance.

KIRTIKUMAR MEHTA: I think in the report itself -- I believe it's in point 28 where certainly I think the words used are legal monopoly. But whether it was market power or not it is a method of what are the substitutes available. It says so in that report.

So I think -- personally I think this is perhaps not such a big difference as these comments may lead you to believe. I think some of the other comments certainly and myself I said that we have difference as regards vertical restraints.

And I explained the reason for vertical restraints essentially from a competition point of view to prevent foreclosure. That is certainly something recognized here, what you call exclusive dealing.

Or a second issue is of price discrimination. This is for -- in the European context you are to look upon it as segmenting

the market. That is quite an important issue for reasons of market integration. And there certainly the emphasis I would say is different.

WILLIAM KOLASKY: Thank you very much. Next we will have comments from James Leavy.

JAMES LEAVY: Mr. Chairman, thank you

very much for inviting me here. I've come a long way. It's my second day here. It's 9:10 p.m., and I'm getting a bit tired. So we have three preliminary issues we have to get through before we actually reach the presentation.

One is can I stay awake for the next ten minutes to make the presentation. The second is can you stay awake for ten minutes to listen to my presentation. And the third is in the absence of my seven-year-old son who is in bed in Paris, can I make my PowerPoint presentation work.

My comments are based on the report that the Licensing Executives Society made in connection with the block exemption regulation although I'm not speaking on behalf of LES.

I'm speaking on my own behalf.

Our comments on the block exemption regulation are perhaps a little bit more controversial than the comments of the American Chamber of Commerce or the American Bar

Association. And I'd like to explain to you why they are a bit more controversial and to try to justify why we've made those comments in the way we have.

In order to do that we actually have to go back to basics and ask ourselves what the role of the block exemption system is in European competition law.

The existence of the block exemption system is linked to the structure of European competition law and the system of obligatory notifications which have arisen out of that structure the way it has worked for the last 30 years or so.

Under Article 81 there's a two-step approach to the analysis of any agreement. Under Article 81(1) you decide whether the agreement

is in principle restrictive of competition. And that's a fairly formalistic analysis. There's not too much economics in that the way it works now and has worked for the last 30 years.

There's very little economics.

Once you have passed that formalistic stage -- and that's fairly easy to get past -- the burden then shifts to business to obtain an exemption under Article 81(3). And if you can't obtain the exemption, you have a problem.

And in principle under Regulation 1762 you cannot get an exemption without going to the Commission and notifying the agreement. And notifying an agreement is a very burdensome business. It takes a long time.

You have to bring a lot of information and you spend a lot of time at it. You give the Commission a lot of information. And your competitors know that you have notified because it is a matter of public knowledge. So people don't like notifying agreements. If they can avoid it, they would like to do that.

If you don't notify an agreement you should have notified, that has very serious legal consequences in Europe. You can be fined, and your agreement is -- even if you do manage to get an exemption after you have notified it, the legal effect of that exemption is back dated only to the time when you notified.

What happened before that is sort of a legal limbo. So it's not a nice thing if you haven't notified and you should have. The block exemption regulations, they provide a means of benefiting from this magic exemption you have to have if your agreement is restrictive of competition under the formalistic test.

The block exemption gives you the benefit of the exemption without having to notify your agreements. That's where the block exemption system arises from. That's where it comes from. That's what we're talking about.

And block exemptions have been adopted in the past in those circumstances where the Commission feels that it has sufficient knowledge

about the types of agreements that are subject to the exemptions that it can say in which circumstances an agreement or a practice can benefit from the block exemption.

And although it is not the official purpose of the block exemption system, the block exemption regulations in practice have become a kind of code of conduct that provides legal security for business. If you follow the rules of the block exemption you are okay. You don't have to notify. Nobody will bother you.

The 1996 regulation covered patent licenses, know-how licenses, and mixed licenses. Now, at the time the Commission wished to introduce a market share threshold test for extending the benefit of the block exemption to certain types of territorial and other restrictions.

There was a big debate about this. It went on for several months. It went all the way up to the Commission itself. It became a political matter. It was decided and discussed

at a full meeting of the Commission.

It wasn't just a technical decision. And the Commission backed down. They backed down under pressure from various business interest groups including LES and other professional groups.

And therefore in its present form the block exemption regulation provides legal security to business which is based essentially on the terms of the contract.

You draw up your contract. You look at the contract. Do we have white clauses? Yes. Do we have black clauses? No. We're okay. We don't need to go any further. We don't need to notify. We have security.

Two things, the Commission is now evaluating the block exemption system for patents and know-how licenses. But at the same time there is a proposal to abolish the notification system all together. And as I say right from the beginning, the block exemption system arises because of the requirement of notifying in order to obtain the famous exemption under 81(3).

So there's some question as to what the block exemption system would do in a community competition law where there was no longer any requirement or any possibility of notifying to obtain an individual exemption.

But we are interested in the fact that the competition director in general is increasingly aware of and influenced by the U.S. approach to the antitrust aspects of licensing.

And this is shown in some of the comments in the Commission's evaluation report: the fact that they do make the point that IP rights are an important factor in economic development; the fact that they do say that licensing is in principle a pro-competitive activity;

And the fact that they also make the point that in order to assess the likely competitive impact of a license you do have to look at things like the structure of the relevant market and the role that the companies to the license play in that market;

And the fact that, yes, it is the case that provisions in license agreements can have a different impact according to whether the agreement is made between competitors or non-competitors, at what stage they are in the market. And so that's the Commission's suggested solution in summary.

There are, in the case of licenses between non-competitors, restraints which are not related to the exploitation of the licensed IP subject to a 30 percent market share, but not including certain hard core restrictions which are always prohibited, and a dominance threshold for restraints related to the exploitation of the licensed IP, and in the case of licenses between competitors, an overall market share threshold of 25 percent and again with a hard core list of restrictions, certain things that you can not do in any case regardless of what your market share is.

I'm being very quick going over this

because I think we are going to have discussion on the actual terms itself. Now, all of this sounds very realistic in the same way that the U.S. licensing guidelines are meant to be and probably are in general terms realistic in their approach to licensing in the real economic environment.

And this is the point that we do want to make very strongly to the Commission. The block exemption is not a set of guidelines that explains official policy.

The block exemption in the European competition structure as it now exists represents a set of conditions which business must absolutely satisfy in order to avoid having to make an individual notification to the Commission if their agreement is formalistically restrictive of competition.

It's a very, very different context that we're operating under. The guidelines are one thing. Block exemption is another. And that is in the case where the burden of proof is essentially on business to justify a license and not on those attacking the license to justify their position.

In the U.S. it's up to those attacking the license, whether it's the authorities or anybody else. The license is prima facie okay under the antitrust laws unless you can show the contrary based on showing the impact of the license or the likely impact of the license in its real economic context.

In the European context we're in a different situation. The burden of proof passes very quickly under Article 81 to business to show why its license agreement should be and has to be exempted. Now, in this context it's important to know that if you benefit by the block exemption that benefit is not absolute.

The Commission can in individual cases move to withdraw the benefit of the block exemption so that even if you say -- you make the availability of the block exemption relatively easy you are not giving a carte blanche to business.

You are not saying that the competition authorities no longer have any control simply because a block exemption applies to a particular contract.

And it's at that stage when the Commission moves to withdraw the benefit of the block exemption, it's at that stage that a set of realistic guidelines to explain the Commission's policy would be very useful and could well be appropriate because when the Commission decides to withdraw the benefit of the block exemption in effect the burden of proof passes to the Commission to show why the benefit of the block exemption should be withdrawn.

