Competition Bureau Canada
Bureau de la concurrence Canada

Enforcement Guidelines

Intellectual Property

Canada

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PREFACE

The Competition Bureau (the “Bureau”), as an independent law enforcement agency, ensures that Canadian businesses and consumers prosper in a competitive and innovative marketplace. The Bureau investigates anti-competitive practices and promotes compliance with the laws under its jurisdiction, namely the *Competition Act* (the “Act”), the *Consumer Packaging and Labelling Act* (except as it relates to food), the *Textile Labelling Act* and the *Precious Metals Marking Act*.

The Bureau endeavours to be as transparent as possible in providing information to Canadians on the application of the laws under its jurisdiction. One of the ways it does so is by issuing enforcement guidelines, which describe the Bureau’s general approach to enforcing specific provisions in the Act.

Intellectual property (“IP”) and IP rights are increasingly important in today's knowledge-based economy. In such an environment, there has been interest in how the Bureau will deal with competition issues involving IP. Accordingly, the Bureau has made it a priority to provide increased clarity on this subject.

These *Intellectual Property Enforcement Guidelines* (the “Guidelines”) articulate how the Bureau approaches the interface between competition policy and IP rights. They describe how the Bureau will determine whether conduct involving IP raises an issue under the Act. They also explain how the Bureau distinguishes between those circumstances that warrant a referral to the Attorney General under section 32 of the Act, and those that will be examined under the general provisions. Because of their subject matter, the Guidelines are necessarily technical in nature and are primarily targeted to IP and competition law practitioners.

These Guidelines are not intended to restate the law or to constitute a binding statement of how the Commissioner will exercise discretion in a particular situation. The enforcement decisions of the Commissioner and the ultimate resolution of issues will depend on the particular circumstances of each case. Final determination of the law is the responsibility of the Competition Tribunal (the “Tribunal”) and the courts.

The Bureau will review these Guidelines annually and will revise them as needed in light of experience, changing circumstances and decisions of the Tribunal and the courts.

John Pecman
Commissioner of Competition

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1. Introduction

Today's economy is increasingly based on knowledge and innovation and driven by rapid advancements in information and communications technologies. New technologies create economic, cultural, social and educational opportunities for people to put ideas to work in innovative ways that increase productivity and create employment and wealth. Adequate protection of IP plays an important role in stimulating new technology development, artistic expression and knowledge dissemination, all of which are vital to the knowledge-based economy.[1] In this context, IP becomes a valuable asset for firms' profitability and growth. However, given the importance of IP, there is a risk that it may be used strategically to engage in anti-competitive conduct.

Owners of IP, like owners of any other type of private property, profit from property laws that define and protect owners' rights to exclude others from using their private property. The special characteristics of IP have made it necessary in many instances for governments to develop laws that confer property rights to IP comparable to those for other kinds of private property.

IP laws and competition laws are two complementary instruments of government policy that promote an efficient economy. IP laws provide incentives for innovation and technological diffusion by establishing enforceable property rights for the creators of new and useful products, technologies and original works of expression. Competition laws may be invoked to protect these same incentives from anti-competitive conduct that creates, enhances or maintains market power or otherwise harms vigorous rivalry among firms. Given that competition law may result in limitations on the terms and conditions under which the owners of IP rights may transfer or license the use of such rights to others, and on the identity of those to whom the IP is transferred or licensed, these Guidelines seek to clarify the circumstances under which the Bureau would consider such intervention to be appropriate and also illustrate situations that would not call for intervention under the Act.

In the interest of transparency, the Bureau recognizes the importance of providing information on its treatment of IP under the Act. This document sets out how the Bureau views the interface between IP law and competition law. It also explains the analytical framework that the Bureau uses to assess conduct involving IP.

[1] The World Intellectual Property Organization ("WIPO") defines IP and summarizes the role of IP rights as follows: "Intellectual property (IP) refers to creations of the mind, such as inventions; literary and artistic works; designs; and symbols, names and images used in commerce. IP is protected in law by, for example, patents, copyright and trademarks, which enable people to earn recognition or financial benefit from what they invent or create. By striking the right balance between the interests of innovators and the wider public interest, the IP system aims to foster an environment in which creativity and innovation can flourish." For more information, see the WIPO website: http://www.wipo.int/about-ip/en/.

The Guidelines discuss the circumstances in which the Bureau, under the Act, would seek to restrain anti-competitive conduct associated with the exercise of IP rights to maintain competitive markets. The approach elaborated in this document is based on the premise that the Act generally applies to conduct involving IP as it applies to conduct involving other forms of property.

The Bureau's overall approach to the application of the Act to IP is as follows:

- The circumstances in which the Bureau may apply the Act to conduct involving IP or IP rights fall into two broad categories: those involving something more than the mere exercise of the IP right, and those involving the mere exercise of the IP right and nothing else. The Bureau will use the general provisions of the Act to address the former circumstances and section 32 (special remedies) to address the latter.

- In either case, the Bureau does not presume that the conduct violates the general provisions of the Act or needs to be remedied under section 32.

- When conduct involving an IP right warrants a special remedy under section 32, the Bureau will act only in the very rare circumstances described in this document and when the conduct cannot be remedied by the relevant IP statute.

- The analytical framework that the Bureau uses to determine the presence of anti-competitive effects stemming from the exercise of rights to non-IP forms of property is sufficiently flexible to apply to conduct involving IP, even though IP has important characteristics that distinguish it from other forms of property.

Circumstances will determine how the Bureau uses its enforcement discretion to respond to any alleged contravention of the Act. Therefore, individuals contemplating a business arrangement involving IP should either consult qualified legal counsel or contact the Bureau when evaluating the risk of the arrangement contravening the Act. The final interpretation of the law rests with the Tribunal and the courts.

When developing these Guidelines, the Bureau considered the current global economic and technological environment and, in particular, the rapid rate of technological changes occurring in many industries. The Bureau also took into account its past enforcement experience, Canadian case law, and guidance documents released in other jurisdictions such as the United States and the European Union. The Bureau recognizes that the interface between competition and IP policy is constantly evolving and that a single enforcement approach may not be appropriate for all jurisdictions. Accordingly, to ensure appropriate coordination between Canadian IP and competition law and policy, the Bureau entered into a Memorandum of Understanding with the Canadian Intellectual

Property Office that will serve to identify areas of mutual interest and facilitate discussions between the two agencies.

The remainder of this document is organized into six parts:

- Part 2 discusses the purpose of IP laws, lists the various statutes that deal with IP, reviews the purpose of competition law and lists the principal provisions of the Act that relate to IP;
- Part 3 discusses the interface between IP law and competition law;
- Part 4 outlines the principles underlying the application of the general provisions and section 32 of the Act to business conduct involving IP;
- Part 5 describes the Bureau's analytical framework, which is sensitive to the particular characteristics of IP;
- Part 6 discusses the Bureau's mandate to promote competition, which may include intervening in proceedings in which IP rights are being defined, strengthened or extended inappropriately; and
- Part 7 presents a discussion and a series of hypothetical scenarios to illustrate how the Bureau would apply the Act to a wide variety of business conduct involving IP, including price-fixing; exclusive licensing; contracting; patent pooling; competitor collaborations; refusals to license; product switching and the settlement of patent litigation proceedings in the pharmaceutical industry; the sending of false and misleading claims; and certain forms of conduct in the context of standards development organizations.

2. Overview of IP Law and Competition Law

2.1 IP Law

IP laws create legally enforceable private rights that protect to varying degrees the form and/or content of information, expression and ideas. The primary purpose of these laws is to promote innovation and creativity by defining the scope of these rights and determining under what circumstances they have been infringed or violated. While the nature and scope of protection provided by each IP-related statute is different, by protecting exclusive rights, the IP laws provide an incentive to pursue scientific, artistic and business endeavours that might not otherwise be pursued.[2]

[2] It is important to note that in the context of patents, in addition to the granting of exclusive rights, the requirement of the inventor to provide and make public, a full description of the invention also plays an important role in stimulating innovation by allowing others to benefit from advances in technology and knowledge.

In the Guidelines, IP rights include rights granted under the *Patent Act*, the *Trade-marks Act*,[3] the *Copyright Act*, the *Industrial Design Act*, the *Integrated Circuit Topography Act* and the *Plant Breeders' Rights Act*. The Canadian Intellectual Property Office ("CIPO") grants or registers ownership for five types of IP: patents, trademarks, copyrights, industrial designs and integrated circuit topographies. The term "IP rights" also encompasses the protection afforded IP at common law and the *Civil Code of Quebec*, including that given to trade secrets and unregistered trademarks.

Patents

Patents cover new inventions (process, machine, manufacture, composition of matter) or new and useful improvements to an existing invention. A patent grants an inventor the right to exclude others from making, using or selling the invention within Canada for 20 years from the date of filing the application. The patent application, which includes a full description of the invention, is available to the public 18 months after filing.

Trademarks

Trademarks are words, sounds or designs (or a combination of these) used to distinguish the goods or services of one person or organization from those of others in the marketplace. Registration protects the trademark from misuse and gives the owner exclusive rights to use it, in association with the goods and/or services for which the mark is registered, throughout Canada for renewable 15 year periods.

Copyright

Copyright is the sole right to produce, reproduce, publish or perform an original literary, artistic, dramatic or musical work (including computer programs) for a limited term. Copyright also applies to performances, sound recordings and communication signals. Generally, copyright lasts for the life of the author, the remainder of the calendar year in which the author dies, and for 50 years following the end of that calendar year.

Industrial Designs

An industrial design consists of the visual features of a shape, configuration, pattern or ornament, or any combination of these features, applied to a finished article. An industrial design must have features that appeal to the eye. To be eligible for registration, the design must be original. Registration provides exclusive, legally enforceable rights for up to 10 years in Canada.

[3] Although the same general competition law principles apply to trademarks as to other forms of IP, the Guidelines are generally concerned with technology transfer and innovation-related issues. Consequently, when applying its enforcement approach to trademarks, the Bureau will additionally consider in its analysis the source and quality differentiation issues that arise in respect of trademarks.

Integrated Circuit Topographies

Integrated circuit topography refers to the three-dimensional configuration of electronic circuits embodied in integrated circuit products or layout designs. Registration offers exclusive rights for up to 10 years on an original circuit design, and protection can extend to the layout design as well as to the finished product.

Plant Breeders' Rights

The Canadian Food Inspection Agency administers the *Plant Breeders' Rights Act,* which grants the owner of a new plant variety the exclusive rights to produce for sale, and to sell, reproductive material of the variety. It provides legal protection for up to 25 years for a variety of tree or vine (including their rootstocks) and 20 years for all other plant varieties.

It is important to note that some remedies are available under the IP-related statutes to protect against abuses. For example, as stipulated in section 65 of the *Patent Act*, commencing three years after the grant of a patent, a party may apply to the Commissioner of Patents alleging abuse of the patent through unduly restrictive licensing conditions. If the Commissioner of Patents is satisfied that there has been abusive conduct, there are a number of actions he/she may take, including ordering that the patent be revoked or licensed to the applicant on such terms as the Commissioner of Patents may think expedient.

2.2 Competition Law

The principle underlying competition law is that the public interest is best served by competitive markets, which are socially desirable because they lead to an efficient allocation of resources. Competition law seeks to prevent companies from inappropriately creating, enhancing or maintaining market power that undermines competition without offering offsetting economic benefits.[4] Market power refers to the ability of firms to profitably cause one or more facets of competition, such as price, output, quality, variety, service, advertising or innovation, to significantly deviate from competitive levels for a sustainable period of time.[5] However, a firm would not contravene the Act if it attains its market power solely by possessing a superior product or process, by introducing an innovative business practice or by other reasons of exceptional performance.[6]

The provisions of the Act that set out when it may be necessary for the Bureau to intervene in business conduct, including conduct involving IP, fall into two categories: those that cover criminal offences and those that cover reviewable

[4] For certain types of conduct, such as price-fixing conspiracies, the creation of market power and the harm to competition is presumed from the conduct.
[5] *R. v. Nova Scotia Pharmaceutical Society,* [1992] 2 S.C.R. 606, defines market power as "the ability to behave relatively independently of the market." *Canada (Director of Investigation and Research) v. The NutraSweet Co.* (1990), 32 C.P.R. (3d) 1 (Comp. Trib.), defines it as the ability to maintain prices above competitive levels for a considerable period.
[6] In the abuse of dominance provision of the Act, subsection 79(4) provides that superior competitive performance is a consideration in determining whether a practice has an anti-competitive effect in a market.

matters. Several reviewable matters provisions state that the Bureau must, before it intervenes, show that the conduct substantially lessens or prevents competition.[7]

Criminal offences include conspiracy (section 45), bid-rigging (section 47), and some forms of misleading advertising and related deceptive marketing practices (sections 52 to 55). These provisions do not require proof of market power or anti-competitive effects. Some of them (sections 45, 47, 52 and 52.01) have a *mens rea* component; that is, proof is required that the defendant had the required intent to engage in the criminal conduct.

The provisions on reviewable matters deal with conduct that is generally pro-competitive but that may, in certain circumstances, significantly constrain competition. Reviewable matters include misleading advertising and related deceptive marketing practices (sections 74.01 through 74.06), refusal to deal (section 75), price maintenance (section 76), exclusive dealing, tied selling and market restriction (section 77), abuse of a dominant position (section 79), anti-competitive agreements or arrangements between competitors (other than “hard core” cartels) (section 90.1), and mergers (section 92).[8]

When a court determines that a firm has contravened the criminal provisions of the Act, it can impose fines, imprisonment and prohibition orders.[9] In addition, parties may bring private actions seeking damages.[10] With respect to reviewable matters, the Tribunal may issue a variety of remedial orders, some of which restrict private property rights. For example, the Tribunal has, in the past, ordered merging firms to divest themselves of assets, including IP, when it concluded that the proposed merger was likely to substantially lessen or prevent competition, thereby overriding the rights of property owners to acquire or dispose of their private property.[11] Similarly, remedies under the abuse of dominant position provision have involved orders affecting IP.[12]

Section 32, which is in the special remedies part of the Act, gives the Federal Court the power, on application by the Attorney General, to make remedial orders if it finds that a company has used the exclusive rights and privileges conferred by a patent, trademark, copyright or registered integrated circuit

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[7] The refusal to deal provision (section 75) and the price maintenance provision (section 76) require proof that the refusal is having or is likely to have an adverse effect on competition in a market. Section 75 also requires that the person's inability to obtain adequate supply is the result of insufficient competition among suppliers. The deceptive marketing practices provisions (sections 74.01 through 74.06) do not include a competitive effects requirement.

[8] Section 103.1 of the Act allows parties to apply to the Tribunal for leave to make an application under section 75, 76 or 77.

[9] See the Bureau’s *Competition and Compliance Framework Bulletin*, November 10, 2015, for a detailed discussion of case resolution alternatives.

[10] See section 36 of the Act.

[11] See *Canada (Director of Investigation and Research) v. Southam Inc.* (1992), 47 C.P.R. (3d) 240 (Comp. Trib.), rev’d (1995), 63 C.P.R. (3d) 67 (F.C.A), rev’d (1997), 71 C.P.R. (3d) 417 (S.C.C.).

[12] See *Canada (Director of Investigation and Research) v. D&B Companies of Canada Ltd*. (1995), 64 C.P.R. (3d) 216 (Comp. Trib.) (hereinafter *Nielsen*).

topography to unduly restrain trade or lessen competition (see subsection 4.2 of these Guidelines for circumstances in which the Bureau may seek to have the Attorney General bring an application under section 32).

When the Federal Court determines that a special remedy is warranted under section 32, it may issue a remedial order declaring any agreement or licence relating to the anti-competitive use void, requiring the licensing of the IP right (except in the case of trademarks), revoking the IP right or directing that other things be done to prevent anti-competitive use. This provision provides the Attorney General with the statutory authority to intervene in a broad range of circumstances to remedy an undue lessening or prevention of competition involving the exercise of statutory IP rights. In practice, the Attorney General likely would seek a remedial order under the Act only on the recommendation of the Commissioner.

3. Interface between IP and Competition Law

3.1 Property Rights

Private property rights are the foundation of a market economy. Property owners must be allowed to profit from the creation and use of their property by claiming the rewards flowing from it. In a market system, this is accomplished by granting owners the right to exclude others from using their property, and forcing those wishing to use it to negotiate or bargain in the marketplace for it, thereby rewarding the owner. This creates incentives to invest in developing, and leads to the exchange of, private property, thus contributing to the efficient operation of markets.

