THE MyCC GUIDELINES ON INTELLECTUAL PROPERTY RIGHTS AND COMPETITION LAW

1.0 Introduction

These Guidelines provide guidance on the approach of the Malaysia Competition Commission (MyCC) with respect to any competition issues under the Competition Act 2010 ('the Act') relating to intellectual property (IP). These Guidelines should be read together with other Guidelines issued by the MyCC, for example, the Guidelines on Market Definition, the Guidelines on Chapter 1 Prohibition and the Guidelines on Chapter 2 Prohibitions. Because of the subject matter, these Guidelines are necessarily technical in nature and enterprises are strongly advised to consult with IP and competition law practitioners in cases of any uncertainty.

2.0 Overview of Intellectual Property Law

Intellectual property refers to creations of the mind, such as inventions; literary and artistic works; designs; and symbols, names and images used in commerce.[1] It comprises of patent, copyright, integrated circuits, industrial design, trade marks, breach of confidence, plant variety and geographical indication.

The purpose of copyright law is to protect aesthetic creation. Under the Copyright Act 1987, the following works are protected: literary, artistic and musical works, sound recordings, films, broadcasts, published edition and also performer's rights. The Layout-Designs of Integrated Circuits Act 2000 protects the design of integrated circuits. Industrial design law is meant to protect the aesthetic appearance of an article and is covered by the Industrial Design Act 1996. Patent law gives protection to the owner of invention which solves a problem in the field of technology. Newly developed varieties of plants can be protected under the Protection of New Plant Varieties Act 2004. Trade marks are commercial identifications such as words, designs, slogans, logos, symbols, signatures, labels, names or any combination thereof. On satisfying certain conditions, the owner of the mark may apply for registration of his goods or services under the Trade Marks Act 1976. On attainment of the above rights, the owner has certain exclusive rights to exclude others from commercialising his intellectual property. Trade secrets like know-how, secret recipes or processes are usually a vital component in IP assignment and licensing agreements. They are protected under the law on breach of confidential information.

3.0 Interface between Intellectual Property and Competition law

[1] See WIPO website at http://www.wipo.int/about-ip/en/ (7.8.2017).

Intellectual Property confers on the rights owners certain manufacturing and marketing exclusivity that enable them to enter into agreements with others with the purpose of commercialising these intellectual assets. These rights of exclusivity may confer on the owner of such rights market power which may affect competition in the market. Nevertheless, the promotion of intellectual property rights (IPRs) incentivises enterprises to produce useful products and services meant to improve the livelihood of mankind and hence, enhance consumer welfare. In a similar manner, competition law aims to prohibit or restrain anti-competitive activities which may result in distortion in the market. The conduct of IP owners may, in some circumstances, make it difficult for rival companies to sell substitute products and technology in the market. Intellectual property owners may also reach a dominant position in the market such that they are able to dictate unfair terms and conditions on other market players.

Intellectual property falls within the purview of competition law as the definition of goods under the Competition Act 2010 (the Act) covers property of every kind, whether tangible or intangible. Generally, the MyCC would consider IP licensing to be pro-competitive. However, any dealing involving IPRs may fall within the restrictions imposed by the Act. For example, the MyCC may be concerned if:

- an enterprise improperly abuses the IP system to obtain undeserved market power (section 4 of the Competition Act 2010), or
- any market power created by the IPR is used anti-competitively (section 10 of the Competition Act 2010).

To illustrate, an agreement between IPR holders may have an adverse impact on downstream competition. Higher prices and excess profits, which do not form part of the proper reward from the innovation, may result from the anti-competitive agreement. Another example is where an IPR holder imposes conditions on a licensee, such as limiting the amount of product that the licensee can produce. The IPR holder is limiting competition in a downstream market in order to charge a higher price for the licence.

It has to be noted that within the intellectual property regime, there are mechanisms to control the abuse of intellectual property rights by the owner. The first relates to the issuance of compulsory licences under Part X of the Patents Act 1983 (the Patents Act). The second relates to the allowance of government use of patented products and processes for certain specified situations under section 84 of the Patents Act. The Patents Act also contains provisions on invalid clauses considered as a form of patent misuse in section 45.

Similar provisions on compulsory licence can be found in section 27(1)(c) of the Industrial Designs Act 1996, sections 31(1) and 27E(1) of Copyright Act 1987, Part V of the Layout-Designs of Integrated Circuits Act 2000 and section 36(1) of the Protection of New Plant Varieties Act 2004.

4.0 Defining the Relevant Market Where Intellectual Property Rights Are Involved

The Guidelines on Market Definition is a separate guideline dealing with market definition. Enterprises are encouraged to be familiar with the way the MyCC defines a market, as the relevant market for competition law purposes adopts a market definition that may not be the way a market is defined in ordinary commercial practice in an industry.

For conduct involving IP, the MyCC would normally define the relevant market based on one of the following: the final or intermediate products incorporating the IP (the product market), the processes or technology incorporating the IP (technology market) or the intangible knowledge or know-how that constitutes the IP (innovation or R&D market). In cases involving the licensing of IP, the MyCC does not define a relevant market around a licence, but rather focuses on what the legal rights granted to the licensee actually protect.

4.1 Goods/Product Markets

The goods/product markets refer to markets incorporating IPRs, including final or intermediate goods made using the IP, for example, markets for computer chips, pharmaceuticals, books and films. The market will be defined to include close substitutes for the goods or services under investigation. When enterprises deal with their goods/product incorporating IP in a manner which would adversely impact on their competitors' ability to compete effectively in either selling or developing new goods/product, it may lead to competition law concerns.

4.2 Technology Markets

Technology markets consist of the intellectual property that is licensed and its close substitutes. This refers to the technologies that are close enough to constitute substitutes to the licensed technology that they significantly prevent the exercise of market power with respect to the intellectual property that is licensed. When rights to intellectual property are marketed separately from the products in which they are used, the MyCC may analyse the competitive effects of a licensing arrangement in a technology market.

In some cases, competition may also be on the basis of product differences (protected by the IPRs) rather than on price. Product differences create brand loyalty which may make consumers insensitive to price. The MyCC would, thus, be sensitive to the possibility that a product based on a particular patent, copyright or trade mark could be in its own separate market for competition law purposes.

If the necessary market data is available, the MyCC will identify a technology's close substitutes to determine the relevant market without having to rely on the Hypothetical Monopolist Test (HMT), especially when the anti-competitive concern is retrospective or has already taken place.

Illustration 1

Alpha holds a patent over a technology to package liquid or semi liquid food products in cartons. Beta seeks a licence for the use of this patented technology in his factory. Alpha offers to provide the licence at 10% higher than normal licensing rate and requires Beta to also purchase plastics use for packaging from it. If there is no substitute for that technology in the market, then the relevant market is that technology, thus, the conduct of Alpha may be anti-competitive.