So what if the centralized notification system is abolished? It gets rid of one of the arguments, in fact the initial argument for having a block exemption in the first place because you no longer have to notify to be exempted, so why do you have the block exemption.

But the burden of proof resolution -- reason for granting a straightforward and presumed exemption will continue to exist because the structure of Article 81 will not have changed even though the centralized notification will no longer exist.

And that second reason, the burden of proof reason, will become even more valid, if you like, since the granting of the exemption which would still be necessary would be in the hands of what I'd call a myriad of national authorities rather than a single entity being the Commission.

And remember again that the block exemption would not be a carte blanche, would not be an absolute benediction to a particular agreement. The presumed exemption could always be overturned. The Commission could withdraw it or national authorities could move to withdraw it.

So our view is as long as Article 81 retains its present structure and approach, that's a formalistic approach to deciding whether

an agreement is restrictive of competition, plus the necessity to justify obtaining an exemption, then we think there should be a system of presumed exemption.

And they are not absolute presumptions. They are rebuttal presumptions based on what we've called the contract, the whole contract, and nothing but the contract, and then a set of guidelines that will tell us as to the basis on which the authorities would seek to overturn a presumed exemption.

And that would indicate to us what sort of things we would have to avoid in order to have the benefit of the exemption threatened.

And if we can therefore make the distinction between the role of the block exemption system or the presumed exemption system and a set of guidelines as to the policy of the authorities, then I think we can have a discussion, a realistic discussion based on many of the proposals which the Commission has discussed in its evaluation report and taking

into account the United States' approach in the licensing guidelines as to what we could put in the block exemption or the presumed exemption regulation on the one hand and the guidelines on the other.

But those would be guidelines not for enterprises to justify why they should get the exemption, but as in the United States, guidelines as to what the policy of the authorities would be where they seek to withdraw the benefit of an exemption given on the basis of an exemption regulation which is based in turn on the contract, the whole contract, and nothing but the contract. Thank you.

WILLIAM KOLASKY: We're into our break period, but I want to ask James one question if he can give me a brief answer perhaps so we don't intrude too much on the break.

With respect to what you described

as the formalistic approach to Article 81 in determining whether or not an agreement is, quote, unquote, restrictive, is that inherent in

the language of Article 81(1) or is that a matter of interpretation by the courts which could be changed to move closer to the U.S. position where the plaintiff has the initial burden of showing harm to competition before the burden shifts to the defendant to show that the alleged restraint is in fact pro-competitive?

As you may know, in the United States we went through that debate over the last several years which was finally resolved by the Supreme Court in the California Dental case.

JAMES LEAVY: In one sense it's not inherent -- it's only inherent to Article 81(1). But I think the presence of Article 81(3) was initially and continues to be an influence on the way in which Article 81(1) is interpreted. If you apply a rule of reason test to determine whether there is a violation of Article 81(1), why would you need Article 81(3)?

I think that the presence of the structure of the article itself almost inevitably gave rise to the type of formalistic

interpretation of Article 81(1) and then the emphasis being placed on what you had to do in order to obtain the exemption under Article 81(3).

If the initial text had just stopped at 81(2), a lot of things might have been different and we might be talking about something else today other than the block exemption regulation.

WILLIAM KOLASKY: I'm sure that some of the other panelists may have comments on this issue as well. But why don't we take our break, and when we resume Peter Alexiadis, Will Tom, and Maurits Dolmans and Mark Janis will share their views with us. Thank you.

(Recess.)

WILLIAM KOLASKY: I threw out a

provocative question right before the break, but I really do want to make sure we get through all of our speakers. So I'm going to turn immediately to Peter Alexiadis.

And any of the panelists do have

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further comments on the question I put to James, perhaps we could discuss that at the end of the session. And I'm now going to turn the chair over to my co-moderator, Bill Kovacic.

WILLIAM KOVACIC: Thank you, Peter. Whenever you are ready. Thank you.

PETER ALEXIADIS: Ladies and gentlemen, I'm pleased to be here. And I thank the Department of Justice and the FTC for the invitation. I'm not going to speak on behalf of humanity at large, but on behalf of myself.

I have a fairly narrow topic which follows fairly naturally in the sequence of what we've heard today in the sense that it's really only realistically viable to assess what the community's response to multilateral licensing agreements is having heard all of the previous speakers.

And they raise a number of interesting issues which will mean now that as I broach some of those areas they will not be new to you.

I've decided to look at the fairly

vexing question of should a revised block exemption regulation have broader coverage so that it embraces all forms of multilateral licensing arrangements including patent pools, reciprocal licensing arrangements, and licenses with respect to joint ventures.

As I said, you've heard a lot of the issues touched upon before by the previous speakers. So I won't go into those. The main issue as far as I'm concerned is as follows.

I believe that in this area at least, unless I'm being overly optimistic, that there is a greater possibility of U.S. antitrust rules and the European competition rules more or less adopting a similar approach. We're hamstrung in

Europe from doing that by two major obstacles.

The first one is the market integration goal which does not embrace comfortably all issues of efficiency in innovation in pursuing the goal of unifying the European Union. And that is not an antitrust goal. But it's a very explicit goal, and it's

one that's replete through the administrative practice and case law.

And we are dealing with a structure of Article 81 which is there which we've inherited which will not go away. And it's the heady cocktail of the way Article 81(1), 81(2), and 81(3) operate which makes the European approach to these things that much more difficult to comprehend.

In essence we've got an absolute prohibition up front. And that absolute prohibition has been interpreted consistently over a number of decades in a very strict way. It is then followed by an absolute sanction of nullity should you breach Article 81(1).

And then it is followed by an express power of the Commission to exempt and only the Commission to exempt should you breach Article 81 (1).

So consequently it leads to the difficulty that the last speaker was alluding to and particularly in the licensing field where the

hub of everything that we're talking about is enforceability because we are not talking about, as we do in a lot of other contexts, whether or not an antitrust regulator is going to be somewhat aggrieved by the anticompetitive conduct going on in the marketplace.

Quite the contrary, in most licensing contexts we are concerned about whether or not the parties can enforce their agreements given what is on the record and given that those agreements will inevitably be challenged in national courts. Again it's important to remember the way the European Union operates.

And why those concerns are less appropriate for multilicensing agreements is because the level of cooperation through parts of an industry or among competitors is such that the enforceability issue becomes less important.

It becomes less important because if you're going to engage in that level of cooperation once you lose trust among one the whole deal is off. Therefore, enforceability

becomes more or less an all or nothing exercise.

Whereas in a licensing context it's key that the licensee not run away with the fruits of your labor on the back of an unenforceability obligation. So I think there we have a chance to move together as two systems. But we probably need to do it incrementally.

Now, I'm just going to quickly run through some of the problem areas that we have and some of the drivers from a substantive point of view and from a procedural point of view again to give you a better context of how we should look at these issues.

First and foremost as I said earlier, the intrabrand competition issues are much more important in Europe than they are in the U.S., and they do not necessarily produce rational competition results all the time.

Dr. Mehta did allude to two instances however where they can produce anticompetitive issues which even in a U.S. context would be taken into consideration even not at the height

level of concern.

We do as a result of a legacy of administrative practice I believe -- and this is where I agree with the ABA commentator who wasn't speaking on behalf of the ABA, but was speaking on behalf of someone. I do agree with her that we have probably had an overfascination with classifying competitors in terms of actual or potential or non-competitors.

And that essentially, again if you look back historically, was the result of a desire by the Commission to try to overcome the difficulties of the absolute prohibition under Article 81(1).

And by classifying or characterizing market actors as not direct competitors, they were able to sidestep the Article 81(1) prohibition and therefore de facto create a type of rule of reason analysis.