3.2 IP Law

IP has unique characteristics that make it difficult for owners to physically restrict access to it and, therefore, exercise their rights over it. The owner of physical property can protect against its unauthorized use by taking appropriate security measures, such as locking it away, but it is difficult, if not impossible, for the creator of a work of art or an invention to prevent his or her property from being copied once it has been shown or distributed. This is exacerbated because IP, while often expensive to develop, is often easy and inexpensive to copy. IP is also typically non-rivalrous – that is, two or more people can simultaneously use IP. The fact that a firm is using a novel production process does not prevent another firm from simultaneously using the same process. In contrast, the use of a physical property by one firm prevents concurrent use by another.[13]

[13] To enforce common law property rights, it must be possible to identify the property's owner and to clearly delineate the boundaries of the property. Both tasks can prove problematic in the case of IP. For other kinds of private property, possession can generally be seen as an indication of ownership. However, since many individuals can possess IP simultaneously, it may be difficult to establish the identity of the original creator and true owner of the IP. Furthermore, since IP is generally intangible, it is often difficult to clearly delineate the boundaries of the property. Without a legal delineation of these boundaries, IP owners may have difficulty showing that others have infringed their property.

Accordingly, IP laws confer on an IP owner the right to unilaterally exclude others from using that property. While each IP-related statute grants this right to varying degrees, and the right may be subject to limitations that vary across statutes, all of the statutes position the owners of the IP to maximize the IP's value through trade and exchange in the marketplace. This claim on the rewards flowing from IP enhances the incentive for investment and future innovation in IP, just as it does for other forms of private property. With the exception of the protections afforded unregistered trademarks and other common law rights, the legal protection of IP is a function of, and does not exist outside the scope of, IP statutory regimes.

3.3 Competition Law

Since the right to exclude, which is the basis of private property rights, is necessary for efficient, competitive markets, the enforcement of the Act rarely interferes with the exercise of this basic right. Enforcement action under the Act nonetheless may be warranted when there are conspiracies, agreements or arrangements among competitors or potential competitors; when anti-competitive conduct creates, enhances or maintains market power;[14] or when firms use deceptive marketing practices.

3.4 Interface

IP and competition laws are both necessary for the efficient operation of the marketplace. IP laws provide property rights comparable to those for other kinds of private property, thereby providing incentives for owners to invest in creating and developing IP and encouraging the efficient use and dissemination of the property within the marketplace. Applying the Act to conduct associated with IP may prevent anti-competitive conduct that impedes the efficient production and diffusion of goods and technologies and the creation of new products. The promotion of a competitive marketplace through the application of competition laws is consistent with the objectives underlying IP laws.

4. Applying the Act to Conduct Involving IP

4.1 Overview of Competition Harm Analysis

In general, the Bureau's analysis for determining whether competitive harm would result[15] from a particular type of business conduct comprises five steps:

- Identifying the conduct;[16]
- Defining the relevant market(s);[17]

[14] An example of conduct involving IP that could create market power is the assignment of patents. See *Apotex Inc. v. Eli Lilly and Co.,* [2005] F.C.J. No. 1818 (F. C.A.).
[15] For ease of discussion, unless otherwise indicated, the Guidelines focus on prospective competitive harm. Note, however, that in many cases, competitive harm may be occurring at the time the Bureau is conducting an investigation or may have occurred at some point in the past.
[16] Some examples of conduct that could involve IP include mergers, pooling of licences, setting standards for products, tied selling and exclusive dealing.

- Determining if the firm or firms under scrutiny possess market power[18] by examining the level of concentration and entry conditions in the relevant market(s), as well as other factors;

- Determining if the conduct would substantially lessen or prevent competition in the relevant market(s); and

- Considering, when appropriate, any relevant efficiency rationales or valid business justifications.

This analysis applies to all industries and all types of business conduct, and is sufficiently flexible to accommodate differences among the many forms of IP protection, as well as between IP and other types of property. For example, the Bureau takes differences among the various forms of IP protection into account when defining the relevant market and determining whether a firm has market power. In addition, although IP rights to a particular product or process are often created and protected by statute and are thus different from other forms of property rights, the right to exclude others from using the product or process does not necessarily grant the owner market power. After it has defined the relevant market and examined factors, such as concentration, entry barriers and technological change, the Bureau can determine whether an owner of a valid IP right possesses market power. The existence of a variety of effective substitutes for the IP and/or a high probability of entry by other players into the market (by "innovating around" or "leap-frogging over" any apparently entrenched position) would likely cause the Bureau to conclude that the IP has not conferred market power on its owner.

While the criminal offence provisions of the Act do not require a finding of market power, under many reviewable matters provisions an order can only be made if a firm has engaged in anti-competitive conduct that creates, enhances or maintains market power. Again, consistent with its approach with respect to all forms of property, the Bureau does not consider an owner of IP to have contravened the Act if it attained market power solely by possessing a superior-quality product or process, introducing an innovative business practice or otherwise through exceptional performance.

Licensing is the usual method by which the owner of IP authorizes others to use it. In the vast majority of cases, licensing is pro-competitive because it facilitates the broader use of a valuable IP right by additional parties.[19] In assessing

[17] Defining relevant markets is a widely used and accepted tool for assessing competitive effects. While the Bureau seeks to define relevant markets as part of its analysis in most investigations, relevant market definition is not necessarily an initial step in the Bureau's analysis, and it may not be a required step in certain cases.
[18] Matters pursued under the criminal provisions or the deceptive marketing practices provisions do not require a finding of market power or an identification of competitive effects.
[19] Licensing is a means by which owners trade IP, and it signals the willingness of IP holders to participate in the marketplace. This ability of owners to exchange and transfer IP can enhance the IP's value and increase

whether a particular licensing arrangement raises a competition issue, the Bureau examines whether the terms of the licence serve to create, enhance or maintain the market power of either the licensor or the licensee.[20] The Bureau will not consider licensing agreements involving IP to be anti-competitive unless they reduce competition substantially relative to that which would have likely existed in the absence of the licence's potentially anti-competitive terms.

4.2 Enforcement Principles

Specific reference is made to IP rights in a number of provisions of the Act.[21] The circumstances in which the Bureau may apply the Act to anti-competitive conduct involving IP or IP rights fall into two broad categories: those involving anti-competitive conduct that is something more than the mere exercise of the IP right, and those involving the mere exercise of the IP right and nothing else. The general provisions of the Act address the former, while section 32 (special remedies) addresses the latter. The Bureau's approach is consistent with subsection 79(5), which acknowledges that the mere exercise of an IP right is not an anti-competitive act for the purposes of the abuse of dominance provision,[22] while acknowledging the possibility that under the very rare circumstances set out in section 32, the mere exercise of an IP right might raise a competition issue.[23]

4.2.1 General Provisions

The mere exercise of an IP right is not cause for concern under the general provisions of the Act. The Bureau defines the mere exercise of an IP right as the exercise of the owner's right to unilaterally exclude others from using the IP. The Bureau views an IP owner's use or non-use of the IP also as being the mere exercise of an IP right.[24]

Unilaterally exercising the IP right to exclude does not violate the general provisions of the Act no matter to what degree competition is affected. To hold otherwise could effectively nullify IP rights, impair or remove the economic, cultural, social and educational benefits created by them, and be inconsistent with the Bureau's underlying view that IP and competition law are generally complementary.

The Bureau applies the general provisions of the Act when IP rights form the basis of agreements or arrangements between independent entities, whether in

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the incentive for its creation and use. Licensing arrangements also promote the efficient use of IP by facilitating its integration with other components of production, such as manufacturing and distribution.

[20] This is the case when the Bureau is assessing a licensing arrangement outside the criminal provisions.

[21] Refer to sections 32, 76, 77, 79 and 86.

[22] Subsection 79(5) reads: "For the purpose of this section, an act engaged in pursuant only to the exercise of any right or enjoyment of any interest derived under the *Copyright Act*, *Industrial Design Act*, *Integrated Circuit Topography Act*, *Patent Act*, *Trade-marks Act* or any other Act of Parliament pertaining to intellectual or industrial property is not an anti-competitive act."

[23] The remedies in section 32 are more extensive than those under the general provisions.

[24] However, as noted in Example 9A, there may be limited circumstances where non-use of an IP right may be seen as something more that the "mere exercise" of an IP right, and therefore could potentially raise issues under the general provisions of the Act.

the form of a transfer, licensing arrangement or agreement to use or enforce IP rights, and when the alleged competitive harm stems from such an agreement or arrangement and not just from the mere exercise of the IP right and nothing else.

Applying the Act in this way may limit to whom and how the IP owner may license, transfer or sell the IP, but it does not challenge the fundamental right of the IP holder to do so. If an IP owner licenses, transfers or sells the IP to a firm or a group of firms that would have been actual or potential competitors without the arrangement, and if this arrangement creates, enhances or maintains market power, the Bureau may seek to challenge the arrangement under the appropriate section of the Act.[25] Part 7 of this document provides a series of hypothetical examples to illustrate how the Bureau would examine the licensing, transfer or sale of IP under the Act.

This approach is consistent with the Tribunal's decisions in both *Tele-Direct,*[26] and *Warner,*[27] in which the Tribunal held that the mere exercise of the IP right to refuse to license to a complainant did not contravene the general provisions of the Act.[28] In its decision in *Tele-Direct*, the Tribunal indicated that competitive harm must stem from something more than just the mere refusal to license.[29]

Underlying this enforcement approach is the view that market conditions and the differential advantages IP provides should largely determine commercial rewards flowing from the exploitation of an IP right in the market to which it relates. If a company uses IP protection to engage in conduct that creates, enhances or maintains market power as proscribed by the Act, then the Bureau may intervene.

When joint conduct of two or more firms lessens or prevents competition, the competitive harm generally flows from something more than the mere exercise of the IP right to refuse. To the extent that conduct, such as joint abuse of dominance or mergers, restricts competition among firms, the presence of IP should not be a mitigating factor. Similarly, the presence of IP should not be an exception or mitigating factor in matters involving criminal conduct, such as

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[25] This analysis would use the concept of a relevant market as discussed in section 5.1. For an example where an assignment of patent rights may create market power, see *Apotex Inc. v. Eli Lilly and Co.*, *supra* note 14.

[26] *Canada (Director of Investigation and Research) v. Tele-Direct (Publications) Inc. and Tele-Direct (Services) Inc.* (1997), 73 C.P.R. (3d) 1 (Comp. Trib.) (hereinafter *Tele-Direct*).

[27] *Canada (Director of Investigation and Research) v. Warner Music Canada Ltd*. (1997), 78 C.P.R. (3d) 321 (Comp. Trib.).

[28] It may be possible to review certain refusals to license under the Act’s price maintenance provision (section 76). See *Stargrove Entertainment Inc. v. Universal Music Publishing Group Canada et al.* (2015), CT-2015-009 (Comp. Trib.), where the Tribunal granted leave to an applicant to make an application under section 76 in respect of an alleged discriminatory refusal to license IP rights.

[29] In *Tele-Direct*, *supra* note 26, the Tribunal stated that, "[it] is in agreement with the Director that there may be instances where a trademark may be misused. However in the Tribunal's view, something more than the mere exercise of statutory rights, even if exclusionary in effect, must be present before there can be a finding of misuse of a trademark."

conspiracy[30] or bid-rigging. All these types of conduct involving IP could be subject to review under the appropriate general provision of the Act.

A transfer of IP rights that lessens or prevents competition is a further example of a situation in which competitive harm results from something more than the mere exercise of the IP right to exclude. Two examples of this are when a licensor ties a non-proprietary product to a product covered by its IP right, and when a firm effectively extends its market power beyond the term of its patent through an exclusive contract. In either case, if the conduct leads to the creation, enhancement or maintenance of market power so as to substantially lessen or prevent competition, the Bureau may intervene.

Sometimes upon examination, what appears to be just a refusal to license or to grant others access to a firm's IP rights turns out to have included conduct that goes beyond such a refusal. Conduct that goes beyond the unilateral refusal to grant access to the IP could warrant enforcement action under the general provisions of the Act. For instance, if a firm acquires market power by systematically purchasing a controlling collection of IP rights and then refuses to license the rights to others, and it substantially lessens or prevents competition in markets associated with the IP rights, the Bureau could view the acquisition of such rights as anti-competitive. If the conduct met the definition of a merger as specified in section 91 of the Act, the Bureau would review the acquisitions under the merger provisions. If the conduct did not meet the definition of a merger, the Bureau would review the matter under either section 79 (abuse of dominance) or section 90.1 (agreements between competitors) of the Act.[31] Without the acquisitions, the owner's mere refusal to license the IP rights would have been unlikely to cause concern.

4.2.2 Matters Outside the General Provisions – Section 32[32]

Only section 32, in the special remedies part of the Act, contemplates the possibility that the mere exercise of an IP right may cause concern and result in the Bureau seeking to have the Attorney General bring an application for a special remedy to the Federal Court. Section 32 has rarely been used.[33]

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[30] The *Copyright Act* provides that section 45 of the Act does not apply to any royalties or related terms and conditions arising under certain collective society agreements filed with the Copyright Board.

[31] The Tribunal recognized in *Canada (Director of Investigation and Research) v. Laidlaw Waste Systems Ltd.* (1992), 40 C.P.R. (3d) 289 (Comp. Trib.) (hereinafter *Laidlaw*), that the abuse of dominance provision could apply to situations involving a series of acquisitions.

[32] The special remedies provided for under section 32 include declaring any agreement or licence relating to the challenged right void, ordering licensing of the right (except in the case of trademarks), revoking a patent, expunging or amending a trademark, or directing that other such acts be done or omitted as deemed necessary to prevent the challenged use.

[33] Informations have only been laid in two cases under section 32 and in both cases the disputes were settled before proceeding to full hearings. See *R. v. Union Carbide of Canada Limited*, December 9, 1969 and *R. v. Union Carbide of Canada Limited*, June 19, 1971. Since these two cases the Bureau has never recommended that the Attorney General bring an application for a special remedy under section 32 and there has never been a remedial order granted pursuant to that section.

The Bureau will seek a remedy for the unilateral exercise of the IP right to exclude under section 32 only if the circumstances specified in that section are met and the alleged competitive harm stems directly from the refusal and nothing else. Such circumstances require the Federal Court to balance the interests of the system of protection for IP (and the incentives created by it) against the public interest in greater competition in the particular market under consideration. Generally, the Bureau would recommend to the Attorney General that an application be made to the Federal Court under section 32 when, in the Bureau's view, no appropriate remedy is available under the relevant IP statute.

Enforcement under section 32 requires proof that competition has been unduly restrained, prevented or lessened. The Bureau expects that such enforcement action would be required only in certain narrowly defined circumstances. The Bureau determines whether the exercise of an IP right meets this threshold by analyzing the situation in two steps.

In the first step, the Bureau would establish that the mere refusal (typically the refusal to license IP) has adversely affected competition to a degree that would be considered substantial in a relevant market that is different or significantly larger than the subject matter of the IP or the products or services that result directly from the exercise of the IP. This step is satisfied only by the combination of the following factors:

> i) The holder of the IP is dominant in the relevant market; and
>
> ii) The IP is an essential input or resource for firms participating in the relevant market – that is, the refusal to allow others to use the IP prevents other firms from effectively competing in the relevant market.

In the second step, the Bureau would establish that invoking a special remedy against the IP right holder would not materially alter the incentives of the right holder or others to engage or invest in research and development. As part of this analysis, the Bureau would consider whether the refusal to license the IP is stifling further innovation.

If factors i) and ii) are present and the second step condition is satisfied, then the Bureau would conclude that incentives to invest in research and development have been harmed by the refusal and a special remedy would help realign these incentives with the public interest in greater competition.

The Bureau recognizes that only in very rare circumstances would each of the factors be satisfied. In particular, the Bureau expects that in most cases a section 32 remedy is likely to undermine innovation incentives. Nonetheless, an example in which each of the factors could arise is in a network industry,[34] when the

[34] A network industry is an industry that exhibits network effects. These effects exist when the value or benefit derived from using a product increases with the number of other users. For example, particular types

combination of IP protection and substantial positive effects associated with the size of the network could create or entrench substantial market dominance so that the protected technology is necessary for a competitor's products to be viable alternatives. Under these narrow circumstances, IP protection can effectively exclude others from entering and producing in the market.[35] However, the Bureau still would have to be satisfied that invoking a special remedy against the IP right holder would not materially alter the incentives of the right holder or others to engage or invest in research and development before recommending that the Attorney General bring an application for a special remedy to the Federal Court (see Example 8).

4.2.3 Matters Possibly Resolved Outside the Act

An illegitimate extension of an IP right could include anti-competitive behaviour. This might involve a patent holder asserting its patent over products that are not within the scope of its patent or a distributor making false claims that it is an official licensee of a trademarked good. Alternatively, the Bureau may receive complaints that infringement of a legitimate IP right should be justified on competition grounds. In such disputes, the Bureau will use its enforcement discretion but in most cases it will choose to leave the matter to be resolved by the appropriate IP authority under the appropriate IP statute (see Example 1).

