CPI's Asia Column Presents:

An Update on the Most Recent Version of China's Anti-Monopoly Guidelines on the Abuse of Intellectual Property Rights

By Koren W. Wong-Ervin[1]

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In March 2017, the Anti-Monopoly Commission of the State Council of the People's Republic of China issued its long-awaited draft of the Anti-Monopoly Guidelines on the Abuse of Intellectual Property Rights (Draft Guidelines). The State Council's draft reportedly combines and draws from the four separate versions issued by China's three Anti-Monopoly Law (AML) agencies and China's patent office.

The latest version incorporates some important prior recommendations, including from The Global Antitrust Institute at Scalia Law School (GAI), namely to avoid the widespread use of presumptions that conduct involving intellectual property rights (IPRs) is anticompetitive, and instead apply an effects-based approach to licensing restraints. There remains, however, several highly problematic provisions and omissions, including:

1. Application of the so-called "essential facilities" doctrine to IPRs;
2. The creation of special rules for conduct involving standard-essential patents (SEPs), including a provision that would create an AML sanction for seeking or enforcing injunctive relief on SEPs upon which the patent holder has made an assurance to license on fair, reasonable, and non-discriminatory (FRAND) terms; and
3. Application of the AML's "unfairly high" pricing prohibition to IPRs.

In addition, as the GAI noted in its comment to the State Council, the Draft Guidelines fail to adopt a compliance-based approach that sets forth basic principles that would allow parties to self-advise. The Draft Guidelines instead set forth a list of factors that the AML agencies will consider when analyzing specific conduct, yet do not explain the significance of each of the factors or how they will be weighed in the AML agencies' overall decision-making process. This approach allows the AML agencies broad discretion in enforcement decision-making without providing the guidance stakeholders need to protect incentives to innovate and transfer technology that could be subject to AML jurisdiction. To this end, the GAI recommended that the State Council include throughout the Guidelines examples similar to those found in other guidelines, for example the U.S. antitrust agencies' recently updated 2017 *Antitrust Guidelines for the Licensing of Intellectual Property* and the Canadian Bureau of Competition's *Intellectual Property Enforcement Guidelines*, to illustrate how the AML agencies will apply the basic principles.

Application of the "Essential Facilities" Doctrine to IPRs

With respect to the application of the "essential facilities" doctrine to IPRs, the GAI respectfully urged that this provision be omitted in its entirety or, at the very least, revised to eliminate any presumption of illegality in favor of an effects-based approach.

First, although a firm's competitors may desire to use a particular technology in their own products, there are few situations, if any, in which access to a particular IPR is necessary to compete in a market. Indeed, those who advocate forced sharing of an "essential" facility often have underestimated the ability of a determined rival to compete around the facility, with resulting benefits

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[1] Koren W. Wong-Ervin is the Director of the Global Antitrust Institute at Scalia Law School at George Mason University, an Adjunct Professor at Scalia Law, and former Counsel for Intellectual Property and International Antitrust at the U.S. Federal Trade Commission.

to consumers. This is particularly true with respect to fast moving technologies, where technological and market developments can present multiple opportunities to work around a competitor's intellectual property (IP), and it is easier to work around an IPR than it is to work around a physical structure. Recognizing this, the U.S. Supreme Court has made it clear that it will treat so-called "essential facilities" claims with great skepticism, stating that courts should be very cautious in recognizing exceptions to the general rule that even monopolists may choose with whom they deal.[2]

Second, potential inventors may be less likely to undertake the research and development that lead to an invention if the inventor's reward for its efforts is reduced by having to share its patent.[3] Conversely, if businesses know they can easily gain access to the patents of other firms, then they have less incentive to innovate and more incentive instead to free-ride on the risky and expensive research of others.[4] The implication of this analysis is that requiring businesses to grant licenses to competitors wishing to use a patented invention is likely to result in less innovation, which will harm consumers in the long run.

Lastly, the GAI recommended that, should the State Council retain this provision, it at least should be revised to explicitly acknowledge that a patentee's ability to license may be limited because the patent has been or may be exhausted. Under the patent exhaustion doctrine, once there has been an authorized sale of a patented item, that sale "confers on the purchaser, or any subsequent owner, 'the right to use [or] sell' the thing as he sees fit."[5] Patent exhaustion eliminates the legal restrictions on what authorized acquirers "can do with an article embodying or containing an invention" whose initial sale (or comparable transfer) the patentee authorized.[6] Given the patent exhaustion doctrine, the licensor may chose not to license its IPR to certain persons or at certain levels of the distribution chain.