4.3 Innovation Market or Research and Development (R&D) Market

An arrangement may have anti-competitive effects that cannot be adequately assessed through the analysis of products and technology market. A licensing arrangement may affect innovation that is related to research and development of new products or services. Or, when technological advances result in innovative products which have no actual or potential competition in the relevant market yet. Hence, it is important to look at the capabilities of enterprises at that time to determine the relevant market. Capabilities are assessed by looking at the enterprise's skills and assets at that time. Thus, an innovation or R&D market consists of the assets (technologies, laboratory, equipment, etc.) comprising R&D related to the identification of commercialisable products or directed to particular new or improved goods or processes, and the close substitutes for that research and development.

Illustration 2

Two of the largest enterprises, Alpha and Beta, specialising in the manufacture of specialised steel for high-rise buildings in Malaysia plan to engage in joint research and development to produce a particular type of high strength steel. They agree to cross-license to each other and no one else all patent rights and use of know-how. The joint venture and cross-licensing arrangement could reduce competition in research and development of this high-strength steel if the market's concentration of the joint venture is substantial.

In such an instance, it is important to identify the enterprises with the necessary capability that would undertake research and development for the specialised steel. If there are many enterprises that are actively involved in research and development of the specialised steel (or can easily switch from other research and development), then the cross-licensing agreement is unlikely to be anti-competitive. If, however, there are only a few firms actually and potentially involved in research and development of the specialised steel, Alpha and Beta may be able to use their strength or ability collectively to reduce investment in or otherwise to retard the pace or scope of research and development efforts of other enterprises. This may affect competition in the R&D market and raise competition concern.

It is important to note that restrictions in the innovation market may also affect competition in the other two markets i.e., goods/product and technology markets. The MyCC will also take into account the markets for the relevant goods/product and technology which depend specifically on the knowledge or know-how, process, or, intermediate or final products towards which the innovation effort is directed.

5.0 Prohibitions under the Competition Act 2010

Conducts involving IPRs could potentially infringe either Chapter 1 or Chapter 2 Prohibitions of the Act. Separate Guidelines on Chapter 1 and Chapter 2 Prohibitions are available.

6.0 Chapter 1 Prohibition

6.1 Section 4(1) Prohibition

Chapter 1 of the Act prohibits anti-competitive agreements between enterprises and anti-competitive decisions by associations.

As explained in the Chapter 1 Guidelines, horizontal agreements are agreements made between competitors (i.e., in the same market) or between those who are not competitors but who operate at the same level in the production/distribution chain. Vertical agreements involve parties at different levels of production/distribution, and involve either a seller and buyer, or a licensor and licensee. These agreements may be of concerns to the MyCC if the purpose or outcome of the agreement is to affect healthy competition in the market by either one of the three ways, i.e., significantly prevent, restrict or distort competition in any market for goods or services.

Illustration 3

Alpha, a car manufacturer, owns registered designs and copyright over individual body parts and components for an X brand car. Alpha does not manufacture its own spare parts but outsource to other companies. Beta, a spare parts manufacturer, seeks a licence from Alpha to produce exhaust pipes for the X brand car. The terms of the licence is that Beta cannot sell its spare parts below the recommended retail price set by Alpha and it is only allowed to sell its product in a designated territory.

As a general rule, the mere fact of ownership of a copyright and design would not be regarded as anti-competitive per se. Intellectual property confers certain exclusive rights which entitle the right-holders to choose who to grant licence to and subject to what terms.

In the example, the facts that the licensee cannot sell the exhaust pipes below a certain price and that it is only allowed to sell in a designated territory show that the agreement may significantly prevent, restrict or distort competition in any market for X brand car's exhaust pipes. The relationship between Alpha and Beta is considered as a vertical relationship as both are not in the same level of supply chain and in the same market.

While distinguishing between horizontal and vertical agreements is usually straight-forward when considering agreements in production and distribution, it is sometimes more difficult to make the distinction when IPRs are involved. Licensing agreements that appear, on the surface, to be vertical (between enterprises at different levels in the production/distribution chain) may also have an adverse effect on horizontal competition in either licensing or product markets.

The following discussion deals with vertical licensing agreement first followed by horizontal agreements in the ensuing section.

6.1.1 Vertical Intellectual Property Licensing Agreements

Intellectual property gives certain exclusive rights to the IP owners including the power to prevent others from commercially exploiting the IP without their consent. Such consent is normally given through licensing agreements for the purpose of production, distribution or sale of goods produced under the IP. The relationship between the IP owner and the licensee would normally be regarded as a vertical arrangement.

Section 2 of the Act defines "vertical agreements" as "an agreement between enterprises each of which operates at a different level in the production or distribution chain." As production, distribution or sale arrangements are not between competitors at the same level, the relationship between the IP owner and the other party may be described as vertical.

A vertical agreement covers situations such as:

- A licensor, who is solely engaged in research and development, licenses to manufacturers.
- A manufacturer, who owns a patent, produces components incorporating the patent and sells those components to a manufacturer downstream who incorporates them into a final product for sale to consumers.

The following part of the Guidelines discusses the various types of vertical restrictions falling under section 4(1) of the Act.

a. *Vertical Price-Fixing*

Such a restriction is concerned with price control exercised by an IP owner over one or more of its manufacturing or selling licensees. Such control may be exercised by fixing a minimum price at which the licensee may sell IP-protected articles or by requiring the licensee to sell at the same price, or not less than the price charged by the licensor in its own sales. The price fixing can also occur at the level of distributors or retailers.

Price fixing is practised because the licensing fees obtained by the licensor are normally based on a certain percentage of the selling price. By insisting on a minimum resale price, the licensor would be able to obtain a higher royalty income. However, by imposing such restriction on all licensees, those who are more efficient in conducting their business would not be able to lower their prices. Hence, there would not be price competition between licensees. The Guidelines on Chapter 1 Prohibition (see para 3.14) indicate that the MyCC will take a strong stance against minimum Resale Price Maintenance as one form of price fixing. Nevertheless, in line with best practices, the effect-based approach would be applied in assessing whether the "effect" of the price fixing would be anti-competitive before making any decision.

Illustration 4

Alpha has a patent on a new type of bifocal lens for eye glasses. It sells unfinished lens blanks to wholesalers who sell to finishing retailers and prescription retailers. The finishing retailers grind lens blanks to prescription. Prescription retailers examine eyes, send the prescription to a finishing retailer, then fit the finished glasses to the frame. Alpha attempts to fix prices at both the wholesale and retail levels on its patented lens and lens blanks.

This agreement may be of competition concern as Alpha attempts to extend its monopoly power beyond that allowed under the patent law. By the release of the products to the wholesalers, the patent rights owned by Alpha are exhausted. Hence, the price fixing features imposed by Alpha at both the wholesale and retail levels may violate the competition law.

b. *Territorial and Field-of-Use Restrictions*

A territorial restriction confines the licensee to the production, use or sale of the licensed goods or processes in a particular territory specified in the licence. A field of use restriction in a patent or copyright licence limits the scope of use of the patent or copyright to a particular purpose or use specified in the licence. In the case of patents, field of use licensing is common where the patented invention may be capable of use in different applications. Where this is so, the patent owner may decide to license the different applications separately to maximise his returns from the patented invention. For example, a particular drug may have curative effects both in human and livestock. To cater for the different scope of exploitation, the patent owner may decide to license an animal feed company to make, use and sell exclusively for the

animal medication field, and a pharmaceutical company, to make, use and sell for human consumption. This would lead to a more effective exploitation of the patent since the patent owner, or a particular licensee, may not have sufficient resources to practise the invention in all fields.