As outlined in section 4.1 above, the Bureau's analytical approach is sufficiently flexible to accommodate the specific characteristics of IP and the differences in the scope and length of protection extended to different IP rights. The following information highlights how the Bureau takes these factors into account when analyzing business conduct involving IP.

5. The Analytical Framework in the Context of IP

5.1 Relevant Markets

Relevant markets provide a practical tool for assessing market power.[36] When the anti-competitive concern is prospective (that is, the conduct is likely to have a future anti-competitive effect),[37] relevant markets are normally defined using the hypothetical monopolist test.[38]

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of software can exhibit network effects because the value of exchanging computer files with other individuals clearly depends on whether these individuals use compatible software.

[35] This does not suggest that markets subject to network effects will inevitably be monopolized. Often, firms form alliances and make a new technology "open" to gain acceptance and build an installed base. These activities tend to be pro-competitive if firms that participate in the process freely compete with each other in the market.

[36] The market definition exercise focuses on demand substitution factors (i.e., possible consumer responses). The Bureau considers the potential constraining influence of firms that can participate in the market through a supply response (i.e., a possible production response) after it has defined the relevant market.

[37] This is generally the case with mergers.

[38] See paragraphs 4.3, 4.4 and 4.5 of the Bureau's *Merger Enforcement Guidelines*, October 2011. Available at: http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/03420.html.

When the anti-competitive concern is retrospective[39] (that is, the conduct has already had an anti-competitive effect), applying the hypothetical monopolist test could lead to erroneous conclusions about the availability of substitutes and the presence of market power. Accordingly, the Bureau takes into account the impact of any alleged anti-competitive conduct that may have preceded the investigation when determining the relevant market. In this context, the Bureau analyzes market definition and competitive effects concurrently.

For conduct involving IP, the Bureau is likely to define the relevant market based on one of the following: the intangible knowledge or know-how that constitutes the IP, processes that are based on the IP rights, or the final or intermediate goods resulting from, or incorporating, the IP.

Defining a market around intangible knowledge or know-how is likely to be important when IP rights are separate from any technology or product in which the knowledge or know-how is used. For example, consider a merger between two firms that individually license similar patents to various independent firms that, in turn, use the patents to develop their own process technologies. Such a merger may reduce competition in the relevant market for the patented know-how if the two versions of that know-how are close substitutes for each other; if there are no (or very few) alternatives that are close substitutes for the know-how; and if there are barriers that would effectively deter the development of conceptual approaches that could replace the know-how of the merging firms. This last condition may be satisfied if the scope of the patents protecting the merging firms' know-how is sufficiently broad to prevent others from "innovating around" the patented technologies, or if the development of such know-how requires specialized knowledge or assets that potential competitors would be unlikely to develop or obtain in a timely manner sufficient to constrain a material price increase in the relevant market.

In cases involving the licensing of IP, the Bureau generally treats the licence as the terms of trade under which the licensee is entitled to use the IP. The Bureau does not define a relevant market around a licence, but rather focuses on what the legal rights granted to the licensee actually protect (i.e., intangible knowledge or know-how, processes, or final or intermediate goods).

The Bureau does not define markets based on research and development activity or innovation efforts alone. The Bureau usually concentrates on price or output effects. However, conduct that reduces the innovation effort of the firms under scrutiny or restricts or prevents the innovation efforts of others may be anti-competitive. The appropriate relevant market definition or definitions will depend specifically on the knowledge or know-how, process, or, final or intermediate good toward which the innovation effort is directed.

[39] This is generally the case with alleged abuse of dominant position.

5.2 Market Power

Whether conduct involving IP results in an increase in market power in the relevant market depends on a number of factors, including the level of concentration, entry conditions, the rate of technological change, the ability of firms to "leap-frog over" seemingly entrenched positions and the horizontal effects, if any, on the market.[40] The order in which the Bureau assesses these factors may vary depending on the section of the Act under which the Bureau is examining the conduct and on the circumstances of the relevant market.

5.2.1 Market Concentration

The Bureau examines the degree of market concentration to get a preliminary indication of the competitiveness of the relevant market. In general, the more firms in the relevant market, the less likely it is that any one firm acting unilaterally, or any group of firms acting cooperatively, could enhance or maintain market power through the conduct being examined. However, a high degree of concentration is not enough to justify the conclusion that the conduct will create, enhance or maintain market power. This is particularly true of industries with low barriers to entry, a high rate of technological change and a pattern of firms "innovating around" or "leap-frogging over" technologies that had previously controlled a dominant share of a market.

To measure concentration in markets for intermediate or final goods, the Bureau typically calculates the market shares of the firms identified as actual participants in the relevant market. These include the firms identified as currently offering products that are demand substitutes as well as those that represent potential supply sources of these products (i.e., firms that are likely to respond to a price increase in the relevant market with minimal investment).[41] Firms that are unable to respond quickly to a price increase or whose entry requires significant investment are not considered to be participants within the relevant market for purposes of assessing market concentration. That said, the potential competitive influence of such firms will be considered as part of the assessment of whether the conduct in question is likely to lessen or prevent competition substantially.

The Bureau generally does not challenge the conduct of a firm that possesses less than a 35 percent market share.[42] Market shares of more than 35 percent indicate circumstances that may warrant further review. Market share may be calculated based on the firms' entire actual output, total sales (dollars or units) or

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[40] The *Merger Enforcement Guidelines*, *supra* note 38, discuss other factors the Bureau considers when it assesses market power. These include foreign competition, business failure and exit, the availability of acceptable substitutes, effective remaining competition, removal of a vigorous and effective competitor, and change and innovation.

[41] The following factors are relevant to determining when a firm will rapidly divert sales in response to a price increase: the cost of substituting production in the relevant market for current production (i.e., switching costs), the extent to which the firm is committed to producing other products or services, and the profitability of switching from current production.

[42] The Bureau generally does not challenge the conduct of a group of firms alleged to be jointly dominant that possess a combined market share of less than 65 percent.

total capacity (used and unused).[43, 44] However, some of these factors may be difficult to assess in cases involving IP. Accordingly, the Bureau's assessment of market power is likely to focus on qualitative factors, such as conditions of entry into the relevant market; whether IP development is resulting in a rapid pace of technological change; and the views of buyers and market participants, as well as industry and technology experts.

5.2.2 Ease of Entry

The Bureau also examines how easily firms can enter the relevant market to determine whether new entrants have the ability to restrain any creation, enhancement or maintenance of market power that may result from conduct involving IP. When assessing effects in markets involving IP, conditions of entry are often more important than market concentration. For instance, evidence of a rapid pace of technological change and of the prospect of firms being able to "innovate around" or "leap-frog over" an apparently entrenched position is an important consideration that may, in many cases, fully address potential competition concerns.

The Bureau also considers the extent to which the conduct itself erects or has erected barriers to entry or, alternatively, induces or has induced competitors to exit the market (see Examples 3B and 4).[45] Entry into markets in which IP is important may be difficult because of the sunk costs associated with developing assets that comprise specialized knowledge. Additionally, IP rights can serve to increase barriers to entry independent of any conduct.[46]

5.2.3 Horizontal Effects

In evaluating the competitive effects of conduct that involves an IP right, whether it is a merger transaction, licensing arrangement or other form of contractual arrangement, the Bureau focuses on whether the conduct will result in horizontal anti-competitive effects, in other words, consequences for firms producing substitutes or firms potentially producing substitutes (see Examples 3A and 3B).

Even though an arrangement may be vertical, such as the acquisition of a retail shoe outlet by a shoe manufacturer or the licensing of the right to use a particular food additive to a food producer, it can still have horizontal effects in a relevant market (see Example 4).

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[43] If the actual participants in the market include firms that represent potential sources of supply for the market, then market shares, even in terms of production capacities, may be difficult to accurately estimate. Accordingly, it must be recognized that the market shares attributed to firms whose products are actually sold within the relevant market will overstate the relative market position of these firms in such circumstances.

[44] The Tribunal stated in *Laidlaw*, *supra* note 31, that market share calculations based on sales may overstate market power when the market is characterized by excess capacity.

[45] The fact that anti-competitive conduct can create barriers to entry was recognized by the Tribunal in *Laidlaw*, *supra* note 31.

[46] Of course, the purpose of providing innovators with IP rights is to foster the development of new products. In this sense, IP rights may encourage firms to participate in environments in which technology changes very rapidly.

5.3 Anti-competitive Effects

Conduct must create horizontal effects for the Bureau to conclude that it is anti-competitive.[47] In this regard, the Bureau analyzes whether conduct facilitates a firm's ability to exercise market power, either unilaterally or in a coordinated manner, in areas such as pricing and output.[48]

Anti-competitive horizontal effects may arise if the conduct increases competitors' costs. For example, a transaction can prevent, or raise the cost of, competitors' access to important inputs. IP licensing arrangements that involve one firm selling the right to use IP to another are inherently vertical, but can have horizontal effects, particularly if the licensor and licensee would have been actual competitors in the absence of the licensing arrangement. In addition, conduct that reduces innovation activity could be anti-competitive if it prevents future competition in a prospective product or process market.

5.4 Efficiency Considerations

A fundamental objective of competition law is to ensure the efficient use of resources through vigorous competition. However, there may be instances in which restrictions on competition can lead to a more efficient use of resources. This may be particularly true of agreements, arrangements and transactions involving IP that are inherently vertical and combine complementary factors. Moreover, there may be instances when creating or increasing market power is justified because of the efficiencies created. Indeed, this principle is consistent with the protection afforded by IP laws, which foster dynamic efficiency and competition by facilitating the creation of valuable works or processes that result in long-term increases in product selection, quality, output and productivity. In providing incentives for investment, IP laws grant exclusivity to the protected works that may result in temporary market power. Consequently, the Bureau considers both the short-term and long-term implications of conduct when analyzing efficiencies in cases involving IP. Efficiencies are explicitly recognized in sections 90.1 and 96 of the Act in the context of agreements or arrangements among competitors[49] and mergers.[50]

If the Bureau concludes that conduct is likely to substantially lessen or prevent competition in a relevant market under either section 90.1 or 92 of the Act, it will, when provided in a timely manner with the parties' evidence substantiating their case, make an assessment of whether the efficiency gains brought about or likely to be brought about by the conduct are greater than and offset the anti-competitive effects arising from the conduct. Part 12 of the *Merger Enforcement*

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[47] For investigations under provisions of the Act that do not require a showing that the conduct has an effect on competition, there is no need to consider anti-competitive effects (see Example 10).

[48] The term 'pricing' includes all aspects of firms' actions that affect the interest of buyers. These include a reduction in quality, product choice, service, innovation or other dimensions of competition that buyers value.

[49] Section 90.1 also applies to agreements between parties that are potential competitors.

[50] Section 95 provides a specific exemption under the merger provision for research and development joint ventures that satisfy certain criteria outlined in the provision.

Guidelines more fully describes the Bureau's approach to the analysis of efficiencies.

5.5 Business Justifications

In assessing whether conduct involving IP is for an anti-competitive purpose under section 79 of the Act, the Bureau considers any pro-competitive rationale for the conduct.[51] For example, a licensing arrangement between an IP owner and a distributor may restrict intra-brand competition, but at the same time further inter-brand competition. A licensing arrangement between two potential competitors also may result in a new product being developed that would not otherwise have been developed. In each case, the level of competition in the market may be enhanced.[52]

6. Competition Policy Advocacy

The Bureau may use its mandate to promote competition and the efficient allocation of resources to intervene in policy discussions and debates regarding the appropriate scope, definition, breadth or length of IP rights.[53] The Bureau may also seek leave to intervene in Federal Court and Superior Court cases when it believes it is important to bring a competition perspective to proceedings that will not be brought by the parties. In other proceedings, when the Bureau believes that IP rights could potentially be defined, strengthened or extended inappropriately, the Bureau may seek leave to intervene to make representations concerning the scope of the protection that should be accorded IP rights.

An example of Bureau advocacy occurred when it applied for and was granted leave to intervene by the Federal Court of Appeal ("FCA") in *Apotex Inc. v. Eli Lilly and Co*.[54] In this case, the Bureau argued that the assignment of a patent could constitute an agreement or arrangement to unduly lessen competition contrary to the former section 45 of the Act. This position meant that section 50 of the *Patent Act*, which gives patentees the right to assign their patents, does not preclude application of the Act to patent assignments. The Bureau's intervention served the purpose of protecting its ability to administer the Act in respect of patent rights. The FCA agreed with the Bureau's position and noted

[51] In *Tele-Direct*, *supra* note 26, the Competition Tribunal stated that, "(w)hat the Tribunal must decide is whether, once all relevant factors have been taken into account and weighed, the act in question is, on balance, 'exclusionary, predatory or disciplinary'. Relevant factors include evidence of the effects of the act, of any business justification and of subjective intent which, while not necessary, may be informative in assessing the totality of the evidence. A 'business justification' must be a 'credible efficiency or pro-competitive' business justification for the act in issue. Further, the business justification must be weighed 'in light of any anti-competitive effects to establish the overriding purpose' of the challenged act..."

[52] In *Nielsen*, *supra* note 12, the Competition Tribunal held that even if there is some justification for the alleged anti-competitive conduct, this must be weighed against any anti-competitive effects.

[53] Section 125 of the Act provides that the Commissioner may make representations to and call evidence before any federal board, commission or other tribunal in respect of competition. Section 126 of the Act provides that the Commissioner may do the same for any provincial board, commission or other tribunal as long as the board, commission or tribunal consents.

[54] *Supra* note 14.

that “this interpretation is consistent with the Competition Bureau’s *Intellectual Property Enforcement Guidelines*”.

7. Application of Competition Law to IP

7.1 Hypothetical Examples Concerning General Business Conduct Involving IP

This subsection provides several hypothetical examples of general business conduct involving IP and outlines the Bureau’s approach to reviewing the conduct under the Act.

Example 1: Alleged Infringement of an IP Right

TAX is a software company that produces and distributes a sophisticated and complex tax management program to help households with their tax planning. TAX has been selling its product for a number of years and is now widely recognized as a leading producer of tax management software.

More than two years ago, a key member of TAX's software engineering team left the company to start her own software business, called UPSTART. Recently, UPSTART began to market its own tax management program. TAX has sued UPSTART claiming that UPSTART must have infringed TAX’s copyright because its software is very similar in appearance and functionality to TAX’s software. UPSTART has complained to the Bureau that TAX is abusing its dominant position by launching frivolous litigation.

Analysis

The Bureau would use its enforcement discretion and likely conclude that this matter would be best left up to the courts to be resolved under the *Copyright Act*. If TAX engages in a practice of launching frivolous litigation to exclude competitors, the Bureau may consider taking action under section 79 of the Act.

Example 2: Price-fixing

Three firms, each of which has developed and owns a patented technique, offer competing cosmetic surgical procedures to treat a particular condition. All three procedures involve several visits to a private clinic over six months, produce no side effects and have approximately equal success rates. The only existing alternative to the three procedures is an expensive medication that causes undesirable side effects in some patients. Each of the three firms has developed a business plan to market its procedure and industry analysts widely agree that competition among the procedures will be the most important factor limiting shareholder returns. Rather than proceed with their business plans in anticipated competition with one another, the three firms agree on a minimum price at which each will perform the procedure as well as a minimum fee to license each procedure to third parties.

Analysis

The Bureau would likely examine this agreement under the conspiracy provision in section 45 of the Act given that it involves fixing prices for the supply of a product. The Bureau would likely take the view that the three participants in the agreement are competitors based on the views of industry analysts and given the fact that each of them supplies treatments that are functionally interchangeable with and comparable to one another. For example, the duration, the success rate and the risk of side effects are approximately the same for each procedure. Moreover, section 45 applies to agreements between parties that are potential competitors. Accordingly, even if the parties had not been in competition when the agreement was concluded or during the term of the agreement, the parties would still be deemed to be competitors for purposes of section 45, as it would be reasonable to believe that they would likely compete with respect to a product in the absence of the conspiracy.

Given that the price-fixing agreement is not ancillary to a broader or separate agreement or arrangement, which itself does not offend section 45, the Bureau would refer the matter to the Director of Public Prosecutions (the “DPP”) for criminal prosecution.

Example 3A: Exclusive Licensing

SHIFT recently developed a new gear system for mountain bikes. Two other firms manufacture systems that compete with SHIFT's. All three of these firms manufacture several varieties of bicycle gear systems and are engaged in research and development to improve gear system technology. SHIFT grants licences for the use of its patented gear system technology to manufacturers of mountain bikes as it does not have the ability to manufacture mountain bikes itself. Three large firms account for 80 percent of the sales of mountain bikes with the balance being supplied by six smaller firms. SHIFT has just granted ADVENTURE, the largest mountain bike manufacturer (accounting for 30 percent of sales), an exclusive licence to use its new patented gear system technology on its mountain bikes. ADVENTURE does not own or have the ability to develop gear system technology. Although SHIFT's new gear system offers a number of features not available on other current products, the demand for mountain bikes with these new features is uncertain. In addition, ADVENTURE expects to incur significant expense developing and promoting mountain bikes that use SHIFT's new gear system technology. SHIFT has refused requests from other mountain bike manufacturers for a licence for this technology. As a result of ongoing research and development, alternative gear system technologies are likely to become available in the future.

