

## Implementing Competition Law in Patent License: Issues and Challenges for Malaysia

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### Abstract

Patent license is established when the patent owner allows the other party to exercise rights granted under the patent grant based on the terms specified in the patent license contract. However, there is no standard form of patent license contract and hence, parties are left with their own discretion to decide the terms to be included in the patent license. The freedom to include terms in the patent license led parties to expand their rights via inclusion of anti-competitive provisions in the patent license. Thus, competition law authority plays its role in determining whether terms included in the patent license affects competition process. In fact, patent license is expected to comply with regulations set by the competition law authority if it contains provisions which are anti-competitive in nature. This research evaluates the legal mechanisms employed by the Malaysia and EU competition authority in order to establish whether the mechanisms have adequately address issues relating to competition law in patent license. It also seeks to identify problems surrounding the patent license contract and explores how it affects the competition law. The findings indicate that while Malaysia has the basic legal mechanism to implement competition law in patent license, which is Competition Act 2010, but review of the Competition Act 2010 and additional legal mechanisms such as Guidelines are necessary to cater the needs arising from the patent license.

**Keywords:** patent license; competition law; Malaysia; Competition Act 2010; legal issues; EU

### 1. Introduction

Patent license refers to the transaction being made between the licensor and licensee concerning rights to be granted to the licensee by the licensor relating to invention owned by patent owner. It usually exists in the form of a written contract, known as license agreement (Hodkinson, 1987). Patent license adopts the characters of a contract namely, it may be made oral or written, enforceable and parties to the contract will be subjected to liabilities and responsibilities (Bielefield & Cheeseman, 1999). In fact, Malaysia requires a patent license to be reduced in written form and signed by the parties (Section 41(2) of Patents Act 1983).

In relation to patent license, there is absent of specific form of patent license contract. Patent license is tailored to the needs of the parties although certain provisions are commonly included in patent license (Power, 1971). The absence of a standard form of patent license provides freedom to the parties to include terms in the patent license contract depending on agreement between them. According to Bowes, the freedom to include provisions in the patent license is to ensure maximum benefit to the parties involved in the patent license as well as the public (Bowes, 1977).

Nevertheless, such freedom led parties to extend rights beyond the patent grant (Diggins, 1955), via inclusion of restrictions terms imposed by the licensor towards the licensee in the patent license. Such restrictions may exist in the form of provisions relating to royalties, territorial restriction, price restriction and patent use restriction (Rupert, 1980). These provisions are sometimes used by the parties to create anti-competitive effect in the competition process (Anderman & Schmidt, 2011). As a result, all contractual restrictions are subject to the rulings of competition legislations in the event it contravenes provisions relating to prohibited business practices underlined by the competition law (Leslie, 2009).

Maskus and Lahouel were of the opinion that licensing restrictions have been widely abused due to few concrete guidelines in existence among developing countries to assist in the area of intellectual property license (Maskus & Lahouel, 2000). One of the suggestions in relation to this problem is to examine practices adopted by various countries when dealing with competition law in the field of intellectual property (Raju, 2013). It is also suggested that a proper legal mechanisms must be in place to ensure effective implementation of competition law (Nguyen, 2010). EU experienced different phases in the evolution of competition law towards intellectual property licensing (Anderman & Schmidt, 2011)

which as a result requires EU to adopt various legal tools to accommodate the implementation of competition law in licensing area. Thus, the following sections examine the legal mechanisms employed by the EU and Malaysia competition authority in implementing competition law in patent license. This article proceeds to lay down issues relating to patent license affecting competition law in Malaysia and provide options to overcome the arising issues in patent license related competition law in Malaysia.

## 2. The European Union Approach in Patent License

This section looks at the various legal mechanisms employed by the EU competition authority in implementing competition law for patent license.