Special Rules for FRAND-Assured SEPs

The GAI strongly urged the State Council to reconsider its approach of applying special rules for FRAND-assured SEPs. Instead, whether particular conduct involving SEPs, including evasion of a FRAND assurance, has net anticompetitive effects should require the same case-by-case, fact-specific analysis as is required for non-SEPs. Imposing special rules for SEPs, including creating presumptions of harm based on breach of contractual commitments such as a FRAND assurance, is not only unwarranted as a matter of competition policy, but also likely to deter participation in standard setting.

Application of the AML's "Unfairly High" Pricing Prohibition to IPRs

For the following reasons, the GAI strongly urged that the State Council not apply the AML's "unfairly high" pricing prohibition to IPRs.

There are many dangers to regulating price, particularly for IPRs. For example, requiring by law that prices be "fair" or "reasonable," or prohibiting a firm from charging "unfairly high" prices

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[2] *See* Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 408 (2004).

[3] *See, e.g., id*.; Sidak, J. Gregory, *How Does the Experience of U.S. Telecommunications Regulation Inform the Forced Sharing of Intellectual Property Rights under Global Competition Law?* (May 17, 2012), https://ssrn.com/abstract=2061895.

[4] *See Trinko*, 540 U.S. at 408.

[5] Bowman v. Monsanto Co., 133 S. Ct. 1761, 1766 (2013) (quoting United States v. Univis Lens Co., 316 U.S. 241, 249-50 (1942)).

[6] *Bowman*, 133 S. Ct. at 1766 & n.2.

risks punishing vigorous competition. In general, competition policy should not prohibit a monopolist from charging whatever price for its products, including its IPRs, it believes will maximize its profits. It is axiomatic in economics and in antitrust law that the "charging of monopoly prices . . . is . . . what attracts 'business acumen' in the first place; it induces risk taking that produces innovation and economic growth."[7] This is particularly important in the case of IPRs; the very purpose for which nations create and protect IPRs is to induce investment in risky and costly research and development. To achieve a balance between innovation and the protection of competition, competition agencies should generally avoid imposing unfairly high pricing prohibitions, particularly in the IPRs context. Instead, monopoly prices should be considered only if they are the result of an independent competition law violation.[8]

In addition, economics teaches that, absent information about actual market transactions, it can be especially difficult to identify a "fair" price. Indeed, it is particularly difficult to assess the "fairness" of prices associated with licensing IPRs both because there is no marginal cost to which the price may be compared, and because IPRs themselves are highly differentiated products making price comparisons among them difficult, if not impossible. The risk of placing overly strict limitations on IPR prices is that the return to innovative behavior is reduced, and consumers suffer in the form of less innovation. Compounding the problem, with such limits in place, IPR holders will face significant uncertainty in determining whether their licensing practices violate competition laws, and legal uncertainty is the enemy of financial investment.

Finally, in order to determine whether a particular price is excessive, the competition agency would need to calculate a baseline price against which to compare the allegedly excessive price. In our experience, competition agencies will not possess the requisite information necessary to determine market prices generally, and royalty rates for inventions in particular. This is a task that is best left to the market or, as a last resort, to the courts in those limited cases when the parties cannot reach agreement.[9]

The GAI's full comment is available at

https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2952414.

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[7] *Trinko*, 540 U.S. at 407; *see also* JOSEPH A. SCHUMPETER, CAPITALISM, SOCIALISM, AND DEMOCRACY 89-90 (George Allen & Unwin 1976).

[8] Douglas H. Ginsburg et al., *Excessive Royalty' Prohibitions and the Dangers of Punishing Vigorous Competition and Harming Incentives to Innovate*, CPI ANTITRUST CHRON. (March 2016), https://ssrn.com/abstract=2748252.

[9] For a discussion of the difficulties of court-determined rate setting, see Anne Layne-Farrar & Koren W. Wong-Ervin, *Methodologies For Calculating FRAND Damages*, LAW360 (Oct. 8-10, 2014), https://www.ftc.gov/system/files/attachments/key-speeches-presentations/wong-ervin_-_methodologies_for_calculating_frand_damages.pdf.