

SUBMISSIONS
TO
INTELLECTUAL PROPERTY & COMPETITION COMMITTEE
BY
DARRYL MISCHLEWSKI

Submissions refer to the numbered sections of the September 1999 issues paper

Executive Summary

1. New products and services entering the market under the protection of I P increase competition
2. New products and services protected by I P are a major source of new wealth creation
3. The majority of new products and services emerge from non commercial research institutes or SME,s
4. In a global economy, Australian I P and competition laws are of little help to Australian resident innovators
5. The I P and competition laws in major markets like Europe and USA are the primary determinants of commercial decision making and strategies relating to new products and services protected by I P
6. The position in the product life cycle of I P protected products or services is a major determinant of whether competition is likely to be impeded by I P rights
7. When the average time taken to recoup development and production expenses is compared the length of protection afforded, the term of copyright protection is excessive compared to patent terms
8. When I P is used to protect the market share and profit margins of mature products it may be anti-competitive.
9. Copyright and trademarks are more likely to be used to protect mature products, than patents.
10. Larger businesses use legal costs and uncertainty to exert pressure on SME,s in I P conflicts
11. Increasing the penalties for large businesses if they lose I P litigation will increase the likelihood of compromise settlements being achieved.
12. The ACCC needs to encourage competition by clearly stating that the use of IP to introduce new products and services into the market is pro competitive.

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I P AND COMPETITION

Globalisation

For Australian companies introducing new products to the market place and creating new wealth the Australian market is almost irrelevant. In planning designing and consulting with customers before the product is launched all leading edge innovative companies look offshore more than in Australia.

The determining factor for these companies is not the I P or competition laws in Australia, but those of USA, Europe and Asia.

Product life cycle

There seems to be little attention paid to the maturity of the market in goods to which I P protection applies.

Using the product life cycle concept, I P protection encourages new players and the launch of new products because it protects the investment made to enter the market. Thus I P is pro-competitive in the early to middle phase of the product life cycle.

In the mature phase I P protects the “cash cow” from direct competition.

This is least expensive for long lived copyright works and trademarks.

For patented products the original patents have generally expired by the time the mature stage is reached and the expensive path of further research and patenting to develop and protect improvements is required. This is not so anti-competitive as it seems, as it is also possible for third parties to develop and patent their own improvements.

Thus the most likely situation for I P to restrict competition is when products are in the mature phase of the product life cycle. Copyright and Trademarks at that stage of the product development protect the product’s marketable features rigidly and provide very effective protection from competition. Patents at the mature product stage can be avoided by designing around the patent, because the patented features of the product are not so rigidly defined in the mind of the purchaser. It is easier to persuade a consumer to buy a functional equivalent product than it is to persuade the consumer to switch from *Coca Cola* or *Mickey Mouse* because consumers are more loyal to the brand or the image than to the function.

6.1 COPYRIGHT

Copyright owners are more likely than Patent owners to obtain a dominant position in the market place and a far greater return on the investment which created the right.

The following is a comparison with regard to computer software.

COPYRIGHT	PATENT
Long term: life + 50 years	Short term : 20 years
No cost to create or maintain the right	To obtain and maintain a patent in Australia alone, costs from \$10,000 to \$20,000
No requirement for invention, simply protects investment in time and labour. Is applicable to all software.	Protects investment in the time and labour needed to create an inventive solution to a problem, as well as the time & labour to write the code
The time to create and put package on market is less indeterminate than for an invention	Greater risk in completing work on time usually more time consuming and more expensive to get to market
Costs of creating the program are usually recovered within two to three years	Longer payback period
Encryption means that competitors may not learn how program works	Patented ideas are made available to the public and are an aid to finding other solutions to the problem which can lead to competitive products.

A patent owner has to make a greater investment in time and money and has less time to use its monopoly position to obtain a return on the investment.

Registered Designs or petty patents protect developments of similar ingenuity to copyright but have very short terms of protection [16 years and 6 years respectively]

The economics of marketing copyright works is geared to obtaining a multiple of the total costs of production and selling of the work within a time span of about two years. This is the usual payback period for books, films and recorded music. Industrial products that are protected by patents and designs take a much longer period to pay back the costs of research, investment in plant and costs of production. The best documented industry for that is the pharmaceutical industry. This leads to the observation that return on investment is much more generous in the area of copyright works.