### 2.1 Basic legislation on competition law

In EU, the most important piece of legislation regulating competition law is The Treaty of the Functioning of European Union (TFEU), formerly known as European Community Treaty (EC Treaty). The TFEU came into being as a result of ratification of Lisbon Treaty which replaces the EC Treaty. The TFEU under Article 101(1) and 102 provides main regulations on competition law in general to be applied throughout the European region. According to Article 101(1) of the TFEU, it provides:

The following shall be prohibited as incompatible with the internal market: All agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the internal market, and in particular those which:

- (a) Directly or indirectly fix purchase directly or indirectly fix purchase or selling prices or any other trading conditions;
- (b) limit or control production, markets, technical development, or investment;
- (c) share markets or sources of supply;
- (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
- (e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts

Article 101(1) of the TFEU above provides rulings relating to anti-competitive agreement whereas Article 102 prohibits conducts which amounts to abuse of dominant position. Article 102 of the TFEU provides:

Any abuse by one or more undertakings of a dominant position within the internal market or in a substantial part of it shall be prohibited as incompatible with the internal market in so far as it may affect trade between Member States.

Such abuse may, in particular, consist in:

- (a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions;
- (b) limiting production, markets or technical development to the prejudice of consumers;
- (c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
- (d) making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

In relation to patent license, paragraph 7 of the Guidelines on the Application of Article 101 of the Treaty on the Functioning of the European Union to Technology Transfer Agreements (2014/C 89/03) (the Guideline) expressly provides that although intellectual property law grants exclusive rights of exploitation, it however does not confer immunity on the intellectual property rights from being intervened by the competition law. This indicates that patent license is subject to the scrutiny of competition law although it is not expressly mentioned by the provisions in the TFEU.

### 2.2 Implementation of competition law in patent license

#### 2.2.1 Patent license is granted block exemption

In EU, although no blanket immunity is given by the competition law in the field of intellectual property, yet, patent license

is granted block exemption under the Commission Regulation (EU) No.316/2014 on the Application of Article 101(3) of the Treaty of the Functioning of the European Union to Categories of Technology Transfer Agreement (TTBER). The TTBER has its basis in the Patent Licensing Block Exemption Regulation which was announced in 1984 and was followed suit by Know How BER (556/89) in 1989. These block exemption regulation were then replaced with a single block exemption known as TTBER (240/96). The TTBER (240/96) continues to be revised and update and the current TTBER in force is TTBER (316/2014) and the Guideline.

The TTBER grants automatic group exemption to patent license so that it will not be subject to Article 101(1) of the TFEU. According to Article 2 of the TTBER, Article 101(1) of the TFEU shall not apply to technology transfer agreement. Technology transfer agreement has been defined by Article 1(1)(c) of the TTBER to mean:

- (i) A technology rights licensing agreement entered into between two undertakings for the purpose of the production of contract products by the licensee and/or its subcontractors
- (ii) An assignment of technology rights between two undertakings for the purpose of the production of contract products where part of the risk associated with the exploitation of the technology remains with the assignor.

According to Article 1(1)(b), technology rights refers to the know how and the following rights, or a combination thereof, including applications for or application for registration of those right, which, among others include patents.

The TTBER operates on the presumption that although license agreements are caught by Article 101(1) TFEU, these agreements however fulfill the conditions for exemptions set under Article 101(3) of the TFEU, namely;

- (1) The agreement contributes to improving the production or distribution of goods or to promoting technical or economic progress;
- (2) The agreement allow consumers a fair share of the resulting benefit;
- (3) The agreement does not impose restrictions which are not indispensable to the attainment of the above objectives;
- (4) The agreement does not afford parties to the agreement the possibility of eliminating competition in respect of a substantial part of the products in question.

However, in order for a patent license to shelter under the TTBER, contracting parties are to observe their market shares and to avoid hardcore restrictions in the patent license. The market share limits requirement under the TTBER requires parties to determine their market share limits based on their relationship, i.e whether parties are competitors or non-competitors. The fact that parties exceed the market share limits does not render the agreement to be caught under Article 101(1) of the TFEU (Para 43 of the Guideline). In fact, they will be assessed within the actual context in which competition would occur in the absence of the agreement (Para 11 of the Guideline) and individual assessment will be carried out to determine the anti-competitiveness of the patent license (Para 43 of the Guideline). It is only when parties include hard core restrictions in the patent license that the patent license will be presumed as falling under Article 101(1) of the TFEU (Para 43 of the TFEU).