Analysis

The Bureau would likely examine the conduct of both firms under the abuse of dominant position provision (section 79) of the Act.

SHIFT and ADVENTURE relate as supplier and customer, and are neither actual nor potential competitors in the markets for gear systems or mountain bikes. Since the firms do not compete, the exclusive licence would likely not lessen competition between the two firms. The Bureau would nonetheless examine the markets for gear systems and mountain bikes to determine if the exclusive licence lessened or prevented competition substantially in either or both of those markets.

Even though SHIFT's new technology is not available to ADVENTURE's rivals and the markets for gear systems and mountain bikes are concentrated, the other mountain bike manufacturers have access to other gear systems from SHIFT and to gear systems from other suppliers. The exclusive licence may have been granted in consideration for ADVENTURE's agreement to incur significant expense in the development and promotion of mountain bikes that use SHIFT's new technology. In addition, SHIFT’s rivals in the gear system market may still sell to ADVENTURE.

In the course of its assessment, the Bureau would consider the competitiveness of the mountain bike market before and after the exclusive licence. SHIFT is not a mountain bike manufacturer and has no obligation to license its gear system to a mountain bike manufacturer. The technology licence mandated the development and promotion of mountain bikes using the technology, thereby enhancing competition without in any way limiting the ability of other mountain bike manufacturers to access or use competing technologies. Consequently, the Bureau would conclude, given the facts of this case, that the exclusive licence arrangement did not raise any competition issues.

Example 3B: Foreclosure by Purchaser

Consider a variation on the situation described in Example 3A, in which ADVENTURE's business has grown to represent approximately 70 percent of mountain bike sales. ADVENTURE has taken advantage of its increasing sales share to independently negotiate long-term exclusive licences and supply arrangements with the three competing suppliers of mountain bike gear systems. The inability of the competing manufacturers of mountain bikes to obtain suitable gear system technology has put a number of them out of business and has substantially cut into the sales of the remaining firms. ADVENTURE has raised the prices of its mountain bikes by 25 percent. Although alternative gear system technologies are under development, it appears unlikely that a viable technology will be tested and in production in less than 36 months.

Analysis

The Bureau would likely examine ADVENTURE's conduct under the abuse of dominant position provision (section 79) of the Act.

The Bureau would initially determine whether mountain bikes comprised a relevant market and assess whether ADVENTURE substantially or completely controlled the supply of product within that relevant market. The Bureau would likely view the apparent lack of effective substitutes and ADVENTURE's high sales share and ability to successfully impose a 25 percent price increase as evidence that ADVENTURE substantially controlled the mountain bike business and that mountain bikes comprise a relevant market.

The Bureau would then consider whether ADVENTURE's exclusive licence agreements, through which it precluded its competitors from obtaining an adequate supply of gear systems, constituted anti-competitive conduct. While an exclusive licence arrangement may enhance competition, as was apparent in Example 3A, the use of an exclusive licence arrangement to effectively control the supply of a competitively essential input may be anti-competitive. In the absence of a compelling business justification, the Bureau would likely view the execution of long-term exclusive licences with each of the suppliers as a practice of anti-competitive acts that prevented ADVENTURE’s competitors from obtaining access to this vital input (gear systems).

The Bureau would then assess the impact of the exclusive licences on competition. It would likely conclude that the adverse impact on the ability of other mountain bike manufacturers to compete that resulted from ADVENTURE preventing them from gaining access to proven gear system technology and the manner in which ADVENTURE successfully imposed substantial price increases constituted evidence that ADVENTURE substantially lessened or prevented competition. Accordingly, the Bureau would likely seek to have the exclusive licences voluntarily terminated. Failing that, the Bureau would likely bring an application before the Tribunal seeking to terminate the exclusive terms of the licences.

Example 4: Exclusive Contracts

SPICE, by virtue of its international patents, is the sole supplier of Megasalt, a unique food additive that has effectively replaced salt in certain prepared foods in most countries. SPICE's Canadian patent recently expired; however, SPICE still has valid patent protection throughout much of the rest of the world. Shortly before its Canadian patent expired, SPICE signed five-year contracts, which included exclusive supply rights, with its two principal Canadian buyers. These contracts prevent the two buyers, which use Megasalt in specially prepared foods for hospitals and other health care institutions, from combining Megasalt with any other salt substitute on the same product line. SPICE does not have long-term exclusive supply contracts with other buyers of Megasalt in Canada or elsewhere. Recently, NUsalt, a firm that has developed a potential alternative to Megasalt, filed a complaint with the Bureau alleging that SPICE's contracts are preventing NUsalt from manufacturing and marketing its product in Canada. NUsalt claims that SPICE's contracts have "locked up" a substantial part of the market, thereby precluding NUsalt from profitably entering Canada.

Analysis

The NUsalt allegations suggest that SPICE, as a result of its contracts with its two largest buyers, is currently exploiting market power within the market for salt substitutes. The Bureau would likely investigate these allegations under the abuse of dominance provision (section 79) of the Act.[55]

The Bureau would initially determine whether salt substitutes comprise a relevant product market. This would entail determining whether salt substitutes are subject to effective competition from other substances (for example, salt) or whether salt substitutes have specific properties and functional characteristics that make other substances ineffective as substitutes. The Bureau would then seek to determine whether SPICE substantially controlled the market in which its salt substitute competed by assessing SPICE's share of sales and barriers to entry to this market. The Bureau would consider all of the factors currently preventing alternative suppliers of salt substitutes from offering their products to customers in Canada, including the effect of SPICE's exclusive supply contracts on the ability of alternative suppliers to obtain sales from a critical mass of customers. Assuming that the Bureau had determined that salt substitutes constitute a relevant market, it would likely conclude that SPICE substantially controlled that market.

The Bureau would then consider whether the exclusive supply contracts, through which SPICE had precluded its principal customers from obtaining salt substitutes from alternative suppliers, constituted a practice of anti-competitive acts. To make this assessment, the Bureau would examine the circumstances surrounding the negotiation and settlement of the exclusive contracts, and the extent to which they were exclusionary and intended to erect barriers to effective competition in the relevant market. As part of this analysis, the Bureau would consider whether there are compelling business justifications for SPICE's exclusive contracts. For example, SPICE may have signed these contracts to ensure that it would have sufficient sales to justify investing in enough productive capacity to realize economies of scale. Also, the restriction preventing buyers from combining Megasalt with other salt substitutes could have a safety or quality rationale. On the other hand, if the Bureau found that the contracts in this case were intended to hold back a sufficient amount of market demand from potential entrants so that the remaining demand would provide an insufficient volume of sales to cover the cost of effective entry and future operating costs in Canada, then the Bureau would likely view the execution of the long-term exclusive licences as a practice of anti-competitive acts.

The Bureau would then assess the impact of the exclusive contracts on competition. In this regard, the adverse impact on the ability of other suppliers of salt substitutes to compete in Canada would be assessed to determine whether the contracts had substantially lessened or prevented competition. If the relevant market is defined as salt substitutes and SPICE's contracts are significantly preventing the entry of potential salt substitute producers, the Bureau may conclude that the exclusive contracts have substantially lessened or prevented

[55] The Bureau may also choose to review the conduct under the exclusive dealing, tied selling and market restriction provision (section 77) of the Act.

competition. By deterring firms from attempting to supply alternative salt substitutes in Canada, the exclusive contracts may cause other buyers in Canada not under contract with SPICE to pay higher prices than they would if SPICE faced effective competition.

The magnitude of the decrease in competition would depend on the extent to which the contracts prevent entry and the expected degree of substitution that would exist between Megasalt and alternative salt substitutes, such as NUsalt, in the absence of the exclusive terms in the contracts. In general, if the contracts are determined to be the principal barrier to new entry and the new entrants' products are likely to be close substitutes for Megasalt, then the Bureau is likely to conclude that the contracts have substantially lessened or prevented competition and would likely seek to have SPICE’s exclusive contracts voluntarily terminated. Failing that, the Bureau would likely bring an application before the Tribunal seeking to terminate the exclusive terms in the contracts.

However, if the Bureau determines that the contracts do not block effective competitive entry in Canada, then SPICE's exclusive contracts would not be considered to have substantially lessened or prevented competition. In this case the Bureau would close its inquiry without seeking remedial measures. Throughout its investigation the Bureau would work collaboratively with competition agencies in other jurisdictions as necessary to determine facts and their analytical approach relevant to the resolution of the matter.

Example 5: Output Royalties

MEMEX currently holds a patent for the design of a memory component it manufactures for use in personal home computers. MEMEX does not manufacture personal computers, but instead sells its memory components and licenses the use of its technology to computer manufacturers. Historically, MEMEX's licensing contracts required that the licensee pay a fee for each MEMEX memory component it installed in a computer. Because of its patent, MEMEX currently faces no competition from other memory component producers wishing to use a similar design; however, MEMEX's patent is due to expire within a year and there is speculation that once it expires, other firms will begin manufacturing and selling memory components based on MEMEX's design. MEMEX has recently introduced a new licence agreement. Under the new agreement, MEMEX grants non-exclusive licences for the use of its technology and memory components to all personal computer manufacturers for a royalty on every computer shipped, regardless of whether any MEMEX memory components are installed. MEMEX claims that the previous licensing policy had the unintentional effect of encouraging computer manufacturers to install too few MEMEX memory components, which detracted from computer performance. MEMEX claims that the new licensing practice provides manufacturers an incentive to install a more appropriate quantity of memory in computers.

Analysis

The Bureau would likely investigate this case under the abuse of dominance provision (section 79) of the Act.

The Bureau would first determine whether memory components that employ MEMEX's technology comprise a relevant market and then assess whether MEMEX substantially or completely controls the supply of product within that market. In view of the rapid rate of technological development and intense competition in the production of integrated circuit devices, the Bureau may conclude that the MEMEX technology competes with other memory technologies, that barriers to entry are sufficiently low that the scope of the relevant market extends beyond the MEMEX technology, or that MEMEX is unable to substantially control the supply of products within the specified relevant market. If the Bureau determines that MEMEX faces effective competition from other suppliers of memory components then it would likely conclude that further investigation is not warranted. If, on the other hand, the Bureau concludes that the memory components supplied by the alternative suppliers are not considered effective substitutes and would not allow computer manufacturers to build computers that could compete with those using MEMEX's memory component, the Bureau might determine that further inquiry was warranted.

Assuming the Bureau determined that the MEMEX technology defines the relevant market and MEMEX substantially controls that market, the Bureau would then consider whether MEMEX's use of its new licensing arrangements constituted a practice of anti-competitive acts. This determination would depend on the specific terms of the contracts and the likely effect they would have on actual or potential competitors in the relevant market. While MEMEX's licensing contracts do not expressly prohibit computer manufacturers from using memory components based on technology other than MEMEX's, they effectively impose a tax on computer manufacturers who use memory components from another supplier.[56] The imposition by a dominant supplier of long-term licensing contracts containing such provisions could preclude competition and maintain the supplier's market power. Accordingly, the Bureau would determine whether these contracts are in widespread use and their duration, and consider MEMEX's business justification for charging the per-computer royalty. It would also consider whether the per-computer royalty deters computer manufacturers from buying memory components from alternative suppliers.

If the Bureau determined that the licensing contracts were a practice of anti-competitive acts, the Bureau would then assess the likely impact of MEMEX's new licensing practice on competition and the price of memory components. If the Bureau determined that this practice creates, enhances or preserves market power, it would likely seek to have the new licensing practice voluntarily terminated. Failing that, it would likely bring an application before the Tribunal seeking to terminate this practice.

[56] A manufacturer who wishes to use alternative memory products must pay twice, once for the alternative component and a second time for the per-computer royalty payable to MEMEX.

Example 6: A Patent Pooling Arrangement

Five firms hold patents on technologies required by producers to develop widgets that conform to an international standard. To facilitate the licensing of their patents, the five firms hire an independent expert to review the patents of each firm and determine those that are essential for implementing the standard based on the underlying technical characteristics of the technologies. Upon completion of the review, the five firms create a patent pool and each of them licenses its essential patents on a non-exclusive basis to the pool. The pool is organized as a separate corporate entity whose role is to grant a non-exclusive sub-licence to all the patents in the pool on a non-discriminatory basis to any party requesting one. The patent pool administrator collects royalties from licensees and re-distributes the revenue to pool members according to a formula that is partly based on the number of patents that each member has contributed to the pool. Each of the five members of the pool retains its right to license its own essential patents outside the pool to third parties to make widgets that conform to the standard or widgets that may compete with those that conform to the standard.

The patent pool agreement specifies that if a final court judgment declares a patent in the pool to be invalid, that patent will immediately be excluded from the pool. In addition, the agreement requires that an independent expert re-assesses the patents in the pool every four years to ensure that they are essential to developing widgets conforming to the international standard. Licensees also have the ability to hire an independent expert to review any patent that they feel is not essential for developing widgets conforming to the standard. If, in either case, the expert concludes that one or more patents are not essential to developing widgets that conform to the standard, those patents are excluded from the pool. The decisions of experts are final and are binding upon the pool members.

The patent pool agreement also includes provisions allowing each pool member to audit the books of the pool administrator, and provisions allowing the pool administrator to audit the books of each licensee to verify royalty amounts. In each case, provisions are put in place to guard against confidential business information being divulged to either pool members or licensees.

Analysis

The Bureau recognizes that patent pools can often serve a pro-competitive purpose by, among other things, integrating complementary technologies, reducing transaction costs and clearing blocking patents. Where patent pools may represent an agreement between competitors or potential competitors, the Bureau would likely review them under section 90.1 of the Act rather than section 45, unless the Bureau has evidence that the patent pool was simply used as a means to facilitate an agreement prohibited under subsection 45(1).[57]

[57] The Bureau's *Competitor Collaboration Guidelines*, December 2009, outline the Bureau's approach for determining whether to pursue an investigation under section 45 versus 90.1. Available at: http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/03177.html.

Despite their potential benefits, patent pools may also raise competition concerns. If the patented technologies inside the pool are substitutes then the pool can be a mechanism for the pool members to restrict competition between themselves and increase royalty rates above levels that would have existed in a competitive market. Alternatively, if a patented technology inside the pool is a substitute for a technology outside the pool, the pool could be used as a bundling mechanism to effectively foreclose the outside technology. Other potential competition concerns are that a pool's members may discriminate among licensees or use the pool to share confidential business information so as to reduce competition in a downstream market.

To evaluate whether a patent pool would likely cause a competition issue, the Bureau would first seek to determine whether each patent placed inside the pool is essential for developing the product or service that is the basis behind the formation of the pool. In the case at hand, if each patent inside the pool is required to implement the widget standard, then the members of the pool cannot be viewed as horizontal competitors; a firm looking to buy technologies to develop widgets conforming to the standard would need permission to use each patented technology in the pool. A pool comprised of only non-competing essential patents would not have the potential to harm competition among suppliers of technology either inside or outside the pool.

In this example, the Bureau would look positively on the fact that pool members engaged an independent expert to determine which of their patents are essential to the widget standard. However, the Bureau would evaluate whether the expert is qualified to provide such an opinion, and whether he/she was provided with the incentive to work independently, without influence from pool members. The Bureau would take additional assurance from the fact that an expert would continue to periodically review the patents to ensure they remain essential, as well as from the ability of licensees to challenge patents by requiring a separate independent review. The fact that any patents found to be invalid would also be removed from the pool would also contribute to the Bureau's assurance that the pool has taken adequate measures to only include essential patents.

Given that the pool administrator issues licences on a non-discriminatory basis to all interested parties, the Bureau would likely conclude that the technologies inside the pool were not being used to distort competition in a downstream widget market. The fact that pool members remain free to license their patents independently to other widget producers provides more evidence that competition in the downstream widget market would not be distorted by the pool.

As a final step, the Bureau would review the pool agreement's provisions relating to the sharing of confidential information and ensure that such provisions provide adequate safeguards against the pool being used to facilitate coordination among pool members or licensees.

Absent any evidence that the patent pool is used to facilitate an agreement prohibited under subsection 45(1), based on the analysis above, the Bureau would likely conclude that the patent pool does not raise any issues under the Act.