Both territorial and field of use licences can be beneficial as they enable the licensee to exploit the licensor's technology to the fullest within the use and territory specified. Generally, field of use and territorial restrictions are not considered as anti-competitive. Nevertheless, there may be circumstances where such restrictions may be of concern. This would include restrictions which: (i) foreclose access to competing technology; (ii) prevent licensees from developing their own technology; (iii) facilitate market allocation; (iv) fix price for any products or service supplied by the licensee; or (v) restrict resale subsequent to the first authorised sale of the patented product (the exhaustion doctrine). Each situation needs to be examined on its particular facts.

c. ***Exclusive Licensing***

This refers to a transaction where the licensor gives a licence to the licensee, under which the licensor gives up his right to use his IPR as well as the right to license others. An exclusive licence, unlike a sole licence, restricts the owner from being involved in the same activity. Generally, an exclusive licence is not likely to infringe the Act unless the licence is coupled with anti-competitive conditions such as price fixing and tying.

d. ***Exclusive Dealing***

Where the licence restrains the licensee from obtaining, distributing or selling competing technologies, this is a form of exclusive dealing. The effect of exclusive dealing is to confine the licensee to use only the licensed technology and restrain him from having access to competing technologies. In the case where the technology is a newly developed technology, such a term would ensure that the licensee would focus his time and energy to develop and promote only the licensed technology, and thus enabling him to compete with existing competing technologies. As a consequence, this would be beneficial to the consumers in the long run.

e. ***Tying***

Tying occurs where a seller refuses to sell product X unless the buyer also takes Y. In the context of patent, the most common method of extending a patent owner's rights in a patent to non-patented products is by the use of tying arrangements. A tying arrangement may consist of either a tie-in or a tie-out. Basically, a tie-in clause is one in which the licensor or vendor makes the purchase, hire or use of a patented article or invention conditional on the purchaser, hirer or licensee also acquiring other goods from the patent owner or his nominee. In a tie-out situation, the purchaser, hirer or licensee is prevented from using certain goods, materials or processes not supplied or owned by the patent owner. In the case of a process patent, a tying

arrangement could, for example, involve the patent owner allowing the licensing of the use of his process patent only if the licensee agrees to practise the process together with the use of the patent owner's machinery.

Tying can be viewed as anti-competitive when (i) the licensor has market power in the tying product, (ii) the arrangement has an adverse effect on competition in the relevant market for the tying product or the tied product and (iii) efficiency justifications for the arrangement do not outweigh the anti-competitive effects. It has to be noted that mere ownership of IPRs does not necessarily confer market power. The licensor may have provided a viable and fair alternative arrangement to the tying arrangement. The arrangement is not intended nor has the effect of extending the scope of the licensor’s patent rights.

f. ***Grant-backs***

A grant-back clause is defined as a clause in a patent licence which provides for licence or assignment to the licensor of any improvement patented by the licensee in the products or processes of the licensed patent. Such grant-back clauses may be of two main types. When the licensor acquires full patent rights to the improvement patents, the grant-back is termed an “assignment-back”. Where the licensee under the clause retains the patent rights to the improvement patents and the licensor is only given the right to use the improvement patents, for example, on a non-exclusive, royalty free basis, the grant-back is called a “licence-back”.

A grant-back is anti-competitive if it is in the form of a complete assignment or exclusive licence. In such a case, the grant-back may inhibit the incentive for the licensee to improve the licensed technology or product.

A grant-back can have pro-competitive effects if it is not exclusive to the licensor but is available to others as well. This is because the licensor is able to benefit from any improvements to his licensed technology and he will be more willing to grant the licence in the first place. The licensee is also not inhibited from improving the product as he is in the position to benefit from any improvements to the licensed technology.

6.1.2 Vertical Arrangement with Horizontal Dimension

A vertical arrangement can also have a horizontal dimension. A resale price maintenance (RPM) obligation can be used by an upstream IP owner to create a cartel at the downstream level by subjecting all its licensees to the same RPM condition. Hence, the practical effect of the vertical arrangement between the licensees would have a horizontal dimension.

In the context of manufacture of goods protected by IP, it is possible that the supplier is also one of the retailers of the manufactured goods. When the manufacturer of the goods imposed RPM conditions on the retailers, the distribution arrangement would have a horizontal dimension as in this case the manufacturer is also competing in the retail market.

6.1.3 Object or Effect

Section 4(1) deals with agreements having the *object* or *effect* being anti-competitive. The particular facts of each case will be assessed to determine whether the agreement has the *object* or *effect* of "significantly preventing, restricting or distorting competition" under section 4(1) of the Act. Enterprises are advised to refer to the MyCC Guidelines on Chapter 1 Prohibition for further guidance.

6.2 Section 4(2) Prohibition

Section 4(2) of the Act treats certain kinds of horizontal agreements between enterprises as anti-competitive. In these situations, the agreements are deemed by the Act to be anti-competitive and the MyCC does not have to determine the anti-competitive effect.

The various instances of possible anti-competitive horizontal agreements are discussed in detail below.

6.2.1 Fixing Purchase Price or Any other Trading Conditions

a. ***Price-fixing***

Horizontal price fixing occurs when IP owners of actual or potential competing technologies agree on the price they will each charge for the licence, which reduces competition in the licensing market. Vertical price fixing is discussed in greater detail in para 6.1.1(a).

b. ***Any Other Trading Conditions***

This could cover a variety of situations including determining the source of supply as explained in Illustration 5 below.

Illustration 5

Alpha and Beta are two trade mark owners in the food and beverage business who licensed the use of their trade marks and trade secrets including secret recipes for fried chicken. Alpha and Beta set up a joint venture company to supply the raw chicken. They agreed among themselves that they would impose on their respective licensees the obligation to obtain their raw chicken supply from this joint venture company as a condition for the use of their licences. The cost of the raw chicken from this joint venture company is higher than the cost of chicken obtained from other suppliers.

In this Illustration, the conduct of Alpha and Beta in obligating their licensees to obtain their supplies of raw chicken from a particular source could be regarded as anti-competitive

because they prevent their licensees from obtain raw chicken from other sources which could supply the same product at a lower cost.

The conduct of Alpha and Beta could be caught by sections 4(1) and also 4(2)(a).

c. ***Sharing Market or Sources of Supply – Section 4(2)(b)***

Actual or potential owners of competing technologies may agree to divide up the customers to whom each will operate, for example, on the basis of geographical territory. This is explained in Illustration 6 below.