### 2.2.2 Specific guideline for patent license

In EU, the existence of the TTBER is supplemented with a guideline known as The Guidelines on the application of Article 101 of the Treaty on the Functioning of the European Union to Technology Transfer Agreements (2014/C 89/03) (the Guideline). The Guideline elaborates on matters relating to the application of TTBER to technology transfer agreement and also manner in which technology transfer agreement need to be assessed under Article 101(1) and 101(3) of the TFEU in the event technology transfer agreement falls outside the ambit of the TTBER.

## 3. Malaysian Approach in Implementing Competition Law in Patent License

### 3.1 Basic legislations on competition law

The main legislation in force pertaining to the implementation of competition law in Malaysia is Competition Act 2010. The Competition Act 2010 is a national legislation on competition which came into effect in 2012. In addition to the main legislation, there are certain guidelines which have been issued by the Malaysia Competition Commission (MyCC) for the purpose of assisting in implementing competition law in Malaysia namely, Guidelines on Market Definition, Guidelines on Anti-competitive Agreements, Guidelines on Complaints Procedure, Guidelines on Abuse of Dominant Position, Guidelines on Financial Penalties and Guidelines on Leniency Regime.

The Competition Act 2010 is silent on the application of its provisions to matters relating to intellectual property especially with regards to patent license. Hence, by way of implication, it can be inferred from the following provisions that

patent license is not excluded from the ambit of competition law.

### 3.1.1 Activities of “commercial nature”

According to Section 3 of the Competition Act 2010, the Competition Act 2010 applies to commercial activity conducted inside and outside Malaysia. By virtue of Section 3(4) of the Competition Act 2010, it provides that commercial activity means any activity of a commercial nature but does not include the following:

- (a) Any activity, directly or indirectly in the exercise of governmental authority;
- (b) Any activity conducted based on the principle of solidarity; and
- (c) Any purchase of goods or services not for the purposes of offering goods and services as part of an economic activity.

In relation to patent license, it is an exercise of rights in the field of commercial. Section 37(1) of the Patents Act 1983 provides that exercising exclusive rights under the patent only confine to acts done for the purpose of industrial or commercial. Therefore, patent license is a form of commercial activity being exercised by patent owner in relation to patent owners' exclusive rights.

### 3.1.2 Patent License is a form of ‘agreement’

Section 2 of the Competition Act 2010 provides that the term ‘agreement’ as indicated by the Competition Act 2010 includes the followings:

Any form of contract, arrangement or understanding, whether or not legally enforceable, between enterprises, and includes a decision by an association and concerted practices.

The elaboration on the term ‘agreement’ provided by Section 2 of the Competition Act 2010 concludes that ‘agreement’ may be in the form of formal or informal arrangement between parties regardless of whether such arrangement is made in oral or written.

In Malaysia, patent license is concluded via ‘written contract signed by the parties’ (Section 41(2) of the Patents Act 1983). Thus, patent license comes within the ambit of ‘agreement’ as mentioned by Section 2 of the Competition Act 2010.

### 3.1.3 Exclusion under Competition Act 2010

In order to identify matters which are excluded from the application of the Competition Act 2010, Section 3 (3) of the Competition Act 2010 identifies commercial activities which are not govern by the Competition Act 2010.

According to Section 3(3) of the Competition Act 2010, the commercial activity regulated by the communication and energy sectors listed in First Schedule of the Competition Act 2010, namely, Communications and Multimedia Act 1998 (Act 588) and Energy Commission Act 2001 (Act 610) are under the supervision of their respective legislations. Effective from 1<sup>st</sup> January 2014, the Federal Government gazetted Petroleum Development Act 1974 (Act 144) and the Petroleum Regulations 1974 (PU (A) 432/1974) to be added in the list of First Schedule of the Competition Act 2010.