Example 7: Agreement to Foreclose Complementary Products

There are five major record labels. The largest two, ROCKCO and POPCO, which together account for more than 65 percent of total sales and 70 percent of all major label artists, have formed a joint venture (DISCO) to develop, produce and market a new generation of digital playback devices. The DISCO technology provides a level of sound quality and other features far superior to those offered by existing technologies. DATCO has also developed a digital sound technology with similar high-fidelity qualities, but which is also portable and allows users to record. The costs of the two technologies are similar, but the technologies themselves are incompatible: music digitally encoded in DISCO format must be re-encoded for playback on DATCO's player. Under the terms of their joint venture agreement, ROCKCO and POPCO agree to not release, or license any other person to release, their copyrighted recordings in a digital format other than the DISCO format. Consistent with that agreement, ROCKCO and POPCO have declined DATCO's request for a licence to convert and release ROCKCO and POPCO recordings in the DATCO format. The other three record labels predict -- correctly -- that consumers will be reluctant to purchase the DATCO technology if they are unable to obtain music from either ROCKCO or POPCO in that format. The other record companies are willing to release their recordings in the DATCO format, but find that there is no market for it and are compelled by popular demand to license the DISCO technology to release their recordings in the DISCO format. As a result of the foregoing, DATCO's digital sound technology, which reviewers have generally viewed as superior to the DISCO technology, is being withdrawn and DISCO is substantially increasing both the price of the playback equipment that it sells and the royalties charged to the other record companies for the use of the DISCO technology to release recordings in the DISCO format. The Bureau has concluded that the joint venture would not meet the definition of a merger as specified in section 91 of the Act.

Analysis

The Bureau would likely examine this case under the agreements and arrangements provision (section 90.1) and/or the abuse of dominance provision (section 79) of the Act.

The matter would not be considered under section 45 because the ROCKCO and POPCO joint venture would not be viewed as an agreement between competitors to fix prices, allocate markets or customers, or restrict output. Even if the refusal to release recordings in another format or grant a licence are considered output restrictions, the ancillary restraints defence would likely apply because they are ancillary and directly related to the broader joint venture agreement to develop the DISCO technology. As well, these restraints appear reasonably necessary to attract a sufficient number of customers to the DISCO technology to make the joint venture viable.

As a first step, the Bureau would consider whether the alleged anti-competitive conduct, namely the refusal of ROCKCO and POPCO to license the reproduction of their copyrighted recordings in the DATCO format, was a mere exercise of their IP rights or involved something more. In this case, the Bureau would likely determine that the terms of the DISCO joint venture agreement and the refusal to license constituted joint conduct and hence would be considered conduct that was beyond the mere exercise of an IP right.

The Bureau may elect to review the agreement under section 90.1 of the Act if ROCKCO and POPCO could be considered competitors in a relevant market. In this example, the important consideration in determining if the firms are competitors is determining if ROCKCO and POPCO would have likely developed the DISCO, or similar, technology independently in the absence of the agreement. If the Bureau were to determine that this would be the case, then ROCKCO and POPCO could have been expected to compete in the market for digital playback devices in the absence of their joint venture and the agreement would be reviewed under section 90.1.

If, on the other hand, ROCKCO and POPCO were determined not to be competitors, the Bureau would elect to review the joint venture agreement under the abuse of dominance provision, on the basis that the joint venture agreement established and provided for the joint abuse of a dominant position. The review would be carried out in accordance with the framework and criteria for abuse of dominance outlined in the previous examples. Whichever provision of the Act would apply, the Bureau would need to establish the affected relevant market or markets, consider barriers to entry and evidence of market power or dominance, demonstrate a substantial lessening or prevention of competition and assess any business justifications or efficiencies.

If the Bureau were to proceed under sections 79 or 90.1, it would need to establish that the DISCO joint venture has substantial market power in either the market for digital sound technology or digital playback equipment. In addition, it would need to find that the DISCO joint venture had engaged in anti-competitive conduct that substantially lessens or prevents competition. The anti-competitive acts in this case would relate to the acquisition and foreclosure by the DISCO joint venture of access by its competitors to the music in the ROCKCO and POPCO music libraries. Foreclosure of access to these materials could prevent alternative sound recording technologies from acquiring the critical mass of desirable music content required for them to achieve viability. This conduct could substantially prevent or lessen competition and lead to the monopolization or the creation of dominance in the markets for digital sound technology and/or digital playback equipment sound reproduction. The foreclosure of other technologies likely would create market power for DISCO in these markets and would be inefficient, as it would reduce consumer choice, lead to increases in the royalties paid by the record companies to use this type of technology and increase the price of playback devices. Given such a finding, the Bureau would likely seek an order requiring that ROCKCO and POPCO divest themselves of DISCO or that ROCKCO and POPCO license their works for release in alternative formats.

Example 8: Refusal to License Intellectual Property
ABACUS and two other firms were the first to market a spreadsheet for personal computers. Electronic spreadsheet software was one of the applications that established personal computers as an essential tool for business. In the first five years, ABACUS out-sold its nearest competitor nearly two to one and its installed base (cumulative sales) grew to 50 percent. In the next two years, its annual market share grew to more than 75 percent and one of the other original firms left the market. At about the same time and after three years of programming, CALCULATOR introduced spreadsheet software that had a number of innovative features not found in ABACUS. However, CALCULATOR soon ran into financial difficulties despite the innovative features and a lower price. CALCULATOR approached ABACUS and requested a licence to copy the words and layout of its menu command hierarchy (for the purpose of this example, assume that permission was required since ABACUS had valid copyright rights in these works). With permission, CALCULATOR could have relaunched its product with a menu command hierarchy identical to that of ABACUS, which would have given CALCULATOR the ability to read ABACUS files and ensured compatibility between the two products. ABACUS refused to grant a licence and publicly announced that it would enforce its IP rights against CALCULATOR if it copied the ABACUS hierarchy. In light of this, several other prominent software makers announced that they were discontinuing their spreadsheet development programs.

An important characteristic of spreadsheets that affects their benefits to a purchaser is network effects. Network effects exist if the value of a product increases with the number of buyers who purchase compatible products. Network effects for spreadsheets arise since the greater the size of the network (the installed base of compatible spreadsheets), the greater the number of individuals with whom files can be shared, the greater the variety of complementary products (utilities, software enhancements and macros), the more prevalent are consulting and training services, and the greater the number of compatible data files.

Analysis
ABACUS's refusal to license its copyrighted works would constitute a "mere exercise" of its IP rights and would, therefore, be subject to review only under section 32 of the Act.

To establish whether ABACUS's refusal created an undue restraint of trade or unduly lessened competition, the Bureau would first determine whether the refusal adversely affected competition in a relevant market that was different or significantly larger than the subject matter of ABACUS's IP rights or the products or services that result directly from the exercise of such IP rights. In this case, competitive harm is alleged in the market for ABACUS-compatible spreadsheets.

Whether the relevant market is determined to be ABACUS-compatible spreadsheets depends on the extent and importance of network effects and switching costs. If network effects are important, consumers that have never purchased a spreadsheet may still purchase the more expensive ABACUS product. Consumers who are already using ABACUS may face significant costs to switch to a new spreadsheet (resulting from, for example, customers' need to re-train personnel, convert existing spreadsheet files to a new format, or purchase new complementary products) and they also would lose the network benefits associated with ABACUS. If network effects and switching costs are material, then existing ABACUS consumers are unlikely to switch and new consumers are likely to choose ABACUS even if it is priced above competitive levels.

If the relevant market is determined to be ABACUS-compatible spreadsheets, then ABACUS would be the only producer and thus have 100 percent control of this market. If, in addition, entry barriers were found to be high, which is likely in an industry experiencing network effects, the Bureau would conclude that ABACUS is dominant. In determining whether the installed base of ABACUS contributes materially to entry barriers, the Bureau would consider the pace of innovation and the potential for a new technology to "leap-frog over" ABACUS despite its advantages (that is, its installed base and the switching costs). The Bureau would also endeavour to determine whether there are other efficient avenues for creating compatibility that would not infringe the IP rights of ABACUS.

If the relevant market is determined to be ABACUS-compatible spreadsheets and the Bureau concluded that this market was significantly larger than the subject matter of ABACUS's IP and the products that result directly from the exercise of such IP rights, then the Bureau would likely conclude that the IP is an essential input for firms participating in the relevant market. On this basis, ABACUS's refusal would satisfy the first step of the Bureau's two-step analysis to determine whether it would seek to have an application brought under section 32.

In the second step, the Bureau would determine whether ABACUS's refusal to license its IP would adversely alter firms' incentives to invest in research and development in the economy. For this analysis, the Bureau would investigate whether ABACUS's ability to prevent compatibility may have a chilling effect on the development of more advanced spreadsheets. In addition, the Bureau would determine whether the choice by ABACUS of the words and layout of its menu hierarchy was likely arbitrary, involved little innovative effort and had little value relative to other substitutes. Related to this analysis, the Bureau would determine whether in the absence of an installed base and switching costs, ABACUS's terms and menu hierarchy would be no better or worse than CALCULATOR's (or any other). If the Bureau concluded that the presence of an installed base and switching costs were the reasons that ABACUS-compatible spreadsheets are a market and that ABACUS had market power, it would consider enforcement action under section 32. In this circumstance a special remedy invoked under section 32 may restore incentives for other firms to engage in research and the development of competing compatible spreadsheet programs.

If the facts of the case suggest potential enforcement under section 32, the Bureau would recommend that the Attorney General seek a special remedy that would allow other spreadsheet firms to gain access to the words and layout of ABACUS's menu hierarchy.

Example 9A: Product Switching[58] ("Hard" Switch)
BRAND is a brand-name pharmaceutical company that sells innovative pharmaceutical drugs. One of its top sellers in terms of revenue, Product A, has been sold in Canada for many years, and continues to be sold, but will lose patent protection in six months. Two years ago BRAND introduced another product, Product B, which takes a slightly different form from and alleviates the same affliction as that treated by Product A. The number of prescriptions for Product B remains low. Product B will remain under patent protection for the next 10 years.

GENERIC, a pharmaceutical company that produces generic drugs, is set to launch a generic version of Product A ("Generic A") as soon as Product A's patent protection expires. Before its patent expires, BRAND withdraws Product A from the market by ceasing to manufacture it and by buying back inventories from wholesalers and pharmacies. BRAND notifies health care professionals that Product A is no longer available. In response to this development, physicians prescribe Product B to patients in place of Product A and a large number of prescriptions for Product A are replaced by prescriptions for Product B. Because Product A is the reference product for (or bioequivalent to) Generic A, pharmacies are prohibited from automatically substituting Generic A for the prescribed Product B. As a result, there is a competition concern that GENERIC's entry may be sufficiently impeded and that through an anti-competitive act, BRAND will successfully maintain its market power.

Analysis
If the Bureau was of the view that BRAND's conduct could be for the purpose of forcing the replacement of sales of Product A with those of Product B to exclude or impede entry by GENERIC and Generic A, the Bureau would not view the withdrawal of Product A by BRAND as a mere exercise of its patent right and thereby conduct exempt under subsection 79(5). The Bureau would also not view the conduct as reviewable under section 32. Accordingly, the Bureau would likely

[58] For an example of a Bureau enforcement matter involving conduct similar to that in this Example, see *Competition Bureau Statement Regarding the Inquiry into Alleged Anti-Competitive Conduct by Alcon Canada Inc.* Available at: http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/03686.html.

examine the conduct of BRAND under the abuse of dominant position provision (section 79) of the Act.

The Bureau would first seek to define a relevant market that encompasses Product A. Given that Generic A is bioequivalent to Product A, the Bureau would likely conclude that both drugs are in the same relevant market. The Bureau would also consider whether other drugs, such as Product B, are sufficiently close substitutes to Product A to be considered in the relevant market. Important evidence as to what drugs may be in the relevant market would come from the evidence of physician/patient switching behaviour when BRAND withdrew Product A from the marketplace.

If the Bureau determined that BRAND was dominant in a relevant market that included Generic A and Product A, it would then proceed to determine whether BRAND's conduct, including that of withdrawing Product A from the marketplace, constituted a practice of anti-competitive acts. In making this determination, the Bureau would examine the likely effect of BRAND's conduct on the ability of GENERIC to enter and compete in the relevant market. For example, the Bureau would examine the possibility of GENERIC marketing Generic A directly to physicians. Ultimately, the Bureau would seek to determine whether BRAND's conduct would either significantly foreclose the entry of GENERIC or delay that entry for a significant period.

The Bureau would also examine whether the purpose of BRAND's conduct was to delay or foreclose the supply of Generic A by GENERIC, or whether there was some other legitimate business justification. For example, if BRAND removed Product A from the market because it was not profitable, that may be viewed as a legitimate business justification. The Bureau would also consult with persons with relevant expert medical knowledge concerning the products at issue. If the Bureau determined that physicians viewed Product B as providing no or trivial medical benefit over Product A, it would doubt any argument advanced that Product B is superior to Product A and the purpose of the withdrawal of Product A was to transition patients to a higher-quality treatment.

If the Bureau concluded that BRAND was dominant in a relevant market and that it had engaged in a practice of anti-competitive acts, it would also assess whether BRAND's conduct had caused a substantial lessening or prevention of competition. As part of this analysis, the Bureau would likely examine the difference between the price of Product B and the price at which Generic A would have been expected to be sold if it had not been delayed or foreclosed by BRAND's conduct. As other evidence of harm resulting from BRAND's conduct, the Bureau would likely cite the negative effect of Product A's withdrawal on limiting physician/patient choice for prescription drugs.

If the Bureau concluded that the constituent elements of subsection 79(1) were met, it would likely seek to negotiate a remedy[59] with BRAND and failing that, bring an application before the Tribunal.

Example 9B: Product Switching ("Soft" Switch)
Consider the same set of circumstances as in Example 9A but where BRAND does not withdraw Product A from the market. Instead, BRAND continues to sell Product A but it stops promoting the drug to physicians.

Analysis
In this circumstance, BRAND's conduct would not likely raise an issue under the Act provided that it did not anti-competitively undermine the prescription base of Product A (e.g., making false or misleading statements about Product A).

7.2 Conduct Involving Patent Assertion Entities

A patent assertion entity ("PAE") can generally be described as a business that acquires or otherwise obtains the legal rights to patents from innovating companies for the purpose of asserting them against potential infringers who are using the patented technologies. Importantly, a PAE does not use or manufacture products based on the patented technologies it acquires.

Some have argued that competitive concerns arise with PAEs asserting that their patents have been infringed and using aggressive tactics in order to extract a settlement payment or licensing royalties. This may result in increased royalties in settlements, relative to the situation if the infringement suits had been brought by the original patentees, as PAEs face different incentives and are not open to infringement counterclaims. PAEs however may also be viewed as beneficial for innovation because the legitimate assertion of patent rights can assist innovators in maximizing their returns from their research efforts, which in turn would provide stimulus for further research. The role of competition law enforcement with respect to PAEs is a rapidly evolving area of thought and, as developments occur, the Bureau will continue to refine its enforcement approach and may revisit its guidance in this area.

There is also a concern that PAEs (among others) may use false and misleading claims in order to extract license fees from small and medium-sized enterprises that pay the fees in order to avoid a possible patent infringement lawsuit.

Example 10: Representations Made in the Context of Asserting Patents
Firm A acquired patents from innovating companies for the purpose of earning revenue by asserting them against firms that are infringing the patented technologies. Following the acquisition, Firm A identified a significant number of

[59] The remedy that the Bureau may seek will depend on the particular facts of the case. In some cases, simply ordering the patentee to make its former product available again for sale may not adequately overcome the anti-competitive conduct. For example, the Bureau may seek an order requiring the brand firm to notify physicians informing them that its former product has been re-supplied.

businesses that it had evidence were infringing the patents, and sent notices by registered mail to all of the businesses. The notices indicated that firm A had acquired the patents, and that it believed that the recipient of the letter had infringed one or more of the patents.

The notice further indicated that if the recipient was indeed infringing one or more of the patents, the recipient would need to pay a significant licensing fee in order to avoid litigation. In its notices, Firm A claimed that many businesses had already paid the licensing fee, and that it would commence legal proceedings against the recipient within two weeks if the licensing fee was not paid immediately. A number of businesses that received these letters complained to the Bureau.

Analysis

Like all businesses in Canada, PAEs must abide by the misleading advertising and deceptive marketing practices provisions of the Act. The Act prohibits making a representation to the public that is false or misleading in a material respect, where the representation is made to promote a product or business interest. Such matters are reviewable pursuant to paragraph 74.01(1)(a) of the Act.

Based on the facts, it is clear that the purpose of the notices in this case was to promote Firm A's business interests by getting recipients to pay and that the notices, which were sent to a significant number of businesses, were sent to members of the public. The Bureau's examination, therefore, would focus on whether the notices included representations that were false or misleading in a material respect.

In determining whether the representations were false or misleading, the Bureau would consider both the general impression created by the notice, as well as its literal meaning. In the example, the representations created the general impression that many businesses had already paid Firm A the licensing fee, and that the firm would commence legal proceedings against the recipient if the licensing fee was not paid immediately.