Illustration 6

Alpha is a collecting society that manages performers' rights in audio and video sound recordings. Beta is another collecting society that manages performers' rights in audio and video sound recordings as well. Alpha and Beta entered into an agreement under which they agreed not to take each other's members, present or future. They also agreed to a common distribution rate for their members and the imposition of an agreed administrative charges for their collection efforts. To make it difficult for their members to leave and join any new collecting society, they agreed to force their members to sign an exclusivity agreement with them that, if a member were to leave the society he would have to give a two-years notice, during which time, he would not be entitled to any royalty distributions. Theta, a new collecting society, wants to enter the market to collect royalties for performers' rights in audio and video sound recordings. Theta later finds out it is unable to enter the market because of the arrangements made between Alpha and Beta. Further, members of Alpha and Beta are reluctant to leave their respective societies for fear of losing their dues.

In this Illustration, the conduct of Alpha and Beta in dividing the market could amount to an anti-competitive conduct because they restrict new entrants into the market by making it costly for members to leave and join the new collecting society which may offer a better deal in terms of distribution rates and may be more efficient in reducing its administrative costs.

The conduct of Alpha and Beta could be caught by sections 4(1) and also 4(2)(a).

Another form of horizontal market division is where competitors agree with each other where to source their supply from as explained in Illustration 5.

d. ***Limiting or Controlling Certain Activities or Markets– Section 4(2)(c)***

i. ***Production***

Horizontal agreements between competitors to limit or control production of goods protected by IP would lead to scarcity of the relevant goods and hence the inevitable increase in price. One classic example of such agreements is the "pay-for-delay" agreements used by the pharmaceutical industry as explained in Illustration 7.

Illustration 7

Alpha is a pharmaceutical company which owns patents for the treatment of disorders in the central nervous system, including depression. The patents over the medicinal products are expiring in two years' time. Alpha heard that Beta and Zeta, two generic producers, are already doing R&D for the release of the generic version of the drugs in the market. Alpha enters into an agreement with both Beta and Zeta, under which Alpha agrees to pay them a certain amount of money if Beta and Zeta were to delay the production and release of their products in the market.

When the patents expire, Alpha, Beta and Zeta would be potential competitors in the manufacture of the relevant drugs if the agreement in question had not been concluded. Hence, the agreement between them would be a horizontal agreement, i.e., a pay-for-delay agreement. The effect of the agreement would be that, even though the patents have expired, Alpha is still the only supplier and manufacturer of the drugs. Competition is, therefore, delayed. This would deprive consumers of alternative suppliers.

This could be an infringement under section 4(2)(c). It could also be an abuse of a dominant position under section 10.

Output restriction is a form of controlling production. This occurs when licensors of actual or potential competing technologies agree on the number of products that can be produced in total by licensees under the licences. By restricting the number of products produced downstream, their price is raised.

ii. ***Market Outlets or Market Access***

Cross-licensing agreements give the rights to two or more members of the agreement to use each other's patents. Some cross-licensing arrangements could be beneficial to both the competitors and consumers. Usually, the basis for cross-licensing agreements is the fact that the boundaries of patents are often unclear and so can only be resolved through expensive litigation. Cross-licensing allows new products to be brought more quickly into the market without the need for expensive litigation.

Patent pools are agreements between two or more parties where they agree to license their patents as a combined package. They are efficient and pro-competitive if they involve complementary technologies and/or essential patents. However, they may reduce competition if the patents involved are substitutes for each other. In this situation, competition between substitute technologies may be reduced in the licensing market and so foreclose some of the substitute technologies to licensees thereby reducing competition in the downstream product market. They might also reduce the incentive to invest in better substitute technologies.

Explanation 1

Complementary patents must be used together to produce a specific output and are not substitutes for each other. Thus, from a technical point of view, it is necessary to use complementary patents together in the production process. Therefore, to produce the desired product, one must either be the owner or the licensee of the complementary patents.

Two patents are considered substitutes if they cover alternative technologies and are non-blocking. The technologies covered by substitute patents can be used in parallel without infringing the other patent. They are therefore potentially competing with each other.

A patent concerning a particular technological field is non-blocking when it does not prevent the use of another patent in the same field because it relies on a technology not covered by the first patent.[2]

Cross licensing or patent pooling, however, can be used to control market outlets or market access. In the context of cross licensing, such practices may be anti-competitive if the licence is restricted only to certain members. A similar situation can occur in patent pooling as explained in Illustrations 8 and 9.

Illustration 8

Alpha and Beta are two firms having numerous competing patents related to specialised, computer-guided laser equipment used for a certain eye surgical procedures. They are the only two firms in Malaysia capable of providing the required equipment for such procedures.

Alpha and Beta entered into an agreement under which they pooled all their patents to a joint company Y, which in turn, licensed back the full portfolio of patents to Alpha and Beta. Under the agreement, both Alpha and Beta were permitted to sub-license the use of the equipment to eye clinics and hospitals. Further, it was also agreed by them that any

[2] World Intellectual Property Organization (WIPO) Patent Pools and Antitrust – A Comparative Analysis, March 2014, p. 4.

prospective licensing to third parties to manufacture the equipment used in the procedures were subjected to Alpha and Beta's veto powers. The veto powers resulted in the pooled patents not being licensed to any third-party manufacturers. Alpha and Beta leased their equipment to eye clinics and hospitals. The patent pooling arrangement required Alpha and Beta to pay Company Y a RM250 fee each time the surgical procedures involving the use of the pooled equipment was performed (per-procedure fee). The fees collected by Company Y would then be distributed equally between Alpha and Beta. Alpha and Beta each charged their sub-licensees a RM250 per-procedure fee. In the absence of the agreement, the level of this fee could range from RM30 to RM250.

In this Illustration, neither Alpha nor Beta had an incentive to reduce this sub-licence fee because the patent pooling agreement obligated each firm to pay this amount to the pool. As a result, consumers would not have the benefit of price competition and hence the resultant decrease in price. The "pay per-procedure" fee functioned as a price floor because as Alpha and Beta are obligated to pay RM250 per use into the pool, neither of them had any incentive to lower the sub-licence fee charged. In the absence of the pool, Alpha and Beta would have competed with each other, resulting in lower prices to eye clinics, hospitals and consumers for the use of each enterprise's patented equipment. The veto power also resulted in the foreclosure of market access to the patented technology.

Illustration 9

Five electronic firms pooled their 27 patents involving technologies for video data storage compression standard. The pool planned to issue a blanket, non-exclusive licence, to each other, at a royalty rate agreed upon by them to the exclusion of non-members of the pool. The pool included only complementary, not competing patents, each of which was deemed essential to comply with the data storage compression standard.

In this Illustration, if the 27 patents involved competing technologies, then there will be anti-competitive concern. This is because the pooling serves as a disincentive for the participants from developing alternative technologies. But if the patents involved assembling complementary components of a single technology, no issue of anti-competition will arise.

iii. *Parallel Imports*

In general, parallel importation of products protected by IPRs is allowed under the relevant IP statutes. However, IP owners may try to circumvent this by means of licensing agreements. The grant of exclusive rights with the purpose of protecting absolutely the marketing of products within a particular territory against the importation of identical products, known as parallel imports, constitutes a breach of the rules designed to protect free competition (Illustration 10, below). This is because competition which, in the absence of that contractual

obligation, would be possible between several licensees or between licensees and other undertakings is prevented.