Once copyright products are established they create a market of their own. Peter Rabbit or Mickey Mouse merchandise, have an identifiable market of buyers. The original costs of creation and production have been recovered but because they are known they have a reputation advantage over new entrants.

6.2 PATENTS

What is patentable

Apart from doubt on medical treatments the Australian law is quite broad. In the past it has been the interpretations that have been narrow not the law. It is probably best to leave it to judicial interpretation.

As to business schemes where these are inventive and utilize some form of technology they are patentable now. [See USA 35473747 issued in 1971 and recent internet commerce patents like USA 5794207 or 5842178]

Disclosure

For leading edge innovators, patents are an important source of technical information and market intelligence.

If the patent system is under-utilised as a source of technical information, it is due to ignorance and cost. I P Australia does promote the use of patent information but at \$15 per specification this makes an average state of the art survey too expensive for first time users.

If I P Australia could subsidize the searching and provision of copies of patents this would assist industry in adopting the practice of patent searching prior to embarking on new product development.

Scope of protection- Biotech

There has been litigation, in Australia and overseas, involving a higher than expected number of biotech patents in the last twenty years. Compared with other patented technologies, biotech patents have had a higher incidence of invalidity, which supports the view that some patents were too broad. This is partly due to the inexperience of patent attorneys and lawyers involved, It was common for biotech companies to employ patent lawyers qualified in biotech and they were often newly qualified and paid little attention to the analogous field of chemical patents. I suspect that this perception will change.

More importantly the question of scope of protection has little to do with Australia. Australian biotech firms seeking to create wealth from new technologies must look to overseas markets, particularly the USA, to do so. The Australian Market is too small and it is the patent and competition laws in overseas countries that have the determining effect on success for these companies.

Parallel importation

Parallel importation of patented goods should be allowed.

No I P rights should prevent parallel importation.

Parallel importation has its greatest impact on consumer goods or business consumables. It is usually attractive because of excessive price differentials between countries. This price difference is usually not caused by the existence of I P rights. Thus I P rights should not be used to maintain the differential which could be exploited except for the existence of I P rights.

Australian Patent Examination

The standard of the search and examination by the Australian patent office is comparable to that of the USA and Europe.

More significantly the standard is to some extent irrelevant as most patents taken out in Australia have equivalents in USA and Europe.

- If the scope of the Australian patent is wider than that of the USA or European equivalent and
- it is only because of that wider scope that there is risk of infringement
- then: it is unlikely that the patentee would initiate litigation unless there were special valid circumstances for the wider scope.

This means that once again the determining factor is the state of the patents in the major industrial markets overseas. The benefit of the doubt given by the Australian office is of little significance in influencing the decision to commence infringement or litigation.

Patents Act overlap with TPA

The origin of sec 144 predated the TPA and was inserted to ratify an amendment to the Paris convention. If possible, it makes sense to keep the Acts separate.

Compulsory Licensing

The provisions are more effective than they are given credit for. They and the trade practices act make it difficult for patentees to refuse licence requests without good reason. In Australia the market size is small enough that in most cases one licensee or one patentee can satisfy the whole market demand. Patentees cannot afford to refuse a licence if they are not satisfying demand themselves or through an existing licence, because this would limit the return on their original investment.

The exception may be in the following circumstances

1. Patentee has two patents to two alternative forms of the one product but only markets one of them.
2. When the product is in the mature phase of the product life cycle a competitor seeks a compulsory licence for the un-exploited patent.

If Sec 44 of the TPA did not exclude IP, it is unlikely to be more readily applied than the compulsory licensing section of the Patents Act. Sec 44 requires that the alternative be uneconomic, but it is economic to develop an alternative to a patented item, because the benefit of doing so would not be limited to the Australian Market.

6.3 DESIGNS ACT

If the proposed innovation patent proceeds, the loss of protection for functional designs under the Designs act will be covered although the term of protection is shorter. Why protection should be shorter, when the costs of development and production and the time to recover investment are similar?

Spare parts are primarily functional designs and should be protected by innovation patents or standard patents.

Parallel importation should be allowed under the Designs Act.

TRADEMARKS

The economic value of a trademark is directly related to the sales value of products or services sold under the trademark and the relative market share of the trade mark. The economic value of a trade mark as a proportion of the sales value increases with increasing market share. The other major impact on value is the volume of buyers. Trademarks have little value where buyers are few in number and greatest value where the number of buyers are large and dispersed, as in consumer marketing.