In addition to the excluded commercial sectors provided under the First Schedule of the Competition Act 2010, the Competition Act 2010 also provides other exclusion under its Chapter 4 via Section 13 of the Competition Act 2010. According to Section 13 of the Competition Act 2010, it provides that prohibitions mentioned in Part II of the Competition Act 2010 shall not apply to matters provided in the Second Schedule of the Competition Act 2010. This indicates that anti-competitive practices, which comprises of anti-competitive agreements and abuse of dominant position will not apply in the following situation:

- (a) An agreement or conduct to the extent to which it is engaged in an order to comply with a legislative requirement;
- (b) Collective bargaining activities or collective agreements in respect of employment terms and conditions and which are negotiated or concluded between parties which include both employersd and employees or organizations established to represent the interests of employers or employees;
- (c) An enterprise entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly in so far as the prohibition under Chapter 1 and Chapter 2 of Part II would obstruct the performance, in law or in fact of the particular tasks assigned to that enterprise.

None of the above provisions expressly indicates that patent license is an excluded subject matter under the Competition Act 2010. Thus, it signals that patent license is within the regulatory regime of the Competition Act 2010.

## 3.2 Implementation of competition law in patent license

### 3.2.1 Patent license is subject to common rules to be applied to other kinds of agreement

Patent license is expected to avoid from contravening the prohibitions set by the competition law under the Competition Act 2010 which are participating in anti-competitive agreement under Section 4 and abuse of dominant position under Section 10 of the Competition Act 2010. According to Section 4(1) of the Competition Act 2010 which provides for anti-competitive agreement, it states that:

*A horizontal or vertical agreement between enterprises is prohibited insofar as the agreement has the object or effect of significantly preventing, restricting or distorting competition in any market for goods or services.*

The explanation regarding the application of Section 4 of the Competition Act 2010 is assisted by the Guideline on Anti-Competitive Agreement which provides clarification on the terms used in the Competition Act 2010 relating to anti-competitive agreement, characteristics of prohibited horizontal and vertical agreements, other kinds of agreements which subject to the ruling of anti-competitive agreement, exemptions from anti-competitive agreement, notifications for guidance and non-application and exclusions under the Competition Act 2010.

By virtue of paragraph 4 of the Guideline on Anti Competitive Agreement, the Malaysian Competition authority endeavor to issue a separate guideline applicable to matters relating to intellectual property and franchise agreement (Para 4 of the Guidelines on Anti Competitive Agreement). Hence, for the time being, the existing Guideline on Anti-Competitive Agreement applies to patent license.

Parties to patent license agreement are also expected not to abuse their dominant position as they can be caught under Section 10(1) Competition Act 2010. According to Section 10(1) of the Competition Act 2010, it provides:

An enterprise is prohibited from engaging whether independently or collectively, in any conduct which amounts to an abuse of a dominant position in any market for goods or services.

Lists of situation which may amount to abuse of dominant position are provided under Section 10(2) of the Competition Act 2010 which are :

- (a) directly or indirectly imposing unfair purchase or selling price or other unfair trading condition on any supplier or customer;
- (b) limiting or controlling production, market outlets or market access, technical or technological development or investment to the prejudice of consumers;
- (c) refusing to supply to a particular enterprise or group or category of enterprises;
- (d) applying different conditions to equivalent transactions with other trading parties;
- (e) making the conclusion of contract subject to acceptance by other parties of supplementary conditions which by their nature or according to commercial usage have no connection with the subject matter of the contract;
- (f) any predatory behaviour towards competitors; or
- (g) buying up a scarce supply of intermediate goods or resources required by a competitor, in circumstances where the enterprise in a dominant position does not have a reasonable commercial justification for buying up the intermediate goods or resources to meet its own needs.