If the Bureau's examination in this example revealed that both representations were true, then they would not raise any concerns under the misleading advertising and deceptive marketing provisions of the Act.

Conversely, if the examination revealed that either of Firm A's claims were not true, in that other businesses had not already paid Firm A the licensing fee, or that Firm A had no intention of commencing legal proceedings against the recipients, then this would raise concerns that the representations were false or misleading. If the Bureau concluded that the representations would affect the likelihood of the recipients taking some significant action in response to the claims, up to and including acceding to the demand, then the representations would also be considered material. In such event, the Bureau would have grounds to file a notice of application with the Tribunal or a court alleging that Firm A had engaged in reviewable conduct contrary to section 74.01(1)(a) of the Act.

If the Tribunal or court found that reviewable conduct did indeed occur, and that Firm A failed to exercise due diligence to prevent the conduct from occurring, it could order the firm not to further engage in the conduct, to pay an administrative monetary penalty, to pay restitution, and to publish a corrective notice.

In addition, the Act provides that if a false or misleading representation is made knowingly or recklessly, then it may contravene the criminal provisions found in section 52 of the Act. In this regard, the Bureau's bulletin on choice of track indicates that in most instances of misleading advertising, the civil track will be pursued, unless certain criteria are satisfied.[60] Cases which meet these criteria can be referred to the DPP for prosecution. Convictions under the criminal provisions can result in fines at the discretion of the court, as well as imprisonment for individuals of up to a maximum of 14 years.

Example 11: Assignment of Patents for Enforcement
OPCO1 is a firm that produces gadgets and has a number of patents related to gadget technology. Historically OPCO1 has enforced its patents itself with limited success – however, recently OPCO1 assigned its patents to PAE, a firm that exclusively enforces IP. Under their arrangement OPCO1 and PAE will split any revenues that result from enforcing the patents. PAE does not have the ability to enforce any other IP pertaining to gadgets.

Subsequently, PAE sues a rival gadget manufacturer, OPCO2, alleging that many of OPCO2's gadget designs infringe the patents assigned to PAE by OPCO1.

Analysis
Because the Bureau considers the assignment of a patent as something more than the mere exercise of an IP right, this conduct would potentially be subject to review under the general provisions of the Act.

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[60] In order to proceed on a criminal track both of the following criteria must be satisfied:

a. There must be clear and compelling evidence suggesting that the accused knowingly or recklessly made a false or misleading representation to the public. An example of such evidence is the continuation of a practice by the accused after complaints have been made by consumers directly to the accused; and
b. If there is clear and compelling evidence that the accused knowingly or recklessly made a false or misleading representation to the public, and this evidence is available, the Bureau must also be satisfied that criminal prosecution would be in the public interest. The factors to be taken into account in making this public interest determination will vary from case to case, and may include the seriousness of the alleged offence and mitigating factors. For more information see the *Misleading Representations and Deceptive Marketing Practices: Choice of Criminal or Civil Track under the Competition Act Bulletin*; http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/01223.html.

As noted in subsection 4.2.1, although the Act may prescribe limits on to whom and how an IP owner may license, transfer, or sell their IP, it does not challenge the fundamental right to do so. The Bureau is of the view that, in general, IP holders arranging their affairs so as to more effectively enforce their IP rights do not raise issues under the Act. This may include engaging the services of firms that specialize in the enforcement of IP rights.[61]

In this case, the Bureau would likely conclude the assignment of OPCO1's patents to PAE simply for the purpose of more effective enforcement does not raise issues under the Act.

7.3 Settlements of Proceedings under the Patented Medicines Notice of Compliance Regulations

The discussion and hypothetical examples in this subsection are designed to illustrate the analytical framework that would be applied by the Bureau in conducting its review of settlements between brand and generic pharmaceutical companies of proceedings under the Patented Medicines Notice of Compliance ("PMNOC") regulations. For details on these regulations the reader may wish to consult Health Canada's publication, Guidance Document: Patented Medicines (Notice of Compliance) Regulations available at: http://www.hc-sc.gc.ca/dhp-mps/prodpharma/applic-demande/guide-ld/patmedbrev/pmreg3_mbreg3-eng.php, or the regulations themselves at: http://laws-lois.justice.gc.ca/eng/regulations/sor-93-133/FullText.html.

The Bureau's enforcement approach to settlements can be summarized as follows:

(i) An entry-split settlement (defined below) pursuant to which the generic firm enters the market on or before patent expiry will not pose an issue under the Act (see Example 12);

(ii) A settlement with a payment (defined below) to the generic firm pursuant to which the generic firm enters the market on or before patent expiry may be reviewed under section 90.1 (see Example 13), or possibly section 79;[62]

(iii) The Bureau will not review a settlement under section 45 unless (a) the settlement extends beyond the exclusionary potential of the patent by delaying generic entry past the date of patent expiry (see Example 14A), (b) the

[61] However, as noted in Example 6 on Patent Pooling Arrangements, issues can arise when a transfer of IP rights results in the combination of IP rights within a single entity, resulting in a substantial lessening or prevention of competition. For instance, transfers that result in patents covering substitutable technologies becoming concentrated within a single entity who can then reduce competition to a degree greater than inherent in the patents individually may raise issues under the Act. As PAE does not hold any other IP rights pertaining to gadgets, the Bureau would not have concerns in this regard based on the facts of this example.

[62] In general, agreements between competitors that may be examined under section 79 include situations where one or more party is dominant, or jointly dominant, and the agreement results in or facilitates conduct that has a negative effect on a competitor that is exclusionary, predatory or disciplinary, such that it has had, is having or is likely to have the effect of preventing or lessening competition substantially in a market.

settlement extends beyond the exclusionary potential of the patent by restricting competition for products unrelated to the patent subject to the PMNOC proceeding (see Example 14B), or (c) the settlement is a “sham” (see Example 14C).[63]

The Bureau recognizes that there are significant differences in the regulatory regimes governing pharmaceuticals in Canada relative to other jurisdictions and that these may have implications for both the incentives of parties to reach settlements and the terms of settlements that may occur in Canada. For example, three unique features of Canada’s PMNOC regulations that govern generic entry prior to patent expiry are the following:

- *Exclusivity for the first generic filer*: In Canada there is no six-month exclusivity period available to the generic firm who is the first to challenge a brand firm’s patent with respect to a particular pharmaceutical formulation. This may limit the ability of settlements in Canada involving the first generic challenger to delay the entry of subsequent generic firms. This in turn may impact the incentives of the brand and the first generic filer to enter into settlements with payments to delay generic entry.

- *Section 8 damages*: Generic firms in Canada who are engaged in litigation under the PMNOC regulations have a contingent claim to damages against the patentee pursuant to section 8 of the PMNOC regulations. The prospect of a brand being liable for these damages is a relevant consideration when evaluating the magnitude of a brand firm’s payment to the generic firm in a settlement agreement.

- *Dual Litigation*: Brand and generic firms in Canada must cope with a system of legal double jeopardy created by the PMNOC regulations. Even after having succeeded in defending a prohibition proceeding brought under the PMNOC proceedings, a generic firm faces the possibility of an infringement action by the brand firm if the generic chooses to launch prior to patent expiry. Similarly, a brand firm whose prohibition application was successful still faces the possibility of proceedings for impeachment of its patent(s). The potential follow-on litigation is a relevant consideration when evaluating the magnitude of a brand firm’s payment to the generic firm in a settlement agreement.

In addition, brand and generic firms in Canada typically face significant restrictions on the prices they are permitted to charge for their products in order to be listed on provincial formularies. The Bureau recognizes such restrictions

[63] In this context, the Bureau considers a “sham” to be a case where the parties recognize that the patent is invalid and/or not infringed and use a purported settlement of the PMNOC proceedings to engage in conduct contrary to Section 45 as opposed to addressing patent-protected rights. That is, the PMNOC regulations and the settlement are used as a disguise for an otherwise naked conspiracy.

may impact the incentives of generic firms to challenge patents and the terms of settlements to PMNOC proceedings.

7.3.1 Introduction

The Bureau recognizes that in many cases parties may wish to settle PMNOC proceedings privately rather than fully litigate a matter and risk an adverse judgement from the court. Settlements also provide a benefit to society at large by easing the burden on the court system and saving limited public resources. However, litigation settlements may pose competition risks if the agreement of the parties goes beyond what is reasonably necessary to reach a settlement, for example including a payment to delay generic competition.

If a settlement does not involve the brand firm providing any consideration to the generic firm other than allowing the generic to enter the market on or before patent expiry (an “entry-split” settlement), the Bureau would not review the settlement under the Act.[64] The Bureau would view the agreed entry date as reflecting a compromise between the parties based on each party’s underlying expectation of succeeding in the PMNOC proceedings. The greater the likelihood that the patent is valid and infringed, the later in the patent term generic entry would be expected. Furthermore, agreements where the only consideration provided by the brand is early generic entry are marked by opposing incentives, with brands seeking later entry and generics seeking earlier entry. If there is no other consideration flowing from the brand to the generic firm there would be no reason to believe that the terms of the settlement were for anything other than a compromise on the patent merits.

In contrast to entry-split settlements, if a settlement involves the brand firm providing compensation to the generic firm in addition to allowing generic market entry (a “payment”), the Bureau may review the settlement under the Act. In this circumstance the payment could create competitive harm if it serves as compensation to the generic firm in return for delaying its entry into the market. Because the brand firm would typically make more profit by keeping the generic out of the market than the brand firm and the generic firm would receive in total by competing in the market (because generics are typically sold at a much lower price than branded drugs, with the difference being savings that would accrue to drug buyers), the parties have an aligned incentive to cede the market to the brand firm and split the profits from preventing competition. The competition concern with the settlement is that the payment obtained by the generic firm may arise from the sharing of the brand firm’s (now guaranteed) supra-competitive profits. Drug buyers may be impacted by this type of settlement through higher prices, and patients may experience delayed access to affordable medicines.

Since a settlement involves more than one party it is not unilateral conduct and the Bureau would view it as potentially something more than the mere exercise of

[64] When reviewing a settlement, the Bureau will also look at other agreements that the settling parties may have made during the same period of time when the settlement was reached.

the patent right. Accordingly, the Bureau would review settlements under the general provisions of the Act (generally section 90.1) rather than section 32. Likewise, the Bureau would not assume that a valid patent of the brand firm was infringed.

The Bureau's approach to assessing competitor collaborations, including settlements that may delay generic entry, is reflected in the *Competitor Collaboration Guidelines* ("CCGs").[65] Accordingly, other than in the narrow circumstances described below, the Bureau would review such a settlement under section 90.1 of the Act because it would not be viewed as an agreement between competitors to fix prices, allocate markets or restrict output (i.e., a "naked restraint" on competition).

However, the Bureau is aware that settlement practices are dynamic and continue to evolve, and circumstances may arise where the Bureau elects to review a settlement with a payment under section 79 if the elements of section 79 are present.

A settlement may be reviewed under section 45 only where it extends beyond the exclusionary potential of the patent or is a "sham". The Bureau anticipates that such circumstances would rarely occur.

7.3.2 Review Under Sections 90.1 and 79 of the Act

Section 90.1 applies to agreements between parties that are competitors or potential competitors. Subsection 90.1(11) defines competitors to include not just actual competitors, but also "a person who it is reasonable to believe would be likely to compete" with respect to the relevant product "in the absence of the agreement or arrangement". Accordingly, the fact that a brand firm and a generic firm did not compete with respect to the relevant pharmaceutical drug when the settlement was concluded or during the term of the settlement would not prevent the Bureau from reviewing the settlement under section 90.1. The Bureau would determine whether the brand firm and the generic firm are potential competitors as part of its analysis of the nature and extent of the relevant market.

Both sections 90.1 and 79 of the Act require the Bureau to establish that a settlement has the effect of causing a likely substantial prevention or lessening of competition. Guided by jurisprudence, the Bureau would likely determine whether a settlement caused harm to competition by adopting a "but-for" test. This test requires determining what would likely have occurred but for the settlement, including whether the brand firm and the generic firm would have been likely to compete earlier than the generic entry date specified in the settlement, and whether entry would have resulted in the discipline of the brand firm's market power through the introduction of a lower cost alternative for drug buyers. This analysis would require determining whether the magnitude of the payment was

[65] *Supra* note 57.

so large that it likely had the effect of delaying generic entry. Importantly, the alternative scenario “but for” a settlement that includes a payment is not necessarily the fully litigated outcome. It is possible that the parties may have reached an alternative settlement that was less restrictive to generic entry.

The form of the payment from the brand firm to the generic firm does not change the Bureau’s fundamental analysis as to whether its effect was to delay generic entry. The payment may involve a simple monetary transfer from the brand firm to the generic firm. Alternatively, the payment could involve a monetary transfer with an agreement by the generic firm to provide the brand firm with particular services such as to market or co-promote products; to provide inventory or backup manufacturing services; to supply raw material or finished drug products; or to enter into development agreements in the form of up-front payments, milestones, sales percentages, or development fees for unrelated products. In these circumstances, the Bureau would consider evidence to determine whether the payment was commensurate with the services provided, rather than a disguised payment to the generic firm for delaying its entry. In making such a determination, the Bureau would consider factors such as (i) a history of collaboration between the brand firm and the generic firm; (ii) whether the brand firm (or similarly-situated firms) typically enters into arrangements for such services; (iii) previous attempts by the brand firm to contract for the service; (iv) any documents reflecting the need for the transaction; (v) any documents reflecting the valuation of services; and (vi) the typical payments for such services in the industry.

In determining if a payment likely had the effect of delaying a generic firm’s entry, the Bureau would consider factors such as (i) the fair market value of any goods or services provided by the generic firm; (ii) the magnitude of the brand firm’s section 8 damages exposure under the PMNOC regulations; and (iii) the brand firm’s expected remaining litigation costs absent settlement. With respect to (iii), expected remaining litigation costs absent settlement may include the expected costs of a subsequent patent infringement action and impeachment counterclaim, and potential adverse cost awards at the prohibition application stage and in an infringement/impeachment proceeding. If a payment was within a reasonable estimate of these factors based on information known at the time the settlement was reached, the Bureau would conclude that the settlement does not raise issues under the Act. The Bureau would also consider other justifications and evidence proffered by the parties.

When reviewing a settlement under section 90.1 of the Act, the Bureau would consider possible efficiencies that could be realized through the settlement. When assessing potential efficiencies, the Bureau would consider factors such as the credibility of the claims, the link to the settlement, the likelihood of the benefits being achieved, and whether the benefits would or could not be obtained in the absence of the settlement. If the Bureau determines that the efficiency exception is not satisfied or cannot determine whether it is satisfied due to insufficient information, it may seek a remedy from the Tribunal to prohibit the settlement. Under section 90.1, the Tribunal may make an order prohibiting any person from doing anything under the settlement, or requiring any person (with the consent of that person and the Bureau) to take any other action.

If reviewing the settlement under section 79 of the Act, the Bureau would consider possible business justifications in its determination of whether the settlement was or was part of a practice of anti-competitive acts. In making its determination, the Bureau would consider a number of factors, including the credibility of the justifications and the link to the settlement. If the Bureau determines that the constituent elements of section 79 of the Act are met, it may seek a remedy from the Tribunal to prohibit the settlement. The remedy sought under section 79 would likely include an order from the Tribunal prohibiting the settlement or the anti-competitive terms of the settlement. The Bureau may also seek an administrative monetary penalty from the parties. In addition, the Tribunal is empowered to make an order directing any or all persons against whom an order is sought to take such actions as are reasonable to overcome the effects of the practice of anti-competitive acts in that market.

7.3.3 Review Under Section 45 of the Act

In very limited circumstances like those in Examples 14A, 14B and 14C, a settlement may reach beyond the exclusionary potential of the patent or be a sham. For example, a settlement could restrict entry beyond the end of the patent term, restrict competition among products not at issue in the PMNOC proceeding, or be entered into even though the settling parties recognize that the patent is invalid and/or not infringed.

While the Bureau will review conduct within the exclusionary potential of the patent (for example when there is a payment for delayed entry before the patent expires) under section 90.1 or 79 of the Act, section 45 focuses on settlements that clearly restrict competition beyond the exclusionary potential of the patent or are shams. In the limited circumstances where the Bureau may review a settlement under section 45 of the Act and where the constituent elements of an offence under that section are satisfied, the Bureau will consider whether the ancillary restraints defence under subsection 45(4) of the Act, or another defence set out in section 45 of the Act, may apply.[66]

Where the Bureau determines that there is sufficient evidence to establish that an agreement satisfies the ancillary restraints defence, it will not refer the matter to the DPP with a recommendation to commence a prosecution under section 45 of the Act. However, the Bureau may seek a remedy in respect of the agreement under section 90.1 of the Act if it is of the view that the settlement is likely to prevent or lessen competition substantially.