In this context, there is a need to differentiate between active and passive sales. Active sales generally refer to the licensee in one territory actively seeking and approaching buyers or a specific group of buyers who are located in the exclusive territory of another licensed distributor. Passive sales include a licensed distributor's responses to the demands of individual buyers who are located in an area which the licensor has assigned to another distributor, including the delivery of products to such buyers. Such responses do not result from active sales.

An IP owner, through exclusive licensing agreements, can restrain its exclusive distributors from engaging in active sale outside the allocated market but must not forbid them from carrying out passive sales, as this would be a severe limitation of market competition. The parallel import of products by way of passive sale is allowed, regardless of whether an exclusive distributor is already active in the same geographical area for the same kind of product.

Illustration 10

Alpha owns the plant variety rights over a certain maize variety in Malaysia and Thailand. It grants Beta, a supplier of seeds, the exclusive licence to register, cultivate and sells the seeds for the Malaysian market. Alpha also gives a similar licence to Theta in Thailand. Under the licence, both licensees are prevented from selling the maize variety outside of their respective territory. On that basis, Beta is unable to supply orders for the maize variety for the Thai market. Similarly, Theta is unable to supply orders for the Malaysian market.

Absolute territorial licence granted to a licensee in order to enable parallel import to be controlled and prevented is considered to be anti-competitive. In this Illustration, the terms of the licence not only prevented active sales but also passive sales by disallowing the licensees from supplying even for orders which they have not actively solicited for.

e. *Technical or Technological Development*

Intellectual property rights can be used to create barriers to entry into the market, if the rights' owners agree among themselves not to license a potential new entrant to use the IP. Such agreements may foreclose competition as well as technical or technological development of the product embedded in the IP as the new entrant needs the protected technology to compete. This agreement could be in breach of section 4(2)(c) which prohibits agreements that have the object of limiting or controlling (i) production or (ii) technical or technological development, as explained in Illustration 11.

Illustration 11

Alpha and Beta are two leading manufacturers of DVD recorders. The two companies' systems are technically different, which means that the discs can only be played on compatible equipment. Alpha and Beta entered into an agreement with other DVD producers to adopt uniform application of technical standards for the DVD system. Under the agreement, they agreed on a royalty-free cross-licence of patents for the purpose of compatibility of discs with DVD recorders from different vendors. The agreement provided for the adoption of the complete system of Alpha by the other parties. No other systems were allowed. Moreover, no change could be made to the Alpha system without the consent of all parties.

In spite of the improved interoperability of discs with DVD machines of different producers, concern may arise on the ground that compliance with the DVD standards led to the exclusion of other, perhaps better, systems. Such exclusion was particularly serious in view of the pre-eminent market position enjoyed by Alpha. This constituted a restriction of competition, which was designed to limit the technical development of other DVD systems.

f. ***Investment***

Any agreements between competing enterprises to reduce investment in relation to either production or R&D which, in the absence of such agreements, the competing enterprises would have embarked on, could amount to an infringement. This would also include the "pay-for-delay" situation which is discussed in paragraph 6.2.1(d)(i).

Illustration 12

Alpha and Beta, two major pharmaceutical companies, are independently involved in R&D for a new and more efficient treatment for disease X. They entered into an agreement to suspend the R&D efforts, in order to maximise the benefits of their existing patented drugs.

This agreement may be of concern as it is likely to be subject to the Chapter 1 Prohibition as the two companies, working together, can be seen to reduce the number of new products likely to be produced, by preventing each company from continuing with independent research projects.

6.3 Effect of the Deeming Provision

Section 4(2) deems the listed horizontal agreements to be anti-competitive. These agreements are deemed to have the object of significantly preventing, restricting or distorting competition.

This means the parties to the agreement that falls under section 4(2) may be liable even though they have small market shares. The safe harbour threshold provided in the Guidelines on Chapter 1 Prohibition is not applicable to section 4(2) infringements. In this situation, the MyCC is under no obligation to define the relevant market and determine the market shares of the parties to the agreement. The only defence for enterprises charged under this section is if they are able to invoke section 5 of the Act to be relieved of their liability.

In other words, the enterprises would have to prove that there is significant identifiable technological, efficiency or social benefits directly arising from the agreement.

7.0 Section 5 – Relief of Liability

For pre-emptive measures, an enterprise wishing to be relieved of liability under section 5 needs to apply for an individual exemption under section 6 of the Act. For agreements that fall under a particular category of agreements (e.g., standard agreements), an application may be made to the MyCC for a block exemption under section 8 of the Act. In the absence of individual or block exemptions, an enterprise alleged to have infringed a Chapter 1 Prohibition can try to invoke section 5 for relief of its liability.

8.0 Chapter 2 Prohibition – Abuse of Dominance

Chapter 2 of the Act prohibits an enterprise from engaging (whether independently or collectively with other enterprises) in any conduct that amounts to an abuse of a dominant position in any market for goods or services in Malaysia.
Intellectual property rights do not necessarily create market power and market share shall not by itself be regarded as conclusive of dominance. Dominance shall be assessed in terms of an enterprise's ability to act without concern about competitor's responses or ability to dictate the terms of competition in a market in Malaysia. Other factors such as barriers to entry, countervailing buyer power, etc. may also be used in the assessment of dominance.

Dominant Position

Ownership of IP will not necessarily confer market power upon its owner. Although the IPR confers the power to exclude with respect to the specific product, process or work in question, there will often be sufficient actual or potential close substitutes for such product, process or work to prevent the existence of market power. In addition, the effective commercialisation of an IP depends on supply and demand conditions and the degree of competition in the market for the protected product, process or work. It is only when there is no close substitute for such product, process or work that there would be market power.

In some circumstances, IP may confer some market power by creating barriers to entry. The owner of a patented technology has the exclusive right over the use of that technology. This in itself would be a legal barrier to other competitors from having access to the relevant market.

Under section 10(1) of the Act, a dominant position can be held either singly or collectively. Collective dominance, i.e., a dominant position held by a number of undertakings, may be established when two or more undertakings, legally independent of each other, present themselves or act together from an economic point of view, in a particular market, as a collective entity. The economic link can be in the form of joint policies or activities, even in the absence of agreement or of other links in law. Collective dominance normally occurs in an oligopolistic market, either by way of merger or concerted practice or tacit collusion (conscious parallelism), and they may be a cause for concern under the Competition Act 2010.

In relation to IPRs, collective dominance may occur through various ways, including patent pooling, cross licensing, etc. For example, when two or more enterprises were to pool their patents, they appear to be a collective entity in the market.

Explanation 2

Tacit collusion (conscious parallelism) may materialise in oligopolistic markets when (1) the market is transparent and, thus, enables undertakings to monitor each other's activities, (2) undertakings are capable of punishing deviators from the tacit agreement and (3) competitive constraints do not jeopardise the implementation of the common strategy.[3] As far as concerted practice between enterprises is concerned, there is no distinction drawn between direct communication and tacit collusion (conscious parallelism).

However, even if an enterprise is found to be dominant in the relevant market due to its IP, that in itself is not illegal unless it abuses its dominant position.