The courts in Europe have done their job as well by trying to skate past the issue of Article 81(1) relative to Article 81(3) and

talking about the effect on competition in general of certain types of agreements.

And a body of jurisprudence has developed over the course of time however in practice -- I'm speaking as a practitioner now -- largely ignored except by the bravest of counsel on the continent when one is looking about legal certainty and this vexed issue of enforceability.

Market definition has also proven to be a highly controversial issue as we have moved to gradually historically attempting to impose more a market based analysis on this rather than the straitjacket approach.

And the difficulty has been the rather obvious one. Namely it's difficult enough trying to configure your marketplace and your market definition at the start of the licensing agreement. But how do you do that two, three, four, five years later, particularly when it's innovative technology?

So again you're running through the bogey of this unenforceability issue right smack

dab in the middle of a licensing arrangement which was perfectly legal a few years ago.

The other issue that has arisen that I find interesting from a practical point of view is the mantra of effective competition, the ability to withdraw the benefits of a block exemption should there be not effective competition in the relevant market covered by the license.

And that is an interesting one as well because the doctrine of effective competition most recently is developing a standard which is no different than dominance.

Therefore you should ask yourself if effective competition means dominance, why don't we say dominance, and why aren't we just concerned about market power in a licensing context and forgetting about a lot of the rest. I just believe that's food for thought.

Another point that Fiona Carlin mentioned earlier was the plethora of competing market share benchmarks which are very, very

confusing to clients. I dare not say that they are confusing to lawyers because we wouldn't have a job unless there was a degree of confusion.

But they are very confusing to clients. And it's difficult for them to tiptoe between the tulips of ten percent, twenty percent, twenty-five percent, and thirty percent at any given point of time and knowing precisely where they stand.

Another point that's worth adding is that in innovative markets and particularly when we are talking about the information society type of products, it's very difficult to get comfort from a block exemption when the marketplace is changing so rapidly. This alludes to the point I was raising earlier about the way things change.

The other point that you should note is that EC competition rules outside the context of Article 81(3) are totally incapable of dealing with the evaluation of efficiencies in the way you would deal with efficiencies under your antitrust rules.

And I think that's borne out by the explicit language of Article 81(3) which is all about evaluating efficiencies. And if it is that explicitly stated there, it doesn't exist anywhere else.

And the fact that we're having a series of ongoing debates now about efficiencies in the context of the merger regulation suggests that we don't have an efficiencies doctrine. We never have had, and we'd like to pretend that we have had.

The other point to note is that people tend to forget a case called Delimitis decided quite a while ago now in the context of EC jurisprudence which made it quite clear that block exemptions are straitjackets. That's precisely what they are, and they're nothing else but that. And I advocate the words of Mr. Leavy in that respect.

So from substance to procedure, there is a difficulty with broadening the scope of the TTBE block exemption for the simple reason that

if we were to seriously contemplate bringing multiparty licensing within its scope we would have to change the enabling regulation under which it is adopted itself.

That is not an insignificant task. I think Fiona Carlin alluded to that as well, that it is not an insignificant task which will take possibly a year if not more. That's the way the EC works. And not only that, it will probably require a complete re-evaluation of all other forms of multiparty cooperation in the context of all other block exemptions.

So you can see that this is not an easy task. And so I'm going to lead you straight to my conclusion, but we'll take a bit longer to get there. Namely I would be very pleased if there was nothing in the block exemption to do with multiparty licensing all together and that it be dealt with separately.

I can speak on behalf of clients to say no matter how tedious it is as an antitrust lawyer to deal with block exemptions, European

business has found it at least a point of certainty, a reference point which they can deal with.

And they like that. And anything which suggests greater flexibility on the part of antitrust regulators is good from an electric point of view. But business doesn't quite see that in as warm and cuddly a light as practitioners would.

The sink of nullity also provides in European law terms a completely different spin on your idea of a safe harbor. Your idea of a safe harbor is a promise on behalf of the regulators to say that we're never going to take action other than in a situation which at least satisfies this criteria.

Under the European system it is virtually having the opposite psychological effect exactly. It is virtually an incitement to challenge the enforceability of agreements because they don't satisfy this criteria.

And that is because of the history of

the way block exemptions have been interpreted because it's in the power of the individual parties to challenge enforceability, not in the hands of the European Commission as would be the case with the DOJ, for example.

The other point to remember as well is the power of exemption lies only with the European Commission, not with the national courts, not with national competition bodies.

We have had difficulties and we will continue to have difficulties with the modernization which is occurring now within the community as more power is devolved from the center to the periphery with the accession nations.

As it becomes quite clear that all these new competition authorities and all these issues which will arise do not have the power of exemption. We have a doctrine in the community which has developed separately called the doctrine of severance.

And namely you're able to rip out

an offending prohibition which is prima facie anticompetitive in order that the remainder of the transaction or the agreement be held on foot.

The difficulty with that has been the difficulty recognized for a number of decades now, that by doing that a national court de facto is kind of giving an exemption in many respects because Article 81(3) refers to agreements.

It doesn't refer to provisions of agreements. It agreements in totality. In practice it has not posed a problem. It has never posed a problem. But the reality has been that a lot of academic writing has been spilled on that issue.

Now, I propose that the way we deal with multiparty licensing agreements is by adopting a balancing test made up of three limbs because ultimately what we are seeking to do in the European Community is what you're seeking to do here. And that is namely to weigh the risks of cooperation against the benefits of innovation.

We're probably better off by shelving the potential actual or non-competitive scenario that we've been looking at in the past and focusing more on the effects of the licenses as to whether or not fundamentally they are vertical or horizontal in nature.

And I propose that we adopt a tripartite test which essentially looks at structure, conduct, and performance in evaluating those. The structural issues will be those that will be underlying the industry in which the licensing arrangement is taking place and an evaluation of market power.

Secondly, we should look at the modalities of the licenses. And I use the word modalities because it is one of the most popular words in European Community jargon and probably means absolutely nothing to anyone here. But we should look at the modalities of the way the licenses work.

And that will help us to understand the relationship between licensor and licensee,

the relationship between the licensor and other suppliers, and the relationship between other licensees so that when we are making -- drawing conclusions about foreclosure and lack of access and so forth that they can be more or less informed by those key drivers.

And thirdly, we should be quite explicit as to what are anticompetitive practices which we foresee that might stem in a worst case scenario from multilateral licensing agreements. So structure of the market.

We should be looking at the underlying products that are developed, and we should be looking at the technology. We do not as yet in Europe have your tripartite breakdown of IP markets in terms of product, technology, and innovation. We do have products and technology however.

I tend to agree with Dr. Mehta that the innovation markets approach doesn't quite sit comfortably with our administrative practice and jurisprudence today. It's probably more relevant in an evaluation of market power at the end of a process. But currently it's a very unruly horse for us to ride.

And I find I probably in general believe that innovation markets are very, very difficult to assess from a licensing point of view. In terms of market power, ultimately the key issue here is whether or not the joint use of IP rights aggrandizes market power and therefore also raises barriers to entry.

And quickly, evolving markets, identifying market power is arguably possibly better addressed by first identifying the likely abuses which are likely to occur.

We've had a lot of historical experience under Article 81 where we have a history of abuse of configuring the market around the abuse rather than going through the analytical step of first identifying the market and then the market power. So we work backwards as a shorthand.

In terms of the modalities of the

multilateral licensing arrangements, we should be trying to determine whether in net they act as an entry facilitator, promote open standards, promote innovation, technology dissemination, lower transaction costs without raising them for others.