[66] As described more generally in the Bureau's CCGs, *supra* note 57, agreements that are directly related to, and reasonably necessary for giving effect to, a broader agreement may be subject to an ancillary restraints defence.

As is the case in general, parties may approach the Bureau at any time to resolve a criminal matter prior to referral to the DPP for prosecution. The Bureau's Immunity and Leniency Programs provide a clear framework for cooperation and the provision of information by cooperating parties during investigations related to Part VI of the Act.[67] However, the DPP has the sole authority to engage in plea and sentencing discussions with counsel for an accused.

While the Bureau may, where appropriate, initially elect to evaluate a settlement under the criminal conspiracy provision of the Act, the Bureau may subsequently decide that circumstances warrant pursuing a remedy under the reviewable matters provisions of the Act at any time prior to referral of the matter to the DPP for prosecution. In cases where the matter is referred, but the DPP elects not to pursue prosecution, the Bureau may choose to re-evaluate whether the settlement should be subject to a remedy under the reviewable matters provisions of the Act.

Example 12: An Entry-Split Settlement

BRAND sells innovative pharmaceutical drugs. One of its top sellers in terms of revenue, product A, will lose patent protection in ten years. GENERIC plans to launch a generic version of product A before BRAND's patent protection for product A expires. There are currently no other generics of product A on the market. Pursuant to the PMNOC regulations, GENERIC serves BRAND with a Notice of Allegation ("NOA") stating that its generic drug does not infringe BRAND's patent and that BRAND's patent is also invalid. BRAND challenges both claims in GENERIC's NOA in court.[68] Rather than have the court reach a decision in the PMNOC proceeding, BRAND and GENERIC enter into a settlement where GENERIC agrees not to market its generic version of product A until five years before patent expiry. As part of the settlement, BRAND agrees not to sue GENERIC for patent infringement when GENERIC enters the market and GENERIC agrees not to take action against BRAND to recover damages that it may be entitled to under section 8 of the PMNOC Regulations. The evidence reveals no other form of consideration, either in the settlement agreement or otherwise. At the time of reaching the settlement, GENERIC had successfully met all regulatory requirements for proving safety and efficacy of its drug.

Analysis

Given that the terms of the settlement specify a market entry date for GENERIC that is on or before the expiry date of the patent and that GENERIC is not receiving any other consideration from BRAND, the Bureau would not take action

[67] For more information, please consult the *Immunity Program under the Competition Act* (available at: http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/03248.html) and the *Leniency Program* (available at: http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/03288.html), as well as their respective FAQs.

[68] For ease of exposition, details of the process under the PMNOC Regulations are deliberately avoided. The reader is advised to consult the documents available through the links provided above for more information about the PMNOC regulations.

against the settlement under the Act. If there were no consideration other than allowing early entry flowing from BRAND to GENERIC there would be no reason to believe that the terms of the settlement were for anything other than resolving the litigation based on the merits of the case.

Example 13: A Settlement with a "Payment"

Consider the same set of circumstances as Example 12, but in this case BRAND provides a monetary payment to GENERIC in addition to allowing GENERIC to enter the market five years before patent expiry.

Analysis

This settlement could pose a competition concern for the Bureau because its terms include a payment from BRAND to GENERIC. If the Bureau were to review the settlement, it would follow its general approach to assessing competitor collaborations as outlined in the CCGs. Because the settlement did not extend beyond the exclusionary potential of the patent and was not a sham, the Bureau would likely review the settlement under section 90.1 of the Act.

For purposes of review under section 90.1 of the Act, the Bureau would typically, as an initial step, define relevant product and geographic markets that include BRAND's product A. If the generic drug is bioequivalent to product A, the Bureau would likely conclude that both drugs are in the same relevant product market.[69] The Bureau would also consider whether other drugs are sufficiently close therapeutic substitutes to product A to be included in the relevant product market. For the determination of the geographic market, the Bureau would consider all regions in Canada where product A was sold.

Section 90.1 of the Act requires the Bureau to establish that a settlement has the effect of causing a substantial prevention or lessening of competition. In determining whether "but for" the settlement BRAND and GENERIC would have been likely to compete earlier than the generic entry date specified in the settlement, the Bureau would examine the size of the payment to determine whether it was likely that the settlement had the effect of delaying GENERIC's entry. In making this determination the Bureau would consider factors such as (i) the fair market value of any goods or services provided by GENERIC; (ii) the magnitude of BRAND's section 8 damages exposure under the PMNOC regulations; and (iii) BRAND's expected remaining litigation costs absent settlement. With respect to (iii), expected remaining litigation costs absent settlement may include the expected costs of a subsequent patent infringement action and impeachment counterclaim, and potential adverse cost awards at the prohibition application stage and in an infringement/impeachment proceeding. If a payment was within a reasonable estimate of these factors, the Bureau would

[69] Mandatory generic substitution rules for drugs on provincial formularies are one of the main reasons that the introduction of generics largely supplants brand-name drugs and are a factor considered when defining relevant markets.

conclude that the settlement does not raise issues under the Act. The Bureau would also consider other justifications and evidence proffered by the parties.

As part of its analysis of whether the settlement substantially prevented or lessened competition, the Bureau would also determine whether earlier entry by GENERIC would have lowered prices paid by drug buyers. This would involve determining the likely price difference that would have prevailed between the BRAND's price of product A and GENERIC's price of product A. In addition, the Bureau would consider if other prospective suppliers of generics of product A had delivered NOAs or were likely to deliver NOAs in the near future and, if so, when they would likely enter the market. If there were other generic suppliers who had delivered NOAs and were involved in PMNOC litigation with BRAND, the Bureau would seek to determine whether BRAND was in the process of negotiating settlements with those generic suppliers and, if so, what terms and conditions were being considered.[70]

If the Bureau determined that the magnitude of the payment was so large that it likely had the effect of delaying entry, the competitive effects from GENERIC's delay were significant, and timely entry from other generic suppliers was not likely to occur on a scale and magnitude to sufficiently constrain the ability of BRAND and GENERIC to exercise market power in the relevant market, it would conclude that the settlement substantially prevented or lessened competition.

For the purpose of an analysis under section 90.1 of the Act, the Bureau will consider possible efficiency gains that may be realized through the settlement. When assessing potential efficiencies, the Bureau will consider factors such as the credibility of the claim, the link to the settlement, the likelihood of the benefits being achieved, and whether the benefits would or could not be obtained in the absence of the settlement.

Where the constituent elements of section 90.1 of the Act are met and where the efficiency exception is not satisfied, the Bureau may seek a remedy from the Tribunal to prohibit the settlement. Under section 90.1, the Tribunal may make an order prohibiting any person from doing anything under the settlement or requiring any person (with the consent of that person and the Bureau) to take any other action.

Example 14A: A Settlement beyond the Expiry Date of the Patent
Consider the same set of circumstances as in Example 13, but with the difference that GENERIC agrees to enter the market no earlier than two years after patent expiry.

Analysis

[70] The Bureau recognizes that in certain instances some documents will be covered by one or more claims of privilege.

In this case the settlement clearly goes beyond the expiry date of BRAND's patent rights. BRAND's patent expires in 10 years and the settlement prevents GENERIC entry within the next 12 years. The settlement provides BRAND with two more years of protection from competition from GENERIC than what BRAND's patent provides (assuming it is valid and infringed). In the absence of a legitimate justification, the Bureau would likely view the settlement as contravening subsection 45(1) of the Act as it reaches beyond the exclusionary potential of the patent and is a market allocation agreement where BRAND is providing a payment to GENERIC as compensation to stay out of a market after the patent expires.[71]

The Bureau would consider any evidence related to an ancillary restraints defence. In considering the defence under subsection 45(4) of the Act, the Bureau would examine whether (i) the restraint, in this case the payment from BRAND to GENERIC in return for the entry date, is ancillary to a broader or separate agreement that includes the same parties; (ii) the restraint is directly related to, and reasonably necessary for giving effect to, the objective of the broader or separate agreement; and (iii) the broader or separate agreement, when considered in the absence of the restraint, does not contravene subsection 45(1). Without evidence that the restraint is reasonably necessary for giving effect to the broader settlement between BRAND and GENERIC, however, the ancillary restraints defence would not apply to the parties' settlement and the Bureau would refer the matter to the DPP for prosecution. If the DPP elected not to pursue prosecution, the Bureau could choose to re-evaluate whether the settlement should be subject to a remedy under the reviewable matters provisions of the Act.

Example 14B: A Settlement beyond the Product Scope of the Patent
Consider the same set of circumstances as in Example 13, but with the difference that, instead of offering a monetary payment, BRAND agrees to withdraw its product from another market where it is currently competing with a product supplied by GENERIC. The product that BRAND agrees to withdraw is not one that is subject to the PMNOC proceeding where the parties reached the settlement.

Analysis
This settlement would be viewed as extending beyond the product scope of BRAND's patent rights. The agreement allows BRAND to settle the PMNOC proceeding by agreeing to limit its competition with GENERIC in a pharmaceutical market that is unrelated to its patent at issue in the proceeding. In the absence of a legitimate justification, the Bureau would view the settlement as a market allocation agreement that may contravene subsection 45(1) of the Act and thus would investigate the settlement under section 45. The Bureau

[71] As mentioned in section 7.3.2 above, the Bureau may review conduct within the exclusionary potential of the patent (for example when there is a payment for delayed entry before the patent expires) under sections 90.1 or 79 of the Act.

would consider any evidence related to an ancillary restraints defence as described in example 14A.

Example 14C: "Sham" Agreement

Consider the same set of circumstances as in Example 13, but with the difference that, during the course of its investigation, the Bureau had reason to believe that both parties recognized that the patent was not valid but that BRAND nonetheless challenged GENERIC's NOA and the parties reached an agreement where BRAND provided a payment to GENERIC as compensation for it agreeing to delay its entry into the market.

Analysis

In this case, if the Bureau had initiated an investigation under section 90.1 of the Act, once it had reason to believe that the parties recognized that the patent was not valid and/or not infringed, it could proceed under section 45 of the Act. The Bureau would investigate whether the parties reached an agreement in contravention of subsection 45(1). An ancillary restraints defence would not be applicable because the settlement was not necessary for any broader or separate agreement. Accordingly, if the Bureau believed that there was a contravention of 45(1) it would likely refer the matter to the DPP for prosecution.

7.4 Collaborative Standard Setting and Standard Essential Patents

The following discussion and hypothetical examples in this subsection are designed to illustrate the analytical framework that would be applied by the Bureau in conducting its review of business conduct involving patents that are essential to collaboratively determined industry standards. The Bureau recognizes that competition enforcement policy in this area is undergoing rapid development. Given this, the Bureau may revisit certain aspects of the guidance in this subsection in the future in light of experience, changing circumstances and court decisions.

The two primary types of industry standards are interoperability standards, which ensure that products made by different manufacturers can interoperate, and performance standards, which set minimal requirements (e.g., performance or safety) for products in an industry. The Bureau recognizes that the development of standards through formal Standards Development Organizations ("SDOs") can provide many procompetitive benefits, such as lowering production costs, increasing efficiency and consumer choice, reducing barriers to entry, and fostering interoperability and innovation. However, the Bureau also recognizes that standards development can pose competition concerns, such as reducing price and/or non-price competition, foreclosing innovative technologies and restricting firms' ability to compete by denying access to the standard or providing access on discriminatory terms.

When patented technologies are incorporated into a standard, one particular competition concern is patent "hold-up". There may be many alternative technologies that could be chosen as a standard so that any given patentee may have limited market power before a standard is chosen. Once a standard is selected, however, irreversible investments may lock firms into the standard, making switching prohibitively costly or impractical. High switching costs may create market power for the owners of patents that cover the standard due to the inability of firms using the standard to easily substitute other technologies to avoid high royalties. One way that patent hold-up can occur is when the owner of a patented technology participating in the standardization process, in violation of SDO rules, fails to disclose its patent to an SDO and then later asserts that patent when access to its patented technology is required to implement the standard ("patent ambush"). This conduct may provide the patent owner with market power that is derived from its technology being necessary to access the standard rather than its *ex ante* value to buyers or licensees.

To reduce the potential for patent hold-up, some SDOs may adopt an IP policy that requires participants to disclose their patents that are essential to the standard that the SDO selects.[72] SDOs may also ask participants to identify their most restrictive licensing terms and conditions, including the maximum royalty rate that they would demand if access to their patents becomes necessary to implement the standard. The Bureau recognizes that SDO participants may rely on such commitments to facilitate bilateral licensing negotiations necessary for the successful adoption of the standard and to provide assurances to firms who wish to use the standard that they will be able to obtain access to the necessary patented technologies. The Bureau also recognizes that before a standard is chosen, SDOs may facilitate negotiations between participants who are potential licensees of the standard and IP owners of rival technologies. Such negotiations provide SDO participants important information that allows them to choose a standard based not only on technical merit, but also on the cost of accessing the IP needed to implement that standard.

In the circumstance that the Bureau were to review joint conduct involving SDO participants, if the Bureau determined that the arrangement was for the purpose of setting an industry standard and there was no evidence that it was for the purpose of facilitating an agreement prohibited under subsection 45(1), the Bureau review would proceed under section 90.1 according to the analytical framework described in the CCGs.

Even when an SDO promotes IP disclosure, patent hold-up can still arise if an owner of a patented technology makes an *ex ante* licensing commitment, such as an explicit maximum royalty rate, to encourage its technology to be incorporated into a standard and then later, if successful, abandons that commitment by charging a royalty higher than the maximum royalty it promised to charge ("reneging on a licensing commitment").[73] The concern in this

[72] References in the Guidelines to SDO "participants" is meant to also include SDO members.
[73] Often participants in SDOs make a commitment to license on fair, reasonable and non-discriminatory terms to all prospective licensees.

circumstance is that the patentee's licensing commitment may serve to provide assurance to the SDO and firms wishing to manufacture standard-compliant products that they would have access to the patentee's technology if it was incorporated into the standard. This assurance, in part, may motivate the SDO to include the patentee's technology in the standard, and/or encourage firms to make irreversible investments to develop standard-compliant products. These investments, together with high switching costs, create a setting in which a SDO participant can gain market power because its patent is necessary to access the standard rather than from its inherent *ex ante* value to buyers or licensees.[74]

Importantly, the Bureau is not a price regulator and will leave the determination of royalty rates to negotiations between parties or the courts. Absent a clear breach of a licensing commitment (e.g., demanding a royalty exceeding an *ex ante* commitment), it will not take enforcement action against a patentee solely based on the magnitude of the royalty that it charges. Similarly, the Bureau will not regulate the specific terms and conditions that a standard essential patentee may impose when seeking to license its patents. Such terms and conditions, however, may be reviewed under the general provisions of the Act if they have the potential to cause competitive harm (e.g., bundling non-essential with essential patents or imposing no-challenge clauses).

Another way that patent hold-up can arise in the context of standard setting is when a patentee makes a licensing commitment before its technology is adopted in a standard and then later seeks injunction orders against firms that are willing to license the technology on terms and conditions meeting the commitment. By seeking an injunction against firms that are "locked-in" to the standard and that face prohibitive costs to switch to alternative technologies, the patentee can "hold up" potential licensees and demand higher royalties than if it did not seek the injunction. The use of injunctions can be particularly problematic when the patentee's patented technologies comprise only a small part of the standard, but can nonetheless block a prospective licensee's ability to manufacture and sell standard-compliant products. Given the significant risk to its business, a prospective licensee that is threatened by an injunction may be compelled to pay a royalty rate greater than the patentee's *ex ante* commitment. Similar to the other cases involving patent hold-up described above, the Bureau's concern with the patentee's conduct is that it could increase the cost of accessing the standard for firms that wish to develop products that incorporate the standard and thereby reduce their incentive to innovate or otherwise produce products that use the standard. The patentee's conduct may result in foreclosure of companies making standard-compliant products. There is also concern that the increased cost of access will result in increased prices to consumers of standard-compliant products or that the conduct excludes alternative technologies that would have been considered for the standard. Finally, the Bureau would also have concerns

[74] The Bureau's competition concerns would be the same regardless of whether the firm reneging on the licensing commitment made the commitment itself or accepted the commitment when it acquired the patent.

that the conduct may weaken incentives for firms to participate in procompetitive standard-setting activity generally.