Abuse of Dominance

Assuming an enterprise has been found to be dominant in a market, the enterprise then has a special responsibility to ensure its conduct does not impair competition in the relevant market. In general, the normal exercise of an IPR will not constitute abuse. Abuse of dominance could occur in two ways: through exploitative conduct or through exclusionary conduct. Sometimes, a particular act may both be exploitative and exclusionary.

a. *Exploitative Conduct*

Exploitative conduct can be defined as attempts by a dominant enterprise to use the opportunities provided by its market strength in order to harm customers directly. A classic example is where the enterprise is able to increase price above competitive level without any constraint. This will be discussed in greater detail in 8.1.1 below.

[3] Ariel Ezrachi, EU Competition Law: An Analytical Guide to the Leading Cases, Hart Publishing, Oxford Portland, Oregon, 2016, p. 317.

b. ***Exclusionary Conduct***

Exclusionary conducts refer to the practices of a dominant enterprise which seek to exclude its equally efficient competitors from the market.

In order to determine whether an exclusionary conduct is anti-competitive, the effect of the exclusionary conduct on competition will be assessed – which means the competitive process (both in the short-run and long-run in the IPR context) and not its impact on competitors. A patented process innovation may give a firm a dominant position in the market due to lower production costs. For such a firm, pricing just above cost may drive most other competitors, who do not have access to the patented technology, out of the market – but this would not be regarded as anti-competitive because effective competition drives inefficient competitors out of the market. This would be a perfectly legitimate use of the IPRs – which rewards innovation.

Where the legitimate use of IPRs can restrict competition in the short term, the focus will not only be on the short-term impact (e.g., on price and output) of any conduct complained of but the impact of the conduct on competition in the long term will also be considered.

8.1 Prohibited Acts Committed by a Dominant Enterprise

The following are some illustrations of the prohibited acts under Chapter 10 and are, therefore, non-exhaustive.

8.1.1 Imposing an Unfair Purchase Price or Other Unfair Condition – Section 10(2)(a)

Examples of unfair conducts include excessive pricing and post expiration royalty. Each of these will be discussed in greater detail below.

a. ***Excessive Pricing***

To determine whether the price is excessive or not, several factors, including cost of development, return of investment and reasonable profit, will be taken into account. The following benchmark may also be considered: (i) the historical cost benchmark – a comparison between the prices of the dominant enterprise and the prices it has charged in the past; (ii) the geographic benchmark – a comparison between the price of a given product over different neighbouring market; and (iii) the competitor's benchmark – a comparison between the royalty charged by the dominant enterprise with the royalty charged by its competitors.

In relation to IP, the issue is more complex. The MyCC acknowledges that the owner of an IP needs to charge above cost in order to recover research and development costs. The ability to charge higher than competitive prices and restrict competition is the essence of IPRs. The MyCC will, thus, be careful to ensure that any intervention on the basis of high prices does

not interfere with the incentives to innovate.

Illustration 13

Alpha, a patent owner of a drug called X, raises the price of X, from RM40 per vial in 2005 to the present RM4,000 per vial – a 10,000 percent increase. To enable it to raise its price without effective constraints, Alpha acquired the rights to its greatest competitive threat, a synthetic version of X, developed by Beta. The acquisition stifled competition by preventing any other company from using Beta's assets to develop a synthetic X drug, preserving Alpha's monopoly and allowing it to maintain extremely high prices for X.

The conduct of Alpha may be of concern to the MyCC as Alpha's conduct may amount to excessive pricing of its drugs.

b. ***Post Expiration Royalty***

Imposition of payment of royalty after the expiration of patent rights may be a form of unfair trading condition on a licensee. Enterprises in a dominant position should exercise caution when they attempt to impose post-expiration royalty.

Illustration 14

Alpha, the owner of various patents for hop-picking, sold a machine to each of its licensees for a flat sum and issued a licence for its use. All the patents will expire on or before 2019, but the licences issued by Alpha to the licensees obligate them to pay royalties for the patents beyond that date. The fact that the licensor is demanding royalties for "the post-expiration period" is a tell-tale sign that the licensor is using the licences to project his monopoly beyond the patent period.

Such a projection of the patent monopoly after the patent expired could be considered an anti-competitive practice. In certain situations, an obligation which may, at first sight, be seen as an attempt to extend the payment of royalty beyond the term of the patent grant, will be allowed if it is, in fact, used as a method of spreading the payments for the use of the patents during the life of the patent. If the agreement relates both to the use of patent rights and use of trade secrets (a hybrid agreement), then any royalty payment beyond the date of the expiration of the last of the patents involved may be valid as relating to a post-expiration payment intended for the use of trade secrets.

8.1.2 Limiting or Controlling Production, Market Outlets or Market Access, Technical or Technological Development or Investment - Section 10(2)(b)

If a patent owner attempts to increase the scope of the monopoly afforded by his patent through the licence agreement, this could be an anti-competitive conduct. Examples of such anti-competitive conducts include non-competition clause, product hopping and pay-for-delay.

a. *Non-competition Clause*

Such clauses are usually inserted with the intention of imposing restrictions on obtaining patents, know-how or trade marks from other companies with regard to the manufacture or sale of competing products, thus prohibiting the use of competing technology or trade marked goods. The clause involves the patent owner using his patent monopoly to suppress the manufacture of possible competing goods not covered by his patent, by, for example, imposing a condition that the licensee would not manufacture any other products other than those covered by the patent licensed.

Illustration 15

Alpha, the owner of a patented device to cut oil pipes, enters into a licence agreement with Beta which gives Beta an exclusive licence to manufacture and use (but not to sell) the pipe cutter. Beta also agrees not to manufacture or use any device which will be in competition with the device or devices covered by the licence agreement. In return, Alpha agrees not to acquire or use any other pipe cutters. The non-competition clause may be of concern as it may suppress the manufacture or use of competitive devices and reduce competitive forces which stimulate newer and better products.

b. *Product hopping*

Product hopping is a tactic by which brand name pharmaceutical companies can try to obstruct generic competitors and preserve monopoly profits on a patented drug by making modest reformulations or incremental changes that offer little or no therapeutic advantages. Prior to facing generic competition, a brand drug company can, for example, simply withdraw its original product, forcing consumers to switch to the reformulated brand drug and enabling the branded product to keep its market exclusivity and prevent consumers from obtaining the benefits of generic competition. Product hopping cases often involve drugs with expiring patent protection but can also arise outside of the context of patent law.[4]

[4] Lindsey M. Edwards, The Need for Clarification on Product Hopping: Open Questions After Namenda and Doryx, American Bar Association, p. 13.

Illustration 16

Alpha owns the patent for the drug NM, used in the treatment of Alzheimer's disease. The drug is currently available in two formulations: a twice-daily immediate release drug, NM IR, and a once daily extended-release drug, NM XR. The patent on the NM IR will expire in a year's time. Faced with the prospect of competition from generic IR, Alpha decided to withdraw virtually all NM IR from the market in order to force Alzheimer's patients who depend on NM IR to switch to XR before generic IR becomes available. The patent on NM XR will only expire 14 years later.