In this case, implementation of Section 10 of the Competition Act 2010 relating to abuse of dominant position in patent license area is assisted by the Guidelines on Abuse of Dominant Position and Guidelines on Market Definition. Manners in which dominant position are established is elaborated by the Guidelines on Abuse of Dominant Position which in most circumstances are indicated by the market shares of an enterprise. As in the case for Guidelines on Anti-Competitive Agreement, Guidelines on Abuse of Dominant Position and Guidelines on Market Definition also provides general rulings which applies to all types of arrangement even though empirical assessment is needed for market power associated with intellectual property (Anderman & Schmidt, 2011).

### 3.2.2 Patent license is subject to individual assessment prior to obtaining exemptions under the Competition Act 2010

Although licensing activities are mostly pro-competitive since it is able to create competition on the downstream market (Peeperkorn, 2003) yet, patent license in Malaysia is still subject to the requirements under Section 5 of the Competition Act 2010 to determine whether such patent license is pro-competitive. The patent license is required to fulfill the four cumulative requirements which are as follows:

- (a) significant identifiable technological, efficiency or social benefits directly arising from the agreement is present;

- (b) without the agreement having the effect of preventing, restricting or distorting competition, the benefits could not have been reasonably provided by the parties to the agreement;
- (c) the detrimental effect of the agreement on competition is in proportion to the benefits granted; and
- (d) the agreement does not permit the enterprise involved to remove competition completely regarding a substantial part of the goods or services.

Hence, patent license is expected to demonstrate that it possesses the above requirements prior to obtaining exemptions from Section 4 of the Competition Act 2010.

## 4. Findings and Discussion

### 4.1 Comparative approach between EU and Malaysia on the implementation of competition law in patent license

The above discussion indicated that EU and Malaysia do not exclude the application of competition law in patent license. EU is aware that patent license comes under the umbrella of competition law in the event that patent license is used as a tool to hinder competition in the market while in Malaysia, patent license is not listed as one of the excluded subject matter in the Competition Act 2010.

Although both jurisdictions demonstrate that competition law applies to patent license, yet EU and Malaysia differs in the manner in which competition law is implemented in patent licence. EU presumed that technology transfer agreements provides economic efficiencies and therefore granted block exemption (Para 41 of the Guideline). It is until and unless such patent license includes hardcore provisions that it is presumed to be infringing Article 101(1) of the TFEU (Para 43 of the Guideline).

In Malaysia, on the other hand, there is no presumption that patent license is pro-competitive. In fact, there is absent of recognition of the pro-competitive effect of patent license under the Malaysian Competition Act 2010 as well as the guidelines. Hence, patent license in Malaysia is subject to individual assessment, which implies that in case of anti-competitive agreement, the patent license needs to be assessed individually based on Section 4 and Section 5 of the Competition Act 2010. For that purpose, general guidelines applicable to all kinds of agreements are used to cater the needs to assess patent license under Section 4 and Section 5 of the Competition Act 2010. These Guidelines provides general application of the competition law to all kinds of agreements.

### 4.2 Options and recommendations for Malaysia

The comparative approach between EU and Malaysia has led to the following recommendations, namely to grant block exemption to patent license in Malaysia and to introduce a specific guidelines to be applied to matters relating to patent license. Patent license deserves to be ruled under a specific guideline since varieties of provisions in the patent license are complex in nature (Nielsen, 2011). In fact, it has been expressly indicated by the Malaysian competition authority under paragraph 4 of the Guidelines on Anti Competitive Agreement that there will be a specific guideline to be used for matters relating to intellectual property (Para 4 of the Guidelines on Anti-Competitive Agreement) but such guideline is yet to materialised.

## 5. Concluding Remarks

The discussion above has set forth the path for implementing competition law in patent license for Malaysia. The EU experienced in this matter has no doubt provides clear indication that implementing competition law in patent license requires additional legal mechanisms apart from the existing legislations. According to Maskusand Lahouel, there is urgent need to develop procedures to ensure that there is no delay on the implementation of competition law in the field of intellectual property (Maskus & Lahouel, 2000). Perhaps, it is high time for Malaysia to consider practices exercised by other jurisdictions relating to the implementation of competition law in the field of patent license.

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