And we probably do so by amongst other things -- and I refer to your April 17th hearings where a list of issues have arisen which I will address in a paper subsequent to this, the types of issues which should be taken into the cocktail mix.

And that's namely the relative importance of blocking patents in the technology mix, the existence of so-called patent thickets, and the constant minor improvements which might be achieved through a multilateral licensing arrangement, the effects of previous anticompetitive conduct in the sector are I think highly relevant, the effects of exclusivity, the number of excluded actors from a multilateral licensing arrangement relative to the market as a whole, and so on.

Last but not least we should be clear about what anticompetitive practices we are concerned about. Clearly de facto an actual cartel-like behavior is of primary concern. And why do we need to identify these issues?

We need to identify these issues because if we do adopt an approach which focuses on vertical and horizontal restraints we've got in community law an existing set of building blocks that we can do that consistently.

And when we're looking at de facto cartel-like behavior, we can refer to the horizontal guidelines that we now have which provide industry with a lot of guidance.

Secondly, we're concerned about foreclosure and raising rivals' costs as that expression has been used earlier. And there again we have some guidance. We have the vertical restraints guidelines, and we have a rule of thumb which talks about 30 percent of the market being foreclosed to raise issues for competitors.

And last but not least, we have the reduction of incentives to engage in R & D which has the result of delaying innovation. And again we can draw on the horizontal guidelines and Article 82 jurisprudence. And in that sense there are a lot of standardization issues which I'm sure Maurits will cover later.

So what should the desired approach be in Europe which over time would start to look very much like a U.S. approach? I will propose that we adopt guidelines for multilateral licensing. I would propose that we exclude it from the block exemption all together.

I would propose that we look at it in terms of clear, vertical, and horizontal issues and market power issues. I propose that we identify clearly the negative effects that we might suppose could result in a worst case scenario so parties know precisely what they are getting into.

And I propose as the previous speaker

said that there be no presumption of illegality at all but we talk about how the competition regulators would like to see these issues on balance so that again it becomes an issue of the parties not having to be concerned about regulation.

Again because enforcement is not an issue that is unlikely to prove burdensome in this situation. Thank you.

WILLIAM KOVACIC: Thank you, Peter. I was wondering if Will perhaps could give his presentation now since Will like Peter will be addressing in many ways multiparty licensing issues. And following Will's presentation, we can take a few minutes to discuss the points that both have raised.

WILLARD TOM: Thank you, Bill, and thank you to both the Antitrust Division and the FTC for having me here today. Like the previous speaker, I am not speaking on behalf of any particular organization or group.

What I would like to do before I get

into the multiparty licensing issues is just make a few comments about the TTBE report itself. I think -- and it may just be my capacity for several self-delusion and my general Pollyanna-ish attitude.

But I really think that it is remarkable the degree of convergence between the Commission and the U.S. authorities in just over five years since the TTBE went into effect. And here I'm not referring simply to the TTBE report itself, but also to the wealth of material that the Commission has produced in the last few years:

The 1999 amendment of Regulation 17 which dispensed with the need for prior notification in the case of vertical agreements, the vertical block exemption that same year, the block exemptions for R & D agreements and specialization agreements, and the guidelines on vertical restraints in the year 2000, and the guidelines on horizontal cooperation agreements in 2001.

If you look at these documents, you will see really I think something of a sea change in approach. And I am much less pessimistic than I think some of the previous speakers like Mr. Leavy as to the ultimate effect and the ability of businesses to function under the European approach.

I think together these documents represent a huge movement away from the black, white, and grayness of prohibited, permitted, and exemptible practices and toward a regime in which the market conditions in which the practices occur play a much more important role.

And in the report itself one also sees indications that Commission staff would like to see a wider scope for intellectual property owners to exploit their intellectual property including licensing exclusive rights not just to particular territories but also to particular fields of use and customer groups and so on.

One also sees a trend toward applying the same basic principles to all forms of

intellectual property, not just patents and know-how but also copyrights and the like. And chief among those principles that they would apply is a distinction between competitors and non-competitors which as we know is a key distinction in the 1995 U.S. guidelines.

And finally I think the block exemption report makes clear that the distinction between competitors and non-competitors is largely defined by what would have occurred in the absence of a license which I think itself was a step forward on the U.S. side in terms of analyzing these issues.

And we ought I think to step back now and again on the U.S. side and recognize that some of the problems that we may see in European approaches are not so far from issues that we have dealt with on this side of the Atlantic and continue to grapple with today.

Yee Wah Chin talked about the basic rule of reason approach and the property approach taken on this side of the Atlantic that patents,

for example, confer no legal monopoly.

But if you look at court decisions, you will see that phrase legal monopoly all over the place. And sometimes it's used as a way of distinguishing it from an economic monopoly, and sometimes it's not. Yee Wah talked about the safety zones outside of which the rule of reason applies.

But of course in a couple of decisions in district courts in pharmaceutical patent settlement cases in the last couple of years we've seen a most quick and heavy handed application of the per se rule in ways that in reading commissioner's statements the agency certainly doesn't seem to have had in mind when they brought their cases. But it's there in U.S. law.

So I think on both sides there is

something of a progression here and something of a struggle with some difficult issues. So what do we make of this for what U.S. enforcers should take away from the European experience which

I gather is the principal purpose of these hearings?

And I think in part you should just be very encouraged by the wide degree of acceptance of the approach that U.S. enforcement policy has gained in Europe over the last few years.

And perhaps one can only hope that the U.S. courts and other U.S. agencies will be as receptive to some of these progressive ideas as our European colleagues have been.

Conversely I guess the dark side of this is that the European experience does not seem to have been terribly helpful in solving the puzzles that still bedevil the U.S. authorities simply because they are very hard issues.

In the U.S., for example, there are situations in patent settlement cases which I've mentioned before and also in mergers where the key question is whether there would have been competition absent a license.

And the answer is that we just don't know. And if you look at the track record over

the last several years you'll see a wide variety of approaches to that very issue.

I mentioned the district courts basically take a don't ask, don't tell approach and simply skip right past the issue of whether this is a horizontal relationship and simply assume that it is.

You see in some of the government cases the approach of what I call the Russian dolls. You open up the antitrust case and inside it there is a patent case. And you've got to dig to the bottom of the patent issues in order to know what the right antitrust answer is.

And there are a number of other approaches as well which we don't have time to go into here. I think the European counterpart in the TTBE report is the reliance on the concept of a sweeping breakthrough to identify a situation in which parties that may look like competitors are not really competitors.

And there I think we're again likely to run into the problem of simply not knowing

until well after the fact. And several of the previous speakers have mentioned to me for certainty when you're trying to put together a license, when you're trying to make investments in reliance of a particular antitrust treatment.

And if you just don't know how it's going to be treated, that's going to present a problem. But I think as the U.S. authorities have found, the desire for certainty is one thing. But finding good ways to give it is another. Another area of puzzlement for U.S. authorities has been the issue of patent thickets.

They have played a huge role, for example, in Intel's defense of the FTC's action against it where Intel basically almost came out and said that patents were a positive hindrance not only to innovation in the semiconductor market but even to having a functioning market at all, and that the reason they flexed their muscles, if you will, was in order to cut through the patent thicket and prevent other players from

holding them up because you had hundreds if not thousands of patents reading on any product you could possibly commercialize in this market.

And what did you do in that area? I think there do seem to be some different approaches in Europe. And you've probably heard some of those approaches this morning. I wasn't here, but I know that some of the essential facility kinds of issues were discussed.

But it's not clear to me that either the U.S. authorities or the Commission would find it a satisfactory approach simply to deem the patents of Intergraph or Digital or Compaq to be essential facilities that had to be licensed royalty free to Intel.