The MyCC would take into consideration that product innovation generally benefits consumers and inflicts harm on competitors. Evidence of "exclusionary or anticompetitive effects" is, therefore, necessary to distinguish between a conduct that defeats a competitor because of efficiency and consumer satisfaction; and a conduct that impedes competition through means other than competition on the merits.

Alpha's hard switch crosses the line from persuasion to coercion and would be regarded as anti-competitive. As long as Alpha seeks to persuade patients and their doctors to switch from NM IR to NM XR while both are on the market (the soft switch) and with generic IR drugs on the horizon, patients and doctors could evaluate the products and their generics on the merits in furtherance of competitive objectives. By effectively withdrawing NM IR prior to generic entry, Alpha forced patients to switch from NM IR to XR - the only other Alzheimer drug on the market.

8.1.3 Refusing to Supply to Particular Enterprises or Group or Category of Enterprises - Section 10(2)(c)

In the context of IP, refusal to license the right to use the IP on fair and reasonable terms could amount to refusal to supply.

a. *Refusal to License Intellectual Property Rights*

In principle, an IP owner has the right to refuse to grant a licence for the use of his IPRs. However, the refusal to grant a licence may, in certain situation, amount to an abuse of dominant position.

A distinction would be drawn between primary and secondary markets involving IPRs. The primary market involving IPRs is the technology or product market in which the enterprise is dominant due to its IPR. However, in a secondary market (or aftermarket) where the dominant enterprise's technology or product is an indispensable input to a derivative product, a refusal to license or supply may constitute abuse. Each case will be examined on its own merit.

Illustration 17

Alpha, Beta and Delta are broadcasters of television programmes in Malaysia. Under Malaysian law, they own copyright in their programme listings. Each publishes its own weekly guide to its own programmes. They provide licences for their daily listings to newspapers and periodicals free of charge. Company A, an entertainment magazine publisher, wishes to include a comprehensive monthly TV guide that covers the programmes of all broadcasters. Company A seeks to obtain licences from Alpha, Beta and Delta. The request was denied by Alpha, Beta and Delta as they want to continue with publications of their own weekly guides.

In this particular case, the conduct may be abusive if (i) the refusal to license prevents the emergence of a new product, namely, a comprehensive monthly guide; (ii) the refusal is without commercial justification; and (iii) the refusal excludes competition in the secondary market.

In this case, the MyCC may be concerned as access has been denied to basic information, the raw material necessary for the compilation of such a guide. Such behaviour can be considered as anti-competitive.

8.1.4 Discriminatory Conditions – Section 10(2)(d)

Discriminating by applying different conditions to equivalent transactions that, among others, discourages new entrants or force an enterprise to exit the market, would constitute an infringement under section 10.

An example of discriminatory condition is when an IP owner, a vertically integrated enterprise, licenses its technology to its subsidiary at a lower rate than to other enterprises which compete with the subsidiary at the downstream level. As a result, the enterprises at the downstream level cannot compete with the subsidiary as they are forced to sell their products to their customers at a higher price. This conduct amounts to a discriminatory practice as the enterprise charges different royalty rates to different users for equivalent transactions.

8.1.5 Forcing Conditions in a Contract which have No Connection with the Subject Matter of the Contract – Section 10(2)(e)

A dominant company may impose certain conditions on other enterprises that seek to use its IP in order to maintain its dominant position. Examples of such practices include tying, grant back and product bundling.

a. ***Tying***

Tying can be an infringement under both sections 4 and 10. The concept of tying has already been explained at 6.1.1(e). The following features would normally be considered:

(i) There must be separate relevant markets for the tying and tied markets;
(ii) The enterprise must be dominant in the tying market;
(iii) The licensee or buyer must be forced to take the two products or licences together; and
(iv) The tie must foreclose competition.

b. *Bundling - Mandatory Patent Package*

The practice of mandatory patent package licensing occurs where the patent owner refuses to grant a licence under one or more of his patents unless the licensee accepts and pays for additional patents which are not required by him.
It could be anti-competitive if the patent owner were to impose on the licensee to accept a licence under one patent on condition of acceptance of a licence under another, or the entire package. There must be an element of coercion, such as where there has been a request by a prospective licensee for a licence under less than all of the patents and a refusal by the licensor to grant such a licence. The mere inclusion of two or more patents in a single licence agreement does not, of itself, constitute patent misuse where the parties mutually agree that a group of patents are to form the subject matter of the licence agreement. It is only where the patent owner refuses to grant a licence under less than all of his patents, or requires a licensee to accept a licence for unwanted or inapplicable patents in order to obtain the use of the desired patents, that the practice is condemned as mandatory or coercive patent package licensing. Therefore, when the licensee is not presented with a take all or none of the patents and no alternative was available, and the package licence is purely voluntary and a licensee who does not want the whole package could obtain a licence on a reasonable basis covering any particular patent he does want, the agreement will be enforceable.

Further, a mandatory package may be permissible in certain situations where interlocking or blocking patents are involved. The expressions “interlocking patents” or “blocking patents” (i.e., complementary patents) refer to patents related to the production of one product whereby a commercially feasible product could not be manufactured under one of the patents without infringing the other.

Illustration 18

Alpha and Beta respectively own blocking/complementary patents covering a device for skimming and filtering the water in swimming pools and vacuuming the sides and bottom of such pools. Both the patents are assigned to Beta. Under the assignment, Beta grants Alpha a royalty-free, non-exclusive licence under both patents. Beta promises to license the patents collectively only, and Beta and Alpha agreed to share royalties according to a set formula. Although the two patents were issued at different times, they together covered only a single article and no commercially feasible device could be manufactured under one of the patents without infringing the other (known as blocking/complementary patents). Beta’s practice of

mandatorily licensing both patents collectively and never individually would not be regarded as anti-competitive.

The case would be different in the case of competing patents as they could possibly be used independently without infringing one another as they produced similar result or product. The bundling of two separate competing patents may be anti-competitive as users are forced to pay for additional licences which they do not require.

8.1.6 Any Predatory Behaviour towards Competitors - Section 10(2)(f)

This is meant to be a catch-all provision but the most common example relates to predatory pricing and refusal to license standard essential patents.

a. *Predatory Pricing*

Predatory pricing occurs when an enterprise sets prices below its costs, deliberately sacrificing profitability, to drive other competitors out of business or the relevant market in order to gain market share. Normally this is done to drive out competitors from the market so that the enterprise can subsequently increase the price above competitive price when there is no competition, to the detriment of the consumers. Most of the cases involving predatory pricing relate to goods. However, when the goods are protected by IPRs, the same principles relating to whether there is anti-competitive pricing would apply. As prescribed by the Guidelines on Chapter 2 Prohibition, several cost concepts can be utilized in determining predatory pricing, which may be equally useful for products protected by intellectual property rights.

b. *Refusal to License Standard-essential Patents, Fair, Reasonable and Non-discriminatory (FRAND) Licence and Royalty Stacking*

i. *Standard-Essential Patents (SEP)*

A patent that protects technology essential to a standard is called a standard-essential patent (SEP). Where products are required to be manufactured according to certain standards, it would only be possible to manufacture such products by obtaining licences to use technologies covered by one or more SEPs.