The Bureau recognizes that a firm's commitment to license on fair, reasonable and non-discriminatory ("FRAND") terms does not mean that it is committing to license on a royalty-free basis. Firms may make large investments in research and development and are entitled to seek royalties to recover the value of their investment. Potential licensees may seek to take advantage of FRAND commitments by "holding out" for a particular royalty or simply by not undertaking licensing negotiations in good faith. Because of this potential problem, in its inquiry to determine the underlying purpose for a patentee seeking an injunction (whether seeking the injunction was, or was part of, a practice of anti-competitive acts under paragraph 79(1)(b)), the Bureau would look for evidence to determine whether the potential licensee was willing to enter into negotiations and pay a FRAND rate. The Bureau accepts that in certain circumstances it may be appropriate for a firm that has made a FRAND licensing commitment to seek an injunction against an infringing party. Circumstances where the Bureau would conclude that the seeking of an injunction could be appropriate include: (i) when a prospective licensee refuses to pay a royalty that is determined to be FRAND by a court or arbitrator; (ii) when a prospective licensee refuses to engage in licensing negotiations; (iii) when a prospective licensee constructively refuses to negotiate (for example, by insisting on terms clearly outside the bounds of what could be considered to be FRAND terms) or (iv) when a prospective licensee has no ability to pay damages (for example, a firm that is in bankruptcy).

The Bureau would likely review conduct that could result in patent hold-up under section 79 of the Act. The Bureau is of the view that conduct such as patent ambush, reneging on a license commitment or seeking an injunction against willing licensees after making a licensing commitment is "something more" than the mere exercise of patent rights. Accordingly, the Bureau would not consider the exception in subsection 79(5) to apply, nor would it review the conduct under section 32 of the Act. The Bureau also recognizes that conduct that may result in patent hold-up could be addressed as a matter of contract law and will consider this possibility when exercising its enforcement discretion in a given case. In some situations, the competitive effects caused by the conduct may not be able to be sufficiently addressed by means other than competition law remedies. For example, parties that were not participants in the SDO may be foreclosed from the market.

In determining whether a patentee undertaking conduct that could result in patent hold-up is in a dominant position as required by section 79, the Bureau would seek to determine whether the patentee had market power in markets that include the standardized technology or markets that include products that implement the standard. In considering dominance, the Bureau would consider not only a patentee's pre-existing market power (i.e., any market power held by the patentee before the conduct), but also market power derived from the conduct.

In determining whether conduct that could result in patent hold-up has had, is having or is likely to have the effect of preventing or lessening competition substantially in a market, the Bureau would look to identify whether, but for the patentee's conduct, there would likely be substantially greater competition in the markets where it has a competitive concern. The Bureau would make these determinations while considering the standard-setting context, which may be characterized by irreversible investments and high switching costs. In particular, the Bureau would examine whether the patentee's conduct created, preserved or enhanced its market power in a market that uses the standardized technology. Central to this examination, the Bureau would look to identify any alternative technologies that the SDO could have turned to at the time the standard was being chosen. The Bureau would also look to identify any alternative technical standards or technologies that firms could turn to as a substitute for the SDO standard after it was chosen. If such alternatives exist, the Bureau would seek evidence on the magnitude of the switching costs that firms would face to switch to these alternatives. If alternative technologies would likely have been chosen as the SDO standard but for the patentee's conduct and if alternatives to the SDO standard did not exist, or if switching costs were prohibitively high, the Bureau would likely conclude that the patentee increased its market power in the market that includes the standardized technology.

The Bureau would also look to determine whether competition would be harmed in markets for products that implement the SDO standard. This analysis would determine whether consumers of standard-compliant products would likely pay higher prices due to manufacturers of these products facing increased costs of accessing the standard. The Bureau would seek evidence as to the effect that royalties had on standard-compliant product prices and the options that consumers could turn to if faced with an increase in these prices.

Example 15: Standards Development Organization with IP Disclosure Policy

A private SDO is selecting a technical standard to allow the interoperability of gizmos. Many of the alternative technologies that could be selected as the standard are proprietary and are patented by firms in the industry who are also participants in the SDO. Given this, the SDO has adopted an IP disclosure policy that requires all participants to disclose any patent rights, or pending patent rights, that they have that are essential to any of the technologies that the SDO is considering as a possible standard. Furthermore, in order for SDO participants to have assurance that patent rights do not block access to the standard, the SDO requires that participants also agree to license their patents on FRAND terms to all prospective licensees if access to their proprietary technology becomes necessary to implement the standard. For added certainty, SDO participants are encouraged to specify the most restrictive licensing terms and conditions they would demand, including the maximum royalty to license their technology. Identification of maximum royalties could aid the SDO in selecting a standard as it allows an assessment of the relative costs of the various technology options in addition to their technical merits.

Analysis
Given the situation described above, the Bureau would not view the SDO's IP policy as raising any issue under the Act.

In general, if the Bureau were to investigate SDO participants for conduct such as the exercise of buyer power among potential licensees, the foreclosure of innovative technologies or the restriction of access to the standard, it would proceed according to the process outlined in its CCGs. Accordingly, if the Bureau determined that a SDO arrangement was to set an industry standard and there was no evidence that the SDO was facilitating an agreement prohibited under subsection 45(1) (e.g., price fixing among IP owners or makers of products compliant to the standard), it would not investigate SDO participants under section 45. Rather, it would proceed, if at all, under section 90.1 according to the analytical framework described in the CCGs.

Example 16: Patent "Ambush"
Firm A is a manufacturer and seller of gizmos and is also a participant in the SDO described in Example 15. After the SDO selects a standard for gizmo interoperability and firms make investments to develop gizmos that conform to the standard, Firm A launches a series of patent infringement suits against gizmo manufacturers that have developed products incorporating the standard by asserting patents that it had not disclosed to the SDO but that it claims cover the gizmo interoperability standard. Firm A was aware of patents implicated by the standard that it was required to disclose pursuant to the SDO's policy, but it did not include the patents in its IP disclosure to the SDO. Nevertheless, Firm A wishes to be compensated for its research efforts and is seeking damages from firms who are using the standard without licensing the patents that it did not disclose. Gizmo manufacturers who have been targeted by Firm A have complained to the Bureau that Firm A's failure to disclose and subsequent infringement actions constitute anti-competitive behaviour.

Analysis
The Bureau would likely review Firm A's conduct under section 79 of the Act.

Given the scenario described, the Bureau's competitive concern would be that Firm A's conduct enhanced its market power beyond that which was inherent in its patents. The purpose of the IP disclosure policy was to provide the SDO with information so that a standard could be chosen, from the various technologies that were being considered, based on technical characteristics as well as cost. By not having full information on relevant patents, the SDO was prevented from undertaking a complete assessment of the potential relevant costs when it chose the standard. Once firms have made irreversible investments in products incorporating the standard, Firm A may have increased market power to charge supra-competitive royalties for its technology if it is costly for firms to abandon the standard and switch to alternative technologies. One concern with Firm A's conduct is that it will increase the cost of accessing the standard for rival firms who wish to develop gizmos that incorporate the standard and thereby reduce their incentive to innovate or produce products that use the standard. Firm A's conduct may result in foreclosure of rival gizmo manufacturers. There is also concern that the increased cost of access will result in increased prices to consumers of gizmos that incorporate the standard or that the conduct excludes alternative technologies that would have been considered for the standard. Finally, the Bureau would also have concerns that the conduct may weaken incentives for firms to participate in procompetitive standard-setting activity generally.

In identifying evidence to support the elements of section 79, the Bureau would look to define relevant product and geographic markets. Given the competitive concerns outlined above, the Bureau would define potentially relevant markets that include the technology designated as the standard as well as gizmos and any other products that use the standard.

In determining whether Firm A's conduct was an anti-competitive act, the Bureau would consider any legitimate business justification that Firm A may advance for its conduct. Absent a legitimate business justification, the Bureau would likely infer from the reasonable, foreseeable consequence of Firm A's conduct that it was for the purpose of having an intended negative effect on competitors (firms with technologies that are substitutes for Firm A patented technologies or rivals of Firm A that develop gizmos incorporating the standard) that was predatory, disciplinary or exclusionary.

The Bureau would take the view that Firm A's conduct of not disclosing certain patents in accordance with the SDO IP disclosure policy and then asserting them against firms developing products incorporating the standard is "something more" than the mere exercise of its patent rights. Accordingly, the Bureau would not consider the exception in subsection 79(5) to apply, nor would it review the matter under section 32 of the Act.

In determining whether Firm A's conduct has had, is having or is likely to have the effect of preventing or lessening competition substantially in a market, the Bureau would look to identify whether, but for Firm A's conduct, there would likely be substantially greater competition in the markets where it has a competitive concern. The Bureau would make these determinations while considering the standard-setting context, which may be characterized by irreversible investments and high switching costs. In particular, the Bureau would examine whether Firm A's conduct created, preserved or enhanced its market power in a market that uses the standardized technology. Central to this examination, the Bureau would look to identify any alternative technologies that the SDO could have turned to at the time the standard was being chosen. The Bureau would also look to identify any alternative technical standards or technologies that gizmo producers could turn to as a substitute for the SDO standard after it was chosen. If such alternatives existed, the Bureau would seek evidence on the magnitude of the switching costs that gizmo producers would face to switch to these alternatives. If alternative technologies would likely have been chosen as the SDO standard but for the patentee's conduct and if alternatives to the SDO standard did not exist, or if switching costs were prohibitively high, the Bureau would likely conclude that Firm A increased its market power in the market that includes the standardized technology.

The Bureau would also look to determine whether competition would be harmed in the market for gizmos that implement the standard. This analysis would determine whether consumers of gizmos would likely pay higher prices due to manufacturers of standard-compliant gizmos facing increased costs of accessing the standard. The Bureau would seek evidence as to the effect that royalties had on gizmo prices and the options that consumers could turn to if faced with an increase in gizmo prices.

If the Bureau concluded that the constituent elements of subsection 79(1) of the Act were met, it would likely seek to negotiate a remedy with Firm A, and failing that, bring an application to the Tribunal.

Example 17: Reneging on a Licensing Commitment
Firm B is a manufacturer and seller of gizmos and is also a participant in the SDO described in Example 15. Firm B has disclosed its relevant patents to the SDO as well as its most restrictive licensing terms, including a commitment to a maximum royalty rate it will seek from prospective licensees if its technology is incorporated into the standard. Given participants' IP disclosures, the SDO chooses a standard that incorporates Firm B's technology and gizmo manufacturers make irreversible investments to develop gizmos conforming to the standard. Subsequently, gizmo producers who have developed products conforming to the standard complain to the Bureau that Firm B is abusing its dominant position by demanding a royalty rate in excess of the maximum it committed to in its promise to the SDO.

Analysis
The Bureau would likely review Firm B's conduct under section 79 of the Act.

As in Example 16, the Bureau's competitive concern would be that Firm B's conduct enhanced its market power beyond that which was inherent in its patents. By misleading the SDO in regard to the maximum royalty it would charge to license its patents, Firm B led the SDO to select a standard with inaccurate information as to the cost that firms would face to access that standard, which may have impacted the SDO's decision as to the technology to adopt as the standard and/or firms' decisions to invest in developing products incorporating the standard. Once implementers of the standard made irreversible investments to develop products incorporating the standard, Firm B gained increased market power and is able to charge supra-competitive royalties for its technology provided that it is costly for firms to abandon the standard and switch to alternative technologies.

The analysis of the elements of section 79 would be similar to that described in Example 16. In particular, in evaluating the purpose of Firm B's conduct to determine whether it constituted a practice of anti-competitive acts, the Bureau would consider whether there was a legitimate business justification for Firm B's seeking a royalty exceeding its maximum commitment. Importantly, as noted in the Bureau's *Enforcement Guidelines on the Abuse of Dominance Provisions*,[75] proof of the existence of some legitimate business purpose underlying the conduct, such as an increased incentive for innovation, is not sufficient. The Bureau would consider a legitimate business justification as a credible efficiency or pro-competitive rationale for the conduct, attributable to Firm B, which relates to and counterbalances the anti-competitive effects and/or subjective intent of the acts. When assessing the overriding purpose of Firm B's reneging on its licensing commitment, the Bureau would examine the credibility of any efficiency or pro-competitive claims raised by Firm B, their link to the abandonment of its licensing commitment, and the likelihood of these claims being achieved.

The Bureau would view Firm B's conduct of committing to a maximum royalty and then subsequently reneging on that commitment as "something more" than the mere exercise of its patent rights. Accordingly, the Bureau would not consider the exception in subsection 79(5) to apply, nor would it review the matter under section 32.

If the Bureau concluded that the constituent elements of subsection 79(1) of the Act were met, it could seek to negotiate a remedy with Firm B and failing that, bring an application to the Tribunal. If there was private litigation involving Firm B and participants from the SDO due to Firm B's reneging on its royalty commitment, the Bureau would use its enforcement discretion and may forbear from bringing an application to the Tribunal if it determined that the remedies from the private litigation would adequately resolve its competition concerns.

Example 18: Seeking an Injunction after Making a Licensing Commitment
Consider a scenario similar to Example 17, but where Firm C (a manufacturer and seller of gizmos) makes a FRAND licensing commitment according to the SDO policy and the SDO ultimately adopts a standard for which Firm C's patented technology is essential. Subsequently, however, Firm C faces difficulties in reaching agreement with willing licensees on terms and conditions for licensing, including acceptable royalties. To protect the patents that it views

[75] *Enforcement Guidelines on the Abuse of Dominance Provisions (Sections 78 and 79 of the Competition Act)*, September 2012. Available at: http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/03497.html.

as being used without adequate compensation, Firm C seeks injunction orders against several firms that have made investments to develop and sell competing gizmos that implement the standard. The Bureau receives complaints that Firm C is abusing its dominant position by seeking injunctions when it had committed to license its patents on FRAND terms.

Analysis

The Bureau would likely review Firm C’s conduct under section 79 of the Act.

The Bureau’s competitive concern would be that Firm C’s licensing commitment served to provide assurance to the SDO and other gizmo manufacturers that they would have access to the standard if they incorporated Firm C’s technology. This commitment, in part, motivated the SDO to include Firm C’s technology in the standard, and/or encourage firms to make irreversible investments to develop gizmos based on the standard. By seeking an injunction against firms that are “locked in” to the standard and that face prohibitive costs to switch to alternative technologies, Firm C can “hold up” potential licensees and demand higher royalties than if it did not seek the injunction. The use of injunctions can be particularly problematic when Firm C’s patented technologies comprise only a small part of the standard but can nonetheless block a prospective licensee’s ability to manufacture and sell gizmos. Given the significant risk to its business, a prospective licensee that is threatened by an injunction may be compelled to pay a non-FRAND royalty rate. The Bureau’s concern with Firm C’s conduct is similar to the concern with Firm A’s conduct in Example 16.

The Bureau would take the view that by making a FRAND licensing commitment and then seeking an injunction against willing licensees of its technology, Firm C is engaging in “something more” than the mere exercise of its patent rights. Accordingly, the Bureau would not consider the exception in subsection 79(5) to apply, nor would it review the matter under section 32 of the Act.

The Bureau recognizes that a firm’s commitment to license on FRAND terms does not mean that it is committing to license on a royalty-free basis. Firms may make large investments in research and development and are entitled to seek royalties to recover the value of their investment. Potential licensees may seek to take advantage of FRAND commitments by “holding out” for a particular royalty or simply by not undertaking licensing negotiations in good faith. Because of this potential problem, in its inquiry to determine the underlying purpose for Firm C seeking the injunction (whether seeking the injunction was, or was part of, a practice of anti-competitive acts under paragraph 79(1)(b)), the Bureau would examine any legitimate business justification and look for evidence to determine whether the potential licensee was willing to enter into negotiations and pay a FRAND rate. The Bureau accepts that in certain circumstances it may be appropriate for a firm that has made a FRAND licensing commitment to seek an injunction against an infringing party. Circumstances where the Bureau would conclude that the seeking of an injunction could be appropriate include: (i) when a prospective licensee refuses to pay a royalty that is determined to be FRAND by a court or arbitrator; (ii) when a prospective licensee refuses to engage in licensing negotiations; (iii) when a prospective licensee constructively refuses to negotiate (for example, by insisting on terms clearly outside the bounds of what could be considered to be FRAND terms) or (iv) when a prospective licensee has no ability to pay damages (for example, a firm that is in bankruptcy).

In determining whether Firm C's conduct of making a licensing commitment and seeking an injunction has had, is having or is likely to have the effect of preventing or lessening competition substantially in a market, the Bureau would look to identify whether, but for Firm C's conduct, there would likely be substantially greater competition in the markets where it has a competitive concern. This analysis would be similar to that described in Example 16.

If the Bureau concluded that the constituent elements of section 79(1) of the Act were met, it would likely seek to negotiate a remedy with Firm C and failing that, bring an application to the Tribunal.

How to Contact the Bureau

Anyone wishing to obtain additional information about the *Competition Act*, the *Consumer Packaging and Labelling Act*, the *Textile Labelling Act*, the *Precious Metals Marking Act* or the Bureau's program of written opinions, or to file a complaint under any of these Acts should contact the Bureau's Information Centre:

Website
www.competitionbureau.gc.ca

Address
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50 Victoria Street
Gatineau, Quebec
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Toll free: 1-800-348-5358
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