And so the puzzle that this whole patent thicket area presents -- and it still remains -- is going to be an issue that neither side is going to find terribly easy to deal with.

And finally there do seem to be some key points of difference between the U.S. and EC approaches in which some of the previous speakers

have alluded to.

Two in particular may be the role of market thresholds which has already been touched on, and the treatment of competition among licensees. On market share thresholds I think there's been mention of the huge furor that erupted when the market share idea first appeared in the initial draft of the TTBE.

And Caldwell -- I don't know if Caldwell is still here in the audience. Caldwell Harrop and I went over to Brussels to appear at a public hearing while the issue was being debated. And it was during the period when the DOJ task force of which I was a member was writing our own guidelines.

And I was invited to speak about the differences between the safe harbor market share provision in the U.S. guidelines and the market share provisions in the proposed block exemption.

And one of the points I made was that under the kind of regime you've described today where you have a prohibition and then an

exemption, the market share plays a very different role from what it does under the safe harbor.

And I think in the event the European Commission solved the problem rather neatly, that is, by taking the market share threshold out of the exemption part of the document and putting in a new withdrawal mechanism where the market share test would play a role.

I think many of these problems are going to be if not disappearing entirely at least being greatly reduced in significance under modernization.

I think we saw some harbingers of that in the treatment of vertical restraints and the abolition of the requirement for prior notification and the statement that the typical course would be to seek retroactive exemptions where necessary in that vertical area.

And I think similar kinds of mechanisms will evolve that really make some of the more nightmarish scenarios that have been

alluded to this afternoon perhaps overblown.

Just briefly on competition among licensees, I would hope that the U.S. authorities in considering the European experience would decide not to imitate the concern expressed in the TTBE report for preserving competition among licensees as an independent value.

I think the U.S. guidelines took very special pains to giving the licensor freedom to create the kind of licensing arrangement that it chose to best exploit its intellectual property, just as a manufacturer has a lot of freedom to create an appropriate distribution system.

And whether one chooses -- whether one as a licensor chooses multiple licensees or a single licensee, whether one chooses licensees that compete with each other versus licensees that have exclusive territories and exclusive customers or fields of use, really should be of no concern to the antitrust authorities.

Let me turn for just a minute to the multiparty licensing issue. I don't think there

is any question that multiparty licensing is becoming more important than ever in industries, particularly the kind I mentioned, semiconductors, now biotech.

I mean in pharmaceuticals you used to have this model of one patent, one product, in effect the notion that the patent covered the new chemical entity, and that was what was important and would allow the innovator to earn a return on its pioneer product.

Now you have in biotech situations what is very reminiscent of the patent thicket issues in electronics. And you will probably see, I would not be surprised, biotech patent pools emerging in the near future.

There are a number of complications that maybe make that less suitable than in a case of MPEG and DVD. But I think you'll see them nonetheless. The approach there has been actually not too dissimilar, business review letters in the U.S., individual exemptions in Europe.

Both approaches have involved comparable delays. There is obviously a difference, and that is the business review letter is purely optional and the individual exemption is not unless you set things up so that retroactive exemptions are available.

But the issue going forward as we get more experience with these kinds of pooling arrangements is how do you set up a system in which these delays will not occur, especially in fast moving industries, point one.

And point two is that the issues are not limited to pooling in the context of standard setting but also situations in which more than two firms contribute both patents and complementary capabilities to a venture. And you see partial solutions I think in the block exemptions for joint R & D and for specialization agreements.

But there again you have some of these market share ceilings of 20 and 25 percent that really limit the usefulness of that approach. So

I think there remains an issue in this multiparty licensing area that will require some work.

I'm not necessarily advocating that it be part of this proposed block exemption because I recognize some of the drawbacks of delay and the need to change the underlying regulation. But it is an issue I think that ultimately will need to be addressed. Thank you.

WILLIAM KOVACIC: Thank you, Will. Because we do want to make sure to give both Maurits and Mark a full opportunity to give their presentations and to perhaps shortchange the discussion rather than give each of them three minutes at the end to go through their talks, we're going to have both of those first.

And then we'll have an extraordinarily efficient and insightful interchange at the end followed by these presentations. So Maurits if you would, please.

MAURITS DOLMANS: Thank you very much, Will. Thank you for inviting me. I'll be talking about the exciting world of

standardization, and in fact this is a world that can excite some people and people get very emotional about this as was remarked this morning.

I'll be talking briefly about how standards organizations can deal with submarine patents. I'll give the example of the ETSI IPR policy which is a case that happened about eight years ago.

And I note that the W3C IPR policy seems to go the same way as the ETSI IPR policy. So that raises some interesting antitrust issues.

I'll then discuss questions relating to non-disclosure or late disclosure or incomplete disclosure of IPRs in the context of standardization. And there are some cases pending in Europe that might be of interest.

And then finally I'll deal with licensing conditions and in what situation -- how can you effectively or efficiently solve a dispute about reasonable and non-discriminatory royalties.

And if we have time maybe we'll touch on compulsory licensing in the standards context because I heard twice a question about that. So I guess it is of interest. So I'll touch on it.

Right. What happened in 1993 with the ETSI IPR policy? ETSI, as some of you may know, is the formal European Telecommunications Standards Institute. It is somewhat of an equivalent of ANSI, but geared towards telecommunications.

And it has both governments as well as customers, users, and competitors in the telecommunications area as its members. What happened was they were very worried about submarine patents.

They were worried about the situation that happened here in Dell, for instance, where a standard was being developed and somebody was lurking in the background with their patent and then popped like a rabbit out of the hat when the patent is adopted -- when the standard is adopted; here is the patent; let's all of you pay

up, please.

To deal with this worry they said, well, it's not only the question of let's all of you pay up, but they might also hold hostage the standards organization saying I'm not going to license; I'm going to be the only player in the standardized market.

So what did ETSI do? They imposed a requirement on all its members to license all of their essential IPRs necessary for a standard, right, unless they were withheld within 180 days from the start of standards work.

This is called a license by default because what happens is standards work usually takes three years in Europe, maybe a little less long here, but it takes a long time.

So if you have half a year to withhold your patents, you don't even know what the standard looks like. You might not even know what patents you have. You might not even be able to declare your patents because there may be pending applications.

And if you then declare what they are, what the content is of the patent application, you may actually lose your patent rights. So this created some problems. But it became a requirement for membership. At least that was the proposal.

And so a number of IT companies complained on Article 81 and Article 82. They said, well, you, ETSI, you consist of a number of competitors and users; you are teaming up; you are concentrating demand under Article 81, and in fact you are dominant in the market for telecommunications standardization, and what are you doing.

As a result of imposing this condition upon us, patentees, or potential patentees, you are either forcing us to accept that we have excluded and that affects our competitive position because we lose the right to influence the standards work.

We lose the right, for instance, to propose technology as a standard. We lose the

right to block a particular standard if we think that standard isn't good for industry. And, secondly, we will not have a chance if we can't participate in the standardization work to gain experience and lead time or timely market entry.

And that can be quite -- because if you know about a standard that is being developed, you can already start research and development in the implementations. You get to market a year or two before the others. You take the cream out of the revenues. So it's quite important to be a member of these organizations.

The Commission solved it by sending a letter to ETSI saying, well, a mandatory license default, mandatory because it was enforced by exclusion from membership, and license by default because everything is licensed unless you withhold it, reduces the incentive to compete through innovation because companies would normally want to differentiate their products.

And if you can't do that because you are compelled to contribute your patents to

standards, it reduces innovation. In addition the Commission took into account the defection of important companies that may have important technologies could affect the quality of European standardization and therefore the quality of standard compliant products.