Once a standard has been agreed upon, manufacturers in the relevant industry would have to use the SEPs to ensure that their products are standard-compliant. SEPS can, therefore, confer significant market power on their holders. Companies owning the SEPs are, thus, in a position to exclude competition by behaving in an anti-competitive way. They may attempt patent hold-up by (i) extracting excessive royalties, (ii) compelling the acceptance of unfair cross licensing terms or (iii) the abandoning of invalidity proceedings.

In the context of IP, it is possible that some patents are set as the standard by certain authorities for certain equipment and gadgets. In that situation, the access to that essential patent would be necessary and the refusal to license that patent could be considered as abusive.

ii. *Fair, Reasonable and Non Discriminatory (FRAND) Terms.*

A patent owner is entitled to obtain a reasonable payment for the use of his patented technology. However, where the SEPs are concerned, the patent owners should not be allowed to prevent the use of the patented technologies if their competitors are willing to accept a licence and pay a reasonable royalty. In the determination of the royalty payment for the access of the SEPs, the standards in the EU and US are that they have to be on fair, reasonable and non discriminatory terms, or FRAND terms. This implies the adoption of the royalty rate of the SEPs before they are declared as a standard (i.e., ex ante value). The SEP holders are not allowed to increase the royalty rate to the increased value of the patents, known as the hold-up value, as a result of the elevation of the patents to SEPs.

iii. *Royalty Stacking*

Royalty stacking can arise when a standard involves numerous patents, perhaps hundreds, if not thousand. In such a case, an issue arises as to whether imposing the same rate of payment if only one patent is involved, for each of all the other patents, an act known as royalty stacking, would be considered to be an abusive conduct. If companies are forced to pay royalties to all patent holders, the royalties will “stack” on top of each other and may become excessive in the aggregate.

Illustration 19

Alpha produces Product A and prices it at RM100. Product A is covered by one patent bearing a one percent royalty. Alpha has to pay a royalty of RM1 to the patent holder in order to commercialise Product A (RM1 royalty burden).

Beta produces Product B and prices it at RM100. Product B is covered by fifty patents, each bearing a one percent royalty. Beta has to pay a royalty of RM50 to all patent holders in order to commercialise Product B (RM50 royalty burden).

Assuming that each patent holder is subject to a FRAND licensing commitment, the one percent royalty charged by the holder of the patent covering Product A is far more likely to be “reasonable” than any of the one percent royalties charged by the holders of the patents covering Product B. This is because in the case of one percent royalty for each of the fifty patents, the total royalty payment would stack up to a staggering fifty percent royalty which could be deemed excessive.

It should be noted that proceedings involving SEPs and FRAND could result in infringement under several provisions of section 10(2), including unfair excessive pricing under section 10(2)(a), refusal to supply under section 10(2)(c) and discriminatory practices under section 10(2)(d).

8.1.7 Buying Up Scarce Supply of Inputs (either Goods or Services) Where There is No Reasonable Commercial Justification - Section10 (2)(g)

This may occur, for example, when a dominant enterprise buys up all the supplies of scarce essential raw materials (substance X) needed for the manufacture of a drug for the treatment of a particular disease Y. Several competing pharmaceutical companies separately owned different patented drugs for the treatment of this disease. However, each of these patented drugs requires the use of substance X. The dominant company Sbuys up all the existing and future supplies of substance X. If the amount bought is not required for the production of its patented drug, this could amount to abuse of its dominant position. This is because there is no reasonable commercial justification for buying up all the existing and future supplies of the scarce inputs. The MyCC may regard this as an attempt to prevent the other competing enterprises from producing their own competing patented drugs.

8.2 Other Abusive Conducts

Section 10(2) does not contain an exhaustive list of abusive conducts. Other conducts which could amount to an infringement under section 10 would include margin squeeze, loyalty rebates and discounts.

a. ***Margin Squeeze (Price Squeeze)***

Margin squeeze refers to "a situation where a dominant vertically integrated enterprise which controls an essential input to a downstream market sets the price for that input at a level which results in an insufficient margin between the price at which it supplies the input to wholesale customers and the price at which it supplies the finished product in a downstream market for an efficient operator."[5] The abuse occurs when a dominant company operates at two levels of the production or distribution chain. If it is dominant in relation to a key input, it can charge a higher price to its downstream competitor which makes it harder for that competitor to compete with it on price in the downstream market.[6]

Illustration 20
Alpha has a dominant position in an essential facility known as 'local loop', that is the final section of the telecommunications network that connects a customer's premises to local switching point. Alpha does not only provide retail services over the local loop to its own

[5] The MCMC, Guidelines on Substantial Lessening of Competition, 11th July 2014, available online at www.skmm.gov.my.

[6] The MyCC, Competition Act 2010: A Guide For Business, p. 46.

customers, but also provides wholesale service to operators that provide retail services.

Alpha deliberately sets its retail price (price it charges its own customer) lower than its wholesale price (price it charges other operators for the local loop access service), despite it being insufficient for Alpha to cover its own downstream costs. Such pricing forces competitors (other operators competing in the downstream) to charge their end-users prices higher than what Alpha charges its own end-users, thus making it difficult to compete with Alpha at the retail level.

The above illustrates how a vertically integrated enterprise with a dominant position in the upstream market may cause a price squeeze by increasing the price for the upstream products (i.e., the input required by the downstream supplier or manufacturer) and by decreasing the price for the dominant enterprise's downstream products. In this respect, a dominant undertaking may restrict the competition in the relevant market via leveraging its market power over the upstream products to the downstream market.

Illustration 21

Alpha is the patent owner of a drug X for the treatment of disease Y. Alpha had previously supplied the drugs to Beta, who acted as the distributor of the drugs to home care services. Alpha then terminated the distribution agreement with Beta and ventured into the market for the drug delivery to home care services itself. Alpha grants distribution licences to third parties on the condition that the price of the drug will be bundled with other services and products such as home delivery, dispensing and the supply of accessory such as fridges and needles. The ultimate price a third party distributor has to pay for a distribution license is higher than what Alpha itself charges for its drug delivery to home care services. As a result of this pricing practice, any distributor who wants to compete with Alpha in supplying the drugs has no sufficient profit margin to sustain its business. Alpha effectively secures a monopoly in respect of home care services drug delivery.

The MyCC may be concerned with such a practice as it may amount to anti-competitive margin squeeze.

b. ***Loyalty Rebates and Discounts***

Loyalty rebates and discounts occur when buyers are required to purchase minimum volumes in order to receive the rebate or discount. According to the Guidelines on Chapter 2 Prohibitions (see paras. 3.22 – 3.24), loyalty rebates and discounts are generally pro-competitive. It is only when it is used to foreclose the market from rivals that it would be regarded as anti-competitive.

Akin to predatory pricing, most of the cases involving loyalty rebates and discounts relate to goods. However, when the goods are protected by intellectual property rights, the same principles relating to whether there is anti-competitive behaviour through loyalty rebates and discounts would apply.