Scope of rights

The effective scope of protection of trademarks is not altered by the absence of disclaimers. Such disclaimers are rare in the USA trademark register and in the systems of most other countries. Its absence in those countries has had no effect on competition. The Trademarks office practice in relation to them is however a source of anxiety for trademark applicants and an unnecessary expense.

Enforcement

Because of the relationship between value, market share, and number of buyers, the temptation to abuse trademark monopolies to inhibit competition increases as the trademark ages and its market share increases. This is particularly evident where trademark owners oppose similar trademarks proposed for use on products or services that are not marketed or licensed by the owner. Often the trademark owners are large and the potential market entrants are small and are forced to retreat by the prospect of expensive litigation. A recent example is *Coca Cola v All-Fect Distributors*.
See comments under section 9.

8**SEC 51(3)**

If the law was applied correctly the absence of sec 51(3) would have no effect on IP contracts relating to **new** products. However until there is certainty about that it should remain in its present form.

Sec 51 (3) provides I P owners with protection from the ACCC. Because there is a lot of ignorance and doubt surrounding what licence clauses are valid, the presence of this exemption removes uncertainty.

The article in the Australian Financial Review [14-01-99 on p30] is evidence of the lack of understanding amongst research institutes of this issue. The persons surveyed by the AFR all represented organizations involved in developing new products and as previously submitted in the early life of a product the existence of I P rights enables the new products to be commercialized.

One disturbing fact is that the NCC final recommendations did not differentiate between mature and new products.

For new products to the market, their very presence is pro-competitive. If the IP owner and its licensees agree to use horizontal arrangements such as cross-licensing patent pooling or insert price and quantity restrictions it is probably for the purpose of ensuring a more rapid increase in market share or a more rapid return on investment.

For mature products the absence of sec 51(3) protection for horizontal arrangements might well cause contracts to be rewritten once the market share has increased to a point where the arrangements become likely to lessen competition. This is more likely to be the case with the longer term I P rights such as copyright and trademark licences or franchises for well established copyright works and well known brands.

The NCC has recommended that the ACCC release guidelines and it would be very helpful to innovators if the guidelines made it clear that arrangements for new to the market products and services would not attract attention until the sales had reached a significant percentage of market share.

CLRC and categories of rights

It has been apparent for many years that copyright has been used as the I P protection of last resort to protect investment in time and labour .

Examples are the use of copyright for computer software, compilations of music or directories, all of which are simply commercial products. The same can be said for two dimensional industrial designs. The protection afforded these commercial products under copyright is much greater than is needed to adequately recoup the expense of creating them.

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ENFORCEMENT OF I P RIGHTS

IP litigation is time consuming and expensive and the temptation exists for large players to use this as weapon. This occurs most frequently with Trademark rights.

In business the cost and time involved in litigation is often used by larger or richer businesses to intimidate or wear down smaller competitors. In the 1980's Cadbury Schweppes sued the company making Pub Squash for passing off its Solo brand. Although Cadbury Schweppes lost the action the smaller competitor eventually went into receivership.

Patents

There is a perception amongst many new patentees that obtaining a patent means that litigation is inevitable. This attitude can make it difficult for sensible commercial negotiations to take place to settle or avoid disputes. My experience has been that a significant number of pre-grant patent oppositions and pre grant court actions are taken less for commercial reasons and more for reasons of personal reputation and company pride in the new innovation.

The likelihood of conflict occurring pre-grant is less than 1 in 10 but is more likely when a close competitor is pursuing a very similar development.

The likelihood, of some form of patent infringement occurring, is about 1 in 8, but the probability of serious, continuing infringement, that warrants litigation, is much lower.

Once patents are granted and their enforcement becomes a necessity, commercial factors are paramount. Post grant litigation is much more expensive and loss of market share or erosion of profit margins are usually weighed up against the alternatives of litigation and compromise such as limited licensing. But once again Australia is usually only a small part of a world wide conflict and litigation here is often only a part of a global conflict.

One **suggestion** for counter balancing the small resources of small companies against the larger resources of larger companies is to legislate to

- increase the damages payout by larger companies if they are found to infringe the I P rights of a smaller company
- have the larger company pay client lawyer costs if it loses an I P enforcement action against a smaller company

Such provisions would change the risk profile for the larger company and make a negotiated settlement more likely.