So there was a settlement reached. And this might be of interest to the W3C as well. The settlement says an IPR policy must call for essential IPR before the standard is agreed, not immediately after the start, but just before it is agreed.

Each member must inform the standards body timely of any essential IPR of which it is aware, whether it is its own or a third party's. The ETSI director will then ask will you please license on fair, reasonable, and non-discriminatory terms.

And if, yes, fine, no problem although we'll come later to the question of what happens if then these terms are a little higher than what the parties originally expected.

But if the license is refused, then

the ETSI director will ask for an explanation, a reasoning. If the reasoning isn't good enough, they may refer it to the European Commission for compulsory licensing.

And if the Commission doesn't want to deal with that or if ETSI doesn't want to deal with the licensing request, they will withdraw the standard. So that's the ETSI IPR policy. What we see in the W3C is there is a big debate going on especially involving the open source community about what should be the internet standardization IPR policy.

And for a while there was the requirement that there is a debate between should it be royalty free licensing or should it be a royalty bearing licensing.

And the April 2002 IPR policy says, well, do you want a royalty free standard and therefore we require everybody to license all essential IPR for free unless they are withheld within 60 days, not 180 days, but from requirements document.

So it is a little later in the standardization process. But if you don't do that, you get kicked out of the standardization work.

So this seems to raise the same competitive concerns in the U.S. as the ETSI IPR policy did in Europe, excluding from membership impacts to competitive position.

Mandatory license by default reduces the incentive to innovate because if you can't withhold the patent then you may be less interested particularly in the internet area which can be quite important, less interested in innovation.

Defection of IT firms could affect because a number of IT firms may decide to get out of the W3C. That could affect the quality of those standards. And my conclusion would be that the open source community should compete and not expropriate.

So what do we do with submarine

patents? Is there an alternative? One alternative is to say we're going to boycott IPR based technology all together. Under EC law a collective boycott raises concerns but could be justified by objective, relevant, and verifiable criteria.

And I think one of the important criteria when you know that there is potentially a patent for a particular technology that's being proposed as an internet standard is not only the quality and the functionality of the technology and the cost of the license that you are involved in, but also the inherent cost in introducing IPRs in open source development work.

And it is a fact that the W3C has been based on open source development work. And there is some very interesting work done by Laurence Lessig and a person whose name I cannot pronounce -- it's in my paper -- explaining how the introduction of IPRs in the open source community will grind open source development to a halt and in fact will take away the very competitive advantage that open source development has.

So it's perfectly legitimate as long as they do it clearly and they reason it for the W3C to say we don't want to have to deal with any patents; we are going to collectively boycott any intellectual property based technology.

Now, what could be a possible solution is to say, well, you have to -- if you propose a technology, if you actively propose your own technology you will be stopped from then later asserting the technology to block a patent, to block it or to charge royalties.

But if a third-party technology is being proposed, or somebody who is not even a member, there should be no requirement to license. There should be IPR searches. And those who do not wish to contribute their technology should not be excluded from the standards work and perhaps a referral in exceptional cases.

Suppose that Microsoft holds a patent

over the head of the open source community and uses that in order to reduce the incentive of the open source community to innovate.

Then that might be a concern that the antitrust authorities might be interested in. Now, what do we do with non-disclosure or late disclosure, the Dell case or the Rambus case?

Well, actually there is a case pending in Europe on these types of matters. There is a case. First of all, not all non-disclosures are in bad faith. People can legitimately forget that they have patents.

In a large, multinational company there may not be perfect communication. There may be legitimate doubt about the scope of a particular patent claim or about the scope of a particular standards technology.

And you may not figure out that your patent applies to a standard until much later after the time that you were supposed to have disclosed. But there is a patent case like this pending in the EU. I can't mention the party I think because it's not public yet.

And I don't have the full information because I only have my client's side of this thing obviously. But this is very interesting because the firm at the time of concealment was before the standard is set. When the standard is not set, right, the technology provider can't define dominant except perhaps in exceptional situations.

So we in Europe have a problem that you wouldn't have over here in the U.S., namely that when the abuse takes place the alleged concealment unless it is in good faith, right, there is no dominance. So Article 82 doesn't apply. And suppose that the technology is particular to the standard, and suppose that higher royalties are charged.

Then by the time that the technology provider is dominant, perhaps to consumers it is no longer relevant. Apparently the Commission then has been thinking about saying we can't say; we can't apply Article 82 or 81 to this. So we'll just say to ETSI that they have to clean up their ETSI IPR policy.

I think there is some possibility namely to argue that if a standard has become successful and a technology is essential for a particular standard, then the exercise of the patent in order to exact very high royalties in an environment which is standardized, where there are barriers to entry, and when there is an artificial monopoly, could be an abuse, especially if there was information available that suggests that the standard would have been changed or withdrawn had they known that the patent was actually relevant for the particular technology.

Now, I know I'm getting into time trouble. So I'm going to skip a little bit. And the rest I would suggest you can read in my paper. But there was an interesting issue we had in Europe in another case which didn't lead to a Commission complaint. But it is nevertheless relevant for some of the discussions we have

today.

What do you do if a patent pool charges excessive royalties? Can you regulate that situation? Now, in Europe I would submit we can, and perhaps in the U.S. you might want to.

First of all, in the standards environment when a patent pool controls the intellectual property development that's essential for a standard, there's no more competition for the market. It's only competition in the market.

There are in fact barriers to innovation. The very existence of a standard is a barrier to innovation because it takes three years to get rid of the standard and replace it by something else.

So in this exceptional situation there might be a need for a degree of price regulation or control. Now, the best regulation is of course provided by the market. So how do you do that, to allow standards organizations to compare technologies, not only the quality and

functionality, but also the price?

In other words, allow them to do a call for proposals. Propose your technology, and let us know how much you are going to charge.

Now, in the U.S. I know this raises concerns because there are questions about whether there's collusion between the buyers in order to get a very low fee for the technology. But this is the only moment where competition still plays.

There is still some intertechnology competition at this particular stage. And it makes sense to allow competition to take place because afterwards it's clear that there is a monopoly supplier, namely the owner of the essential patents.

Now, what happens if that didn't happen, if there was no ex ante competition? So we were confronted -- this is the PC industry --

confronted with very high demands for royalties by patent pools.

And they were saying, well, it's one

thing for the patent pool to ask a high royalty of a device which is specifically designed to do the thing to which the patents apply.

But we are a PC manufacturer. A PC can be used for many, many different purposes. There is only one little component in a PC. PC margins are very, very thin. We can't support much royalties.

We think that the six-and-a-half dollars you are asking for for the device is too much. Now, how do you solve that? Do you solve that through regulation?

A better way and what we did in that particular case is the patent holders stepped out of the pool for a moment and started to sue one of the PC manufacturers and asked for injunctive relief in order to force them to the negotiating table or force the debate of six-and-a-half dollars per device.

So the argument we developed is that in a patent pool situation where the patent pool has promised to license on fair, reasonable, and

non-discriminatory terms, where the exemption or business review letter has said that they have to license on fair, reasonable, and non-discriminatory terms, where they are in fact dominant because they are a dominant monopoly -- they are in fact a monopolist technology provider for this particular standard, right, and where the injunction would kick out -- would mean that in the downstream market for PC manufacturing there would be an impact on competition.

In these situations a patent pool shouldn't be allowed to ask for injunctive relief. They are estopped from doing that because they have promised to license on fair, reasonable, and non-discriminatory terms.

And the antitrust authority and the rest of the community has relied on that to their detriment. And for these reasons it would be a violation of Article 82 and possibly the condition of Article 81(3) that was applied to get an exemption.

It would be a violation of competition

law to ask for injunctive relief. What you would ask for is damages. And what are the damages? Well, damages are what you would have earned had you had fair, reasonable, and non-discriminatory terms.

What does this mean? This means the court is going to look at what the damages are, what the royalty should be. And of course as soon as they realized that they ran to the negotiating table and settled because you don't normally want a court to settle the royalty -- to set the royalties for you.

So I think this is an important means for antitrust authorities to ensure that royalties are fair, reasonable, and non-discriminatory and to ensure that in situations where a patent hasn't been properly declared, where somebody simply says like Sun has done in a number of environments: We have a patent, we're not telling you what it is, but we have a patent.

You can't check the validity. You

can't check whether it's essential. You can't even check whether the patent really exists. In a situation like that the patent owner shouldn't be allowed to ask for injunctive relief.

Compulsory licensing for standards, is there still time for that or do you want to wait for questions? Compulsory licensing, do you want to discuss that or do you want to wait for questions? I have probably exceeded my time.

WILLIAM KOVACIC: Maurits, maybe we could take Mark's presentation and then use the discussion to come back. Thank you.

MAURITS DOLMANS: Thank you very much.

MARK JANIS: Thank you. I'm still sitting here wondering about compulsory licenses and standards. I have to retool very quickly here. Thank you. I'm glad to be here. I feel it necessary to give a disclaimer because everyone else did, and I would feel left out if I didn't.

So I really am just speaking on behalf of myself, as if I would be speaking on anyone

else's behalf. It is relevant to a point that I want to make though. I come here as a patent law expert and an antitrust law novice.

So if I do say anything untoward about antitrust law, it should not be attributed to my esteemed colleague, Professor Hovenkamp. So that disclaimer I suppose is important. I do want to turn the discussion a little bit to patent law.

And I think Mr. Tom gave me an opening there when we talked about the Russian dolls and the notion that there might be a beautiful and elegant antitrust law doll and inside it a shocking and homely patent law doll.

That's really what I want to talk

about here. And to me this takes us back I guess to the starting point of a lot of the antitrust analyses that have been talked about here and then back beyond or ahead of the starting point. And here's simply what I want to claim or what I want to plead for.

And that is that antitrust regulators on both sides of the Atlantic really should take

care lest they assume away serious patent law issues that really precede antitrust analysis in certain of these areas. And the one that comes most clearly to mind to me is the area of patent pooling and cross-licensing.

So let me -- if you will indulge me for just a couple of minutes here, let me give you a little patent law talk here to explain what I mean.

A simple, simple scenario where I've got a patent that has a claim to a pioneering invention, you have a patent that has a claim to an improvement invention, and we both wish to manufacture the improved product, all those are variables that are important to the story. We think we know what may well happen.

You and I will enter into a cross-licensing arrangement. It will be a bilateral, simple cross-licensing arrangement. And we know -- and it seems very straightforward superficially at least -- we know where the antitrust analysis of that simple cross-licensing

arrangement will start.

If we look at the DOJ, the U.S. guidelines, they tell us as I see them anyway to start out by asking whether the patents that are being cross-licensed are blocking or non-blocking and then go on from there.

What about the European analysis? Where is the starting point there? I'm a little less clear I would say. It gets us into Article 5.1 of the TTBE and confusion there I would say.

But if you look at the evaluation report on the TTBE, it includes a lot of language that begins to look like it is very similar to U.S. standards, and other speakers have mentioned that.

So there is abundant language in the evaluation report suggesting that we should pay attention to the notion, the concept of blocking positions. It's part of the proposed definition of competitor and so forth.

It seems to be the same starting point. And it seems to be very straightforward

except to a patent lawyer I would maintain. So I want to ask a little bit about how did we get to this starting point? And how we get to this starting point of calling a patent blocking or non-blocking requires a very complicated patent law analysis.

At least two conclusions are embodied in that label, blocking versus non-blocking, one conclusion about patent scope, and a second conclusion about patent validity and enforceability. Ordinarily I think it would necessarily be included in the notion of blocking.

And so let me just develop that just a little bit for you starting with this conclusion about patent scope. What does that entail? Well, of course it entails interpreting the claim language of the patent. That is simply the most controversial issue in the last five years of U.S. patent law with many variant approaches. That's the starting point.

Secondly, this analysis of claim scope

might well entail an analysis of infringement at least -- and I don't really know how this purports to be done.

But at least if we I guess hypothesize the product that both parties think that they want to make and then conduct an infringement analysis to see if both patents would be infringed by that product, that would be a way to ask whether these claims block or whether they overlap.

But the infringement analysis is itself complicated. It is a fact laden analysis. It may entail inquiry into the patent law doctrine of equivalents, especially if there is a question about design-arounds which as I understand it often arises in this context.

And the doctrine of equivalents I suppose is the second most volatile issue, maybe the most volatile issue. We'll find out soon in U.S. patent law because there is a major case pending right now in front of the Supreme Court dealing with that issue.

So what do I conclude from this little bit of ranting here on the claim scope issue? First of all purely as a matter of U.S. law certainly in many of these cases reasonable minds could differ as to this conclusion of blocking, the conclusion about claim interpretation and infringement.

So the idea of blocking versus non-blocking, as I see it anyway as a patent lawyer, is not a simple concept. Secondly, again purely as a matter of U.S. law without even making any comparative analysis this distinction between blocking and non-blocking depends on application of legal standards that themselves are volatile, that change over time.

So it seems to me at least in theory that one could undertake a purely proper analysis in year one and conclude that there are blocking patents involved in an arrangement, and by year five conclude that under the proper application of the then existing standards there is no blocking, particularly depending on variations

in the doctrine of equivalents there.

So that's just another thing to keep in mind. Finally a comparative observation, and that is that European law, European patent law on claim interpretation and the doctrine of equivalents, claim scope, is not necessarily harmonized with U.S. law.

European law, much of this is a matter

of national law. I suppose it's also in part a matter of applying Article 69 of the EPC. So it's sort of a mixture I suppose of European and national matters. But you can see how differences could arise.

It's clear from recent history that there is a lot of variation in approaches to matters like the doctrine of equivalents across Europe.

So you would have to conclude I think or you might conclude at least looking at all of this that even if European competition law arrives at the same or very similar standards for its antitrust analysis of a patent pool or of a

cross license, this does not mean that case outcomes are necessarily going to be the same, far from it because there's so much room for differences of opinion in this threshold determination of blocking versus non-blocking.

This is a very simplified rendition of the situation I think. It can get much more complicated than that because the situation that I've given you is the simplest type of situation: two parties, one claim of one patent, and one claim of another patent.

And you do have to talk in terms of claims of patent, not in terms of blocking patents. That's really a misnomer. It is really a matter of blocking claims. Most patents, most all patents include multiple claims of varying scope.

And so again at least in theory when you talk about claim one of one patent lying in a blocking relationship, a mutually blocking relationship with claim one of another patent, what about claim two of the first patent and its

relationship to claim one of the other patent?

What about claim two of the other patent and its relationship with claim one of the first patent, and so forth and so on?

And you can see that if you step through this analysis you could have not really a bunch of patents in a patent pool all of which or many of which are blocking.

You could have one claim that's mutually blocking with another and another with its one-way blocking. You could have complementary. You could have all sorts of variations.

And one wonders then how you would really evaluate that for competition law purposes. So again the main point here is simply -- and others have written about this in the literature as well. And the main point here is that you do have to be awfully careful about the use of this threshold determination even as a matter of U.S. law.

I think there might be an insight here

for legislative policy. I'll throw this out and see what you think about it. Perhaps you would say given these uncertainties at least as a matter of U.S. law the blocking versus non-blocking distinction might still be useful.

We might not want to discard it all together if we can't come up with anything better. But if it's embodied as sort of a weak presumption in a document that is a set of guidelines that's rather general, maybe that's appropriate. Maybe that's the best we can do.

And perhaps that is the correct way to characterize current U.S. law. What about European law though? I think there may be an insight here for European law. And that is that it might be a mistake to vest this blocking versus non-blocking distinction with sort of a talismanic significance in a very elaborate formalistic legislative document.

And where does that lead me? It probably leads me to a point of agreement with several of the other speakers who said we should

have some kind of guidance, European competition law regulation of patent pools.

But it should be in the form of guidelines, not in the form of a block exemption that looks like the old style, formalistic type of block exemption. So maybe that's an insight that flows from some patent law considerations here.

I think I perhaps should stop there. I mentioned that there is another conclusion bound up in this analysis of blocking versus non-blocking. It is the conclusion about validity and enforceability of patent rights.

That bleeds over I think into other types of competition law standards as well, whether a patent is necessary, whether a patent is essential for purposes of a patent pool. I think only a valid patent would be essential, I think. So you could see the same kind of considerations.

And I think this reinforces my point that I just made earlier. There is lots of room

for judgment and lots of room for differentiation on matters of patent validity and enforceability.

Indeed the standards between U.S. and

Europe are not harmonized, definitions of prior art, different approaches to eligible subject matter for business methods and maybe for software as one of the other speakers mentioned earlier.

So the antitrust analysis that flows from this is not likely to be the same either even if antitrust standards themselves are the same. So I will stop there. I think there are other issues that are touched by this same sort of phenomenon.

And compulsory licensing is one. No challenge clauses are another. These are issues that have to be informed by an understanding of patent law as well as competition law. And I thank you for your attention.

WILLIAM KOVACIC: Thank you, Mark. In the few minutes we have remaining I'd like to just start by perhaps giving Kirti a couple of

minutes if he wishes to react to some of the comments that he's heard in this second segment.

Much of the discussion has focused directly or indirectly on specific features of the EU regime as well as efforts to assess the wisdom of existing approaches. So, Kirti, if you wanted to take a few minutes to comment on other presentations, please do.

KIRTIKUMAR MEHTA: Thank you very much. Just briefly I think one comment on Mr. Leavy's presentation. I think our legislation, our Article 81(1) I think the rather clear that the burden of proof for showing 81(1) violation is to the authority, the Commission if the case may be.

And certainly for the parties it is to show that it meets the criteria of 81(3) and 81(3) is not something over which we have discretion. If those conditions are met, then the agreement is compatible.

I think maybe in that regard what I learned or what I understood the message was that

introducing things that could make this less clear would be a problem.

I will say if you want to make a block exemption, meet the requirements of the deeds that have been put forward. And to counteract the criticism of its primitive nature now, then I think we can only move forward by bringing it more economic thinking.

And of course this will mean perhaps that sometimes you will have to face the problem of market definition and so on. But at the end you will get a more economics based regulation.

I think on the other -- there were interesting comments on multiparty licensing. As I mentioned we have ourselves looked at that issue and invited comments. What I didn't hear is why those were in favor or what are the reasons, the positive reasons. That would be good to know.

It's true that when you come to patent pools, you know, pooling or complementary blocking patents would be good because this would lead to lower price for consumers. But if on the other hand you are pooling substitute patents, it's not clear what will happen.

Probably the prices to consumers may rise. So these are issues that we are going to be going into in looking at what are the benefits of patent pools or multiparty arrangements.

There again we will then -- today now don't say much about royalties, but whereas we will have to look upon it because then you are looking at the incentives to innovate and so on.

Similarly with the standards, very interesting paper that was made whereas we didn't get to the end of it. But I think our policy on standards agreements, standardizing agreement is very often we ask the question to the parties that come to us as to why you think this is restrictive of competition.

Often open standards activities are not restrictive competition. And there we are not asking people to notify that. But we certainly I am sure you will agree that our approach is that standard competition is also -- can be good for the consumer.

So where that thrives, why not in but to take a policy which enables not to have a very wide interpretation of restrictive agreements. Thank you.

WILLIAM KOVACIC: Perhaps one other question, and our panelists don't necessarily have to have well formulated views on this now. But it's certainly something that we'd be glad to accept your thoughts on for the record as they occur to you.

And this is a point that Will raised earlier, that is Will raised the very useful question of what should U.S. policy makers take away from the European experience, especially recent efforts to engage in a continuing assessment of the EU antitrust IP regime.

I was wondering if our panelists might have other thoughts about approaches both in process or in content that U.S. policy makers given your reflection on the two regimes might consider emulating.

Any thoughts about that? And again if that's too much to formulate at the moment, it's not your last chance to contribute. But if you do have an immediate reflection, I'd welcome that.

MAURITS DOLMANS: Mine would be too controversial.

WILLIAM KOVACIC: We are tough enough. Please.

MAURITS DOLMANS: Don't discard all leveraging claims because I think leveraging claims can -- there are situations where leveraging is efficient. But there are also situations where leveraging is inefficient.

And the European Community is looking at the Microsoft case right now. And I must say of course I have an ax to grind there. But I think if you look at tying law in Europe and so forth it does make some sense in spite of what's been suggested.

PETER ALEXIADIS: I would second that.

I don't have an ax to grind yet in Microsoft, and I won't mention any particular clients, but it's my experience that leveraging is real. It can be pro-competitive and it can be totally defensive and foreclosing.

It needs to be looked at in a very skeptical fashion however because it is a very easy claim to make. And that's the only warning I'd give. But I think it is real whether we want to call it leveraging or some other word, Maurits. But I still think it's real.

WILLIAM KOLASKY: Other thoughts? I simply want to express my thanks to the panelists. It's become a very avid custom in these hearings that our participants do not simply present microwaved versions of other views but throw themselves wholeheartedly into offering a fresh perspective on these difficult issues.

And we are collectively struck again -- today is good proof of it -- of just how much we've benefited from that extraordinarily thoughtful effort to shed light on these issues.

So I want to express my thanks to you for giving us the benefit of this wonderful thought and simply to mention that tomorrow we go to the Pacific Rim at 9:30 at the FTC. Bill?

WILLIAM KOLASKY: I would echo what Bill has just said. We really do thank you enormously for coming here and sharing your experiences and your thoughts with us. It's obvious that we covered many, many subjects today, each of which warrants, merits a great deal more discussion.

It's also clear that we do have a great deal to learn from one another's experiences. I don't think you have to worry that we are going to jettison leveraging all together. We just do impose certain limiting principles on the use of leveraging arguments.

But what I do want to emphasize is that one of the reasons we held this session today and are holding the session tomorrow on Asia is that we do think it is important to open up a very substantial trans-Atlantic dialogue over these types of issues because we do think that convergence is important. And so I hope that this is not the end of our discussion, but only the beginning.

WILLIAM KOVACIC: I can only underscore as strongly as possible Bill's last comment. One of the most exciting and encouraging developments I think has been simply the process of competition authorities and the scholarly and practicing community in a process that has not involved any binding compulsion to devote effort to advancing the electric debate.

And that discourse has been extraordinarily fruitful as our panelists have observed today. And a major reason as Bill said for these proceedings is to see that that remains front and center a key element of what the policy making community does not future.

WILLIAM KOLASKY: With that, can we give our panelists a hand? Thank you.

(Applause.)